National Cooperative Highway Research Program
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Volume 1—2014 Supplement

Construction Contract Law

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2004 Edition

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2014 Supplement

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Washington, DC

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THE TRANSPORTATION CONSTRUCTION CONTRACT

A. ROLE OF FEDERAL TRANSPORTATION LEGISLATION AND FUNDING

1. Background Through 2011

In the United States, legal requirements governing highway and bridge construction contracts are closely associated with project funding, an essential aspect of highway and bridge construction. Project funding and associated legal requirements have undergone significant changes in recent decades. They continue to evolve, in ways that have given rise to considerable uncertainty as this volume is being revised and updated, and which may have a considerable impact upon transportation for years to come.

a. Development of the Existing System of Federal Funding and Legal Requirements

In order to understand how project funding issues affect contractual provisions governing highway and bridge construction projects, it is important to consider, albeit briefly, how arrangements for funding transportation projects have evolved over time, what role the relationship between the federal and state governments plays in transportation funding and related legal requirements, and how currently pending policy debates over funding and the federal-state relationship may shape transportation construction contracting for decades to come.

In the early years of the United States, state legislatures typically enacted single charters, one at a time, to authorize special-purpose corporations to build specific individual turnpikes and later, plank roads, with legal powers limited to those roads only. By the early 1900s, state legislatures were consolidating authority to construct, operate, and maintain highways and bridges into the hands of state highway commissions, and granting them broader and more general statewide powers.

In 1916, during World War I, Congress enacted legislation providing federal funding to states to develop an integrated network of highways. In 1921, shortly after the end of that war, Congress passed legislation restricting such federal-aid funding to a set of principal roadways, the origin of what would eventually become the Federal-Aid Primary Highway System. In 1944, during World War II, Congress authorized both the use of federal funds for urban extensions of the primary system and development of a Federal-Aid Highway Secondary System.[1]

Following World War II and continued congressional provision of federal highway funding in 1950,[2] President Eisenhower signed key legislation in 1956, including the Federal-Aid Highway Act, which created the Interstate highway system, and the Highway Revenue Act, which created the federal Highway Trust Fund and linked motor fuel taxes to roadway construction.[3] These Acts, and later related enactments,[4] established the basic pattern for the funding of public highways for the next 50 years.[5]

A decade later, legislation enacted under President Johnson in 1966 established the U.S. Department of Transportation (USDOT), including its Federal Highway Administration (FHWA).[6] Many states then enacted legislation creating analogous state Departments of Transportation (DOTs). Federal statutes governing federal aid to states for interstate and state highways continued to develop during the 1960s, 1970s, and 1980s.[7]

During the 1990s and early 2000s, Congress enacted three federal surface transportation statutes, building upon prior legislation, which had significant impact upon federal legal requirements governing state construction of federal-aid highways and bridges. In 1991, Congress passed the Intermodal Surface Transportation Efficiency Act of 1991, commonly referred to as "ISTEA."[8] Several years later, Congress passed the Transportation Equity Act for the 21st Century of 1998, commonly referred to as "TEA-21."[9] Then, in 2005, Congress passed the Safe, Accountable, Flexible, Efficient, Transportation Equity Act: A Legacy for Users, commonly referred to as "SAFETEA-LU."[10]

The periodic congressional enactment of comprehensive multi-year federal surface transportation legislation, over the more than 50-year period between 1950 and 2005, put in place a standardized but evolving set of funding, requirements, and expectations. Congress would, through such legislation, authorize federal aid to states and localities for the construction of highway, bridge, and other surface transportation projects. Con-

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[1] Allison L. C. de Cerreno, *Why Partnerships? Historical and Legislative Background on Public-Private Partnerships for Surface Transportation*, published in PARTNERSHIPS FOR NEW YORK—INNOVATIVE TRANSPORTATION FINANCING AND CONTRACTING STRATEGIES: OPPORTUNITIES FOR NEW YORK STATE, University Transportation Research Center/NYSDOT, Mar. 8, 2006, at 4.

[2] The Federal Aid to Highway Act of 1950, Pub. L. No. 81-769, 64 Stat 785.

[3] The Federal Aid to Highway/Interstate Highway Act of 1956, Pub. L. No. 84-627, 70 Stat. 374.

[4] The Transportation Act of 1958, Pub. L. No. 85-726, 72 Stat. 731.

[5] de Cerreno, *supra* note 1, at 4.

[6] Department of Transportation Act, Pub. L. No. 89-670, 80 Stat. 931 (1966).

[7] *See, e.g.*, the Highway Beautification Act of 1965, Pub. L. No. 89-285, 79 Stat. 1028; the Federal Aid Highway Act of 1973, Pub. L. No. 93-87, 87 Stat. 250; the Transportation Assistance Act of 1982, Pub. L. No. 97-424, 96 Stat. 2097; and the Surface Transportation Act of 1987, Pub. L. No. 100-17, 101 Stat. 132.

[8] Pub. L. No. 102-240, 105 Stat. 1914 (1991).

[9] Pub. L. No. 105-178, 112 Stat 107 (1998).

[10] Pub. L. No. 109-59, 119 Stat. 1144 (2005).

gress would also enact or amend related federal requirements governing the planning, funding, design, and construction of federal-aid highway and bridge projects. States would be required to accept such requirements as a condition of receiving federal aid. USDOT, FHWA, and state DOTs would then implement such requirements through USDOT and FHWA regulations, federal-aid project funding agreements between FHWA and state DOTs, FHWA administrative policy guidance to state DOTs, and development of a pattern of custom and practice between USDOT, FHWA, and state DOT officials in the course of ongoing administration.

Most of the provisions of these federal statutes, including ISTEA, TEA-21, and SAFETEA-LU, were codified successively into provisions of Title 23, Highways, and Title 49, Transportation, of the United States Code (USC). Regulations promulgated by FHWA and USDOT implementing such legislation, and elaborating upon its requirements under authority delegated by Congress, were codified into provisions of Title 23, Highways, and Title 49, Transportation, of the Code of Federal Regulations (CFR). FHWA also provided administrative guidance to state and municipal DOTs through a series of formal administrative issuances. Prior to December 1991, the issuance was known as the Federal-Aid Highway Program Manual. From December 1991 to January 2010, it was known as the Federal-Aid Policy Guide (FAPG). The issuance of FHWA Orders 1321.1C and 1340.3 on January 6, 2010, terminated the FAPG and replaced it with an administrative body known as the Federal-Aid Highway Program Policy and Guidance Center.[11]

This 50-year sequence of federal statutory enactments culminating in SAFETEA-LU, accompanied by FHWA and USDOT regulations and FHWA administrative guidance to state and municipal DOTs, has created a complex framework of federal law governing state and municipal DOTs that apply for and receive federal financial assistance ("federal aid") for the design, construction, and capital reconstruction of Interstate and other state and municipal highways and bridges. Federal law is not the only law governing state and municipal DOTs, which under our federal constitutional system derive their specific powers and duties from state constitutions and state legislative enactments. It has served, however, as a powerful force for nationwide standardization of law and practice governing the planning, design, construction, and reconstruction of Interstate, state, and municipal highways and bridges.

b. The Challenges Confronting Future Transportation Funding and Requirements

By its terms, SAFETEA-LU, the most recent of these comprehensive enactments of federal highway aid and requirements, was originally scheduled to expire in 2009. Due in significant part to the national economic crisis of 2008–2009 and its ongoing impacts, and to policy debates over the best way to address major new federal-aid highway funding legislation, Congress did not enact such legislation for several years. Instead, Congress extended the effective date of SAFETEA-LU nine times between 2009 and June 2012.[12] Congress also, however, made significant reductions in the federal-aid funding remaining available for the second half of fiscal year (FY) 2011.[13]

In considering continued funding of state and municipal construction of highways and bridges, Congress was also confronted by revenue problems. Since the 1950s, federal funding for highway construction has come from federal and state taxes on sales of gasoline and other motor fuels. The 18.4 cents per gallon federal gas tax was last increased in 1993, however, and its purchasing power has since been eroded by inflation to the equivalent of 11 cents per gallon in 1993 dollars.[14] Due to generally stable or declining fuel consumption resulting from rising fuel prices, poor economic conditions, and increasingly fuel-efficient vehicles, revenues from motor fuel sales taxes have remained stable or declined, limiting revenues available for highway and bridge projects. In recent years, Congress has had to supplement gas tax revenues by also appropriating some general funds for transportation purposes in order to meet transportation infrastructure needs.

As one analyst has pointed out, however, political demands for budget cuts and resistance to raising taxes greatly complicate the challenge of generating sufficient revenues to provide strong support for infrastructure renewal.[15] A major newspaper noted in 2011 that a national advocacy group had called for ending the federal gas tax.[16] In July 2011, the Chair of the House Transportation and Infrastructure Committee introduced a

[11] *See* http://www.fhwa.dot.gov/pgc/.

[12] *See* Ben Goad, *Transportation: Congress Passes Two-Year Highway Bill*, PRESS-ENTERPRISe, June 29, 2012, http://www.pe.com/local-news/politics/ben-goad-headlines/20120629-transportation-congress-passes-two-year-highway-bill.ece, last accessed Sept. 7, 2013; and Keith Laing, *Highway Bill Negotiators Like Ike—The Hill's Transportation Report*, http://thehill.com/blogs/transportation-report/highways-bridges-and-roads-/235885-highway-bill-negotiators-like-ike, last accessed Sept. 7, 2013. *See also* articles listed in Section 1, note 25, *infra*.

[13] *Government Shutdown Averted; Transportation Suffers Significant Spending Cuts*, Weekly Transportation Report, AASHTO JOURNAL, Apr. 15, 2011; *see* http://www.aashtojournal.org/Pages/041511appropriations.aspx, last accessed on Sept. 7, 2013.

[14] Editorial, *The Clear Case for the Gas Tax—Without It, the Highway System Would Crumble Further and the Economy Would Suffer*, N.Y. TIMES, Aug. 16, 2011, at A20, available at http://www.nytimes.com/2011/08/16/opinion/the-clear-case-for-the-gas-tax.html.

[15] Larry Ehl, *Analysis: Looming Big Shifts in Federal Transportation Funding*, TRANSPORTATION ISSUES DAILY, May 26, 2011; *see* http://www.transportationissuesdaily.com/analysis-looming-big-shifts-in-federal-transportation-funding/, last accessed on Sept. 7, 2013.

[16] Editorial, *The Clear Case for the Gas Tax*, *supra* note 14.

bill to restrict federal transportation funding to the revenues generated by the federal gas tax and other existing highway fees. Neither the proposal to repeal the federal gas tax, nor the proposal to limit federal highway funding to gas tax revenues alone, offered any indication of how the United States might deal with the estimated $72 billion backlog of bridges needing repair, a figure almost double the size of the $37 billion Highway Trust Fund, which reflects only the need for bridge repairs and not the need for highway repairs.[17]

The issue of how federal surface transportation funding might be allocated by congressional legislation, in ways affecting the use of such federal funding by state DOTs, also became the subject of public debate. One national foundation recommended that expenditures from the Trust Fund for coordination of urban projects by metropolitan planning organizations (MPOs); expenditures for highway and bridge projects currently classified as High Priority Projects, Projects of Regional and National Significance, and the National Corridor Infrastructure Improvement Program; and expenditures for highway congestion mitigation and air quality (CMAQ) projects, transportation enhancements, and scenic byways, as well as roads in national parks and forests, mass transit, Amtrak, high-speed rail, and ferry boats, be reduced or eliminated. The foundation argued that this would allow the reallocation of funding for such purposes to support more capital construction of highways and bridges. It also argued that this would allow the transfer of discretionary control over surface transportation capital funding from the federal government to state governments, which it advocated for policy reasons.[18]

c. The 2011 "Minibus" Legislation

In mid-November 2011, Congress enacted so-called "minibus" federal budget legislation, H.R. 2112, providing continued funding for highway and bridge construction projects for FY 2012.[19] This legislation renewed federal highway funding for less than 1 year from the date of enactment, and, absent further legislation, left such funding to expire shortly before the 2012 elections. According to one early report, the USDOT budget for FY 2012 as enacted by the "minibus" legislation included significant reductions in funding for highway and bridge projects: a reduction in the nationwide Highway Obligation Limitation from $41.107 billion in FFY 2011 to $39.144 billion in FY 2012, a reduction of $1.963 billion or 4.7 percent from FY 2011; and a reduction in Highway Traffic Safety Grants from about $620 million in FY 2011 to $550 million in FY 2012, a reduction of $69 million or 11.1 percent from FY 2011.[20]

Contrary to longstanding past practice of allowing authorized but unexpended funds to be carried over from one fiscal year until the next, H.R. 2112 expressly prohibited such carryovers, stating that: "None of the funds appropriated in this Act shall remain available for obligation beyond the current fiscal year, nor may any be transferred to other appropriations, unless expressly so provided herein."[21] H.R. 2112 also expressly rescinded all unobligated balances of funds previously available for programs administered by the FHWA under 22 prior congressional enactments.[22]

The House-Senate Conference Committee Report on H.R. 2112 indicated that H.R. 2112 authorized the Secretary of Transportation, in order to cover FHWA administrative costs, to reallocate for that purpose up to $16 million from 14 discretionary highway programs, including: Delta Region Transportation Development; Ferry Boats Discretionary Projects; Highways for LIFE Demo Projects; Innovative Bridge Research and Deployment; Interstate Maintenance Discretionary; National Historic Covered Bridge Preservation; National Scenic Byways; Public Lands Highway Discretionary; Railway-Highway Crossings Hazard Elimination in High-Speed Rail Corridors; Transportation, Community, and System Preservation; Truck Parking Pilot Program; Disadvantaged Business Enterprises Services; On-the-Job Training Services; and, Value Pricing Pilot Program.

The Conference Committee Report on H.R. 2112, included this statement regarding highway funding:

> The conferees acknowledge this obligation limitation will deplete almost all resources from the Highway Trust Fund by the end of fiscal year 2012, causing the FHWA to begin cash management procedures that may result in States not receiving timely reimbursement of highway construction expenses. Further, without enactment of a new surface transportation authorization bill with large amounts of additional revenues this year, the Highway Trust Fund will be unable to support a highway program

[17] Ehl, *supra* note 15.

[18] Ronald D. Utt, Setting Priorities for Transportation Spending in FY 2011 and FY 2012, Heritage Foundation Web memo no. 3141, Feb. 9, 2011, available at http://www.heritage.org/research/reports/2011/02/setting-priorities-for-transportation-spending-in-fy-2011-and-fy-2012.

[19] The text of H.R. 2112 is available on the Internet at http://www.gpo.gov/fdsys/pkg/BILLS-112hr2112pp/pdf/BILLS-112hr2112pp.pdf, last accessed Sept. 1, 2013.

[20] Federal Funds Information for States (FFIS), Jim Martin Table: Latest House and Senate Action on FY 2012, available at http://www.ffis.org/node/2493, last accessed on Sept. 1, 2013; and the referenced table, Major Discretionary and Mandatory Program Funding, available at http://www.ffis.org/sites/ffis.org/files/public/publications/2011/FY_2011_Final_and_FY_2012_Latest_11_15_11.pdf, last accessed on Sept. 1, 2013. While the table was prepared prior to enactment of the "minibus" funding legislation, it reflected the spending levels shown in the House-Senate conference report for that legislation issued a few days before the legislation was enacted.

[21] H.R. 2112, § 403.

[22] *See* text of H.R. 2112 at 304, lines 14 through 24, under the heading "Rescission," expressly rescinding any unobligated funds previously remaining available under Public Laws 91–605, 93–87, 93–643, 94–280, 96–131, 97–424, 98–8, 98–473, 99–190, 100–17, 100–202, 100–457, 101–164, 101–516, 102–143, 102–240, 103–122, 103–331, 106–346, 107–87, 108–7, and 108–199.

in fiscal year 2013. The conferees strongly urge the committees of jurisdiction to enact surface transportation legislation that provides substantial long-term funding to continue the federal-aid highways program.[23]

d. Negotiations Toward Further Legislation

Following enactment of the "minibus" legislation in November 2011, various issues reportedly complicated negotiations over a longer-term, more comprehensive federal-aid transportation funding bill. There were significant disputes over how to make up for the $10 billion to $14 billion projected annual shortfall in federal motor fuel tax revenues as compared with the projected need for federal-aid funding, and over the content of such legislation.[24]

2. 2012: Moving Ahead for Progress in the 21st Century Act

a. Enactment and Legislative Comments

As an advanced draft of the update to this volume was under review, Congress passed on June 29, 2012, and President Obama signed into law on July 6, 2012, a new federal surface transportation statute, to be known as the Moving Ahead for Progress in the 21st Century Act (MAP-21), P.L. 112-141, providing $105 billion in federal-aid funding for 2 years and 3 months, from June 29, 2012 until the end of FY 2014 in September 2014.[25]

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[23] *See* Conference Report on H.R. 2112, Consolidated and Further Continuing Appropriations Act, 2012, CONG. REC., H7433 et seq., at H7546, Nov. 14, 2011.

[24] Democratic legislators reportedly sought to include $1.4 billion in funding in the legislation for the Environmental Protection Agency's (EPA) Land and Water Conservation Fund. A bill passed by the Senate also included two additional provisions sought by Democrats: one shifting more federal-paid funding to repairing existing highways rather than building new ones, and another establishing a new coordinated policy for linking freight and ports. Republican legislators pursued provisions to streamline the environmental review process for transportation projects. They also sought to provide states with greater flexibility to redeploy funding from highway safety improvement projects, CMAQ projects, and transportation enhancement projects, including highway beautification, bike path, and sidewalk lighting projects, to be used instead for regular highway projects considered to have higher priority. Republican legislators further sought to include certain non-transportation provisions in the legislation, including federal approval of the Keystone XL oil pipeline project, notwithstanding unresolved environmental issues, and limitation of the EPA's authority to regulate coal ash generated by coal-fired electric generating facilities. *See* Ben Goad and Keith Laing, *supra* note 12; and *see* Ted Barrett & Deirdre Walsh, *Congress Strikes Tentative Deal on Highway Bill, Sources Say*, CNN.com, June 28, 2012, http://www.cnn.com/2012/06/27/politics/congress-transportation-bill/index.html; Corey Boles, Congress Approves Student Loan, Highway Bill, MarketWatch.com, June 29, 2012, http://www.marketwatch.com/story/congress-approves-student-loan-highway-bill-2012-06-29; Meredith Shiner, House, Senate Clear Highway Bill Deal, RollCall.com, June 29, 2012, http://www.rollcall.com/new/House-Senate-Clear-Highway_Bill-Deal-215868-1.html?pos=hfxt; Tom Cohen, Congress OKs Highway Funds/Student Loan Bill, CNN.com, June 29, 2012, http://www.cnn.com/2012/06/29/politics/congress-highway-bill/index.html; Ezra Klein, Suzy Khimm, Sarah Kliff & Brad Plumer, *Highway Bill Showdown: Five Things to Know*, WASHINGTON POST, June 29, 2012, http://www.washingtonpost.com/blogs/ezra-klein/wp/2012/06/29/highway-bill-showdown-five-things-to-know/; Ed O'Keefe & Rosalind S. Helderman, *Student Loan Extension, Highway Funding Approved by Congress*, WASHINGTON POST, June 29, 2012, http://www.washingtonpost.com/politics/student-loan-extension-highway-funding-approved-by-congress/2012/06/29/gJQAk98PCW_story.html?hpiud=z3; Corey Boles, Congress Passes Bill on Highways, Student Loans and Flood Insurance, WALL STREET J., June 29, 2012, search http://online.wsj.com/article/SB10001424052702303649504577496761419420828.html; Frank Thorp, Congress Sends Student Loan and Transportation Package to Obama, MSNBC.com, June 29, 2012, http://firstread.msnbc.msn.com/_news/2012/06/29/12483144-congress-sends-student-loan-and-transportation-package-to-obama?lite; Nathan Hurst, Bipartisan Deals Shape Highway Bill, CONG. Q., http://public.cq.com/docs/news/news-000004114526.html; all last accessed on Sept., 2013.

Negotiations between the House and Senate were reportedly further complicated when major public-policy advocacy organizations strongly opposed the legislation, and directly warned legislators that they would hold any votes in favor of the legislation against the legislators in the November 2012 election. A reporter quoted Rep. Steve LaTourette (R-Ohio), described as a key ally of House Speaker John Boehner, as saying that "One of the biggest problems has been that conservative think tanks have prevented Mr. Boehner from getting 218 votes for a piece of legislation." See Keith Laing, *Conservative Groups Rev Up Opposition to Highway Bill–The Hill's Transportation Report*, June 29, 2012, http://thehill.com/blogs/transportation-report/highways-bridges-and-roads/235533-conservative-groups-rev-up-opposition-to-highway-bill; last accessed on Sept. 7, 2013. As that article indicates, both the Heritage Foundation and the Club for Growth issued public statements on the day before Congress voted on the final legislation, indicating that they would hold any votes supporting the legislation against candidates in the 2012 elections.

Despite these conflicts and pressures, House and Senate Negotiators, led by House Transportation and Infrastructure Chairman John L. Mica (R.-Fla.) and Senate Environment and Public Works Chairwoman Barbara Boxer (D-Cal.), who also chaired the House-Senate Conference Committee, were finally able to reach agreement on a bill, almost 3 years after SAFETEA-LU had reached its original expiration date. *See* Hurst, op. cit.

[25] MAP-21, Pub L. No. 141, 126 Stat. 104 (2012). The version passed by both houses of Congress and signed into law by the President was H.R. 4348, the final House bill embodying the agreement reached by the House-Senate Conference Committee. For the text of the legislation as enacted, *see* http://www.gpo.gov/fdsys/pkg/BILLS-112hr4348enr/pdf/BILLS-112hr4348enr.pdf, last accessed on Sept. 8, 2013. For the House-Senate Conference Committee Report on the legislation,

The legislation, H.R. 4348, passed the House by a vote of 373–52, and the Senate by a vote of 74–19. According to news reports, a majority of both parties' lawmakers supported the legislation, and every Democratic member of the House who voted supported it.[26]

Both news reports and the Conference Committee Report made it clear that the final bill's provisions reflected a political compromise carefully negotiated between the House and Senate. As enacted, the legislation provided significant funding for transportation projects beyond projected federal motor-fuel tax revenues. It reportedly provided this funding by allowing U.S. companies to reduce their contributions to private-sector defined-benefit workplace pension plans, which effectively increased Federal Pension Benefit Guaranty Corporation taxes on such pension plans; and by allocating 80 percent of any fines recovered from the 2010 Deepwater Horizon oil spill to be distributed to Gulf states to help cover the costs of reconstruction projects.[27]

House Speaker John Boehner thanked both parties for working to resolve disagreements on how to pay for the legislation, while commenting that the bill was "far from perfect." Senate Majority Leader Harry Reid was quoted as saying that the legislation proves that when both parties work together, "we can do a lot to move our economy forward." While House Transportation and Infrastructure Chairman John R. Mica (R-Fla.) had previously sought legislation that would have provided longer and more extensive federal-aid funding, he acknowledged that "with the financial condition of the United States, it's the best we could do right now."[28] One prominent construction industry executive commented that while the provisions streamlining the environmental approval of federal-aid transportation projects were welcome, the two years of funding provided was still too short to give states sufficient time to plan major infrastructure projects. He was quoted by media as saying that "you have a transportation bill that has a 2-year horizon and it takes far longer than that to plan a major transportation infrastructure project."[29]

b. FHWA Summary of MAP-21 Legislation

Within a month after the President's approval of MAP-21, FHWA posted a summary of its provisions on the FHWA Web site, at http://www.fhwa.dot.gov /map21/summaryinfo.cfm.[30] Readers may find this summary useful, since the full text of this legislation is more than 700 pages long. Aside from the provisions providing continued funding under SAFETEA-LU for the remainder of FY 2012, the new provisions of the bill will go into effect on October 5, 2012. While detailed analysis of MAP-21 will require close examination both of the Conference Committee's report[31] and the full text of the legislation the following summary is provided as an introduction to its provisions.

From FHWA's perspective, MAP-21 strengthens America's highways by expanding the National Highway System (NHS) to include principal arterials, and by establishing a new program, the National Highway Performance Program, to preserve and improve important highways. It establishes a performance-based program to improve decision-making about transportation investments through performance-based planning and programming. MAP-21 creates jobs and supports economic growth by authorizing $82 billion in FY 2013 and 2014, increasing TIFIA funding, providing other surface transportation funding, and improving freight movement. It supports USDOT's safety agenda by continuing the Highway Safety Improvement Program (HSIP) and other safety efforts, including motor carrier safety inspection programs. MAP-21 streamlines federal highway transportation programs by consolidating the program structure into a smaller number of core programs, eliminating smaller programs while generally continuing the eligibilities involved through the core programs. It also accelerates project delivery and promotes innovation in the development of projects through changes in the planning and environmental review process.[32]

MAP-21 establishes six core highway formula programs, incorporating activities carried out under some previously existing formula programs. The six new core programs are the National Highway Performance Program (NPP), Surface Transportation Program (STP), CMAQ, HSIP, Railway-Highway Crossings (involving a funding set-aside from HSIP), and Metropolitan Planning. In addition, MAP-21 creates two new but non-core formula programs, the Construction of Ferry Boats and Ferry Terminal Facilities Program and the Transportation Alternatives (TA) Program; creates a new discretionary program, the Tribal High Priority Projects (THPP) Program; and continues five other preexisting

see Joint Explanatory Statement of the Committee of the Conference, June 29, 2012, at 1, http://docs.house.gov/billsthisweek/20120625/CRPT-112hrpt-HR4348.pdf, last accessed on Sept. 8, 2013. For links to both in alternate formats, *see also* http://www.fhwa.dot.gov/map21/legislation.cfm, last accessed July 25, 2012.

[26] *See* Boles, Thorp, O'Keefe & Helderman, and Shiner, *supra* note 24.

[27] *See* Boles, *supra* note 24. As one article pointed out, this was a temporary stop-gap solution under which Congress and federal and state transportation agencies will once again be confronted by the need to address the gap between federal motor fuel tax revenues and highway and bridge capital program needs in 2014. *See* Klein, Khimm, Kliff and Plumer, *supra* note 24.

[28] O'Keefe & Helderman, *supra* note 24.

[29] Boles, *supra* note 24.

[30] FHWA, Moving Ahead for Progress in the 21st Century Act (MAP-21), A Summary of Highway Provisions, July 17, 2012, http://www.fhwa.dot.gov/map21/summaryinfo.cfm, last accessed on Sept. 7, 2013.

[31] Joint Explanatory Statement of the Committee of the Conference, June 29, 2012, http://docs.house.gov/billsthisweek/20120625/HR4348crJES.pdf, last accessed on Sept. 7, 2013.

[32] FHWA, *supra* note 30.

discretionary programs while eliminating at least a dozen other preexisting discretionary programs, but allowing previous eligibilities from the THPP Program; and continues five other preexisting discretionary programs, while eliminating at least a dozen other preexisting discretionary programs, but allowing many of the eligibilities from those previous programs to continue under the core programs.[33]

FHWA describes the transportation investments made possible by MAP-21. MAP-21 extends SAFETEA-LU funding for the remainder of FY 2012. It then authorizes FY 2013 and 2014 funding at 2012 levels, with adjustment for inflation: $40.4 billion from the Highway Trust Fund for FY 2013, and $41.0 billion for FY 2014. MAP-21 provides FHWA with separate authorizations of $454 million for FY 2013 and $440 million for FY 2014, to support administrative costs; but designates more than $30 million per year of those funds for other purposes specified in the legislation. FHWA also indicates that, under MAP-21, there will be a new approach to administering funding formulas, as detailed in the summary on its Web site. [34]

i. Impact Upon TIFIA Funding.—FHWA's summary indicates that MAP-21 significantly increases the funding available for federal assistance under the Transportation Infrastructure Financing and Innovation Act (TIFIA) program of federal credit assistance to eligible projects. It makes $750 million in TIFIA subsidy authorizations available for FY 2013, and $1 billion for FY 2014, with each $1 billion in subsidies supporting roughly $10 billion in actual lending capacity. MAP-21 also includes a 10 percent TIFIA set-aside for rural projects, increases the share of project costs eligible for TIFIA funding, and sets up a rolling application process.[35]

ii. Impact Upon Tolling.—FHWA indicates that MAP-21 amends the previously existing 23 U.S.C. §129, governing state or other imposition of tolls upon highways constructed or improved using federal-aid funds. MAP-21 removes the requirement for execution of an agreement with USDOT prior to imposing tolls under the mainstream tolling programs, although the agreement requirement continues in effect for tolling pilot project programs. The legislation also mainstreams the imposition of tolls upon new Interstate highways and adds lanes on existing Interstates. It continues both the Value Pricing Pilot Program and the Interstate System Reconstruction and Rehabilitation Pilot Program. MAP-21 also requires that all federal-aid highway toll facilities implement technologies by October 1, 2016, for the interoperability of electronic toll collection.[36]

iii.—Impacts Upon the Highway Trust Fund.—FHWA indicates that MAP-21 extends the imposition of federal motor-fuel taxes, the primary source of revenue for the Highway Trust Fund, through September 30, 2016 (2 years after the end of the FY 2014 funding authorized by the legislation). It also notes, however, that motor-fuel tax revenues are insufficient to support the Highway Trust Fund at the levels needed to support authorized expenditures, and that MAP-21 thus also includes some transfers from the General Fund and the Leaking Underground Storage Tank Trust Fund to bring Highway Trust Fund revenues up to the levels necessary for the FY 2013 and 2014 surface transportation programs. It also notes that MAP-21 continues to provide funding of up to $10 million per year from FHWA administrative funds to provide ongoing support for FHWA's Highway Use Tax Evasion Program.[37]

iv. Accelerating Project Delivery.—MAP-21 continues and enhances the existing statewide and metropolitan transportation planning processes. It requires both a long-range plan and a short-term transportation improvement program (TIP). The legislation also ties the planning process to transportation system performance criteria established elsewhere in the legislation.[38]

According to FHWA, MAP-21 also includes various provisions to improve efficiency, effectiveness, and accountability in transportation funding, planning, design, and construction and to accelerate project delivery. In particular, MAP-21 expands authority for the use of categorical exclusions from National Environmental Policy Act (NEPA) environmental impact statement requirements to cover projects to reconstruct highways damaged in disaster emergencies, projects receiving only limited federal aid, and multi-modal projects. MAP-21 also provides for earlier interagency coordination during the environmental review process, greater linkage between planning and environmental review activities, consolidation of environmental documents, and use of a programmatic approach to environmental reviews whenever possible. Further, the legislation makes it easier for agencies to preserve or acquire rights of way prior to completion of the NEPA environmental review process.[39]

v. Implementation of Performance Management Measures—FHWA indicates that perhaps the most important aspect of the MAP-21 legislation is its requirement for federal-aid transportation programs to transition into performance-oriented and outcome-based programs. MAP-21 establishes national performance goals in the following areas: safety, infrastructure condition, congestion reduction, system reliability, freight movement and economic vitality, environmental sustainability, and reduced delays in project delivery. In consultation with state DOTs, MPOs, and other stakeholders, the U.S. Secretary of Transportation will establish performance measures for pavement conditions. He will also establish performance measures for the Interstate and NHS highway systems, bridge conditions, injuries and fatalities, traffic congestion, on-road mobile-source emissions, and freight movement on the

[33] *Id.*

[34] *Id.*

[35] *Id.*

[36] *Id.*

[37] *Id.*

[38] *Id.*

[39] *Id.*

Interstate system. States and MPOs will then be required to set their own performance targets in support of those measures, incorporate such targets in their planning processes, and show how their transportation programs and project selections will help achieve those targets. If states fail to maintain minimum standards for Interstate pavement and NHS bridge conditions, or to make significant progress toward their state plan targets, they will be required to undertake corrective measures.[40]

vi. Description of New Core Programs—.FHWA devotes a fair amount of time to describing specific details, including new performance-oriented requirements, of the new core surface transportation programs created or continued by MAP-21. These include the National Highway Performance Program (NHPP), authorized at an average of $21.8 billion per year; Surface Transportation Program (STP), providing an annual average of $10 billion in flexible funding; HSIP, with average annual funding of $2.4 billion; the continued CMAQ Program, with an average annual funding level of $3.3 billion; the TA Program, which provides for a variety of alternative transportation projects previously covered under separately funded programs; and the Federal Lands and Tribal Transportation Program. FHWA also provides briefer treatment of other, non-core programs, including Emergency Relief, Workforce Development and Disadvantaged Business Enterprise (DBE), Bridge and Tunnel Inspection, Projects of National and Regional Significance, Construction of Ferry Boats and Ferry Terminal Facilities, and the Appalachian Development Highway System. Finally, it discusses a variety of research, technology deployment, training, and education programs. While these will not be discussed in detail here, readers with specific interests in any of these programs are referred to FHWA's Web site.[41]

3. Impact of Long-Term Funding Uncertainties Upon States

While the enactment of a new 2-year federal surface transportation funding bill may relieve some of the uncertainty of future federal funding for surface transportation, this legislation will, at least according to its current terms, be in effect for only 2 years, which is considerably less than it has taken in the recent past to plan a typical major transportation project. The long-term uncertainty that this creates may well have major impacts upon state DOTs, many of which also face state funding issues. Investments in transportation infrastructure have played a major role in state budgets over the past several years. As indicated in Table 1, a review of data from FHWA's publicly available Highway Statistic Series of annual reports [42] on federal-aid highway funding, non-federal-aid highway expenditures, and total highway construction expenditures between 2005 and 2008 shows that eight of our country's largest states have made extensive investments in transportation infrastructure during that period.

Table 1. Combined Federal Aid (FA) & Non-Federal Aid Highway Expenditures for Eight Selected States, 2005–2008

Rank		Total FA + Non-FA Hwy $$ 2005–08
1	Texas	$28.3 billion
2	Florida	$19.6 billion
3	California	$17.1 billion
4	New York	$11.9 billion
5	Illinois	$11.5 billion
6	Pennsylvania	$9.7 billion
7	Michigan	$9.6 billion
8	North Carolina	$7.7 billion

Due to changes in economic conditions since that period, however, states may now face much greater challenges in generating sufficient resources to continue making transportation infrastructure investments at this level. During the preparation of this update, the authors researched the situations confronting several state DOTs, and interviewed officials in some of those agencies. Given the geographic and economic diversity of the United States, it is not surprising that the results varied considerably from state to state. The results clearly indicated, however, that at least some states with large populations will face major transportation capital funding shortfalls if federal funding legislation providing federal motor fuel tax revenue to the states is not renewed or expanded.

a. Texas

Based on FHWA data, Texas expended approximately $28.3 billion in combined federal-aid and non-federal-aid highway projects between 2005 and 2008, giving it the largest state highway capital construction program in the United States during that period. This almost certainly made a positive contribution to the state's economic development and performance during that period.

[40] *Id*.

[41] *Id*.

[42] FHWA's Highway Statistic Series of annual reports, including but not limited to reports on Highway Finance Data and Information and on the Motor Fuel and Highway Trust Fund, are available at http://www.fhwa.dot.gov/policy information/statistics.cfm. The data presented and discussed in this report are drawn principally from Table SF-12B of the FHWA Highway Statistics reports for the years 2005 through 2008, for highway construction expenditure data, and from Table SDF of the FHWA Highway Statistics reports for the years 2005 through 2009, for motor fuel tax revenue collection and usage. Construction expenditure data are not yet available for 2009 and subsequent years.

There are strong indications, however, that Texas may not be able to continue transportation investments at this pace in the future. Much of that funding total came from FHWA federal-aid funding, which for reasons indicated above is currently in doubt for future years. While Texas DOT receives motor fuel tax revenues, it does not receive any state general-fund revenues. With both automobiles and trucks becoming more fuel efficient, motor fuel tax revenues are projected to decline in future years. Texas has also used debt funding to cover the state match for federal-aid project funding in past years, and its annual debt-service costs reportedly may soon exceed the annual amount the state can afford to spend on new projects. The Chairs of both the Texas House Transportation Committee and the Texas Senate Transportation and Homeland Security Committee have been publicly quoted as characterizing the transportation funding situation now confronting Texas as a "crisis."[43]

The Center for Transportation Research at the University of Texas predicts that, over the next 20 years, the state will need to expend $315 billion on the state's highways and bridges in order to keep traffic conditions at current levels, but will generate projected motor fuel tax revenue of only $160 billion during the same period, resulting in a $155 billion shortfall in transportation funding over the next 20 years in that state alone. News reports have quoted both the current and former Chairs of the Texas House Transportation Committee as indicating that, with the state facing an overall budget crisis, transportation needs are unlikely to receive immediate attention. They both express hope that the Texas Legislature may be able to devote more attention to transportation funding needs during its next session, in 2013.[44]

b. Florida

Based on FHWA data, Florida expended approximately $19.6 billion in combined federal-aid and non-federal-aid highway projects between 2005 and 2008, giving it the second largest state highway capital construction program in the United States during that period.

Like other states, however, Florida faces pressing fiscal issues on many fronts. In 2011, the Florida State Legislature diverted $150 million from gas tax revenues to support education spending, which affected the funding of an estimated $334 million in highway projects.[45]

Planning to use highway and bridge construction to help spur economic recovery, and facing inadequate gas tax revenue and the diversion of gas tax revenue to support nontransportation expenditures, Florida DOT is now requiring contractors to obtain private-sector financing for many of its projects, and increasing the use of tolls to finance highway and bridge projects.[46] As of August 2011, Florida DOT has reportedly let 11 projects totaling about $900 million that require contractor financing. On one such project, the Interstate 4 / Selmon Expressway project in Tampa, the contractor is reportedly financing $180 million of the $394 million cost of the project.[47] Florida DOT has also begun increasing capacity on some highways by adding toll lanes, including a project on I-95 in Miami-Dade County. Florida DOT reportedly plans to pursue additional toll-funded capacity expansion projects on I-4 in Orlando, I-75 in Tampa and south Florida, I-95 in Jacksonville, and I-110 in the Florida panhandle.[48]

c. New York

Based on FHWA data, New York State expended approximately $11.9 billion in combined federal-aid and non-federal-aid highway projects between 2005 and 2008, giving it the fourth largest state highway capital construction program in the United States during that period.

Historically, the construction of transportation infrastructure has been essential to economic growth. New York State now faces significant challenges, however, in obtaining sufficient funding to support ongoing transportation infrastructure needs. Of the state's roughly 17,300 bridges, 36 percent have condition ratings under 5. New York's Office of the State Comptroller reportedly estimates that the state will need $250 billion to maintain its transportation, sewer, and water systems over the next 20 years. Even including projected levels of federal aid, the state will only have about $170 billion in infrastructure funding during the same period, leaving a projected shortfall of $80 billion in infrastructure funding during the next 2 decades.[49]

There are a variety of reasons for these transportation funding challenges. New York State Department of Transportation (NYSDOT) officials note that while current federal law requires each state receiving federal-aid funding to prepare a STIP, a multi-year plan for the state's surface transportation capital program, the preparation of the STIP is increasingly complicated by

[43] Gary Scharrer, *State Highway Fund Crisis: Are We There Yet?*, HOUSTON CHRONICLE online edition, http://www.chron.com/disp/story.mpl/metropolitan/7404396.html, last accessed on Sept. 7, 2013.

[44] Nolan Hicks, *Texas Highway System Nearly Running on Empty*, HOUSTON CHRONICLE online edition, http://www.chron.com/disp/story.mpl/metropolitan/7462915.html, last accessed on Sept. 7, 2013.

[45] *Id*.

[46] Scott Judy, *Low on Gas Taxes, Florida Accelerates Contractor Financing*, Engineering News-Record.com, Aug. 16, 2011; http://enr.construction.com/infrastructure/transportation, subscription service, last accessed Sept. 7, 2013.

[47] *Id*.

[48] *Id*.

[49] Joseph Spector & Tim Henderson, *Hard Rides, Hefty Costs: Many of State's Bridges are in Poor Shape—But So are Budgets*, Albany, N.Y., TIMES UNION, Sept. 26, 2011, at A-1.

multiple factors.[50] Seemingly routine choices by fiscal staff about allocation of available program funding can have significant consequences caused by differences between federal and state laws governing projects and the resultant costs of compliance with such laws. Examples of such differing requirements, which can dramatically increase costs, include, but are not limited to, NEPA and New York State's State Environmental Quality Review Act (SEQRA), Federal DBE requirements and state Minority and Women's Business Enterprise (M/WBE) requirements, and Federal Davis/Bacon and state labor law prevailing rate wage requirements. Complying with such requirements can account for as much as 30 percent of the cost of a federal-aid project. Federal requirements for Internet posting of detailed data on transportation projects, imposed by Congress in connection with American Recovery and Reinvestment Act (ARRA) stimulus funding, are also time-consuming and expensive with which to comply.[51]

The cumulative impact of these transportation funding challenges is significant. NYSDOT is responsible for a transportation system including more than 15,000 centerline miles of Interstate and state highways and approximately 17,300 bridges. When NYSDOT was created in 1967, it had about 15,000 employees to design, build, operate, and maintain those facilities. As of 2011, it has about 8,700 employees, less than 60 percent of its original staff. The impact of funding challenges upon the transportation construction industry has also been substantial, with the construction trades facing unemployment of 25 to 30 percent in New York State as of the summer of 2011.

After a number of years of considering but not adopting legislative proposals, New York State enacted legislation in 2011 authorizing NYSDOT, the New York State Thruway Authority, the New York State Bridge Authority, and certain other state agencies to use public–private partnerships (PPP) or design-build procedures for any projects over $1.25 million.[52] While innovative methods of transportation capital funding such as PPP or the creation of a National Infrastructure Bank are definitely worth further consideration, there may be some risk that they might not provide a comprehensive solution to existing funding problems.

d. Maryland

Like Florida DOT, the Maryland Transportation Authority is reportedly increasing highway and bridge tolls to offset declining gas tax revenues. For the first time since the 1970s, the Authority voted in September 2011, effective November 2011, to increase tolls on the Chesapeake Bay Bridge. The Authority also reportedly plans to use toll funding for a $1 billion project to construct express toll lanes on I-95 near Baltimore, among other projects.[53] The toll increases appear likely to impose added costs upon interstate commerce; the Maryland Motor Truck Association reportedly estimates, for example, that truckers who transport shipping containers from the Port of Baltimore through the Fort McHenry Tunnel will see toll increases from the current $12 each way to $18 each way starting in January 2012 and $24 each way starting in July 2013, totaling an estimated $3,000 per truck per year in increased operating costs.[54]

e. Missouri

Faced with severe budget challenges, Missouri DOT has reportedly made major cutbacks in its highway capital construction program, its agency staffing, and its maintenance equipment. From 2006 to 2011, Missouri's annual highway construction program reportedly averaged $1.2 billion a year. In June 2011, however, saying that "We are facing a transportation funding crisis in Missouri," Missouri DOT's Director presented the Missouri Highways and Transportation Commission with a plan proposing a highway construction program of about $600 million a year, or roughly half the prior annual average, for the next 5 years. The plan also proposed consolidating several existing divisions within Missouri DOT's Central Office. While Missouri DOT's existing structure of 10 regional offices had been in place almost unchanged for almost 90 years, since 1922, the plan further proposed cutting the agency's number of regional offices from 10 to 7, closing 135 Missouri DOT field facilities, and selling more than 740 trucks and other pieces of construction equipment from Missouri DOT's existing maintenance fleet. Along with these organizational steps, the plan proposed reducing the size of Missouri DOT's workforce by 1,200 employees. While the Director reportedly expressed hope that much of this could be accomplished through attrition and transfers, he acknowledged that layoffs might also be necessary.[55] The Missouri Highways and Transportation Commission reportedly adopted the plan with only minor revisions in June 2011.[56]

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[50] Group interview by Peter Shawhan with NYSDOT officials Ronald Epstein, Owen Shevlin, David Roth, Kyle Wood, Robert Crowley, and Michael McDermott in Albany, N.Y., June 27, 2011.

[51] *Id*.

[52] *See* ch. 52 of the New York State Laws of 2011.

[53] Katherine Shaver, *Tolls Increase on Maryland Roads, Bridges and Tunnels*, WASH. POST, Sept. 22, 2011, http://www.washingtonpost.com/local/commuting/tolls-increase-on-md-roads-bridges-and-tunnels/2011/09/22/gIQAHwJUoK_story.html, last accessed on Sept. 7, 2013.

[54] *Id*.

[55] *MoDOT Transportation Funding Crisis*, Kansas City infoZine, May 5, 2011, available at http://www.infozine.com/news/stories/op/storiesView/sid/47400/, last accessed on Sept. 7, 2013.

[56] *MoDOT Goes Small*, Kansas City infoZine, June 9, 2011, available at http://www.infozine.com/news/stories/op/storiesView/sid/47778/, last accessed on Sept. 7, 2013.

f. Kansas

During 2010, the Governor of Kansas cut $257 million from the State Highway Fund. In response, the Secretary of Kansas DOT announced in March 2010 that he was suspending $86 million, or 65 percent, of the $133 million in state-funded projects that Kansa DOT had planned to have under contract for the remainder of the state's fiscal year. He pointed to federal funding for $112 million in ARRA stimulus projects as "the saving grace" that allowed the DOT's construction program to continue, at least during the summer of 2010.[57]

B. METHODS OF CONTRACTING FOR TRANSPORTATION CONSTRUCTION

1. Competitive Bidding—The Design-Bid-Build Method

State and federal law nearly always requires that public works projects be procured through a competitive selection process.[58] Most transportation construction projects have traditionally used the "design-bid-build" method, or competitive sealed bidding. Using this method, the transportation agency designs the project, either with its own staff or through a consultant, and prepares the project plans and specifications. The agency then advertises the project for bids, and selects the lowest responsible bidder to build the project. Some state transportation agencies have obtained legislative authority to use other methods such as design-build and PPP; however, most agencies still use the design-bid-build method for most projects.

The 2000 Model Procurement Code for State and Local Governments includes processes for competitive sealed bidding as well as competitive sealed proposals, which are used for design-build and other alternative contracting methods.[59] The Model Code no longer states a statutory preference for competitive sealed bidding, although it is still the default source selection method.[60]

Procedures for selection of contractors to construct, maintain, improve, and repair public highways are based on state statutes and administrative rules.[61] These rules have no common law antecedents, and thus they constitute a set of positive policies and requirements that distinguish the conduct of public officials from the practices of those in private business. Two objectives underlie the development of most of today's laws and regulations requiring competitive bidding—the prevention of favoritism in spending public funds, and the stimulation of competition in the construction industry.[62]

The importance of complying with statutory bidding procedures is illustrated in cases in which governments have attempted to use the public contracting process to help achieve policy and program goals, especially in connection with social and economic issues and public safety. When an agency modifies its competitive bidding procedures to accommodate extraneous public interests, disappointed bidders may challenge the award as violating bidding requirements.[63] This occurred when a transportation authority awarded a contract to paint subway stations to a nonprofit corporation engaged in rehabilitating the work habits of persons with poor employment records resulting from alcoholism, drug addiction, imprisonment, or "social disability." The organization's clients came from governmental and quasi-public sources, and its program implemented the state's social services laws. The painter's union successfully challenged the transportation authority's award. The court held that neither the good intentions of the contracting agency nor the laudable work of the contractor could overcome the statutory requirement for competitive bidding:

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[57] Transportation Secretary Miller Responds to KDOT Budget Cuts, Kansas DOT news release, Mar. 5, 2010, available at http://www.ksdot.org/offtransinfo/pressrel2010.asp, last accessed on Sept. 7, 2013.

[58] Portions of this section are derived from Dr. Ross D. Netherton, *Competitive Bidding and Award of Highway Construction Contracts,* Transportation Research Board, The National Academies, Washington, D.C., 1976, included in the first edition of SELECTED STUDIES IN HIGHWAY LAW, vol. 3., at 1175 or supplemented *id*. at 1214–51 (1988).

[59] AMERICAN BAR ASSOCIATION, MODEL PROCUREMENT CODE FOR STATE AND LOCAL GOVERNMENTS (hereinafter "ABA Model Code") § 3-202 (2000). A number of states have enacted some variation of the Model Code as their state procurement code. In those states, the commentary contained in each section of the Model Code may be useful as legislative history. In addition, the ABA regularly publishes compilations of cases decided under state law in states that have enacted the Model Code. For further discussion of the development of the 1979 Model Code, *see* C. Cushman, *The ABA Model Procurement Code: Implementation, Evolution, and Crisis of Survival*, 25 PUB. CONT. L.J. 173–98 (1996); and F.T. vom Baur, *A Personal History of the Model Procurement Code*, 25 PUB. CONT. L. J. 149–72 (1996) (written by chairman of ABA committee that drafted 1979 Model Code).

[60] ABA Model Code, *supra* note 59, at xiii.

[61] Aschen-Gardner, Inc. v. Superior Court In and For County of Maricopa, 173 Ariz. 48, 839 P.2d 1093, 1095–96 (1992) (competitive bidding for public works projects is required only when mandated by statute); *see also* Smith v. Intergovernmental Solid Waste Disposal Ass'n, 178 Ill. Dec. 860, 605 N.E.2d 654, 664, 239 Ill. App. 3d 123 (1992) (in absence of statute requiring it, competitive bidding is not necessary for public agency to enter into valid contract); *but see* City of Philadelphia v. Commonwealth of Pa. Dep't of Envtl. Resources, 133 Pa. Commw. 565 577 A.2d 225, 228 (1990).

[62] Computer Shoppe v. State, 780 S.W.2d 729, 737 (Tenn. App. 1989) (public bidding statutes are intended to promote public interest by aiding government in procuring best work or materials for lowest practical price, providing bidders with fair forum for competing for government contracts, and protecting public from its officials' self-dealing, extravagance, and favoritism).

[63] District Council No. 9, Int'l Bhd. of Painters & Allied Trades v. Metropolitan Transp. Auth., 115 Misc. 2d 810, 454 N.Y.S.2d 663, 667 (1982).

> The intent of the bidding statute is to prevent favoritism, improvidence, extravagance, fraud and corruption and to promote economy in public administration and honesty, fidelity and good morality in administrative officers. This policy is so strong that a violation of [it]…renders a public works contract void.
>
> Thus, the questions become whether…the [transportation authority] has the right to make an exception for contracts, that clearly contemplate public works, when the contractor is an organization that is itself performing a valuable service in the public interest….As well motivated as this sentiment may be, the statute does not support [the authority's action].[64]

Even though avoidance of favoritism and fraud is important, it is not the most important purpose of public bidding rules. The primary objective has always been to obtain a full and fair return for an expenditure of public funds.[65] This may be accomplished by extending invitations for public contract work on an open and equal basis to all persons who are able and willing to perform the work. Through effectively supervised competition among the parties, the public is assured that there will be a real and honest cost basis for the work desired.[66]

Therefore, competitive bidding requirements serve multiple purposes, and statements of these purposes by the courts have varied in emphasis. An illustrative list of the major objectives of competitive bidding is found in *Wester v. Belote*:

> [T]o protect the public against collusive contracts; to secure fair competition upon equal terms to all bidders; to remove, not only collusion, but temptation for collusion and opportunity for gain at public expense; to close all avenues to favoritism and fraud in its various forms; to secure the best values [for the public] at the lowest possible expense; and to afford an equal advantage to all desiring to do business with the public authorities, by affording an opportunity for an exact comparison of bids.[67]

a. The Essential Principles of Competitive Bidding

i. The Form of Competitive Bidding Rules.—An agency satisfies the objectives of competitive bidding when it follows uniform procedures relating to: 1) public advertisement to bidders inviting the submission of proposals; 2) preparation of plans, specifications, and related information about the work and the location where those materials may be obtained by prospective bidders; 3) formal submission of proposals to the contracting agency, together with the deposit of financial security guaranteeing that the bidder will accept the award of a contract if it is the lowest responsible bidder; 4) consideration of proposals under uniform criteria, and 5) award of contracts to lowest responsible bidders.

Any effort to fully describe the law relating to competitive bidding and award of contracts must take into account statutes, administrative regulations, and the informally followed practices of the contracting agency. Patterns regarding the mix of statutory and administrative elements in the law vary from state to state. Connecticut's statute illustrates an unusually broad delegation of procedural rulemaking authority to administrative officials:

> The commissioner may, at any time, call for bids to construct, alter, reconstruct, improve, relocate, widen or change the grade of sections of state highways or bridges.
>
> All bids shall be submitted on forms provided by the commissioner and shall comply with the rules and regulations provided in the specifications….[68]

In contrast, other states leave certain aspects of bidding to administrative judgment, and specify other aspects in statutes. Such variations in the form of competitive bidding laws reflect the tension between allowing flexibility and curbing the agency discretion that pervades public contract law. The Model Code sets out very general requirements, with more detailed requirements left to agency regulations.[69]

ii. Single or Separate Contracts.—Public works agencies customarily have wide discretion as to when to subdivide a project and award separate contracts for each segment or component of the work. Because this decision determines the monetary size of the contract, the agency's decision in this matter may directly affect the number and type of available bidders. However, compelling economic, engineering, and financial reasons may influence an agency's decisions regarding the dividing of contracts. As long as these considerations are reasonable, courts have tended to uphold the contracting agency's actions in determining the size and scope of the contract.

However, if the specifications issued by the contracting agency result in limiting the bidding or otherwise impairing free competition in the selection of public contractors, the award may be enjoined or nullified, or the agency may be required to reject all bids and readvertise on more appropriate terms. For example, an

[64] *Id*. at 667–68 (citations omitted).

[65] *See, e.g.,* City of Atlanta v. J.A. Jones Constr. Co., 260 Ga. 658, 398 S.E.2d 369, 370, *on remand*, 198 Ga. App. 345, 402 S.E.2d 554, *cert. denied*, 111 S. Ct. 2042 (1990).

[66] Carbro Constr. Co. v. Middlesex County Util. Auth*.,* 233 N.J. Super. 116, 558 A.2d 54, 58 (1989) (curtailing local discretion and requiring strict compliance with bidding requirements protects public against favoritism, extravagance, and corruption).

[67] 103 Fla. 976, 723–24, 138 So. 721, 722 (1931).

[68] CONN. GEN. STAT. ANN. § 13a-95 (1999).

[69] ABA Model Code, *supra* note 59.

agency was not allowed to arbitrarily divide a project for installation of traffic signals into separate contracts for procurement of materials, equipment, and labor where these items were parts of an integrated project. The apparent purpose of the separation was to keep each contract under the statutory minimum price for requiring competitive bidding.[70]

On the other hand, where these items are not necessarily integrated in the type of construction work called for, they may be provided under separate contracts. Specialty work frequently is sufficiently different from basic construction tasks to warrant separation of contracts.[71] Separate contracts have also been upheld for construction of two similar facilities where the projects were to be paid for from separate funding sources.[72]

Although state laws mandating separate bidding for different construction trades are not normally applicable to transportation construction contracts, the Ohio Supreme Court addressed the question of whether a state separation statute applied to a contract for the construction of roadside rest areas. A local mechanical contractors association sought to enjoin the advertisement, claiming that the state bidding law required separate contracts for each mechanical trade involved in the project.[73] In this case, each rest area involved construction of public facilities and storage buildings with janitors' and storage rooms, and installation of a complete wastewater treatment system. Examining the Ohio DOT's statutory authority to enter into contracts, the court concluded that although the legislature had not authorized construction of roadside rest areas in specific terms, ample authority could be inferred from other legislation making the agency responsible for highway and roadside conditions.[74] The more difficult question was whether the DOT was subject to a statutory requirement that state contracts involving plumbing, gas fitting, steam heat and power, and electrical equipment must be awarded in separate contracts for each mechanical trade involved.[75] Construing the applicable statutes, the court held that they required the DOT to advertise and award separate contracts for each mechanical trade involved in the desired work.[76]

Because transportation construction programs generally use standard specifications and procedural manuals, the room for discretionary combining or splitting of projects for bidding is reduced.[77] Competitive bidding practices have been standardized along lines that courts, agencies, and contractors agree are reasonable and feasible and that do not weaken the process of procurement by competition. This standardization has also contributed to stabilizing this aspect of bid preparation.

iii. Lump Sum Versus Unit Price Bids.—Another aspect of bidding that is normally left to the discretion of the contracting agency is whether bids must be submitted in the form of a lump sum for the entire project or in a series of prices for units of work or materials. Lump sum bids are favored where construction jobs involve a variety of operations and it is impractical to break down the work into a few basic units of materials and labor. Ultimately, the success of this method requires complete and accurate specifications, detailed work plans, and accurate quantities of labor and materials. Failure to provide full guidance on these technical matters increases the risk of excessively high bids, as bidders attempt to price risks that they cannot reasonably evaluate.

Unit price bidding is favored where a project requires large quantities of relatively few standardized materials and construction operations, or where the exact quantities of materials and labor are not known in advance. A proposal form is furnished to bidders, containing the agency's estimate of the quantities to be used in the project. In submitting its bid, the contractor inserts the unit price as requested, and extends the unit prices by the agency's estimated quantities.[78]

When a contract is bid on a unit price basis, reasonable variations may be made in the work without the necessity of formal change orders. However, this flexibility applies only to items originally covered in the contract. If material discrepancies occur between the estimated and actual quantities required for the work, the agency may reconsider the original contract.

In a bid based on unit prices, discrepancies may occur between the total unit price shown in the bid and the same price as calculated by multiplying the unit price by the number of units to be furnished. If bidding instructions anticipate such situations and specify which figure will be accepted, the parties to the contract

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[70] National Elec. Contractors Ass'n, Puget Sound Chapter v. City of Bellevue, 1 Wash. App. 81, 459 P.2d 420, 421 (1969) (where bidding statute was written in conjunctive, "improvement, including materials, supplies, and equipment," a project could not be broken out into separate contracts for materials and installation).

[71] *See*, *e.g.*, *infra* notes 75 and 76.

[72] Daves v. Village of Madelia, 205 Minn. 526, 287 N.W. 1, 123 A.L.R. 569 (1939).

[73] Mechanical Contractors Ass'n of Cincinnati v. State, 64 Ohio St. 2d 192, 414 N.E.2d 418 (1980) (rest areas were considered part of the highway, thus the Department of Transportation was authorized to contract for their construction and improvement).

[74] *Id.* at 420–21.

[75] OHIO REV. CODE ANN. §§ 153.02, 153.03 (1985 Supp.), repealed 1996.

[76] A dissent argued, however, that the Director of Transportation could act under special highway enabling legislation and award contracts for highway and bridge work in any manner deemed advantageous to the public. 414 N.E.2d at 421–22 (citing OHIO REV. CODE § 5529.05).

[77] *See* UTAH CODE § 72-6-102 (agency required to adopt standard plans and specifications for construction and maintenance of state highways).

[78] State Highway Admin. v. David A. Bramble, Inc., 351 Md. 226, 717 A.2d 943, 944 (1998).

are held to resolving discrepancies by that means. Whether the bid must be rejected will depend on how much discretion an agency's statute allows in resolving bidder mistakes.[79] One court has held that the contracting agency could not reject the bid as being ambiguous when this error occurred.[80] Another has held that the agency had the right to reject a bid in spite of an "errors in bid" formula contained in the bid advertisement, where accepting the bid would have allowed the bidder to choose between two differing price totals.[81] Where the specifications clearly require that both unit prices and total prices for each bid item be included, a bid may be found nonresponsive for failure to include both.[82] A Louisiana court addressed this issue:

> Even though DOTD's rigid specifications as to the bid form may have seemingly harsh results, any interpretation but the most literal would contravene the stricti juris nature of the public contract laws. As our brethren on the Fourth circuit have noted:
>
> "[B]idding in accordance with the advertisement is essential to satisfy the purposes for which the public bid laws were enacted. If public bidding is an honest attempt at getting the best value for tax moneys, then every bidder must be held bound by the terms of the advertising. To allow anything less than a bid conforming on its face to the advertised specifications would constitute an open invitation to the kind of impropriety and abuse the public bid laws were designed to prevent."[83]

One cause of confusion may be a contracting agency's reservation of the right to award contracts on only a part of the total work described in the bid advertisement. In *Devir v. Hastings*, a municipal agency requested bids for resurfacing four streets, but reserved the right to award contracts for less than all four.[84] The bid advertisement specified that bids must be submitted on a per yard basis. The challenger argued that the agency's reservation deprived bidders of a common basis for such a unit price bid. The court held, however, that prospective bidders could determine both the minimum and maximum amounts of material needed and so could compete on an equal footing.

b. Advertisement for Bids

i. General Requirements for Advertisement.—For competition to be fostered in public bidding, 1) everyone qualified and desiring to bid on the project must be adequately informed of it, and 2) all bidders must be given equal opportunity to bid and have their bids considered on the same terms. Requirements for public advertisement of projects and invitations to bid are implemented through a publication of a formal call for proposals or invitation for bids. This must contain the essential information about how bids should be submitted, and must inform bidders of all the essential features of the project.[85] For example, Louisiana's public procurement statute, which is based on the Model Code, requires that the invitation for bids contain all contractual terms and conditions applicable to the procurement, as well as the evaluation criteria to be used.[86] Requirements of state laws regarding advertisement for bids on highway construction are found in Appendix A.

The requirement for public advertisement, and the terms on which it must be provided, are based in statute.[87] Typically, statutes relating to advertisement of public works projects set forth the times, places, and forms of publication of the advertisement. Most statutes favor newspapers of general circulation in the county where the work is to be done as the principal means of advertisement.[88]

In addition, since contractors often do business in multi-state regions, they may be contacted more easily through industry trade journals than through local newspapers. Therefore, contracting officers in many states are either directed or authorized to publish notices of their projects and invitations to bid in these trade journals. Other devices for accomplishing this same purpose include publication in an "official newspaper" of the state, and listing in a departmental bulletin published by the state transportation agency.[89] Some states also post information about projects and bid opening dates on their Internet Web sites. Colorado allows Internet publication as follows: "The executive director of the department of transportation may invite bids using electronic on-line access, including the internet, for purposes of acquiring construction contracts for public projects on behalf of the department of transpor-

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[79] *See* ABA Model Code, *supra* note 59, at § 3-202(6) and commentary.

[80] Pozar v. Dep't of Transp., 145 Cal. App. 3d 269, 193 Cal. Rptr. 202 (1983).

[81] Colonnelli Bros. v. Ridgefield Park, 665 A.2d 1136, 1139 (N.J. Super. A.D. 1995).

[82] V.C. Nora, Jr. Building & Remodeling v. State, Dep't of Transp. and Dev., 635 So. 2d 466, 472–73 (La. App. 3d. Cir. 1994).

[83] *Id*. (quoting Gibbs Constr. v. Board of Sup'rs of L.S.U., 447 So. 2d 90 (La. App. 4th Cir. 1984)).

[84] 277 Mass. 502, 178 N.E. 617 (1931).

[85] *See* ABA Model Code, *supra* note 59, at § 3-202(2), (3), and commentary.

[86] Pacificorp Capital v. State, Through Div. of Admin., Office of State Purchasing, 647 So. 2d 1122, 1124 (La. App. 1 Cir. 1994), *writ denied*, 646 So. 2d 387 (1994).

[87] In the absence of legislation, public advertisement for bids would be entirely discretionary with the contracting agency, and when utilized would follow procedures designated in the contracting agency's resolution authorizing the contract. Failure to comply with the requirements of such a resolution may defeat the validity of a contract just as surely as failure to comply with procedures specified by statutes or regulations. Reiter v. Chapman, 177 Wash. 392, 31 P.2d 1005, 1006–07, 92 A.L.R. 828 (1934).

[88] *See* App. A.

[89] *See* ALASKA STAT. § 36.30.130 (1998) (publication by the procurement office is required in Alaska in the online Public Notice System for 21 days prior to bid opening); MISS. CODE § 65-1-85 (requiring publication in newspaper of general circulation published in state capital, having general circulation throughout the state).

tation."[90] Electronic bidding will be discussed later in Section f.

Agencies must strictly comply with the statutory time for publication of bid announcements. Where exact dates are not given, the rules must be construed so that the agency accomplishes the legislative purpose of adequate and reasonable notice. Confusion has occasionally arisen over the method of correctly calculating the period over which notices must appear. One typical style of drafting this provision states that the agency shall advertise "for two consecutive weeks" in designated newspapers. An Ohio court gave this interpretation: "In our opinion, the work 'for' [means that]…such advertisement is required 'during the continuance of' or 'throughout' the period of two weeks….[I]t follows that two full calendar weeks must elapse subsequent to the date of the first publication before the date fixed for receiving the bids."[91]

Some statutes address this potential statutory construction problem by specifically requiring publication "at least once per week" for 2 consecutive weeks.[92]

Federal approval is required before any advertisement for bids or undertaking of bids in federally funded projects. FHWA requires that a minimum of 3 weeks must be available to bidders before the opening of bids.[93] However, the FHWA Division Engineer is authorized to approve shorter periods in special cases.[94] Ultimately, the question of justification is likely to be a practical one. FHWA recognizes that advertising longer than 3 weeks is desirable for "large, complicated projects that will require considerable time for study and developing of cost data before realistic bids can be prepared."[95] In contrast, small, simple problems of construction and maintenance can be prepared and submitted on short notice.

ii. Content of Bid Advertisements.—Bidding statutes have a variety of approaches to informing prospective bidders of the nature of the work required. The contracting agency's announcement must be sufficient to indicate the character, quality, location, and timetable of a construction project, or the type, quantity, and delivery requirements for purchases of supplies and construction materials.[96] When a bidder claims that there is a patent ambiguity in bid documents, a court limits its inquiry to whether a reasonable person could find gross discrepancies, obvious errors in drafting, or a glaring gap.[97] Bid documents are subject to the same rules of interpretation as are contracts: the documents must be interpreted so as to give meaning to all parts and in a manner that does not create internal conflicts.[98] An agency's exercise of discretion in adopting bid specifications is reviewed for arbitrary action.[99]

Requirements relating to the content of bid advertisements often vary according to the transportation system involved. Within a state, there may be separate laws regarding state highways, county and municipal roads, turnpikes, and transit systems. Each may differ regarding the information that bid advertisements must contain. For example, Kansas's law relating to contracts of the state highway commission and the county boards of commissioners illustrates these differences. Notice of state highway projects must "specify with reasonable minuteness the character of the improvement contemplated, the time and place at which the bids will be received, and invite sealed proposals for the same…."[100]

For projects undertaken by county boards of commissioners, the public notice must

> specify with reasonable minuteness the character of the improvement contemplated, where it is located, the kind of material to be used, the hour, date and place of letting of such contract, when the work is to be completed, and invite sealed proposals for the same. Such other notice may be given as the board may deem proper….[101]

In addition to the character and location of the work, some states have added other items in which there is special interest. Examples include notice that prevailing wage rates must be paid to laborers on the job,[102] whether prequalification of subcontractors is required,[103] whether bids must lie on the entire project unless the contracting officer formally determines that a separation is necessary,[104] and that bid bonds will be required in specified amounts.[105] It is also common for statutes to require that bid invitations reserve to the contracting agency the right to reject all bids if it is

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[90] COLO. REV. STAT. § 24-92-104.5 (1999); *see also* D.C. CODE § 2-303.03 (C-1) (2002) .

[91] State *ex rel.* Dacek v. Cleveland Trinidad Paving Co., 35 Ohio App. 118, 171 N.E. 837, 840–41 (1929).

[92] *See*, *e.g.*, 29 DEL. CODE § 6962(b) (1998).

[93] 23 C.F.R. § 635.112(b) (1999).

[94] *Id*.

[95] FEDERAL-AID POLICY GUIDE, Oct. 9, 1996, Transmittal 16 (nonregulatory USDOT administrative guidance supplement to 23 C.F.R. § 635.112).

[96] *See* Wilson Bennett, Inc. v. Greater Cleveland Regional Transit Auth., 67 Ohio App. 3d 812, 588 N.E.2d 920, 925, *jurisdictional motion allowed*, 53 Ohio St. 3d 717, 560 N.E.2d 778 (1990), *cause dismissed*, 57 Ohio St. 3d 721, 568 N.E.2d 1231 (1991) (invitation to bid and specifications present common basis for bidding).

[97] Fry Communications v. United States, 22 Cl. Ct. 497, 509 (1991).

[98] Vanguard Security v. United States, 20 Cl. Ct. 90, 103 (1990).

[99] Glacier State District Services v. Wis. DOT, 221 Wis. 2d 359, 585 N.W.2d 652, 656 (1998) (specifications reviewed to determine whether they were arbitrary or unreasonable).

[100] KAN. STAT. ANN. § 68-408 (1999).

[101] KAN. STAT. ANN. § 68-521(a)(1999); *see also*, *e.g.*, S.D. Codified Laws § 5-18-3 (2001) (requirements for advertising of state highway projects) and § 31-12-14 (2001) (requirements for advertising county road projects).

[102] OR. REV. STAT. § 279.312(1)(a) (1999).

[103] 29 DEL. CODE ANN. § 6962(c) (1999).

[104] CAL. PUB. CONT. CODE § 10141 (1999).

[105] MONT. REV. STAT. § 18-2-302 (1999).

deemed appropriate.[106] They may also require that the notice include information as to where the project plans, specifications, and other pertinent papers may be inspected.[107] Where bid specifications set out the factors on which bids may be evaluated, they are not necessarily required to include the relative weight that will be given to those factors.[108]

Contracts in which federal-aid funds are used must comply with certain requirements of federal law or regulations, which must be mentioned in the project advertisement. Federal-aid regulations call for specific assurance that state procedures afford all qualified bidders a nondiscriminatory basis for submitting proposals and having their proposals considered.[109] State transportation agencies may not impose statutory or administrative requirements that provide in-state or local geographical preference in the solicitation, licensing, or prequalification or selection process. If there are any features of state law that may operate in a manner to prohibit submission of a bid, or prevent consideration of a bid made by a qualified contractor, the project advertisement must state that those features are not applicable to the advertised contract.[110] In addition, all advertisements must advise prospective bidders that, as a condition precedent to federal approval of the contract, the successful contractor must execute and file with the state transportation agency a sworn statement that it has not been a party to any collusion or restraint of free competitive bidding in connection with the project.[111] In addition, the bidder must file a lobbying affidavit certificate pusuant to 49 C.F.R. Part 20, indicating that no funds were expended for lobbying, and provide an additonal affidavit certifying, pursuant to 49 C.F.R. Part 29, that it has not entered into any agreement, participated in any collusion, and is not currently under suspension, debarment, voluntary exclusion, or determination of ineligibility by any federal agency, is not indicted or convicted, and has not had a civil judgment against it for any matter involving fraud or official misconduct for the past 3 years.

Finally, federal-aid regulations specifically state that bid advertisements shall not be issued until the provisions of regulations and directives covering administration of the Uniform Relocation Assistance Act have been met and that all needed right-of-way has been acquired,[112] or that all necessary arrangements have been made for it be undertaken and completed for proper schedule coordination. In the event the requirement that all right-of-way be available is not met before advertisement, the advertisement must include appropriate notice identifying all locations where right of possession and use has not been obtained.[113]

iii. Change of Specifications Following Advertisement.—The project announcement and bidders' proposals are considered to be only invitations and offers, either of which may be changed or withdrawn without penalty prior to the opening of bids and contract award. However, limits are placed on an agency's reserved right to make changes by addendum during the bidding process. Properly issued and provided to all prospective bidders, the addendum becomes part of the invitation for bids.[114] A change announced unilaterally by the contracting agency after advertisement of a project must not give any bidder or group of bidders an unfair advantage, nor may the contracting agency include in the contract any provision benefiting the successful bidder that was not within the terms or specifications that were the basis for the bidding.[115] Extensions of time for performance and agreement to accept substitute materials or modified designs are common types of changes that test the application of this rule. Where the change made in the originally announced terms or specifications is substantial, the validity of the competitive award can be preserved best by readvertising the project for bids, giving consideration to the changed terms.

If a contracting agency decides to make additions or modifications in the specifications or bidding instructions after they have been advertised but before the bids are opened, it must make those changes in a manner that assures that all bidders receive notice of them.[116] If statutory procedure is silent on the notification method, the contracting agency's own bidding instructions may provide the necessary guidance. In the absence of any such guidance, the agency still is responsible for notifying all prospective bidders in a manner that ensures the integrity of the bidding process. Accordingly, where an addendum page was disseminated by simply inserting it into the packets of bidding documents remaining to be picked up by prospective bidders, it was held that the agency had not fulfilled its duty of notification.

> But where as here, an alternative procedure for giving notice of an addendum to the plans and specifications is utilized after the statutory notice has been published…the alternative procedure so utilized, as a matter of law, must, as a minimum, establish actual knowledge

[106] *See*, *e.g.*, 23 ME. REV. STAT. ANN. § 753 (2002).

[107] *Id; see also* Ragland v. Commonwealth, 172 Va. 186, 200 S.E. 601, 602–03 (1939) (Plans and specifications placed on file for public inspection or as a reference to bidders become the only authentic and binding specifications).

[108] Dunnuck v. State, 644 N.E.2d 1275, 1279 (Ind. App. 1 Dist. 1994).

[109] 23 C.F.R. § 635.110 (1999).

[110] 23 C.F.R. § 635.112(d) (1999).

[111] 23 C.F.R. § 635.112(f) (1999).

[112] 23 C.F.R. § 635.309(c) (1999).

[113] 23 C.F.R. § 635.309(c)(3) (1999).

[114] Leaseway Distribution Centers v. Department of Admin. Servs., 49 Ohio App. 3d 99, 550 N.E.2d 955, 960 (1988).

[115] Lake Constr. & Dev. Corp. v. City of New York, 221 A.D. 2d 514, 621 N.Y.S.2d 337, 338 (1995).

[116] *See* Air Support Services Internal v. Metropolitan Dade County, 614 So. 2d 583, 584 (Fla. App. 3 Dist. 1993) (public bid requirements may not be materially altered after submission of bids); Glynn County v. Teal, 256 Ga. 174, 345 S.E.2d 347 (1986) (agency cannot make material changes in plans and specifications without notice to prospective bidders); 29 Del. Code § 6923 (g) (2001).

> on the part of the prospective bidder of the fact of the addendum. Thus, as a matter of law, where a challenge to that alternative procedure is promptly entered by an actual bidder who presents a prima facie case that he was unaware of the addendum to his prejudice, the bidding procedure employed…fails and the trial court is required to order the board to reject all bids….[117]

In issuing an addendum, the agency must be careful that the addendum provides all of the information that it expects bidders to abide by, and that it states very clearly what is being amended in the original invitation for bids. For example, in *Air Support Services International, Inc. v. Metropolitan Dade County*, the court held that the agency could not impose the time limit for submission of bids that was included in the invitation for bids where none was given in the addendum that extended the time for submission.[118] The court found that the addendum implied that bids would be due by the close of business on the date indicated, rather than at the earlier time of day stated in the original invitation for bids.

Most agencies' procedures limit the time that an addendum may be issued, and may prohibit the issuance of an addendum within a certain short period of time before bid opening. This time limitation acknowledges that late-issued addenda may not reach all bidders prior to bid opening, and also recognizes that bidders may need time to adapt their bids to the new specifications. Thus a Louisiana court found that an addendum issued within 72 hours of bid opening was issued improperly.[119] Not all bidders had been informed of the change, resulting in bidders submitting bids on different specifications. The court enjoined the Parish from awarding the contract, thus requiring the agency to reject all bids.[120]

c. Bid Security Deposits

The purpose of the statutory requirement for a bid security deposit is to assure that the bidder is acting in good faith, and that if its bid is successful it will enter into the contract and furnish the necessary bonds for performance of the work and for payment for labor and materials.[121] Maine's statute is an example:

> Each bidder must accompany his bid with a deposit of a good and sufficient bid bond in favor of the State for the benefit of the department, executed by a corporate surety authorized to do business in the State, or certain securities, as defined in Title 14, section 871, subsection 3, payable to the Treasurer of State, for an amount which the department considers sufficient to guarantee that if the work is awarded to him, he will contract with the department for its due execution….[122]

Statutes or regulations typically specify the amount of the deposit, either as a percentage of the total amount of the bid, or a fixed dollar amount determined by the contracting agency, and the acceptable method or methods of providing the security. A comparative summary of state statutes and regulations relating to bid security deposits is given in Appendix B. In most instances, the statutes and regulations also specify how security deposits will be released or returned to unsuccessful bidders.[123] For example, Alabama's statute provides that all bid bonds except those of the three lowest bidders will be returned immediately after determination of the low bidder, with others returned after the contract is executed.[124] Requirements for bid bonds may also be detailed in standard specifications, consistent with the agency's statutory authority.[125]

State statutes may also specify the form of the bid bond. Where a statute required the bonds for public works projects to be written by a surety that was currently on the United States Treasury Department Financial Management Service list of approved bonding companies, bid bonds were held to be covered by that requirement.[126] More typically, statutes require that the bond be issued by a surety authorized to do business in the state.[127]

When bidders may satisfy security requirements by furnishing a surety bond, the surety's obligation typically covers the difference between the amount of the bid and the amount the contracting agency must pay to another contractor to perform the work covered by the bid.[128] When bidders may meet security requirements by depositing a check or bank draft, they must post a specific dollar sum, which is then subject to forfeiture if the bidder fails to execute the contract.

Whether bid security deposits are penalties or liquidated damages has frequently been questioned. One court has considered the forfeiture of the bid bond to be liquidated damages, intended to compensate the agency for its costs in awarding to the next low bidder or read-

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[117] Boger Contracting Corp. v. Bd. of Comm'rs, 60 Ohio App. 2d 195, 396 N.E.2d 1059, 1064 (1978) (emphasis in original).

[118] 614 So. 2d 583, 584 (Fla. App. 3 Dist. 1993).

[119] Grace Constr. Co. v. St. Charles Parish, 467 So. 2d 1371, 1374 (La. App. 1985).

[120] *Id*.

[121] ABA Model Code, *supra* note 59, at § 5-301.

[122] 23 ME. REV. STAT. ANN. § 753 (2002).

[123] *See* Environmental Safety and Control Corp. v. Auburn Enlarged City Sch. Dist., 167 A.D. 2d 876, 561 N.Y.S.2d 972 (1990).

[124] *See* ALA. CODE § 39-2-5 (2001 supp.).

[125] *See* WASH. REV. STAT. § 47.28.090 and Washington State Department of Transportation, *Standard Specifications for Road, Bridge and Municipal Construction*, § 1-02.7 (2002).

[126] Gibson Roofers v. Terrebonne Parish Consol. Gov't, 577 So. 2d 362, *writ denied*, 580 So. 2d 672 (La. App. 1 Cir. 1991).

[127] *See* KAN. STAT. ANN. § 68-410 (2000).

[128] City of Cheyenne v. Reiman Corp., 869 P.2d 125, 127 (Wyo. 1994) (forfeiture of bid bond is liquidated damages for low bidders' failure to execute contract or proceed with construction); WYO. STAT. § 15-1-113 (2002); *see also* Nebraska Standard Specifications § 103.05 (forfeiture of bid security for failure to execute contract is not penalty but rather in liquidation of damages sustained).

vertising.[129] Another has interpreted the bid bond as a penalty, noting that the bid bond document describes the amount of the bond as a "penal sum."[130] The language of these forms has not, however, been considered conclusive proof of their intention or effect. When questions of enforcement have arisen, courts have allowed the circumstances to govern each case, and forfeiture of security deposits may be avoided where unusual hardship or inequity would result.

Much of the reported litigation over interpretation of bid security requirements arises from circumstances where bidders want relief from bid mistakes.[131] However, one case involved the bidder's deliberate refusal to execute the contract because of alleged failure of the contracting agency to perform. A successful bidder believed that the contracting agency would not be able to furnish the needed right-of-way by the time of execution, and delayed executing the contract.[132] Ultimately, the contractor had to forfeit its deposit when the court held that the contracting agency had adequate legal authority to obtain the right-of-way through condemnation, and was under no obligation to acquire the land in advance of the contract execution. Unless conditional terms are set out and accepted in the bid, the bidder is not relieved of its contractual duty under the bid merely because it believes that the contracting agency will not be able to perform its part of the contract.

Compliance with bidding procedure is an administrative function, and courts do not substitute their judgment for that of the contracting agency in the absence of fraud. So where an agency rejected a bid because the bidder's security deposit check was not properly certified, the court upheld the agency's action over arguments that the defective certification complied with the intent of the law.[133] Depending on statutory requirements, the requirement of a bid bond may be considered permissive and subject to waiver by the agency.[134] Also, where the contractor's signature on the bond is not necessary for enforcement of the bond, the requirement of that signature may be waived.[135] However, a bid could properly be rejected because of the surety's failure to use the bid bond form required by the agency, where the failure resulted in required information being omitted.[136] This was found to be an error of substance and not merely of form, because required information was not provided to the agency.

d. Other Bidder Requirements

Some agencies may require attendance at the pre-bid conference as a condition for having the contractor's bid considered. Where the invitation for bids expressly stated that a bidder's attendance at the pre-bid meeting was mandatory in order for its bid to be considered, the agency did not violate competitive bidding requirements when it rejected the low bidder who had not attended the pre-bid meeting. [137] Because of concern about particular site conditions, the agency had determined that prospective bidders must visit the site before bidding, and had written the specifications to require attendance at a pre-bid meeting held at the site. The court did not rule as to whether the agency had authority to waive the attendance requirement, but found that it was not arbitrary to refuse to do so.[138]

e. Submission of Bids and Award of Contract

i. Authority of Contracting Agencies.—Procedures for submission of bids and award of contracts for public works projects are based on statutory provisions. The validity of an award depends on strict compliance with these statutes.[139] In some instances, statutes describe in detail the steps that bidders and agencies must take in moving from bid filing to contract award. However, these procedural requirements may also be promulgated as rules. Where administrative rules are within the agency's statutory authority and are consistent with the implicit requirement that they be designed to strengthen free and open competition among qualified bidders, they have withstood challenge as unconstitutional delegations of rulemaking authority.

ii. Submission, Opening, and Acceptance of Bids.—Requirements designating the time and place for filing bids, and the form of the bid, may be set out in the contracting agency's regulations, in its standard specifications, and in the instructions issued with the proposal form.[140] Strict compliance with these requirements is essential. Contracting agencies, either by statute or administrative rules, generally reserve the right to reject any bid that fails to adhere to these require-

[129] *See* City of Cheyenne v. Reiman Corp., 869 P.2d 125, 127 (Wyo. 1994).

[130] Powder Horn Constructors v. City of Florence, 754 P.2d 356, 366–68 (Colo. 1988).

[131] *See* § 3.

[132] Coonan v. City of Cape Girardeau, 149 Mo. App. 609, 129 S.W. 745 (1910).

[133] Menke v. Bd. of Educ., Indep. School Dist. of West Burlington, 211 N.W.2d 601 (Iowa 1973) (bank used rubber stamp to certify check instead of officer's handwritten signature).

[134] F.H. Myers Constr. Corp. v. City of New Orleans, 570 So. 2d 84, 85 (La. App. 4 Cir. 1990); Thigpen Constr. Co. v. Parish of Jefferson, 560 So. 2d 947, 953 (La. App. 5 Cir. 1990); LSA-R.S. 38:2218(A).

[135] State v. Integon Indem. Corp., 105 N.M. 611, 735 P.2d 528, 530 (1987).

[136] M & L Industries v. Terrebonne Parish Consol. Gov't, 602 So. 2d 321, 322 (La. App. 1 Cir. 1992) *writ denied*, 604 So. 2d 1010.

[137] Scharff Bros. Contractors v. Jefferson Parish School Bd., 641 So. 2d 642 (La. App. 5 Cir. 1994), *writ denied*, 644 So. 2d 399, *reconsideration denied*, 648 So. 2d 384 (1994).

[138] *Id.* 641 So. 2d at 644.

[139] Percy J. Matherne Contractor v. Grinnell Fire Protection Systems Co., 915 F. Supp. 818 (M.D. La. 1995), *aff'd*, 102 F.3d 550 (5th Cir. 1995) (public bid law is mandatory, and any contravention of its provisions renders the contract null and void).

[140] *See*, *e.g.*, Hawaii Corp. v. Kim, 53 Haw. 659, 500 P.2d 1165, 1169 (1972) (contracting officer could set out bidding procedure in absence of a specific statute doing so).

ments.[141] Courts have upheld these technical requirements as mandatory for both bidders and contracting agencies and have taken the position that these requirements may not be waived.[142] It is customary for state transportation agencies to require that proposals be submitted on official bid forms that include specific instructions as to the time and place for submission of bids, and that warn that proposals received after the time and date designated will be returned to the bidder unopened.[143]

Bidding statutes and rules normally specify that bids will be opened in a public session, which all bidders may attend.[144] Courts have reached varying results on the issue of whether the time for submission of bids must be strictly complied with. The Washington Supreme Court has held that the timeliness requirement could be held to have been complied with when the bidder mailed its bid in enough time to reach the agency prior to bid opening, even though it did not arrive on time. [145] However, most courts have taken a much stricter approach. For example, the Georgia Court of Appeals held that the agency's award to an untimely bidder was improper, and upheld an award of bid preparation costs.[146] The court discussed at some length the importance of adhering to a strict rule of timely submission, noting how bidders often adjust their prices up to the last minute before bids are due.[147] Thus, even an additional few minutes could be a material advantage that the untimely bidder would have over the other bidders. The Virginia court also held that the statement in the invitation for bids fixing the time for submission of bids is a material and formal requirement that must be strictly complied with, and that cannot be waived.[148] An Ohio appellate court held that while there is a presumption that the clocks in the agency's building are correct, it is a rebuttable presumption and the rejected bidder may be allowed to show that its bid was submitted in a timely fashion. [149]

The rule on opening of bids in accordance with the terms set forth in the advertisement of the project and bidding instructions, together with a corollary requirement that the award will be announced at that time or within a specified or a reasonable time thereafter, are mandatory duties that contracting agencies owe to bidders. Thus, where an agency issued the original invitation for bids specifying that bids must be submitted on the due date by 1:00 p.m., then issued an addendum extending the date without setting a time, it was to presume that bids were due to be submitted by the close of business that day and not at 1:00 p.m.[150]

Postponement of scheduled bid openings and contract award without strong justification may be challenged as abuse of discretion. Generally, the need to introduce changes in project specifications, or to enable bidders to evaluate and reflect such changes in their bids, has been the most readily accepted justification for postponement.[151]

There is no contract until the bid is accepted and a contract is awarded by the agency. The agency's acceptance of the low bid may be conditional.[152] In *Dick Fischer Development No. 2, Inc. v. Department of Administration*, an agency acknowledged the submission of the low bid with a notice that indicated that the contract would be awarded provided that no bid protests were filed within 5 days.[153] The notice provided that if a protest was filed, the award would be held in abeyance until the protests were resolved. The project was then canceled before the protests were resolved. The court held that there was no breach of contract, because no contract had been formed due to the failure of a condition precedent, which was the resolution of bid protests.

The rules are positive and explicit regarding acceptance of bids that do not fully and precisely meet all formal requirements set forth in regulations and instructions. Bids that are technically defective or deficient must be considered "irregular" or "informal," and may be rejected. The rules calling for rejection of irregular bids are generally stated in permissive terms. As a result, the possibility of waiver of technical defects is always present.[154] However, the courts recognize a distinction between nonmandatory bidding requirements that can be waived and mandatory requirements that

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[141] MONT. REV. STAT. § 18-2-303(3) (1999) (agency may not accept bid that does not comply with statutory requirements).

[142] Hawaii Corp. v. Kim, 53 Haw. 659, 500 P.2d 1165, 1169 (1972).

[143] *But see* Gostovich v. City of West Richland, 75 Wash. 2d 583, 452 P.2d 737 (1969) (holding that where a bid was mailed more than 24 hours before the time for bid opening, and there was no suggestion of fraud or undue competitive advantage, the bid could be accepted despite its late arrival).

[144] *See* ABA Model Code, *supra* note 59, at § 3-202(4).

[145] *Gostovich*, 452 P.2d at 740. Query whether this would still apply when more reliable and commonly used methods of delivery, such as overnight mail, are now available to contractors.

[146] City of Atlanta v. J.A. Jones Constr. Co., 195 Ga. App 72, 392 S.E.2d 564, 569 (Ga. 1990), *rev'd on other grounds*. 260 Ga. 658, 398 S.E.2d 369, 370 (1990). The Supreme Court upheld an award of bid preparation costs, but reversed awards of lost profits and damages for violations of due process.

[147] *Id.* 392 S.E.2d at 566.

[148] Holly's, Inc. v. County of Greensville, 250 Va. 12, 458 S.E.2d 454, 457 (1995).

[149] PHC, Inc. v. Village of Kelleys Island, 71 Ohio App. 3d 277, 593 N.E.2d 386, 387 (1991).

[150] Air Support Services Int'l, Inc. v. Metropolitan Dade County, 614 So. 2d 583, 584 (Fla. App. 3 Dist. 1993).

[151] Yonkers Contracting Co. v. Tallamy, 283 A.D. 749, 127 N.Y.S.2d 646 (1954).

[152] Dick Fischer Dev. No. 2, Inc. v. Department of Admin., State of Alaska, 778 P.2d 1153 (Alaska 1989).

[153] *Id*.

[154] Wilson Bennett, Inc. v. Greater Cleveland Regional Transit Auth., 67 Ohio App. 3d 812, 588 N.E.2d 920, 925 (1990), *cause dismissed* on joint applications to dismiss, 568 N.E.2d 1231, 57 Ohio St. 3d 721 (1991).

cannot be waived without impairing the essential competitive nature of the contract award.[155] Further discussion of nonresponsive bids is addressed in Section 2.A.5. of this volume, below.

f. Electronic Bidding

The use of the Internet in our daily lives is increasing. The Internet has fostered a dramatic change to the bidding and letting process. Electronic bidding is the transfer of proposal data between the contracting agency and its contractors. Electronic bidding can either supplement or replace the traditional bid documents. Electronic bidding can be one-way, where the contractor submits the bid information on a floppy disc or CD that either supplements or replaces the paper copies. In this method the contract proposal should contain language declaring which bid shall govern, in instances where the electronic and paper copy do not match. The second category is two-way, where the contractor submits its bid over the Internet. State transportation agencies have utlized bid preparation software packages, which include Trns.port Expedite, part of the American Association of State Highway Transportation Officials (AASHTO) suite of products.[156]

As of May 2006 there were at least 33 state highway agencies that permitted contractors to submit electronic bids. Generally, if allowed by state law and policy, the Internet advertising of bids in lieu of traditional means on federal-aid projects is allowed by FHWA if it determines that this would generate "adequate publicity." FHWA policy permits electronic bidding, and allow bids to be announced by means other than reading them aloud, such as posting on the Internet. Similarly, electronic submittals and electronic signatures are considered acceptable. State highway agencies have secured licenses to use bid systems such as "Bid Express" and other systems to implement electronic bidding. State laws should be examined to determine whether any changes are necessary. Electronic bidding is widely accepted, and certain highway agencies now require only electronic submissions and prohibit paper submissions.[157]

g. Bidder Preferences and DBE Requirements

One or both of these items may be required as an element of bid responsiveness. Both are addressed in detail in Section 4.

h. Determination of Lowest Responsible Bidder

i. Time for Award and Execution.—Some states' statutes provide for a time period in which the agency must award the contract, and a subsequent time period in which the contractor must execute the contract.[158] An Ohio court has held that the statutory time period for award and execution, which was 60 days, could be extended by mutual agreement of the parties, which could be implied from the parties' conduct.[159] The court further noted that the only entities that may invoke the 60-day limit are the parties, either of whom may withdraw its consent to further extensions of time.[160]

The Model Code allows the award to be made electronically. The award is required to be made in writing, and the Model Code defines "written or in writing" to include electronic means.[161] Once an award of a contract has been made, it may not be withdrawn by the agency.[162]

ii. Selection of Lowest Responsible Bidder.—State statutes generally require that public works contracts shall be awarded to the "lowest responsible bidder."[163] A comparison of state statutes regarding award of contracts is found in Appendix C.

One court has noted that even in the absence of a statutory requirement to do so, public policy requires the award of contracts to the lowest responsible bidder where the agency has chosen to solicit bids.[164] This term is often used without any language reserving the contracting agency's ability to consider any factors other than price. However, some statutes allow additional criteria for selection of successful bidders, such as Illinois' statute, which is based on the Model Code:

Bids shall be evaluated based on the requirements set forth in the invitation for bids, which may include criteria to determine acceptability such as inspection, testing, quality, workmanship, delivery, and suitability for a particular purpose. Those criteria that will affect the bid price and be considered in evaluation for award,

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[155] This is discussed more fully in § 2 infra.

[156] FHWA, CONTRACT ADMINISTRATION CORE CURRICULUM PARTICIPANT MANUAL AND REFERENCE GUIDE, § III, State Procedures, 2006, http://www.fhwa.dot.gov/programadmin/contracts/core02.cfm, last accessed Sept. 8, 2013.

[157] FHWA Web site, Construction Program Guide Electronic Contracting, *see* http://www.fhwa.dot.gov/construction/cqit/econtract.cfm, last accessed Sept. 8, 2013.

[158] *See* WASH. REV. CODE § 47.28.100 (contractor must execute within 21 days after award).

[159] Prime Contractors v. Girard, 655 N.E.2d 411, 101 Ohio App. 3d 249 (Ohio App. 11th Dist. 1995).

[160] *Id.* 655 N.E.2d at 416.

[161] ABA Model Code, *supra* note 59, at §§ 3-202(7), 1-301(26).

[162] Fumo v. Redevelopment Auth. of Philadelphia, 541 A.2d 817, 820, 115 Pa. Commw. 542; *appeal granted*, Greek Orthodox Cathedral of St. George v. Fumo, 557 A.2d 727, 521 Pa. 625; *appeal dismissed*, 568 A.2d 947, 524 Pa. 32; *reargument denied*, 580 A.2d 294, 525 Pa. 292 (1990).

[163] *See*, *e.g.*, Pataula Electric Membership Corp. v. Whitworth, 951 F.2d 1238, 1241 (11th Cir. 1992), *reh'g denied*, Georgia Power Co. v. Pataula Elec. Membership Corp., 506 U.S. 907, *appeal after remand*, Flint Elec. Membership Corp. v. Whitworth, 68 F.3d 1309, *opinion modified*, 77 F.3d 1321 (11th Cir. 1996) (Georgia law requires award to lowest responsible bidder).

[164] City of Philadelphia v. Commonwealth Dep't of Envtl. Resources, 577 A.2d 225, 228, 133 Pa. Commw. 565 (1990).

such as discounts, transportation costs, and total or life cycle costs, shall be objectively measurable. The invitation for bids shall set forth the evaluation criteria to be used.[165]

In a variation on determining the lowest responsible bidder, statutes may allow the agency to consider factors such as the time that the bidder proposes to take to complete the project in addition to the contract price. Arizona enacted a statute allowing "A + B" bidding, in which the agency may select the low bidder based on a combination of A) the contract price, plus B) the calendar days needed to complete the project.[166] In order to assign value to the calendar days, the agency determines the cost to the traveling public of using roads that are under construction.[167]

Court decisions also provide a working definition of "lowest responsible bidder" that fits the pattern formed by most statutes and reflects the interests of the public and the capabilities of contract administration techniques. These decisions address both the elements of "bidder responsibility" and "bid responsiveness." Generally, a bid will be considered "responsive" if it promises to do what the bid specifications demand, and a bidder is considered "responsible" if it can perform the contract as it has promised.[168]

Bidder responsibility thus includes a wide range of factors in addition to the capacity to supply labor and materials, and may involve business morality or trustworthiness.[169] It may also include the bidder's previous performance on similar contracts.[170] However, the obligation to award to the lowest responsible bidder does not allow the agency to choose the "most responsible;" once a bidder is qualified as responsible, the agency may not compare relative degrees of responsibility.[171] However, if statutory authority includes "best bidder," the agency may conduct a qualitative determination as to which bidder was the lowest and "best."

Most of the factors bearing on a contractor's ability to perform satisfactorily generally are discovered in the processes of licensing and prequalification.[172] Thus, most instances in which a contracting agency rejects the lowest-priced bid in favor of a higher-priced offer occur because the rejected bid fails to meet some technical specifications of the project. Responsiveness to the advertised specifications is an essential element of the competitive bidding process. The contracting agency's duty to assure compliance with this requirement may be enforced either by a bidder who is passed over or by a taxpayer who has standing to challenge the agency's action. An unsuccessful bidder may be able to challenge the legality of the contracting agency's action by way of injunctive or declaratory relief or by mandamus.[173] Some courts have held that in the absence of a statute, an unsuccessful bidder does not have standing to challenge an award unless it is also a taxpayer. [174] In an Ohio case, the fact that the challenger paid gasoline taxes was insufficient to establish standing as a taxpayer, even though the project was funded with federal gas tax dollars.[175] The use of a "special fund" required a showing that the plaintiff had a special interest in the use of that fund, that its own property rights were in jeopardy, and that it would sustain damages different from those sustained by the public generally.[176]

However, some statutes specifically allow unsuccessful bidders to challenge contract awards, even if they are not also taxpayers.[177] A bidder on a federal contract has been found to have standing under the federal Administrative Procedure Act to challenge the award of a federal contract.[178]

iii. Rejection of All Bids.—A contracting agency may reject all bids received for a particular project and readvertise the contract. Although it is arguable that this authority is implicit in the agency's general power to select the lowest responsible bidder, the authority of state transportation agencies to reject all bids is generally set forth in statute.[179] Therefore, actions challeng-

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[165] 30 ILL. COMP. STAT. 500/20-10(e) (1999); Model Code, *supra* note 59, at § 3-202(5).

[166] ARIZ. REV. STAT. § 28-6923(I).

[167] *See* Arizona DOT's Web site for information about A+B Bidding at http://www.dot.state.az.us/roads/constgrp/A+BGuide.pdf.

[168] Taylor Bus Service v. San Diego Bd. of Educ., 195 Cal. 3d 1331, 1341–42, 241 Cal. Rptr. 379 (1987); *see also* Irwin R. Evens & Son, Inc. v. Board of Indianapolis Airport Auth., 584 N.E.2d 576, 585 (Ind. App. 4 Dist. 1992) (bid is responsive if it conforms in all material respects to the agency's bid specifications).

[169] Boydston v. Napa Sanitation Dist., 222 Cal. 3d 1362, 1369, 272 Cal. Rptr. 458, *reh'g denied*, 273 Cal. Rptr. 331, 222 Cal. 3d 1362 (1990); Trap Rock Indus. v. Kohl, 59 N.J. 471, 284 A.2d 161 (1971).

[170] Nevada State Purchasing Div. v. George's Equipment Co., 105 Nev. 798, 783 P.2d 949, 954 (1989); Hanson v. Mosser, 247 Ore. 1, 427 P.2d 97, 101 (1967).

[171] Boydston v. Napa Sanitation Dist., 462, 222 Cal. 3d 1362, 1369, 272 Cal. Rptr. 458 (1990) (citing City of Inglewood-Los Angeles County Civic Center Auth. v. Superior Court, 7 Cal. 3d 861, 103 Cal. Rptr. 689, 500 P.2d 601 (1972)); *see also* Bowen Eng'g Corp. v. W.P.M., Inc., 557 N.E.2d 1358 (Ind. App. 2 Dist. 1990).

[172] *See* Section 2 *infra*.

[173] Conway Corp. v. Construction Eng'rs, Inc., 300 Ark. 225, 782 S.W.2d 36, 41, *cert. denied*, 494 U.S. 1080 (1989).

[174] L & M Enterprises v. City of Golden, 852 P.2d 1337, 1339 (Colo. App. 1993) (contractor not among class of persons protected by public bidding statute); Michael Facchiano Contracting v. Pa. Turnpike Comm'n, 153 Pa. Commw. 138, 621 A.2d 1058, 1059 (1993) (disappointed bidder must be a taxpayer to sue; has no property interest in contract and has suffered no injury entitling it to a remedy).

[175] Ohio Valley Mall Co. v. Wray, 104 Ohio App. 3d 629, 662, N.E.2d 1108 (1995).

[176] *Id.* 662 N.E.2d at 1111.

[177] *See*, *e.g.*, ALA. STAT. § 41-16-31.

[178] Clark Constr. Co. v. Pena, 930 F. Supp. 1470, 1475 (M.D. Ala. 1996).

[179] ABA Model Code, *supra* note 59, at § 3-301. In the absence of a legislative reservation of the right to reject all bids, courts have recognized that public authorities have this right

ing the use of this authority tend to look for violations of agency procedures or actions that exceed the scope of the contracting officer's lawful discretion. An agency's decision to reject all bids is subject to judicial review under a variety of standards. However, in most jurisdictions, the decision will be sustained unless it was arbitrary or otherwise unlawful.[180]

In some cases it has been held that public authorities claiming the right to reject all bids must show that they had a rational basis for doing so.[181] Others have required that there be a finding of just cause or best interest of the state.[182] Louisiana's statute was amended to include a requirement that the agency have just cause for rejecting all bids.[183] In overturning a lower appellate court, the Louisiana Supreme Court held that this amendment indicated the Legislature's intent to change the awarding agency's previous broad discretion in rejecting all bids.[184] Some states' statutes require that the agency set out in writing its reasons for rejecting all bids.[185] Where there is such a requirement and it is fulfilled, no further demonstration of facts supporting rejection of all bids is necessary.[186]

If bids are to be rejected, fairness requires that determination and notification be prompt, but no standard for measurement of promptness fits all cases. Where there is a statute requiring the agency to award the contract within a certain period of time, it may be implied that if the agency is going to reject all bids, it should do so within that same time period.[187]

Where rejected bidders are entitled to an administrative hearing, the hearing officer's inquiry is narrow and is limited to whether the purpose of competitive bidding has been subverted or whether the agency acted fraudulently, arbitrarily, or illegally.[188] However, one court has held that where all bids are rejected, as opposed to the low bidder being rejected individually, a rejected bidder is not entitled to a hearing.[189]

A contracting agency may be denied the right to exercise its authority to reject all bids because of its own mistakes or procedural errors. Such questions have been raised when illegal bids were accepted,[190] bids exceeded estimated costs or appropriated funds for the contract,[191] errors were committed in official estimates,[192] and acceptance of a bid was withdrawn prior to notification of the bidder.[193] In *Clark Construction Company v. Pena*, Clark was the low bidder for a federally funded contract being awarded by the Alabama Department of Transportation (ADOT).[194] FHWA refused to concur in the award to Clark due to ADOT's omission of a traffic control note in the approved plans and specifications. The ADOT then rejected all bids and readvertised the project. Clark sued to enjoin the award after the second round of bidding. The federal court found that the omission of the traffic control note was immaterial to the integrity of the bidding process. The Department admitted that but for FHWA's lack of concurrence, it would have awarded the contract to Clark. The court held that both ADOT and FHWA had violated the Federal Highway Act, and permanently enjoined the award and ordered ADOT to accept Clark's original bid.[195] The court sought to avoid sending a message to future bidders that their chances of obtaining government contracts would be dependent on the agency's not making "careless mistakes of questionable importance," and also sought to prevent public officials from violating bid award requirements at will.[196]

In another federal case involving the review of a rejection of all bids, the court held that clear and convincing evidence would be required in order to support reinstatement of the canceled solicitation, as reinstatement amounted to a form of injunctive relief.[197]

An agency was found to have exceeded its power when it rejected all bids and intended to readvertise,

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implicit in their contracting authority. *See* Annotation, 31 A.L.R. 2d 469 (1953).

[180] William A. Gross Constr. Assoc., Inc. v. Gotbaum, 150 Misc. 2d 478, 568 N.Y.S.2d 847 (1991).

[181] Computer Shoppe v. State, 780 S.W.2d 729, 737 (Tenn. App. 1989).

[182] *See* WASH. REV. STAT. § 47.28.090.

[183] New Orleans Rosenbush Claims Service v. City of New Orleans, 653 So. 2d 538, 544 (La. 1995) (applying La. Stat. Ann. – R.S. 38:2214).

[184] Starlight Homes, Inc. v. Jefferson Parish Council, 632 So. 2d 3, 4 (La. 1994); *reconsideration denied*, 638 So. 2d 1079 (1994) (prior to amendment of statute, court held that rejection of all bids did not require a showing of just cause, as rejection of low bidder would require).

[185] *See*, *e.g.*, CAL. PUB. CONT. CODE § 10185; COLO. REV. STAT. § 24-92-105 (1998).

[186] Vining Disposal Service v. Board of Selectmen of Westford, 416 Mass. 35, 616 N.E.2d 1065, 1067 (1993).

[187] New Orleans Rosenbush Claims Service v. City of New Orleans, 653 So. 2d 538 (La. 1995) (at end of 30-day period for agency to award contract, mandamus will lie to compel award).

[188] Fort Howard Co. v. Department of Management Services of State of Florida, 624 So. 2d 783, 784 (Fla. App. 1 Dist. 1993).

[189] Gannett Outdoor Co. v. City of Atlantic City, 249 N.J. Super. 217, 592 A.2d 276, 278 (1991).

[190] Hankins v. Police Jury, 152 La. 1000, 95 So. 102 (La. 1922).

[191] Williams v. City of N.Y., 118 A.D. 756, 104 N.Y.S. 14 (1907), *aff'd* 192 N.Y. 541, 84 N.E. 1123 (1908); Marshall Constr. Co. v. Bigelow, 29 Haw. 641 (1927).

[192] Charles L. Harney, Inc. v. Durkee, 107 Cal. App. 2d 570, 237 P.2d 561 (1951).

[193] Schull Constr. Co. v. Board of Regents of Educ., 79 S.D. 487, 113 N.W.2d 663, 3 A.L.R. 3d 857 (1962).

[194] Clark Construction Co. v. Pena, 930 F. Supp. 1470 (M.D. Ala. 1996).

[195] *Id.* at 1492 ("the ADOT must resubmit Clark Construction's original bid and the FHWA must concur and/or approve said bid"). The court also noted that its holding vindicated ADOT's original position. *Id.* at n.19. *See also* 23 U.S.C. § 112(b)(1).

[196] *Id.* at 1491.

[197] RADVA Corp. v. United States, 17 Cl. Ct. 812, 818–19, *aff'd*, 914 F.2d 271 (1989).

hoping to get a bid for the same amount as a low bid that had been properly rejected as nonresponsive.[198] Also, a board that had authority to negotiate with the lowest bidder could not do so after notifying all other bidders that all bids were being rejected and that the project would be readvertised.[199] In another case, however, the court held that the expectation of attaining better bids for surplus property constituted a rational basis for rejecting all bids.[200] Also, a New Jersey court found that a concern for obtaining lower bids was an adequate reason to reject all bids.[201]

iv. Right of Low Bidder to Award of Contract—Throughout the process of awarding contracts through competitive bidding, public contracting agencies must act in accordance with due process. Accordingly, rejection of the lowest bid received may be challenged as taking or injuring the bidder's right to the contract award.[202] Where it appears that a contractor has a legitimate property right or liberty interest that is entitled to protection, due process requires that the contracting agency grant a hearing in which the rejected bidder is told the reasons for the action and has an opportunity to answer and explain the agency's concerns.[203] Due process protections are required only where property rights or liberty interest are involved, however, and neither courts nor legislatures have been inclined to recognize that every unsuccessful bidder has lost the right to pursue a livelihood when it is not awarded a contract in a properly conducted competition.[204] On the other hand, an agency's actions or written materials may serve to create an entitlement to due process, where it has represented that contracts will always be awarded to the lowest responsible bidder.[205]

v. Rejection of Low Bidder.—The process of receiving, recording, and accepting bids; determining the lowest responsible bidder; and awarding a contract on the basis of that determination has been characterized as being judicial or quasi-judicial in nature, and not merely a ministerial function.[206] Accordingly, courts have been cautious about overruling contracting authorities in the exercise of discretion.[207] There is a presumption that the power and discretion of government officials in awarding bids has been properly exercised.[208] As a rule, agency decisions are not upset except where the challenger shows that fraud, deceit, or flagrant abuse of discretion has prejudiced the competitive bidding.[209] Within a wide range of lawful methods, administrative discretion is permitted to control selection of the lowest responsible bidder, just as it is accepted in determining the prequalification of bidders. As in the case of prequalification of bidders, courts reserve the right to intervene where it appears that abuse of discretion may threaten the policy of competitive award of public contracts.

Determination of the lowest responsible bidder is an "exercise of *bona fide* judgment, based upon facts tending reasonably to the support of such determination."[210] However, contracting agencies may be challenged for arbitrary and capricious action where circumstances suggest that this may have been the case.[211] The agency has an implied contractual duty to consider solicited bids in a fair and honest manner.[212] Thus, when the agency's decision to reject the low bid is challenged, the standard of review is whether the agency acted fraudulently, arbitrarily, illegally, or dishonestly.[213] The fact that the agency acts in error may not be sufficient to overturn its decision under this standard. In one case, the agency's own erroneous estimate was the basis for rejection of all bids, yet because there was no evidence

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[198] Petricca Constr. Co. v. Com., 37 Mass. App. Ct. 392, 640 N.E.2d 780, 782 (1994).

[199] Building and Constr. Trades Council of Northern Nevada v. State *ex rel.* Public Works Bd., 108 Nev. 605 (1992), 836 P.2d 633, 636.

[200] Feldman v. Miller, 151 A.D. 2d 755, 542 N.Y.S.2d 777 (1989).

[201] Marvec Constr. Corp. v. Township of Belleville, 254 N.J. Super. 282, 603 A.2d 184, 187 (1992).

[202] *Compare* LaCorte Elec. Constr. and Maintenance v. County of Rensselaer, 152 Misc. 2d 70, 574 N.Y.S.2d 647, 649 (1991) (low bidder has liberty interest but not property interest in award of contract) *with* Scott v. Buhl Joint School Dist. No. 412, 123 Idaho 779, 852 P.2d 1376, 1384 (1993) (low bidder has property interest in contract award).

[203] *Id.*; Triad Resources and Systems Holdings v. Parish of Lafourche, 577 So. 2d 86, 89, *writ denied*, 578 So. 2d 914 (La. App. 1 Cir. 1990) (bidder whose bid is substantially unresponsive is not entitled to due process).

[204] *See* Envirologix Corp. v. City of Waukesha, 192 Wis. 2d 277, 531 N.W.2d 357, 364 (1995) (statutory bid requirements are intended to benefit public and low bidder has no fixed right to award of contract).

[205] Pataula Elec. Membership Corp. v. Whitworth, 951 F.2d 1238, 1242 (11th Cir. 1992) (Georgia law recognizes that the lowest responsible bidder may have a property interest in award of the contract, based on agency's "vendor manual" that stated that "contracts or open-market purchases will in all cases be awarded to the lowest responsible bidder." This was sufficient to create an entitlement.).

[206] Even when public bidding and contract award is carried out by a legislative body, the same standard applies; the legislative body is not afforded the same level of discretion that it is in legislative actions. Pittman Constr. Co. v. Parish of East Baton Rouge, 493 So. 2d 178, 181 (La. App. 1 Cir. 1986) *writ denied*, 493 So. 2d 1206.

[207] Great Lakes Heating, Cooling, Refrigeration and Sheet Metal Corp. v. Troy School Dist., 197 Mich. App. 312, 494 N.W.2d 863 (1992).

[208] Colonnelli Bros. v. Village of Ridgefield Park, 284 N.J. Super. 538, 665 A.2d 1136 (1995).

[209] Ghilotti Constr. Co. v. City of Richmond, 45 Cal. 4th 897, 903, 53 Cal. Rptr. 2d 389, 392 (Cal. App. 996).

[210] Inge v. Bd. of Pub. Works, 135 Ala. 187, 33 So. 678, 681 (1902).

[211] Catamount Constr., Inc. v. Town of Pepperell, 7 Mass. App. 911, 388 N.E.2d 716 (1979).

[212] Kila, Inc. v. State, Dep't of Admin., 876 P.2d 1102, 1105 (Alaska 1994).

[213] Overstreet Paving Co. v. State, Dep't of Transp., 608 So. 2d 851, 852–53 (Fla. App. 2 Dist. 1992).

of fraud or arbitrary action, the agency was not required to accept the low bid.[214]

In one case, the award to the second lowest bidder was held to be arbitrary since the contracting agency acted contrary to the preponderance of the evidence in the bids, and appeared to be persuaded by the fact that the second lowest bidder had had similar contracts for the agency in the past.[215] In other instances, however, judicial review has upheld the contracting agency's action in rejecting low dollar bids for reasons bearing on the bidder's responsibility[216] and bid responsiveness.[217]

The extent of a contracting agency's discretion in basing contract awards on factors other than dollar cost is limited by the terms of the advertised specifications and bidding instructions, and the agency may not utilize extraneous factors. The validity of a contract may be questioned if the bid documents are indefinite or misleading, and capable of being interpreted in different ways by different contractors. If an irregularity in the bid documents contributes to contractors submitting bids on different terms or with unequal information, the bidding process and any contract awarded will be considered invalid. [218] Where the specifications for a construction project did not give any date for completion of the desired work, or state that the length of construction time would be a determining factor in the award, it was held that that contracting agency acted arbitrarily in using that factor to reject the lowest bid in favor of a higher one that called for an earlier completion date.[219] In another case, it was held to be arbitrary for an agency to induce bidders to submit high quality offers, implying that selection would be made on the basis of best value, and then reject the highest quality offer on the basis of a relatively insignificant price difference.[220]

On the other hand, where matters are clearly stated in the specifications or bidding instructions as being necessary for the performance of the contract or pertinent to the selection of a contractor, courts generally uphold rejection.[221] Bids must conform to the bid specifications in all material respects. However, not every deviation will cause an agency to find a bid to be found nonresponsive. The deviation must be substantial and must give the bidder an advantage over competitors.[222] Thus, when a bidder failed to include the time for project completion, supply pertinent data that affected budget considerations, and include an affirmative action plan, its bid was properly rejected as nonresponsive.[223] Errors such as lack of a corporate resolution or a signature of an authorized individual authorized to bind the bidder to a contract will also be considered a substantial error that renders the bid nonresponsive.[224] A further discussion of nonresponsive bids is contained

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[214] Department of Transp. v. Groves-Watkins Constructors, 530 So. 2d 912 (Fla. 1988).

[215] Berryhill v. Dugan, 89 Commw. 46, 491 A.2d 950, 952 (Pa. Commw. Ct. 1985).

[216] Turnkey Constr. Corp. v. City of Peekskill, 51 A.D. 2d 729, 379 N.Y.S.2d 133 (1976) (lack of experience in building construction, insufficient financial resources, and reason to believe that if awarded the contract bidder intended to assign it to another for performance); L&H Sanitation v. Lake City Sanitation, 585 F. Supp. 120 (E. D. Ark. 1984) (bidder only recently organized and not incorporated at time of bid, lacked any experience in proposed construction, submitted a contingent bid); John Carlo, Inc. v. Corps of Engineers, 539 F. Supp. 1075 (N. D. Tex. 1982) (lack of integrity of bidder's present officers and association with contractors having unsatisfactory records of integrity and performance); Keyes Martin & Co. v. Director, Division of Purchase and Property, 99 N.J. 244, 491 A.2d 1236 (1985) (recent publicity on possible conflict of interest deemed sufficient to conclude that award to lowest bidder would undermine public confidence); Automatic Merchandising Corp. v. Nusbaum, 60 Wis. 2d 362, 210 N.W.2d 745 (1973) (second lowest bidder offered greater amount of new equipment than lowest bidder); Cave-of-the-Winds Scenic Tours, Inc. v. Niagara Frontier State Park and Recreation Comm'n, 64 A.D. 2d 818, 407 N.Y.S.2d 301 (1978).

[217] International Telecommunications Systems v. State, 359 So. 2d 364 (Ala. 1978) (low bidder's samples failed tests for specifications); E.M. Watkins & Co. v. Board of Regents, 414 So. 2d 583 (Fla. App. 1982) (low bidder's material variance with bidding instructions determined to give it advantage over other bidders); Conduit and Foundation Corp. v. City of Philadelphia, 41 Pa. Commw. 641, 401 A.2d 376 (Pa. Commw. 1979) (low bidder's material variance with bidding instructions determined to adversely affect other bidders); William v. Board of Supervisors, of Louisiana State Univ. Agric. and Mechanical College, 388 So. 2d 438 (La. App., 1980) (irregular and incomplete bid); Gibbs Constr. Co. v. Board of Supervisors of Louisiana State Univ., 447 So. 2d 90 (La. App. 1984) (attendance at pre-bid conference); Monoco Oil Co. v. Collins, 96 Misc. 2d 631, 409 N.Y.S.2d 498 (1978) (failure to describe pricing formula); Land Constr. Co. v. Snohomish County, 40 Wash. App. 480, 698 P.2d 1120 (1985) (failure to list certified women's business enterprise as a subcontractor in violation of bidding instructions); Kuhn Constr. Co. v. State, 366 A.2d 1209 (C. Cl., Del. Ch. 1976) (failure to list specialty subcontractors held to be material to statutory requirement for bidding, and omission cannot be waived without encouraging bid shopping); LeCesse Bros. Contracting v. Town Board of Town of Williamson, 62 A.D. 2d 28, 403 N.Y.S.2d 950 (1978) (failure to give names of manufacturers of equipment as required in bid instructions); L. Pucillo & Sons, Inc. v. Mayor and Council of Borough of New Milford, 73 N.J. 349, 375 A.2d 602 (1977) (failure to bid on 5-year contract option in addition to 1, 2, and 3-year options was not minor irregularity that could be waived, but rather was substantial departure from instructions).

[218] Brewer Envtl. Indus. v. A.A.T. Chemical, 73 Haw. 344, 832 P.2d 276, 278 (1992).

[219] Gerard Constr. Co. v. City of Manchester, 120 N.H. 391, 415 A.2d 1137 (1980).

[220] Latecoere Int'l. v. U.S. Dep't of the Navy, 19 F.3d 1342, 1360 (11th Cir. 1994).

[221] *See, e.g.*, City of Philadelphia v. Canteen Co., Div. of TW Services, Inc., 135 Pa. Commw., 575, 581 A.2d 1009, 1013 (1990) (failure to follow bid instructions rendered bid nonresponsive).

[222] Kokosing Constr. Co. v. Dixon, 72 Ohio App. 3d 320, 594 N.E.2d 675, 680 (1991).

[223] *Id.* 594 N.E.2d at 680.

[224] Stafford Constr. Co. v. Terrebonne Parrish School Bd., 560 So. 2d 558, 560 (La. App. 1 Cir. 1990).

in Section 2.B.2.d. of this volume. Such an error could be used by a bidder to withdraw its bid after bid opening, giving it an unfair advantage over other bidders who could not do the same thing without forfeiting their bid bonds.[225] The bidder bears the risk that its bid might contain a nonwaivable error; the contracting agency is under no duty to examine bids for errors and inform bidders accordingly.[226]

After bid opening, the agency may not allow bidders to correct substantive errors. Some states prohibit this by statute, as in Illinois: "After bid opening, no changes in bid prices or other provisions of bids prejudicial to the interest of the State or fair competition shall be permitted."[227]

However, this does not mean that communication between agency personnel and bidders is not allowed after bid opening. The agency may have a duty to contact a bidder to confirm a bid if the agency suspects that there is a mistake.[228] In *Clark Construction Company v. Pena*, it was discovered after bid opening that ADOT had omitted a traffic control note from the plans and specifications.[229] ADOT contacted the bidder, who assured ADOT that the omission of the note would have no effect on its bid. FHWA then refused to concur in the award to Clark, contending among other things that the communication amounted to "reverse bid rigging" under an FHWA policy memorandum. The court held that FHWA's and ADOT's rejection of Clark as the low bidder was without a rational basis, and found that the communication was not an attempt by ADOT to gain a price reduction but rather was a means of evaluating the materiality of the omission.[230]

However, any attempt by the agency or the contractor to negotiate after the opening of bids is generally found to be improper, at least in the absence of a statute that permits negotiation with the low bidder.[231] The contract may be found invalid where post-bidding negotiations with the apparent low bidder result in awarding a contract on specifications that have been altered from those originally advertised.[232] Courts have been clear on the issue that a contract cannot be awarded on terms that are different from those in the invitation for bids.[233] This rule is based on one of the underlying policies of competitive bidding—assurance against favoritism, fraud, and corruption. In order to effectively guard against favoritism and corruption, all bidders must be equally situated, and there must be a common standard for evaluating bids. A contracting agency may not contract, even with the low bidder, for terms that were not included in the bid specifications.[234] Thus a low bidder could not attempt to modify its bid and attempt to negotiate a more favorable contract for itself, since to do so would give the bidder an unfair competitive advantage over other legitimate bidders, and post-bid negotiations would violate competitive bidding.[235] For federally aided projects, 23 C.F.R. § 635.113 prohibits negotiation with contractors following the opening of bids and before the award of the contract.

In *Arkansas Highway and Transportation Department v. Adams*, the transportation department's refusal to negotiate with the low bidder was upheld, as was the department's rejection of the low bid because of its failure to include either a unit price or an extended price on a specified item.[236] It was therefore impossible for the agency to discern what the unit price for that item was. The court noted that the department's published specifications authorized it to reject a bid that lacked a unit price on a bid item and that the department had a policy of not accepting a bid from which a unit price for a bid item could not be determined.[237] Where the agency's specifications or regulations are rational, then the fact that the bidder did not follow them must be considered a "rational basis" for rejecting a bid.

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[225] *But see* Leaseway Distribution Centers v. Dep't of Admin. Servs., 49 Ohio App. 3d 99, 550 N.E.2d 955, 960 (1988) (even though signature was missing from cover page as required, signature on addendum was adequate to bind the bidder to its bid as addendum was part of bid documents).

[226] Dep't of Transp. v. Ronlee, Inc., 518 So. 2d 1326, 1328–29 (Fla. App. 3 Dist. 1987), *review denied*, 528 So. 2d 1183 (1988) (it was not inequitable for agency not to have informed bidder of bid error of less than 2 percent where bidder also discovered error on its own).

[227] 30 ILL. COMP. STAT. 500/20-10(f) (2001).

[228] ABA Model Code, *supra* note 59, at § 3-202(6) and commentary.

[229] 895 F. Supp. 1483 (M.D. Ala. 1995).

[230] *Id*. at 1491.

[231] *See* Building and Constr. Trades Council of Northern Nevada v. State *ex rel.* Public Works Bd., 108 Nev. 605, 836 P.2d 633, 636 (1992) (statute allows Public Works Board to negotiate with low bidder after it has notified other bidders that their bids have been rejected, that the project will not be rebid, and that it intends to negotiate with low bidder, citing N.R.S. 341.145(3)).

[232] Thelander v. City of Cleveland, 3 Ohio App. 3d 86, 444 N.E.2d 414, 427 (1981).

[233] Palamar Constr. v. Township of Pennsauken, 196 N.J. Super. 241, 482 A.2d 174, 179 (A.D. 1983). The court held, however, that attachment of post-bid conditions by the agency that were more favorable to the agency was allowed if the contractor agreed to the conditions; the bidder was not required to concede to the added conditions as it was entitled to the contract as it had been bid. 482 A.2d at 181. *See also* Transactive Corp. v. N.Y. State Dep't of Social Services, 665 N.Y.S.2d 701, 705 236 A.D. 2d 48 (N.Y. App. 1997) (post-bid negotiations are proper if they do not involve a departure from the original specifications or require any concessions to the low bidder).

[234] *See* Ariz. Board of Regents *ex rel.* Univ. of Ariz. v. Main Street Mesa Assocs., 181 Ariz. 422, 891 P.2d 889, 893 (Ariz. App. Div. 1 1994) *review denied* (1995) (where sale of public land was governed by competitive bidding laws, the agency may not negotiate with the high bidder for terms not included in the bid specifications; court's holding was based on general rule of competitive bidding that agency may not negotiate with lowest bidder for terms that materially depart from the invitation for bids).

[235] Lake Constr. & Dev. Corp. v. City of N.Y., 221 A.D. 2d 514, 621 N.Y.S.2d 337, 338 (1995).

[236] 300 Ark. 16, 775 S.W.2d 904, 905–06 (1989).

[237] *Id*. at 905.

The Arkansas court in *Adams* noted that the agency had previously waived the defect of failure to include a unit price where the unit price could be derived from the extended price. However, in Louisiana, the result was the opposite in *V.C. Nora, Jr. Building and Remodeling, Inc. v. State Department of Transportation and Development.*[238] The court held that based on the strict language of the statute, the agency did not have discretion to waive the failure to include a unit price, even though the unit price could be derived from the extended price.[239] The statute stated: "The provisions and requirements of this Section, those stated in the advertisement for bids, and those required on the bid form shall not be considered as informalities and shall not be waived by any public entity."[240]

The court noted that this was a harsh result, but found that the strict language of the statute left the agency with no discretion to waive such a defect in the bid.[241]

i. Determination of Lowest and Best Bidder

One state statute adds "best" to the lowest responsible bidder determination. Section 24-02-23 of the North Dakota Century Code provides that every contract over $50,000.00 must be awarded to the responsible bidder submitting the lowest and best bid. Unfortunately, there are no reported cases in North Dakota interpreting this best bid statute. Similar best bid provisions are, however, contained in bidding statutes in Ohio. The best bidder provisions permit the owner to evaluate more than price and allow consideration of other factors spelled out in the solicitation. The word "best" is understood to refer to the qualifications of the bidder to perform the work. "Best" conveys discretion on the awarding authority to consider quality, feasibility, and qualifications of the bidder in addition to the price. In *United States Wood Preserving Co. v. Sundmaker,* 186 F. 678. 693 (Ohio, 1998), the Sixth Circuit Court of Appeals upheld the Ohio best bidder case law and the municpalities' acceptance of a higher "best bid." In *Prime Contractors, Inc. v. City of Girrad*, the Court of Appeals of Ohio upheld a public works best bidder determination, indicating that the municipality did not abuse its discretion.[242] The court noted that a municipal corporation is not automatically required to award to the company submitting the lowest bid, but is allowed to engage in a qualitative analysis as to which bidder is better. The court found no abuse of discretion, since the criteria upon which the decision was based was set forth in the bidding proposal. Further, the Supreme Court of Ohio, in *City of Dayton ex rel. Scandrick v. McGee*, rejected a lowest and best bidder determination because the City applied an unannounced residency requirement not contained in the solicitation, which the Court found to be an abuse of discretion.[243] In summary, use of the "best bidder" language can provide public transportation agencies with more discretion in their bid determinations, provided that this is statutorily authorized, and that the criteria and factors are disclosed and specified in the solicitation documents.

j. Effect of Failure to Follow Required Procedures

Bidding procedures set forth in statutes and administrative rules are regarded as jurisdictional prerequisites for valid exercise of a contracting agency's authority. Courts have made it plain that they seek constructions of these rules that will fully carry out the intent of the law in varying situations, but will not weaken the effectiveness of the law through exceptions. Thus, the agency's failure to comply with all the specified steps before an award may result in failure to create any enforceable obligation or liability on the part of the public agency. Where an agency does not follow exactly its specified procedures, the resulting contract is void.[244]

Abuse of discretion may be found when a contracting agency fails to furnish enough or the right sort of guidelines and instructions for bidders, which could prejudice the entire bidding process.[245] For example, an agency that did not disclose its policy of preferring resident bidders until after bid opening was held to have modified its requirements without proper notice to bidders.[246] In another case, the award was set aside and the agency was required to readvertise the contract where the bid specifications gave incorrect directions to bidders regarding the required amount of the bid bond.[247] The specifications did not state that the amount of the bid bond would be 10 percent of the contract price, not to exceed $20,000, as the statute required. Rather, they required 10 percent of the bid amount, which in the case of some bids was over $40,000. Some contractors had referred instead to the statute, providing only the $20,000 statutory bond amount. The court held that this gave some bidders an advantage over others, and set aside the award.[248]

In other cases, the agency's own handling of the bids and of the award process may result in a material de-

[238] 635 So. 2d 466 (La. App. 3 Cir. 1994).

[239] *Id.* at 472.

[240] LSA-R.S. 38:2212(A)(1)(b) (2000).

[241] *See* Section 5, *infra*, for further discussion of waivable and non-waivable errors.

[242] 101 Ohio App. 3d 249, 655 N.E.2d 411 (1995).

[243] 67 Ohio St. 2d 356, 423 N.E.2d 1095 (1981).

[244] Failor's Pharmacy v. Dep't of Social and Health Servs., 125 Wash. 2d 488 886 P.2d 147, 153 (1994) (failure to comply with statutorily mandated procedures is ultra vires and renders contract void); *see also* Spiniello Constr. Co. v. Town of Manchester, 189 Conn. 539 456 A.2d 1199, 1202 (1983); Terminal Constr. Corp. v. Atlantic County Sewerage Auth., 67 N.J. 403, 341 A.2d 327 (1975).

[245] Dayton, *ex rel.* Scandrick v. McGee, 67 Ohio St. 2d 356, 423 N.E.2d 1095 (1981).

[246] *Id.* 423 N.E.2d at 1097.

[247] Waste Disposal, Inc. v. Mayor and Council of Borough of Roselle Park, 145 N.J. Super. 217, 367 A.2d 449 (1976).

[248] *Id.* 367 A.2d at 450.

viation from bidding laws. For example, the court in a New Jersey case found that even though the agency had posted bids on an electronic bulletin board shortly after bid opening, the agency's failure to total bid items and announce the bid totals warranted rejection of bids.[249] In another case, where the agency's bid documents indicated that it would accept the unit item price where there was a discrepancy between the unit price and the total, it was held to be an error to reject the low bidder whose unit price was not ambiguous.[250]

Contractors who perform construction work or supply materials under an innocent impression that their contracts were awarded through correct procedures understandably complain of the hardship resulting from application of this rule. But even where the public agency accepts and uses the results of a contractor's work, the contractor may not recover in *quantum meruit*.[251] Allowing recovery in *quantum meruit* where the bidding requirements have been violated would undermine the policies of competitive bidding. In addition, the contractor may be required to repay to the agency any funds received under the arrangement. This is particularly so where the public contract has been obtained through fraud or corruption, whether on the part of the agency official or the contractor.[252] This harsh result has been found to be necessary to deter corruption and collusion in bidding.[253]

Apparent exceptions to this rule have been noted, chiefly where courts have been able to find factual bases for enforcing an implied contract, or have found that in addition to noncompliance with bidding statutes, there was proof of fraud in the award.[254] In the absence of such findings, however, contractors have little prospect of recovering for work performed because theories of quasi-contract will not be applied to promises that are beyond the authority of a public agency to make.

[249] Statewide Hi-Way Safety, Inc. v. N.J. Dep't of Transp., 283 N.J. Super. 223, 661 A.2d 826 (A.D. 1995) (dismissed as moot, but DOT's argument was rejected as to future cases).

[250] Pozar v. Dep't of Transp., 145 Cal. App. 3d 269, 193 Cal. Rptr. 202, 203 (1983).

[251] J & J Contractors/O.T. Davis Constr., A.J.V. v. State, by Idaho Transp. Board, 118 Idaho 535, 797 P.2d 1383, 1384–85 (1990) (contractor may not recover if contract is void, as opposed to voidable); Trujillo v. Gonzales, 106 N.M. 620, 747 P.2d 915, 917 (1987) (violation of Open Public Meetings Act); Lanphier v. Omaha Public Power Dist., 227 Neb. 241, 417 N.W.2d 17, 21 (1987) (quantum meriut was available to the contractor where the city had authority to contract, but not where there was no authority).

[252] Curiale v. Capolino, 883 F. Supp. 941 (S.D.N.Y. 1995). However, in *J & J Contractors*, *supra* note 251, the agency was prevented from recovering what it had paid the contractor because it had not appealed the determination made by the hearing officer on the contractor's claim. 797 P.2d at 1385.

[253] *Id.* at 951.

[254] Gerzof v. Sweeney, 16 N.Y.2d 206, 211 N.E.2d 826, 264 N.Y.S.2d 376 (1965), *cited in* Curiale v. Capolino, 883 F. Supp. 941 (S.D.N.Y. 1995).

Failure of a contracting agency to follow mandatory procedures in conducting bidding and award of contracts has been alleged in a variety of situations. An award was challenged where the agency did not compel the successful bidder on a highway construction contract to give assurance that it would pay prevailing wage rates as required by state law.[255] Also, the contracting agency's award was protested where the agency accepted an apparently late bid upon the bidder's claim that the bid clock was fast, and thereafter failed to notify the apparently successful bidder of a bid protest.[256]

k. Permissible Types of Combined Bidding by Contractors

In contrast to combinations that arise from collusion, other types of combinations for purposes of bidding are permitted. Where contracting agencies have projects that are unusually large, or that have an unusually wide range of specialty requirements, it may be impossible for one contractor to undertake the work desired in a single contract. Under these circumstances, joint bids by contractors who combine their resources to organize and perform this work provide a sensible solution.

Courts' acceptance of the practice of joint bidding by contractors has emphasized the distinction between these open agreements and the secrecy typically associated with collusive combinations. An early decision of a New York court illustrates this view:

> [A] joint proposal, the result of honest cooperation though it might prevent the rivalry of the parties, and thus lessen competition, is not an act forbidden by public policy. Joint adventures are allowed. They are public and avowed and not secret. The risk as well as the profit, is joint and openly assumed. The public may obtain at least the benefit of the joint responsibility, and of the joint ability to do the service. The public agents know, then, all that there is in the transaction, and can more justly estimate the motives of the bidders and weigh the merits of the bid.[257]

Subcontracts and joint ventures are both subject to scrutiny to assure that they are genuine, because either technique can be abused and become a threat to fair competition. It is contrary to public policy for bidders on a public works project to agree that some of them will refrain from bidding in favor of others. It is also contrary to many states' public bidding laws, as in Kentucky: "Any agreement or collusion among bidders or prospective bidders which restrains, tends to restrain, or is reasonably calculated to restrain competition by agreement to bid at a fixed price, or to refrain from bidding, or otherwise, is prohibited."[258]

[255] Lynch v. Devine, 45 Ill. App. 3d 743, 359 N.E.2d 1137 (1977).

[256] Washington Mechanical Contractors v. United States Dep't of the Navy, 612 F. Supp. 1243 (N.D. Cal. 1984).

[257] Atcheson v. Mallon, 43 N.Y. 147, 151 (1870).

[258] KY. REV. STAT. § 45A.325 (1999).

i. Joint Ventures.—Where construction work is carried out under a single contract, unusually large or complex projects may require assembling financial resources and administrative or technical workers on a scale greater than any single contractor can provide through its own efforts and resources, or through its own staff plus the use of subcontractors. A practical accommodation of the rules of competitive bidding to the needs of contractors and contracting agencies is offered in the practice of accepting bids from two or more contractors acting in a joint venture. In this type of bid, groups of contractors combine their assets, plant, and personnel in a joint effort.

Joint ventures are similar to ordinary business partnerships. The parties share the work, the prospects of profits, and the risks of loss. The terms on which the parties share the responsibilities and results of the work are set forth in written agreements.[259] The main difference is that joint ventures are created to perform one specific job, whereas partnerships are continuing arrangements.[260] In establishing a joint venture, it is not enough to merely adopt a particular joint name. One seeking to prove that a joint venture exists must show that there is a community of interest in the venture between the two contractors, an agreement to share the profits and losses in a project, and a mutual right of control or management over the project.[261] A joint venture is not a legal entity apart from the two or more contractors comprising it. A joint venture was not a "resident" for the purpose of taking advantage of a state preference statute where neither of the two joint venturers were resident corporations.[262]

Remedies available to the parties in the event of a dispute are generally the same as those applicable to partnerships, with some differences. Among partners, the usual remedy is for the aggrieved partner to sue for an accounting. However, in joint ventures, one may sue the other for breach of the contract defining the terms of their cooperative undertaking, or for contribution to the plaintiff's losses.[263]

Joint venture bidding is permitted so long as it is a bona fide cooperative effort among its parties. Joint venture bids must fully disclose the terms of the cooperative effort the parties will undertake. Secret agreements under which several contractors undertake to share the work, risks, and profits of a project are not proper or enforceable, regardless of whether they result in a single bid for the parties to the arrangement or separate bids by all parties according to a prearranged plan.[264]

Joint venture bids have the advantage of pooling the capacity of several contractors and allowing prequalification for projects that no one of them is capable of performing individually. When such bids are filed, the bid should indicate what percentage of the dollar amount of the contract should be debited against the prequalification capacity rating of each joint venture. Where bidders do not allocate the proportions to be debited, the contracting agency should make this determination as it deems to be in its own best interest. Apportionment of the prequalification capacity rating debit among the parties to a joint venture bid does not in any way divide the responsibility of each for the execution and performance of the contract if it is awarded to them.

ii. Subcontracts.—Under a subcontract, all details of the subcontractor's work are defined in the agreement between the subcontractor and the prime contractor. The prime contractor is responsible to the contracting agency for the performance of the subcontract along with the rest of the contract work, except as to those requirements that state or federal law imposes directly and individually on both the prime contractor and the subcontractor. An example of such a requirement is the Contract Work Hours and Safety Standards Act, which requires both the prime and subcontractors to comply with federal standards for hours of work and worker safety.[265]

l. Competitive Bidding Requirements for Federal and Federally Aided Highway Construction Contracts

Selection of contractors for federal agency construction projects is governed by the requirements of 41 U.S.C. § 5, which provides that, unless otherwise specified in appropriation legislation or unless they come within an authorized exception, contracts for materials, supplies, or services for the government must be awarded through public advertisement and competitive bidding. The authorized exceptions to this rule include contracts in which 1) the amount involved does not exceed $25,000; 2) immediate delivery of materials or performance of services is required because of "public exigencies"; 3) only one source of supply is available; or (4) the services required must be performed by the contractor in person and are of a technical or professional nature, or are under government supervision and paid for on a time and materials basis.[266]

A similar statute applies to federal-aid highway projects where construction is performed under contracts awarded by a state highway agency or a local govern-

[259] But see Libby v. L.J. Corp., 247 F.2d 78 (D.C. Cir. 1957) (existence of a joint venture may be implied from the parties' conduct even if not in writing).

[260] Ben Fitzgerald Realty Co. v. Muller, 846 S.W.2d 110, 120 (Tex. App. 1993).

[261] *Id.* at 121.

[262] Bristol Steel and Iron Works v. State, Dep't of Transp. & Dev., 504 So. 2d 941 (1987), *writ granted*, 505 So. 2d 1131 and 505 So.2d 1132, *rev'd* 507 So. 2d 1233 (1987) (finding that one of joint venturers was resident and that employee stock option plan did not constitute a "change in ownership" so as to form basis for finding that contractor did not meet statutory requirement of not having had change in ownership in previous 2 years in which it had state license).

[263] Alpine Constr. Co. v. Gilliland, 178 N.W.2d 530, 23 Mich. App. 275 (1970).

[264] Hoffman v. McMullen, 83 F. 372 (9th Cir. 1897).

[265] 40 U.S.C. §§ 327–333(a) (1999).

[266] 41 U.S.C. § 5 (1999).

ment using federal funds.[267] Exceptions to this requirement are not specified in the statute, as in the case of direct federal construction. However, the Secretary of Transportation is authorized to approve modifications of the usual methods of advertisement for proposals, provided that those methods "shall be effective in securing competition."[268] Alternatives to public bidding may be allowed where the state demonstrates that another method is more cost effective or that an emergency exists.[269]

FHWA regulations applying to projects that are in any part paid for with federal funds also address competitive bidding requirements.[270] These regulations require that federal-aid highway construction work must be performed by contract awarded to the lowest responsible bidder, unless it is undertaken by the state as a force account activity, or unless the agency demonstrates that either an emergency or a more cost-effective method exists.[271] For work performed by contract, the state highway agency must assure the opportunity for free, open, and competitive bidding, including adequate publicity of the advertisement or call for bids, and must comply with the procedures in the regulation. State transportation agencies may not issue invitations for bids on such projects until compliance with the provisions of applicable FHWA regulations and directives is approved by the FHWA division administrator.[272] Arrangements for performance of work as force account projects require that the FHWA division administrator find that those arrangements are cost effective, and that the state determine that the project can be staffed and equipped satisfactorily and cost effectively.[273]

FHWA regulations limit the extent to which subcontracting may be used and specify that prime contractors must perform at least 30 percent of the total contract price with their own personnel.[274] However, if any of the contract work requires "highly specialized knowledge, abilities or equipment not ordinarily available in the type of contracting organizations qualified and expected to bid on the contract," that work may be designated as specialty work and may be deducted from the total contract price before computing the amounts for prime and sub contractors to perform.[275]

The minimum time for advertisement of bids is prescribed by federal regulations as 3 weeks prior to the date for opening bids, except where shorter periods may be justified by special circumstances and approved by the FHWA division administrator.[276] Prior approval of the administrator must also be obtained if the agency issues any addenda setting out major changes to the approved plans and specifications during the advertising period, and the state transportation agency is required to give specific assurance that all bidders received such addenda.[277]

A bidder must file an affidavit that it did not engage in any action in restraint of free competitive bidding in connection with the contract being awarded.[278] Finally, in the interest of increasing small business participation in federal-aid highway construction, state transportation agencies must schedule contract lettings in "balanced programs" as to size and type of contracts to assure opportunities for all sizes of contractors to compete in the federal-aid program.[279]

m. Exceptions to the Competitive Bidding Rule

Statutes and regulations specify certain circumstances in which competitive bidding procedures do not apply. The most common exceptions are concerned with the amounts of money involved in a contract, the need to respond to emergency situations, and the impracticality of procuring certain services through price competition. Further discussion of emergency contracting is addressed in Section 1.A.2.n. of this volume.

i. Statutory Minimum Amounts.—Most statutes and ordinances that impose competitive bidding requirements apply only to contracts that involve more than specified minimum amounts of money. The rationale of this exception appears to be the practical consideration that when less than this minimum amount is involved, the cost of administering competitive bidding procedures is more expensive than the risk of loss to the public justifies. Minimum levels set by statute typically are low, so that only the most minor projects are within the scope of the exception.[280]

Questionable contracting practices and ambiguities in contract language are responsible for a large share of the cases in which the application of this exception is challenged. Even with a clear statutory designation of the minimum amount required for competitive bidding, it is still possible for a contracting officer to be indefinite about the contract's total amount because unit prices rather than job prices are quoted. In such cases, evidence suggesting advance knowledge of the ultimate magnitude of the contract's cost, implying intent to circumvent the competitive bidding law, is important. Thus, where a contract was negotiated to purchase gravel at a fixed price per yard for use in road and street repair, and thereafter 74 separate purchases (each costing less than $500) were made on identical terms over a period of 8 months, the court concluded that the arrangement violated the law requiring com-

[267] 23 U.S.C. § 112(a) (1999).

[268] *Id*. at § 112(b).

[269] *Id*.

[270] 23 C.F.R. § 635.104 (2000).

[271] 23 C.F.R. § 635.204(a) (2000).

[272] 23 C.F.R. § 635.112 (2000).

[273] 23 C.F.R. § 635.104 (2000).

[274] 23 C.F.R. § 635.116 (2000).

[275] 23 C.F.R. § 102 (2000) (definition of specialty work); 23 C.F.R. § 635.116 (2000).

[276] 23 C.F.R. § 112(b) (2000).

[277] 23 C.F.R. § 112(c) (2000).

[278] 23 C.F.R. § 112(f) (2000).

[279] 23 C.F.R. § 107 (2000).

[280] *See* App. C.

petitive bidding for all public contracts in excess of $500.[281] Stating that the legislature could not have intended to allow its main objective to be "circumvented by multiple small open-market purchases," the court emphasized that nothing in the record indicated that the contracting agency could not and did not realize the full extent of its need for road repair material.[282]

Closely related to these cases are situations in which the agency has deliberately split a public construction project so that it can be performed under several contracts, some or all of which may fall below the statutory minimum amount for competitive bidding. Sound engineering, financial, and administrative reasons may support the decision to split a single project into segments for contracting. However, where it appears that this has been done for the purpose of evading a mandatory competitive bidding statute, the court may find the negotiated contracts invalid.[283]

ii. Specialized Personal and Professional Services.—Contracts for personal or professional services form another generally recognized exception to mandatory competitive bidding procedures.[284] A leading case on this matter has explained the exception as follows:

> The theory upon which the doctrine rests is that the competitive bidding statutes cannot be rationally or practically applied to contracts for the employment of architects or other persons whose services are required because of the special training, skill, and scientific or technical knowledge necessary to the object to be accomplished…The value of such services is not to be measured by a mere matching of dollars, so to speak; it is not to be determined upon the irrational assumption that all men in the particular class are equally endowed with technical or professional skill, knowledge, training, and efficiency, nor are such services rendered more desirable because afforded more cheaply in a competitive bidding contest. The selection of a person to perform services requiring those attributes calls for the exercise of a wise and unhampered discretion in one seeking such services, for it involves not only those attributes, but the qualities of reputation and personal and professional trustworthiness and responsibility as well.[285]

Similar views have been expressed about the services of artists,[286] auditors and accountants,[287] traffic engineers,[288] and real estate appraisers.[289] Contracts for insurance coverage have also been held to be contracts for "extraordinary, unspecifiable services" that fall outside the requirement for competitive bidding.[290]

Procurement of personal or professional services without competitive bidding is justified because it does not involve work that conforms to specifications that allow for contractors' performances to be evaluated by relatively objective standards. Accordingly, contracts calling for services that require personal or professional judgment, in which the contracting agency specifies an objective but not the methods of the desired work, have been exceptions to the competitive bidding mandate. This rule has been extended to include services requiring aesthetic, business, or technical knowledge and judgment, and professional or scientific skill and experience.[291]

In line with this reasoning, contracts for architectural and engineering services are regularly put into this category.[292] Under federal law, the Brooks Architects-Engineers Act allows the solicitation of architectural and engineering services based on factors other than price:

> The Congress hereby declares it to be the policy of the Federal Government to publicly announce all requirements for architectural and engineering services, and to negotiate contracts for architectural and engineering services on the basis of demonstrated competence and qualification for the type of professional services required and at fair and reasonable prices.293

Although the Brooks Act does not require prequalification of engineering and architectural firms, it does encourage federal agencies to have firms submit annual statements of qualifications.[294] After the agency considers the qualifications of interested firms, the Act requires the hiring agency to select the three most qualified firms after "conduct[ing] discussions with no less than three firms regarding anticipated concepts and the relative utility of alternative methods of approach for

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[281] Fonder v. City of Sioux Falls, 76 S.D. 31, 71 N.W.2d 618 (1955)

[282] *Id.* 71 N.W.2d at 621.

[283] Miller v. McKinnon, 20 Cal. 2d 83, 124 P.2d 34 (1942).

[284] Amherst Columbia Ambulance Service Ltd. v. Gross, 437 N.Y.S.2d 137 (1981).

[285] Louisiana v. McIlhenny, 201 La. 78, 9 So. 2d 467, 471 (1942) (employment of landscape architect) (quoting Gulf Bitulithic Co. v. Nueces County, 297 S.W. 747, 753 (Tex. App. 1927)), *reh'g denied*.

[286] Adams v. Ziegler, 22 Cal. App. 2d 135, 70 P.2d 537 (1937).

[287] Cochran County v. West Audit Co., 10 S.W.2d 229 (Tex. Civ. App. 1928).

[288] City and County of San Francisco v. Boyd, 17 Cal. 2d 606, 110 P.2d 1036 (1941); Flottum v. City of Cumberland, 234 Wis. 654, 291 N.W. 777 (1940).

[289] Doverspike v. Black, 535 A.2d 1217, 1219, 126 Pa. Commw. 1 (1988) *aff'd on reargument*, 541 A.2d 1191, 126 Pa. Commw. 11 (1988); Parker v. Panama City, 151 So. 2d 469 (Fla. Dist. Ct. App. 1963).

[290] Local 1081 of Communications Workers of America, AFL-CIO v. Essex County, 255 N.J. Super. 671, 605 A.2d 1154 (N.J. Super. A.D. 1992).

[291] Attlin Constr. v. Muncie Cmty. Sch., 413 N.E.2d 281, 287 (Ind. App. 1980), (construction manager was acting similar to architect or engineer).

[292] State v. Brown, 422 N.E.2d 1254, 1256 (Ind. App. 1981) (field supervision and coordination of activities at construction site performed by construction manager were professional services, and did not have to be competitively bid).

[293] 40 U.S.C. § 542 (1999) (Brooks Architects-Engineers Act).

[294] 40 U.S.C. § 543 (1999).

furnishing the required services."[295] The agency may then proceed to negotiate a contract with the top qualified firm at "compensation which the agency head determines is fair and reasonable to the Government. In making such determination, the agency head shall take into account the estimated value of the services to be rendered, the scope, complexity, and professional nature thereof."[296]

Courts have not always agreed with contracting agencies that a particular contract was for personal services that should be contracted for in this manner. Contracts for architects and engineering services are usually not in question, as they will likely be covered either by the Federal Brooks Act or by a state "Little Brooks Act." In contrast, a contract to film the construction of a major highway bridge was held not to be one for "personal services."[297] That contract was considered to be one for the purchase of the films rather than for professional services. A contract to manage the sale of advertising space and display facilities in an airport was also not considered a contract for specialty services.[298] The same result occurred where a public agency contracted for inspection and enforcement of an electrical code for building construction. Denying that it could be regarded either as "professional" or "extraordinary unspecifiable services" under the state's public contracts law, the court reasoned that since inspection specifications had been issued for use in administration and enforcement of the law, the work may have required special skill but did not demand special knowledge or professional judgment and was thus subject to competitive bidding rules.[299] In another case, contracts for feasibility studies of programs for environmental protection and rehabilitation of lakes were challenged because the specifications were very detailed and appeared to be conducive to an objective evaluation.[300] The test is whether the nature of the work desired makes it impossible or impractical to draw specifications satisfactorily to permit competitive evaluation. Mere data collection without a requirement for analysis or opinion was looked upon more as something subject to competitive bidding.[301]

Less assurance of coming within the exception for specialized services exists for an individual hired to supervise actual construction operations. Where services under the contract involve overall management responsibilities, they generally are held to be within the exception. For example, in *Gulf Bitulithic Co. v. Nueces County*, the local government employed a contractor to act as its representative to supervise and manage an extensive road construction program. [302] Holding that the contracting agency was not required to award this contract through competitive bids, the court said:

> If [the statute] be so construed as to bring…this case within its provisions, the very object of the statute would be defeated, for the obvious reason that, when a county does a given piece of construction work, paying for the materials and labor, the ultimate cost thereof is necessarily largely dependent upon the skill, experience, and business judgment exercised in the management and supervision of such work.…It would be ludicrous indeed if a county should publish to the world that it desired to let to the lowest bidder a contract to supervise the building of an elaborate road system…Under such an advertisement, it might be compelled to place the supervision of this immense construction program and disbursement of this vast sum of money under one of its local road overseers….[303]

Each construction management contract must be evaluated on its own merits. Where the amount of managerial discretion and responsibility is sufficient, the contract will be considered one of a technical or professional nature. Where this character cannot be established, the parties must comply with competitive bidding statutes applicable to the contracting agency. Where an arrangement called for a contractor to design a building and perform some of the functions of a construction manager—i.e., coordinating solicitation and acceptance of subcontracts, but not performing any construction or supplying any materials—it was held that competitive bids were not needed.[304] However, where the construction manager had duties such as guarantee of a maximum price based on the subcontractor's bids, it was considered to be more like a general contractor, and competitive bidding was required.[305]

This problem is also illustrated where a public agency contracted with an engineering consultant to advise it on the best way to proceed in arranging for the design, construction, and operation of facilities for management and recycling of solid waste. Award of the

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[295] *Id*.

[296] 40 U.S.C. § 544 (1999). The ABA Model Code, supra note 59, § 5–205, contains similar requirements. Although price is still a factor in these agreements, the main difference between these statutes and competitive bidding statutes is the point in the process at which price is considered.

[297] Photo-Art Commercial Studies, Inc. v. Hunter, 42 Or. App. 207, 600 P.2d 471, 474 (1979).

[298] Transportation Displays, Inc. v. City of New Orleans, 346 So. 2d 359, 363 (La. App., 1977).

[299] Township of Burlington v. Middle Dep't Inspection Agency, 175 N.J. Super. 624, 421 A.2d 616, 622 (1980); *but see* SCA Services of Georgia v. Fulton County, 238 Ga. 154, 231 S.E.2d 774 (1977) (contract to provide garbage disposal service) and Trane Co. v. County of Broome, 76 A.D. 2d 1051, 429 N.Y.S.2d 487 (1980) (contract to provide air conditioning repair service by air conditioning unit manufacturer was held to involve use of specialized skill and expertise and so was exempt from competitive bidding).

[300] Aqua-Tech, Inc. v. Como Lake Protection and Rehabilitation Dist., 71 Wis. 2d 541, 239 N.W.2d 25 (1976).

[301] *Id*.

[302] 11 S.W.2d 305 (Tex. Comm'n App. 1928).

[303] *Id.* 11 S.W.2d at 309–10.

[304] Mongiovi v. Doerner, 24 Or. App. 639, 546 P.2d 1110 (Or. App. 1976); Attlin Constr. v. Muncie Community Sch., 413 N.E.2d 281 (Ind. App. 1980).

[305] City of Inglewood-Los Angeles County Civic Center Auth. v. Argo Constr. Co., 7 Cal. 3d 861, 103 Cal. Rptr. 698, 500 P.2d 601, 604 (1972).

consultant's contract by negotiation rather than competitive bidding was challenged, alleging that the consultant did not come within the "scientific knowledge and professional skill" exception because it did not itself design the plant, but merely acted as a "broker" of the services of others. The court disagreed, and held that as long as the services contracted for involved scientific knowledge and professional skill, it did not matter whether they were provided by an original source or through a broker.[306] The court noted that: "Competitive bidding requires 'full, clear, definite [and] precise' specifications, for there must be a common standard by which to permit the comparison of bids."[307]

The precise specifications necessary to competitive bidding of necessity may preclude innovation by bidders. Where the agency wanted bidders to propose the best system for a waste recycling program, this ability to submit innovative proposals was essential. It was thus found to be exempt from competitive bidding requirements.

Installation of computer networks was held to be an exception where the court characterized the contract in question to involve "inextricable integration of a sophisticated computer system and services of such a technical and scientific nature" as to constitute a professional service within the statute.[308] However, although the purchase of computer systems and hardware may be considered the purchase of technical equipment and services, courts are more likely to hold that they are equipment purchases that are governed by public bidding requirements.[309]

iii. Response to Emergencies.[310]—Bidding statutes may provide exceptions for emergency situations in which the temporary necessity for quick action to protect public safety and welfare overrides the interest in promoting competition. Generally, definitions stress imminent danger to life or destruction of property, or a similar expression of unforeseen, unusual, and unacceptable hardships or costs.[311]

Courts have required a showing that preventive measures could not have avoided or lessened the risk.[312] Accordingly, resort to emergency procedures has been approved when an agency needed to take immediate action to restore interrupted supplies of water, heat, and electricity,[313] or to stop pollution of the public water supply.[314] On the other hand, courts have not fully sanctioned exceptions to competitive bidding where the purpose was to expedite construction of an addition to a courthouse to accommodate a new judge,[315] or repair roads in spring following a normal winter.[316]

Economic advantage and convenience for the public agency are not enough to constitute an emergency, even though the contracting officer believes in good faith that these benefits can be more readily obtained for the public through direct negotiation than through advertisement for competitive bidding.[317] Thus, it was invalid for an agency to declare an emergency and invoke the emergency exception to competitive bidding where it found that if the project were bid the prices would likely be unreasonable.[318]

In the absence of statutory emergency contracting procedures, the exception may be implied from the nature of the contract and other provisions of the public contracting laws.[319] In such cases, the special circumstances of the case also are influential. Unexpected necessity requiring prompt action must be shown.[320] An emergency situation has been described as one that demands immediate attention, and that threatens the public health and safety of a community.[321] In that case, an excavator had been hired to excavate a malfunctioning sewer line. While the line was exposed, falling rock punctured the line. The excavator repaired the line and sought additional compensation. The court held that the district was authorized to allow the additional work

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[306] Waste Management, Inc. v. Wisconsin Solid Waste Recycling Auth., 84 Wis. 2d 462, 267 N.W.2d 659, 665 (1978).

[307] *Id.* 267 N.W.2d at 665.

[308] Autotote Limited v. New Jersey Sports and Exposition Auth., 85 N.J. 363, 427 A.2d 55, 59 (1981).

[309] Pacificorp Capital, Inc. v. State, Through Div. of Admin., Office of State Purchasing, 612 So. 2d 138 (La. App. 1 Cir. 1992).

[310] Please note that § 1(A)(2)(n), Emergency Contract Award Procedures, of this volume, prepared as part of the 2011 update to this volume, provides a more detailed discussion of contracting procedures and contract awards in emergency situations, including developments since 2005.

[311] ABA Model Code, *supra* note 59, at § 3-206.

[312] Grimm v. City of Troy, 60 Misc. 2d 579, 303 N.Y.S.2d 170, 175 (Sup. Ct. 1969) (a resolution of the contracting agency reciting certain facts and declaring that they constitute an emergency is not conclusive, but is sufficient prima facie evidence of an emergency to shift the burden of proof to the party attacking the validity of the award).

[313] Merchants Nat'l Bank & Trust Co. v. City of Grand Forks, 130 N.W.2d 212 (N.D. 1964).

[314] Northern Improvement Co. v. State**,** 213 N.W.2d 885, 887 (N.D. 1973) (statute did not include exception for emergencies, court refused to imply one).

[315] Reynolds Constr. Co. v. County of Twin Falls, 92 Idaho 61, 437 P.2d 14 (1968).

[316] Bak v. Jones County, 87 S.D. 468, 210 N.W.2d 65 (1973).

[317] Reynolds Constr. Co. v. County of Twin Falls, 92 Idaho 61, 437 P.2d 14, 23 (1968).

[318] *Id.* 437 P.2d at 23.

[319] *See* General Building Contractors of N.Y. State v. State of N.Y., 89 Misc. 2d 279, 391 N.Y.S.2d 319, 322 (1977); *but see* Smith v. Graham Co. Comm. College Dist., 123 Ariz. 431, 600 P.2d 44, 47 (1979) (even if an emergency existed, college still needed authority to avoid competitive bidding in an emergency; in fact, leaky roof had existed for some time and college had had time to bid project); Northern Improvement Co. v. State, 213 N.W.2d 885, 887 (N.D. 1973) (statute did not include exception for emergencies; court refused to imply one).

[320] *See, e.g.,* Martin Excavating, Inc. v. Tyrollean Terrace Water & Sanitation Dist., 671 P.2d 1329 (Colo. App. 1983).

[321] *Id.* 671 P.2d at 1330.

to be done by that contractor on an emergency basis without advertising for new bids.[322]

Where emergency circumstances meet the criteria for an exception to the statutory competitive bidding rules, the extent of the exception and the alternative procedure generally are specified in the statute. To the extent the statute sets forth alternative procedures, such procedures must be complied with fully in order to produce valid contracts. Where the statutory requirements are not complied with, the contractor may not be entitled to payment either under the contract or in quasi-contract.[323] In other words, the emergency is not a defense to having failed to comply with the applicable statutes.

Emergency procedures generally allow the contracting agency to determine that the emergency exists; there is not a requirement for a formal declaration of emergency.[324] Such a finding may be challenged by a prospective bidder or by a taxpayer, depending upon the state's requirements for bid protests generally.[325]

Alternative emergency procedures vary substantially in detail. However, because the need for speedy action is critical in an emergency, a common feature of all such procedures is the temporary suspension of the mandatory requirement for advertisement over a specified period. When freed of this requirement, some agencies have found it most advantageous to procure supplies, services, and construction through direct negotiation with contractors whose capabilities are known from past performance. In some instances, statutory provisions for emergencies specify this course. In others, the requirement of competitive bidding is retained in the emergency situation, but the contracting agency is authorized to compress the process into a shorter time period,[326] or negotiate a contract subject to approval of the contract by the governor.[327]

In a few cases, special reporting and accounting requirements are established for expenditures of public funds in emergency situations where regular competitive bidding procedure was not followed. An example is the emergency exemption in the Illinois Procurement Code, which applies in emergencies involving public health, public safety, immediate repairs needed to avoid further loss or damage of state property, disruption to state services, or the integrity of state records.[328] Under this law, an agency must report funds spent in emergencies to the state's Auditor General within 10 days after execution of the contract, with full details of the circumstances. Quarterly reports by the Auditor General to the Governor and Legislative Audit Commission permit both offices to thoroughly review these transactions and evaluate any apparent abuse of the emergency procedures.[329]

Statutory provisions for award of contracts to deal with emergencies involving construction or repair of public works wisely avoid restrictive definitions of situations in which the procedures for competitive bidding may be bypassed in favor of speedier action. But as courts have supplied the definition of emergency situations in questionable cases, they generally have insisted that a strong and direct danger to public health or safety be present. Accordingly, in cases where sewer lines were threatened by falling rocks and where sewer lines beneath a river needed repair to seal a break, the circumstances did not justify avoidance of competitive bidding rules.[330] Similarly, the need to build a temporary floating bridge to replace a structure damaged by a windstorm did not justify limiting bidders by prequalification to the builder of the floating bridge, despite the fact that use of a major regional highway was interrupted until the temporary bridge was in place.[331] Nor did the possible threat to public safety from prison riots justify avoidance of competitive bidding in the award of a contract for construction of prison facilities to relieve overcrowding.[332] While the court in that case acknowledged that the state had effectively documented the potential danger to public safety if the overcrowded conditions were not relieved, it explained that to be within the intent of the exemption, "an emergency must involve an accident or unforeseen occurrence requiring immediate action; it is unanticipated or fortuitous; it is a sudden or unexpected occasion for action and involves a pressing necessity."[333]

Whether an emergency exists for the purpose of entering into emergency contracts without competitive bids is an issue that is fully reviewable by the courts. Otherwise, agencies could claim to have emergencies in an effort to circumvent competitive bidding.[334] In an action challenging the negotiation of a pay phone contract for the state prison system on an emergency basis, the court held that the agency's declaration of emergency is "clothed with a presumption of correctness," and was reviewable only for whether it was arbitrary, capricious, or unreasonable.[335] The court noted that the

[322] *Id*. at 1331.

[323] Bak v. Jones County, 89 S.D. 468, 210 N.W.2d 65 (S.D. 1973) (contractor not entitled to payment for work on rain-damaged roads did not comply with statutory requirement of filing plans and specifications).

[324] *See, e.g.*, WASH. REV. CODE § 47.28.170 (2000).

[325] *See Grimm*, *supra* note 312.

[326] *See, e.g.,* WASH. REV. CODE § 47.28.170 (2002).

[327] FLA. STAT. tit. 26, § 337.11(6)(a) (2000).

[328] 30 ILL. COMP. STAT. 500/20-30(c) (1999).

[329] 30 ILL. COMP. STAT. 500/20-30(c) (1999).

[330] Northern Improvement Co. v. State, 213 N.W.2d 885 (N. D. 1973); Martin Excavating, Inc. v. Tyrollean Terrace Water & Sanitation Dist., 671 P.2d 1329 (Colo. App. 1983).

[331] Manson Constr. & Eng'r Co. v. State, 24 Wash. App. 185, 600 P.2d 643 (1979).

[332] General Bldg. Contractors of N.Y. State v. State, 89 Misc. 2d 219, 391 N.Y.S.2d 319 (1977) (prison overcrowding was not an adequate basis for declaration of emergency, as it had been known since riot occurred at Attica in 1971).

[333] *Id.* 391 N.Y.S.2d at 321.

[334] Union Springs Tel. Co. v. Rowell, 623 So. 2d 732 (Ala. 1993).

[335] *Id.* 623 So. 2d at 734.

"emergency" declared in that case was one of limited duration and was intended only to cover the gap in time between the expiration of one contract and the finalization of a new one, and not to circumvent bidding.[336]

iv. Contracts of a Special Nature.—Most states recognize contracts for public utility services and contracts for land acquisition or lease by an agency as being among the situations in which it is impractical to insist on strict compliance with competitive bidding procedures. Exemption of contracts for supply of electricity, heat, water, and other public utilities from competitive bidding rules generally is explained in terms of the monopolistic nature of the utility and the public regulation of its prices. Another situation in which practical considerations have justified an exception to mandatory competitive bidding involves the purchase of real property for public use. Because the specific site and condition of land are among the chief factors that make it desirable or necessary for public use, the purpose of encouraging competition among suppliers is not served by the kind of bidding provided for in the statutes. Reference to the "uniqueness of land" generally suffices to justify an exception for purchases, rentals, and other acquisitions of land or rights in land.[337]

Another exception occurs where complex construction tasks are part of a larger integrated project in which engineering plans, design, and construction phases must be coordinated within the framework of financing plans. Thus, the contract for construction of an underground parking garage for a retail shopping mall redevelopment project was held to be sufficiently special in its nature due to its financing to warrant award of the contract through negotiation rather than competitive bid.[338]

Depending on statutory language, capital improvements such as replacement of heating and air conditioning systems in buildings may not be within the scope of competitive bidding. In a Nebraska case, the statute required bids on "contracts for supplies, materials, equipment and contractual services."[339] The court found no specific requirement in that language that a contract for capital improvements be competitively bid.[340] However, most definitions of "public works" are likely to be broad enough to encompass capital improvements to public facilities.

When construction contracts required competitive bidding, the court held that the purchase and installation of prefabricated, portable buildings were not subject to that requirement.[341] Work performed to assemble and attach the prefabricated pieces was incidental to delivery of the materials, all of which were easily relocatable at the option of the owner. Similarly, a court held that a contract for cartographic services to prepare tax maps for use in public works planning and land acquisition did not have to be awarded through competitive bids, because the work did not involve actual physical construction activity on publicly owned land or structures.[342] With this rationale, the same statute was construed to exclude contracts for repairing and resurfacing roofs of existing buildings.[343]

Where statutes provide that public agencies shall give preference to certain charitable or quasi-public entities in awarding contracts for public work, the limits of such exceptions generally must be defined by the courts. Thus, a decision to call for competitive bids to make identification photographs for drivers licenses was successfully challenged as contrary to a statute requiring state offices to obtain needed services from charitable nonprofit agencies for handicapped persons whenever they were competent to provide the service at fair market value.[344] In another case involving the same nonprofit agency, the court held that it was proper to award a contract to the agency for the operation of rest areas prior to the statutorily required determination of fair market price.[345] The court reasoned that delay in award of the contract would have required closure of the rest areas, and the contract contained a termination for convenience clause that could be invoked if the determination of fair market price were reversed.

Where a preference or an exception to the competitive bidding statute is not specific, but is based on an implicit exception favoring organizations with programs that perform valuable services in the public interest, its limits are interpreted restrictively. In the case of a contract awarded for painting subway stations, the court

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[336] *Id.*

[337] Massey v. City of Franklin, 384 S.W.2d 505, 506 (Ky. App. 1964) (building purchase not subject to bidding requirements). However, statutes that allow an agency to lease land that it owns may require that the land be leased to the highest bidder. *See*, *e.g.*, Sellitto v. Borough of Spring Lake Heights, 284 N.J. Super. 277, 664 A.2d 1284 (1995) *cert. denied*, 143 N.J. 324, 670 A.2d 1065 (1995) (statute allowing county or municipality to lease land or buildings to person who will pay highest rent does not require competitive bidding; however, another controlling statute did require competitive bidding; remanded with order to lower court to enjoin lease with cell phone company).

[338] Graydon v. Pasadena Redevelopment Agency, 104 Cal. App. 3d 631, 164 Cal. Rptr. 56, 64 (1980).

[339] Anderson v. Peterson, 221 Neb. 149, 375 N.W.2d 901, 906 (1985).

[340] *Id.* 375 N.W.2d at 906 ("Nebraska statutes covering county expenditures and competitive bidding comprise a crazy quilt of legislation."); N.R.S. § 23-324.03.

[341] Steelgard, Inc. v. Jannsen, 171 Cal. App. 3d 79, 217 Cal. Rptr. 152, 161 (1985).

[342] Andover Consultants v. City of Lawrence, 10 Mass. App. Ct. 156, 406 N.E.2d 711, 714 (1980).

[343] Commonwealth v. Brown, 391 Mass. 157, 460 N.E.2d 606, 609 (1984) (definition of "construction" did not include reconstruction, alteration, repair, or remodeling).

[344] Pa. Indus. for Blind and Handicapped v. Larson, 496 Pa. 1, 436 A.2d 122, 124 (1981).

[345] Pa. Indus. for Blind and Handicapped v. Department of General Services, 541 A.2d 1164, 1166, 116 Pa. Commw. 264 (1988).

rejected arguments that a law authorizing rehabilitation and development of job skills of persons with poor employment records due to alcoholism, drug addiction, imprisonment, or other socioeconomic disability had the effect of excluding contracts for this program from the competitive bidding rule. While this argument should not be taken lightly, the court said, "the countervailing policies embodied in…the Public Authorities Law run too deeply to permit the contract at bar to wade through them by implication."[346]

v. Extensions of Existing Contracts.—The necessity for competitive bidding may also be raised where an awarding authority executes an extension or renewal of a previous contract for those services rather than advertising for bids. In holding that such an extension was invalid because it was awarded by negotiation rather than bidding, the court distinguished between a right to renew an existing contract and an authorization for the parties to enter into negotiations at the contract's expiration if the parties desire to do so.[347] The right to renew an existing contract under identical terms is not the same as a provision that allows negotiations. The latter is inoperable where the contract is subject to competitive bidding.[348] The court noted two Washington cases that made this distinction. *Miller v. State* involved a contract for purchase of light bulbs.[349] At the expiration of the contract, the agency negotiated for the renewal of the contract with the vendor. The court held this new contract was void because the agency had not complied with competitive bidding requirements.[350] However, in *Savage v. State*, the contract contained a provision allowing for extension of the contract, at the State's option, for 1-year periods up to 3 years, on the same terms.[351] The court found this provision to be valid, as it was clearly an option-to-renew clause as opposed to a negotiation provision. The provision extended the existing contract, and did not create a new one.[352]

An agency may also run the risk of being accused of circumventing competitive bidding when it amends an existing contract, rather than advertising for a new contract at the end of the contract term. Generally, a competitively bid contract cannot be materially amended.[353] One method of analyzing whether amendment is justified, rather than advertising for a new contract, is to question whether there is justification for a sole source for that particular contract. If there is, then it makes sense for the agency to simply extend the existing contract and document its reasons for doing so. However, if the contract would not meet the criteria for a sole source, the agency should advertise for bids.

vi. Methods of Noncompetitive Award of Contracts—Where an exception to the requirement for competitive bidding already exists, a contracting agency has a choice of several methods of awarding a contract. These include 1) procedures for soliciting bids from a limited number of selected potential bidders who are prequalified, sometimes wherein negotiations with one or more bidders may result in modifications of specifications, work methods, performance criteria, or price; and 2) negotiations with a sole source. The contracting agency is allowed substantial discretion in selecting the method that best serves the public interest. However, its judgment must always be consistent with the policies requiring that negotiated awards must be made with the maximum competition that is practicable, and that the use of a noncompetitive award should be limited to the minimum needs of the contracting agency. Also, a sufficient justification for the exception must always exist before a noncompetitive award is permitted, and should be documented.

vii. Sole Source Contracts.—When a contracting agency undertakes negotiations with a sole source, the agency must be able to show that the sole source possesses a unique capability to furnish the property, services, or performance required to meet the agency's minimum needs.[354] The determination that a particular source is in fact the sole source available for specified products or services may not be based on the unsupported opinion of the agency's contracting officer. It must be based on showing that the appropriate effort was made to investigate potential sources without success in finding any others. Generally, three requirements must be met: 1) the goods or service offered must be unique; 2) the uniqueness must be substantially related to the intended purpose, use, and performance of the goods or services sought; and 3) the entity seeking to be declared a sole source must show that other similar goods or services cannot perform desired objectives of the agency seeking those goods or services.[355] Uniqueness alone does not suffice, as any products may be shown to be "unique."[356]

A distinction must be made between a sole source contract and one in which the specifications are so narrowly drawn that only one bidder will be able to meet them. While the former, if supported by the above criteria, is a legitimate method of avoiding competitive bidding, the latter is not.[357] This is discussed more fully in Section 1.B. regarding "or equal" clauses.

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[346] District Council No. 9, Int'l Bhd. of Painters & Allied Trades v. Metropolitan Transp. Auth., 115 Misc. 2d 810, 454 N.Y.S.2d 663, 669 (1982).

[347] Browning-Ferris Indus. of Tenn. v. City of Oak Ridge, 644 S.W.2d 400, 402 (Tenn. App., 1982); *see also* Edwards v. City of Boston, 408 Mass. 643, 562 N.E.2d 834 (1990).

[348] *Browning-Ferris*, 644 S.W.2d at 402.

[349] 73 Wash. 2d 790, 440 P.2d 840 (1968).

[350] *Id*. at 843.

[351] 75 Wash. 2d 618, 453 P.2d 613 (1969).

[352] *Id*. at 616.

[353] Baxley v. State, 958 P.2d 422 (Alaska 1998).

[354] *See* ABA Model Code, *supra* note 59, at § 3-205.

[355] General Electric Co. v. City of Mobile, 585 So. 2d 1311, 1315–16 (Ala. 1991).

[356] *Id*. at 1315.

[357] Unisys Corp. v. Department of Labor, 220 Conn. 689, 600 A.2d 1019, 1023 (1991) (question is whether specifications are

n. Emergency Contract Award Procedures

Most state DOTs have been forced, at one time or another, to perform repairs to Interstate and state highways and bridges on a sudden, unanticipated, emergency basis, as a result of natural disasters such as earthquakes, landslides, rockfalls, floods, ice storms, tornadoes, and hurricanes. They have also been compelled to provide in-kind emergency assistance to municipalities for repair of off-system municipal transportation facilities as the result of such natural disasters. At least one state DOT, NYSDOT, has further been confronted with emergency repair activities as the result of a terrorist attack.

Emergency situations require prompt responses. These can be difficult to carry out in a timely way under FHWA's standard federal-aid program requirements and traditional state highway letting statutes, which require preparation and publication of detailed plans, advertising for competitive bids, detailed review of bids, and the like. State DOTs faced with emergency situations must thus determine how to accomplish the rapid performance of emergency repair work despite the existence of such statutory requirements. Where the President issues a federal disaster emergency declaration and Federal Emergency Management Agency (FEMA) financial aid becomes available, state DOTs must also make sure that the procurement procedures they follow do not render them ineligible to receive reimbursement from FEMA for the emergency work they perform. Further, both federal agencies and state-level external control and audit agencies are also aware of and sensitive to the risk of abuse of emergency procedures to bypass normal procurement requirements in situations that do not truly qualify as emergencies.

Federal statutes, FHWA, FEMA, the Federal Office of Management and Budget (OMB), and the National Cooperative Highway Research Program (NCHRP) have issued guidance for state DOTs on contracting in emergency situations.[358] Certain other state statutes must be taken into account as well, particularly with regard to external control agencies and the performance of off-system work on municipal transportation facilities.[359]

1. Federal Requirements

Where emergency repairs are to be performed on Interstate or state highways or bridges, which may be eligible for FHWA-administered federal aid, state DOTs must be cognizant of applicable FHWA and FEMA requirements. There are at least three sets of applicable FHWA and FEMA requirements:

The emergency situation must be one falling within the requirements of FHWA regulations.[360] FEMA also requires that the President must have declared a federal disaster emergency pursuant to the Federal Stafford Act.[361]

FHWA requires, that emergency repairs must be undertaken during or immediately following the occurrence of the disaster in order to minimize the extent of the damage, protect remaining facilities, or restore essential traffic.[362]

FHWA requires that emergency repair work may be accomplished by contract, or by negotiated contractor or public agency force account methods, and that all projects for permanent repairs or reconstruction must be procured in accordance with FHWA regulations.[363] FEMA also has a variety of related requirements, too numerous and detailed to summarize here, but deserving of careful attention in an actual emergency response in order to avoid loss of eligibility for federal reimbursement.[364]

2. State Statutes and Regulations

In a survey conducted during 2007, NCHRP found that at least 31 states had adopted statutes or regulations providing for contracting in emergency situations.[365] At least some major states have not enacted such authorization, however. It is thus advisable for state DOT in-house counsel to research, preferably under non-emergency conditions prior to the occurrence of any emergency, whether their state has enacted emergency contracting legislation or regulations, and what other state statutes may come into play in the event of a disaster emergency.

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drawn to the advantage of one manufacturer, not for reasons in public interest but to assure award to that manufacturer).

[358] *See, e.g.*, 23 U.S.C. §§ 112(b)(1) and 23 U.S.C. 125; FHWA regulations, 23 C.F.R. §§ 635.104, 635.120, 635.204, 635.309, 668.103, and 668.105(i); Dwight A. Horne, Director of FHWA Office of Program Administration, Memorandum, Information: Procurement of Federal-Aid Construction Projects, June 26, 2008; available at http://www.fhwa.dot.gov/construction/080625.cfm, last accessed on Sept. 7, 2013; FEMA regulations, 44 C.F.R. Part 13; OMB Circular A-102; and JULIA L. PERRY, ESQ. & MARGARET L. HINES, ESQ., EMERGENCY CONTRACTING: FLEXIBILITIES IN CONTRACTING PROCEDURES DURING AN EMERGENCY (NCHRP Legal Research Digest 49, 2007).

[359] *See, e.g.*, New York State Finance Law § 112; and New York State Executive Law §§ 28, 29, and 29-a.

[360] 23 C.F.R. § 635.204; *see also* Horne, *supra* note 358.

[361] PERRY & HINES, *supra* note 358, at 12.

[362] 23 C.F.R. § 668.103; *see also* Horne, *supra* note 358.

[363] 23 C.F.R. § 668.105(i), citing 23 C.F.R. pts. 635 and/or 636 in connection with permanent repairs or reconstruction; *see also* Horne, *supra* note 358.

[364] For a brief introductory summary, *see* PERRY & HINES, *supra* note 358, at 12–13. In the experience of the authors of the update to this current volume, FEMA requirements are in practice sufficiently complex that it may be advisable for state DOTs to keep on staff at least one employee having accumulated expertise regarding FEMA requirements and procedures in order to maximize recovery of federal reimbursement for emergency repairs and minimize avoidable losses of eligibility for reimbursement.

[365] *Id.* at 4 n.3.

In general, state statutes authorizing emergency contracting typically require the written recording of a determination that an emergency exists; limit emergency contracting to supplies, services, and construction activities necessary to meet the emergency in question; and authorize limitations upon the competitive bidding process in order to enable rapid response to emergency conditions. The need to spend "use it or lose it" funds in order to avoid the lapse of funds at the end of a fiscal year is generally not considered to justify the invocation of statutory authorization for emergency contracting.[366]

a. Who may issue an emergency contract?

The statutes of each individual state must be checked to determine which public officials are authorized to issue emergency contracts. At least 12 states authorize the Commissioner or other chief executive officer of the state DOT to issue emergency contracts; and at least five states authorize the state director of purchasing or procurement to do so.[367]

b. When may emergency contracting procedures be used?

While the statutes of each individual state must be checked, NCHRP's 2007 survey determined that such statutes typically authorize emergency contracting and the waiver of normal contracting requirements when emergency conditions threaten public health, safety or welfare, government property or operations, or the provision of necessary or mandated government services, and when there is no time to comply with the procedures usually required for contracting. Several states also require that emergency contracting be reserved for situations in which following standard procedures will not meet public need, and that once the emergency has been met, permanent repairs or reconstruction must be undertaken following standard, nonemergency state procurement procedures.[368]

c. The "where and when" alternative to express emergency authority

Several states, including some that do not have state statutes expressly authorizing emergency contracting, have developed an alternative approach using standard state highway contract letting statutes. Under this approach, the state DOT uses standard letting procedures to award annual contracts to perform emergency repairs on a standby, "where and when," or "if and where directed" basis. Since the exact cost of specific repairs to specific facilities cannot be determined in advance, such contracts typically require bidders to bid on unit or lump-sum prices of certain specified types of repairs, with the bidder having the lowest aggregate total of such prices winning the contract. In order to cap the state's potential financial exposure to stay within the limits of existing funding appropriations, the amounts of such contracts are limited to a specified maximum "not to exceed" amount. In the event of a major disaster emergency, such amounts may be increased through orders on contract (change orders) approved by external control agencies (where required), if the state provides additional emergency funding appropriations.[369]

d. Contracting with municipalities for off-system emergency repairs

Providing state assistance to municipalities in the form of a state DOT performing "off system" emergency repairs to municipal highways or bridges, instead of or in addition to Interstate or state highways, can pose a variety of legal and financial problems for state DOTs. State statutes granting statutory authority to state DOTs for construction and reconstruction of highways and bridges typically limit such authority to Interstate and state highways, and leave the construction of municipal roads up to the municipalities. In at least some states, such limitations may be waived, and the state DOT may legitimately undertake "off system" emergency repairs to municipal facilities, when the Governor formally declares the existence of a state disaster emergency and orders state agencies to assist municipalities.[370]

Things are not always so straightforward, however. As a practical matter, the declaration of a state disaster emergency may transfer the cost of responding to an emergency from municipal officials, governments, and taxpayers to state officials, governments, and taxpayers. During periods of tight state budgets and stringent fiscal constraints, state Governors may be reluctant to issue a formal state declaration of a disaster emergency, knowing that this will have an adverse effect on the state budget and use up scarce funds needed for other purposes. Either Governors or state legislators may then seek to prevail upon state DOTs to provide such emergency assistance anyway, even in the absence of a formal disaster declaration—which is beyond the statutory authority of many state DOTs, and could also leave state DOT personnel without the benefit of state legal defense or indemnification in the event of an accident occurring during such operations.

In some states, there are statutory provisions authorizing state DOTs to provide emergency assistance to municipalities, at least under some specified situations, if the municipalities commit to reimburse the

[366] *Id.* at 5–6.

[367] *Id.* at 7.

[368] *Id.* at 7–8.

[369] New Jersey DOT uses this approach; see PERRY & HINES, *supra* note 358, at 8. To the knowledge of the authors of the update of this current volume, NYSDOT has also been using this approach for a number of years.

[370] *See, e.g.*, New York State Executive Law §§ 28, 29, and 29-a. For an example of a Governor's declaration of a state disaster emergency under those statutes, *see, e.g.*, Governor Cuomo's Executive Orders No. 17 of August 25, 2011, and No. 19 of September 1, 2011.

state DOT for the cost of doing so.[371] Where the state DOT is under political pressure to provide emergency assistance to a municipality, but the Governor refuses to declare a formal state disaster emergency, the solution in such states may be for the state DOT to enter into a contract with the municipality to provide emergency response services, with a municipal commitment of future reimbursement. Such a contract need not be lengthy, and may be in the form of a letter agreement, with a municipal official countersigning and faxing back a letter agreement prepared by the state DOT, so long as such arrangements are cleared with external control agencies if appropriate. For municipalities facing stringent fiscal constraints, at least part of the reimbursement commitment may be in the form of in-kind services rather than cash payment. Such arrangements, while involving at least some degree of risk, appear preferable to leaving members of the public at risk due to lack of response to genuine emergency conditions, and also preferable to undertaking "off system" work without the benefit of any written arrangement to cover it.

3. Range of Contracting Options

State DOTs always have the option of performing repair work under standard state highway letting statutes, with advance publication of plans, published advertising for competitive bids, and the like. This may well be done for long-term, permanent repairs or reconstruction in the wake of a major disaster. The problem, of course, is that standard letting procedures are too time-consuming for state DOTs to be able to use them in providing timely, short-term relief during and immediately after the occurrence of a disaster emergency.

Where federal-aid funds are involved, state DOTs may be constrained not only by FHWA regulations, but also by federal statutes, the Federal Acquisition Regulations (FARs), and Federal OMB administrative guidance concerning contracting practices. Under the Federal Brooks Act, for example, contracting officers are required to obtain as much open competition as the circumstances will allow, although simplified acquisition procedures may be acceptable for engineering services, contracts below a certain dollar value, and task orders placed under Indefinite Delivery/Indefinite Quantity contracts.[372] The FARs also recognize that there may be circumstances where contracting officers need some discretion, noting that "contracting officers should be allowed wide latitude to exercise business judgment."[373]

Depending upon the specific circumstances, contracting options may range from using accelerated award procedures to let publicly advertised contracts incorporating detailed requirements for contractors to document actual costs; to using faxed or telephoned requests for proposals to a limited number of selected firms, with a contract which is not fully detailed but provides at least some level of written contract requirements, and compensation rates drawn from other existing contracts or standard pricing in the industry; to limited competition or sole source contracts based on telephone or fax proposals.[374]

It should be noted that the MAP-21 legislation enacted in 2012 directs the U.S Secretary of Transportation to designate as a categorical exclusion under NEPA "the repair or reconstruction of a road, highway or bridge damaged by a declared emergency or disaster…if the repair or reconstruction is in the same location and with the same specifications as the original project and is commenced within two years of the declaration of emergency or disaster."[375]

4. Record-Keeping Requirements

While it must be recognized that emergency repairs by state DOT forces or contractors during disaster emergencies are often carried out under highly challenging field conditions, state DOT officials would be well advised to keep written records that are as detailed as possible under the circumstances. The more that state DOT officials depart from standard procedures in arranging such work, the more documentation they may later be asked to produce in order to justify their actions. Especially in circumstances where emergency response measures are arranged by telephone and fax under time pressure while a disaster emergency is still occurring, it is important for contracting officers to keep written or computer notes of which contractors they are dealing with, what specific conditions and locations they are asking each contractor to address, what work they are authorizing, and what agreements are reached regarding payment terms. The lack of such records can prove highly disruptive in the aftermath of a disaster emergency, and can cause state DOTs significant problems in the face of later inquiries.[376]

5. What Can Go Wrong?

Since emergency contracting is generally undertaken during the occurrence or the immediate aftermath of a disaster emergency, which are circumstances creating a large number of unanticipated and somewhat unpredictable stresses and pressures, Murphy's Law defi-

[371] *See, e.g.*, New York State Highway Law § 55, authorizing NYSDOT to provide emergency snow and ice control operations for municipalities that agree to pay reimbursement for the costs of doing so.

[372] 40 U.S.C. §§ 541 et seq., cited in PERRY & HINES, *supra* note 358, at 6 n.16.

[373] FAR § 1.602-2, cited and quoted in PERRY & HINES, *supra* note 358, at 4 n.1.

[374] PERRY & HINES, *supra* note 358, at 8-9.

[375] See Joint Explanatory Statement of the Committee of the Conference, June 29, 2012, at 2, http://docs.house.gov/billsthisweek/20120625/HR4348crJES.pdf, last accessed on Sept. 7, 2013.

[376] *Id.* at 9.

nitely applies: if it can go wrong, it will. State DOT personnel directly engaged in field performance of emergency work during a major disaster emergency may be at considerable personal risk of death or injury. More prosaically, problems typically encountered during emergency contracting, as noted by an NCHRP study, include: the absence of any written record of which work what contractors were orally ordered to perform; accidentally award of the same work to more than one contractor; failure to provide timely notice that the contractor will be required to document costs; issuance of vague or inaccurate work orders that fail to accomplish necessary work but result in performance of unnecessary work at incorrect locations; issuance of work orders by persons lacking authority to do so; awarding a sole-source contract when at least some limited competition would have been possible; and submission by contractors of inflated charges without adequate supporting documentation.[377] As is often said, hindsight is always 20-20. In the event of expensive contracting problems occurring in connection with a major disaster emergency, hindsight may be exercised by FHWA, FEMA, federal or state auditors, federal or state legislative committees, or the news media, who may be predisposed to focus more on what went wrong than on what went right.

6. New York City Experience with 9/11 Emergency Contracts

While most emergency situations affecting transportation facilities arise from natural disasters, at least one such situation has arisen from a terrorist attack. The September 11, 2001 (9/11), attack by Al Qaeda upon the World Trade Center in New York City killed more than 2,600 people—including three members of the staff of the New York Metropolitan Transportation Council (NYMTC), the MPO for the New York Metropolitan Area, whose offices were on the 83rd floor of the Trade Center's North Tower. The attack not only destroyed the buildings of the World Trade Center complex and buried a large area in debris, but also caused extensive damage to adjacent and nearby streets and a significant arterial highway, Route 9A.

The New York Fire Department lost 343 firefighters and 15 emergency medical technicians, the Port Authority of New York and New Jersey Police Department lost 37 police officers, and the New York Police Department lost 23 police officers who responded to that attack. Responding fully to that emergency made demands on far more than just emergency response agencies. In addition to those agencies, other New York City agencies, NYSDOT, and the New York National Guard sent personnel to the World Trade Center site following the attack to search for survivors amid the debris and clear wreckage. Some of those personnel would later develop chronic respiratory difficulties as a result.

New York's Governor issued an Executive Order declaring the event to be a state disaster emergency, and directing state agencies to take all necessary steps to respond to it. The damage was so extensive, the conditions at the site were so unpredictable, and the need for rapid response was so great, that extensive contracting was required to augment the efforts of government agencies. Both the exceptional circumstances and time pressures made it virtually impossible to use traditional design-bid-build contracting methods for such purposes.

Instead, the Port Authority of New York and New Jersey, the owner of the World Trade Center site, used a Request for Proposals (RFP) process to select demolition contractors to remove the debris, clean up the site, and perform temporary emergency repairs to forestall risks such as possible water damage to New York City's subway system. In order to protect against the risk of criminal fraud affecting the cleanup efforts, the Port Authority included in its cleanup contracts requirements for the contractors to employ Independent Private Sector Inspector Generals, or IPSIGs, to monitor the work on an ongoing basis in order to deter, detect, and prevent waste, fraud, and abuse from inflating the cost of the work.

NYSDOT also used orders on contract (change orders) and supplemental agreements to existing highway projects in order to repair the damage to Route 9A, the arterial highway adjacent to the World Trade Center site.

7. New York State Experience with Hurricane Irene, 2011

Following the occurrence of extensive damage to state and municipal highways and bridges caused by disastrous flooding due to Hurricane Irene in August 2011, New York State's Governor issued two Executive Orders, No. 17 of August 25, 2011, and No. 19 of September 1, 2011, invoking the emergency provisions of New York State Executive Law §§ 28, 29, and 29-a. In Executive Order No. 19, the Governor temporarily suspended the applicability of Highway Law § 38(1), (2) and (3) (the State's competitive bidding requirement for highway contracts) and Article 4-C of the Economic Development Law, "in the event that the Commissioner of Transportation determines it necessary to authorize the award of emergency contracts and/or to combine design and construction services in contracts and to use such services when needed." The Governor also temporarily suspended Section 112 of the State Finance Law (requiring approval of all state contract awards or amendments by the State Comptroller) "to the extent consistent with Article V, Section 1 of the State Constitution, and to the extent that the Commissioner of Transportation determines it necessary to add additional work, sites and time to State contracts or award emergency contracts." The Governor further suspended Section 136-a of the State Finance Law (requiring selection of architectural and engineering firms through competitive RFP on a best-qualified rather than lowest-

[377] *Id.* at 9.

cost basis) "to the extent that the Commissioner of Transportation determines it necessary to combine design and construction services in one contract and/or to obtain design and construction inspection services." Beyond that, the Governor suspended Section 163 of the State Finance Law (requiring procurement of commodities and materials through competitive bidding conducted by the State Office of General Services) "to the extent of allowing the Commissioner of Transportation to purchase necessary commodities and materials without following the standard procurement process." Finally, the Governor suspended Article 8 of the State's Environmental Conservation Law, 6 New York Codes, Rules and Regulations (NYCRR) Part 617 (environmental regulations) and 17 NYCRR Part 15 "to the extent that the Commissioner of Transportation determines the work is immediately necessary for the replacement, rehabilitation, or reconstruction of structures and facilities in response to the emergency and is performed to cause the least change or disturbance in the environment as is reasonably practicable under the circumstances."

These Executive Orders considerably enhanced NYSDOT's ability to respond rapidly and flexibly in order to repair the state and municipal highways and bridges damaged or destroyed by the flooding caused by the hurricane.

o. Maintenance Contracting: Work Order, Job-Order, On-Call, Where and When, and Evergreen Contracting

Traditionally, state DOT contracting programs have focused on the capital construction or reconstruction of highways and bridges. Operations, maintenance, and repairs of limited scope have generally not been eligible for federal-aid reimbursement, and have traditionally been performed by state DOT employees. With many states facing fiscal pressures and demands to reduce state payrolls, however, some state DOTs have considered ways to contract out at least some portion of their maintenance programs.

The Federal MAP-21 legislation enacted in 2012 may make some changes in this area. The Conference Committee report on the legislation indicates that it creates a new NHPP to improve maintenance on both the Interstate system and an extended NHS.[378]

One approach involves job-order contracting (JOC). Although originally developed for the provision of building maintenance services, in recent years this method of contracting has begun to be adapted to highway maintenance contracting as well. A job-order contract has been described as a "long-term, indefinite-delivery, indefinite-quantity contract for construction services delivered on an on-call basis through firm, fixed-price delivery orders that are based on pre-established unit prices."[379] Among the claimed benefits of JOC are that, by using a single consolidated procurement process and contract for delivering multiple items of work through a work-order process over a specified period, rather than bidding out each item of work as a separate contract, this approach delivers the performance of work more rapidly, and also reduces the agency's overhead costs for contract letting, award, and administration.[380]

At least one state, Arizona, has enacted statutory authorization for this method of maintenance contracting.[381] The statute provides for the agency to use an RFP procurement process. For job-order-contracting construction services, the statute requires the RFP to include:

> (a) The department's project schedule and project final design and construction budget or life cycle budget for a procurement that includes maintenance services or operations services.
>
> (b) A statement that the contract will be awarded to the offeror whose proposal receives the highest number of points under a scoring method.
>
> (c) A description of the scoring method, including a list of the factors in the scoring method and the number of points allocated to each factor.
>
> (d) A requirement that each offeror separately submit a technical proposal and a price proposal and that the offeror's entire proposal be responsive to the requirements in the request for proposals.
>
> (e) A statement that in applying the scoring method the selection team will separately evaluate the technical proposal and the price proposal and will evaluate and score the technical proposal before opening the price proposal.
>
> (f) If the department conducts discussions pursuant to paragraph 5 of this subsection, a statement that discussions will be held and a requirement that each offeror submit a preliminary technical proposal before the discussions are held.[382]

In crafting an RFP for job-order-contracting maintenance services, an agency might, as an example, specify multiple standard items of maintenance construction work, such as repair or reconstruction of culverts of

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[378] *See* Joint Explanatory Statement of the Committee of the Conference, June 29, 2012, at 2, http://docs.house.gov/billsthisweek/20120625/HR4348crJES.pdf, last accessed on Sept. 7, 2013.

[379] Lisa Cooley & Mary Gauer, *You Want How Much For That Change Order?*, BUILDINGS, July 1, 2010, available at http://www.buildings.com/ArticleDetails/tabid/3334/Default.aspx?ArticleID=10181, last accessed on Sept. 8, 2013; *see also JOC—Taking the Struggle out of Construction*, an online publication of the Center for Job Order Contracting Excellence, available at http://www.jocexcellence.org, last accessed on Sept. 8, 2013.

[380] *Key Benefits to JOC*, an online publication of the Center for Job Order Contracting Excellence, available at http://www.jocexcellence.org/joc_benefits.htm, last accessed on Sept. 8, 2013.

[381] ARIZ. REV. STAT. § 28-7366, Construction-manager-at-risk construction services and job-order-contracting construction services; available at http://www.azleg.gov/FormatDocument.asp?inDoc=/ars/28/07366.htm&Title=28&DocType=ARS, last accessed on Sept. 8, 2013.

[382] ARIZ. REV. STAT. § 28-7366(F)(3).

specified lengths to state DOT standards, or pavement defect repairs of a specified type for a specified length of highway, within a specified region of a state, and solicit unit-price bids for each of the items of work, with the contract to have a specified duration and specified minimum and maximum prices. Firms could submit technical proposals for what equipment and methods they would use to perform the work, and unit-price bids for each standard item of work set forth in the RFP. The agency would use the scoring method set forth in the RFP to score the technical proposals first, before opening and scoring the price proposals, and then completing the scoring of the entire proposals.

"Where and When" contracting is a somewhat comparable approach, using traditional highway construction lowest responsible bidder letting statutes to award contracts for on-call emergency repairs to highways or bridges within a specified region of a state and a specified time period, subject to a specified maximum amount. These are typically bid on a cost plus profit basis, with the low bidder being the firm that bids the lowest profit margin percentage to be applied to costs in determining compensation for work performed under the contract.

"Evergreen" contracting is an approach to maintenance contracting that provides for maintenance construction services to be performed for a time period of specified length, but also provides for optional renewal of the contract upon the completion of the initial time period for the same length of time, unless and until the contract is cancelled by either party. The U.S. General Services Administration (GSA), for example, has established Evergreen options for federal agencies to award multiyear, renewable contracts with commercial suppliers under the GSA Schedules Program.[383]

Maintenance contracting does have potential drawbacks as well as benefits, however. In return for the perceived benefits, the government agency gives up direct control over maintenance personnel, equipment, and supplies, depending upon a contractor to provide a timely response of acceptable quality. This may be adequate for routine tasks performed on a non-emergency basis, but leaves the agency without direct control over the delivery of services in emergency conditions, even though the agency is accountable to elected officials and the public for prompt delivery of emergency response measures under such circumstances. In addition, while this may lead to adequate results if the contractor proves to be competent, well managed, and effective, it may also leave the agency temporarily without at least some of its maintenance resources if the contractor proves to be incompetent, poorly managed, or ineffective and has to be terminated for cause and replaced through a new round of procurement.

p. Alternate Bids

When engineering problems can be solved by alternative means, the contracting agency may face a dilemma in preparing its plans and specifications. The goal of competitive bidding is to achieve economy in construction costs, and engineering judgment may honestly differ on the best way to achieve this goal. Rather than designate one particular method of construction or one list of materials that must be used, contracting agencies may ask for proposals on alternative approaches, specifying only the end result, and leaving it to the bidders to select materials, methods, and other aspects of their bids. In some cases, this approach has official status in directives to the contracting officer to solicit proposals on all feasible methods as a basis for awarding a contract. In others, the highway agency's governing legislation may not mandate the solicitation of alternative bids, but may accord the contracting officer the authority to proceed in this way where circumstances make it desirable.[384] Bidding on alternatives may take the form of instructions to prepare bids on alternative methods or specifications for accomplishing the contracting agency's objective. In such cases the bids are evaluated for returning the greatest value for the money spent. Success in using this type of bidding requires clear and complete specifications and instructions, and proposals that are carefully prepared and responsive.[385]

An illustration of the issues raised by another type of alternate bidding is provided by *L.G. DeFelice and Son, Inc. v. Argraves*, involving contracts for construction of the Connecticut Turnpike.[386] In the notice to prospective bidders, the highway commissioner requested alternate bids, one for construction of reinforced concrete and one for bituminous concrete pavement. The notice stated that the agency would determine the type of pavement to be used after it received bids, and after it had fully investigated all factors, including costs. Plaintiff was the low bidder on bituminous concrete, and in this bid was lower than the lowest bidder on reinforced concrete paving. Accordingly, when the highway commissioner awarded the contract to the low bidder for the reinforced concrete paving, plaintiff sought to enjoin the award as being contrary to the legal requirement for award to the lowest responsible bidder. The court denied the injunction, stating:

> [T]he great weight of authority supports the proposition that the awarding official may exercise his discretion to determine after the receipt of alternative bids which alternative to select and to select the lowest responsible bidder under that alternative…The court will not interfere with the exercise of discretionary powers vested in a public official in the absence of fraud, corruption, im-

[383] *See* http://www.gsa.gov/portal/content/198473, last accessed on Sept. 8, 2013.

[384] Ericsson GE Mobile Communications v. Motorola Communications & Electronics, 657 So. 2d 857 (Ala. 1995).

[385] V. C. Vitanza Sons v. Murray, 90 Misc. 2d 893, 396 N.Y.S.2d 305 (1977).

[386] 19 Conn. Supp. 491, 118 A.2d 626 (Super. Ct. 1955).

> proper motives or influences, plain disregard of duty, gross abuse of power or violation of the law.[387]

The Connecticut court stressed the significance of statutory language granting the contracting agency discretion in calling for bids and selecting the lowest responsible bidder.

Projects that allow bidding in the alternative may raise questions regarding practices that are prohibited. They adversely affect the quality of competition in the bidding process, even though there is no corruption or conspiracy in the bids, and no actual loss or unnecessary extravagance suffered by the public agency. Where such practices are found, contracts involving them are considered unlawful or may be set aside.[388] For example, a contract that allowed alternative proposals for all major bid terms was found to have allowed bidders to "rewrite the bid advertisement" and thus prevent fair competition by preventing an exact comparison of the bids.[389] The court found that under the circumstances, there was no fair and reasonable method to determine the highest bidder for a lease.

Other instances in which these results were considered to be present were where one submitted a high bid on one alternative and an excessively low bid on the other, with the intention of underbidding others on the total project and so securing contracts for all of the work. Bidders who use this practice to advance an "all or none" strategy may reduce the risk of having only their excessively low bid accepted by claiming it was made by mistake and must be rejected. However, the prospect that a "high-low" bidder may be able to manipulate the award and gain an advantage over other bidders might leave the bid vulnerable to challenge.

Circumstances may alter results, however, and were held to do so in *Sempre Construction Co. v. Township of Mount Laurel*.[390] An agency asked for bids on excavation work, reserving the right to award the contract on "base bids" or "base plus alternates." One construction company, making no secret that it wanted all of the work or none of it, submitted a high base bid and an extremely low bid for the alternates. The contractor's action was upheld by the court when challenged by a competing bidder, because the high-low bids were free from any technical defects by which the bidder might be relieved from its duty to accept an undesired contract.

Where contract specifications call for bidding on alternative materials or methods of work, such specifications sometimes have been challenged as being inadequate for competitive bidding. Where bidding on alternatives is permitted, the contracting officer has the advantage of comparing the bidders on a range of materials and technical aspects, as well as on price. It is to be expected that greater economy for the contracting agency will result. However, bidders may believe that the call for consideration of alternatives introduces too much uncertainty into bid preparation and evaluation.

Federal regulations permit alternate bidding for federally funded highway construction projects on the NHS. The FHWA suggests that alternate bidding should be used when more than one alternate is judged equal over the design life. The bidding documents should clearly indicate the design criteria and the type of alternate option, and that there is a reasonable possibility that the less costly design approach will be acceptable.[391]

Whether asking for alternate bids or modified alternatives, the contracting agency's specifications must be full, accurate, and complete as to each of the alternatives. They must be presented in a manner that allows opportunity for free competitive bidding on each alternative. Where they meet these criteria, these methods of calling for bids are reconcilable with the principles of competition.[392] It is not fatal to alternative bidding that the agency wants to reserve its selection of one alternative over the other after seeing the prices for each. "The very concept of alternative specification bids approved in these cases is calculated to allow the responsible government entity to weigh the costs and benefits of different types of proposals after the costs are known."[393]

Under the best of circumstances, however, efforts at completeness and accuracy are subject to inadvertent discrepancies in the specifications. Where such discrepancies are discovered, a rule of reason applies. If they fail in some material aspect to inform potential bidders of the terms on which bids will be compared or performances required, the specifications are defective, and any contract awarded on them is subject to cancellation.[394]

Bidding on alternative specifications may be accomplished on separate proposal forms or in a single consolidated form. Instructions on the preparation of bids must be followed fully and exactly. Where a single combined bid form is used, it is customary for the instructions to require that all spaces must be filled, and all items of information must be furnished for each alternative. Failure to comply with this requirement exposes the bid to the risk of rejection because of its irregularity.[395]

q. Confidentiality of Contractor Records

Because of state and federal laws requiring full disclosure of records held by or used by public agencies, agencies and contractors must rely on specific exemp-

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[387] *Id.* at 496, 118 A.2d at 628.

[388] Owensboro Grain Co. v. Owensboro Riverport Auth., 818 S.W.2d 605, 608 (Ky. 1991).

[389] *Id*.

[390] 196 N.J. Super. 204, 482 A.2d 36 (1984).

[391] FHWA, *supra* note 156, § IV, Other Issues, at 5–6; http://www.fhwa.dot.gov/programadmin/contracts/coretoc.cfm.

[392] *See* J.J.D. Urethane Co. v. Montgomery County, 694 A.2d 368, 372 (Pa. Commw. 1997) and cases cited therein (alternatives requested regarding elevator or stairway).

[393] *Id*. at 371.

[394] State *ex rel.* Hoeffler v. Griswold, 35 Ohio App. 354, 172 N.E. 438 (1930).

[395] Baxter's Asphalt & Concrete v. Liberty County, 406 So. 2d 461 (Fla. App. 1981).

tions from these statutes in order to assert that some contractor records are confidential. Some states provide exemptions for all documents submitted in the public bidding process.[396] Others address only the financial information submitted in the prequalification process.[397]

In addition, agency records pertaining to the procurement process will ordinarily be publicly available unless protected by a specific exemption. In federal procurement in which the FARs apply, those rules prohibit the government from releasing any source selection information during procurement proceedings, including the ranking of bids, proposals, or competitors. The disclosure of this information to one bidder has been held to give that bidder an advantage over others.[398]

2. Accelerated Project Contracting Methodology

In addition to delivery systems previously discussed, numerous transportation agencies have also implemented accelerated delivery systems for traditional low-bid contracts. These include:

a. A + B Bidding and Lane Rental [399]

Cost plus time bidding is more often called A + B bidding. This involves considering the cost of time in the low bid determination. In this method, each bid consists of two components: the "A" component is the traditional bid of all contract items and the dollar amount for all contract bid items, and the "B" component is the total number of calendar days required to complete the project as estimated by the bidder.[400] The bid for award consideration is based upon the combination of the bid for all contract items and the associated cost of time according to the following formula:

Bid award cost = A + (B x Road User Cost/Day).

The road user cost is determined by the owner and specified in the bid package. This formula is used to determine the lowest bid for award, and not used to determine payment to the contractor. This method is in wide use, and perceived advantages include accelerating the construction schedule. Schedule reduction may also occur through the use of incentive provisions, which are often included in the same contract.

For projects with high road user impacts, the A +B method can prove to be an effective technique. It gives the contractor the flexibility to set its own completion date, and its operational efficiency is rewarded, yielding reductions in project impacts. Additional advantages include keeping projects on schedule, reducing the engineering costs of construction inspection, limiting inconvenience to the traveling public, contributing to contractor creativity, and enhancing safety. This approach is not suitable for all projects, however.[401] Principal disadvantages include increased cost, increased attention required by transportation officials when changes are encountered, and the need to ensure that quality is not compromised. Other disadvantages include difficulty in developing cost of time charges that are realistic when using two different set of rules governing time charges, higher costs than traditional bidding, additional inspection and testing personnel requirements, and generation of increased contractor claims and disputes.[402]

The calculation of road user cost is necessary for any highway project using any of the incentives/disincentives, lane rental fees, or liquidated damages (that include road user fees). It is a measurement of the impact the transportation facility has on the traveling public. Road user costs may include costs associated with travel time, vehicle operation accidents, and air quality. The need for defensible incentive/disincentive provisions mandate that road user costs be based upon reasonable estimates. FHWA has provided numerous studies and references that can provide guidance on developing road user costs.[403]

Lane rental

Similar to cost plus time bidding (A + B bidding), the goal of lane rental is to encourage contractors to minimize road user impacts during construction. Under lane rental, a lane rental fee is specified in the contract. Lane rental provisions impose charges on contractors for closing a lane to traffic during construction. In other words, the lanes are "rented" to the contractor for the time period needed to construct the project. The contractor submits its estimated duration in its bid documents. If the contractor finishes the project during the specified period a rental fee is not charged. However, if the contractor requests additional days to finish the project, a rental fee is deducted from monthly progress estimates. The most substantial benefit is reduced traffic during construction. Disadvantages include increased construction cost, worker safety issues, and extra documentation and coordination.[404]

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[396] D.C. CODE § 2-354.17 (2012) (documents submitted in response to invitation for bids or request for proposals will be treated as confidential).

[397] WASH. REV. CODE § 47.28.075 (2000).

[398] Ralvin Pacific Properties, Inc. v. United States, 871 F. Supp. 468, 472–73 (D.D.C. 1994).

[399] Coverage of issues from ANDERSON & DAMNJANOVIC, SELECTION AND EVALUATION OF ALTERNATIVE CONTRACTING METHODS TO ACCELERATE PROJECT COMPLETION (NCHRP Synthesis 379, 2008), available at http://onlinepubs.trb.org/onlinepubs/nchrp/nchrp_syn_379.pdf, last accessed on Sept. 7, 2013.

[400] *Id.* at 15–16.

[401] FHWA, *supra* note 156, § IV, at 4; *see* http://www.fhwa.dot.gov/programadmin/contracts/coretoc.cfm, last accessed on Sept. 7, 2013.

[402] ANDERSON & DAMNJANOVIC, *supra* note 399, at 15.

[403] FHWA, *supra* note 156, § IV, at 9.

[404] ANDERSON & DAMNJANOVIC, *supra* note 399, at 16.

b. Lump Sum Bidding

Although not widely used, lump sum bidding has been used by Florida DOT. Under lump sum bidding, a contractor is provided bid documents that do not contain bid quantities tables. The contractor develops its bid based on its own quantity analysis of the plans and information provided. The perceived advantages include reduced design effort to prepare bid packages, since unit item quantities are not provided, and reduced time spent by field inspectors to measure quantities. Perceived disadvantages include increased potential for front end loading, contactors adding more contingencies to bid prices, and potential contractor compromises in quality.[405] Any costs associated with changes or unforeseen conditions, as well as additional work, will be negotiated using the state's standard practices.[406] The lump sum bidding selection process, and the no excuse bonus provision, are also being employed in the Special Experimental Project (SEP)-14 for the Central Texas Regional Mobility Authority for the 5.1 mi toll facility.[407]

c. Incentive/Disincentive [408]

Incentive/Disincentive (I/D) provisions are in wide use in today's transportation agencies. I/D provisions for early completion serve to motivate contractors. They permit a certain amount of compensation for each day critical work is completed ahead of schedule and assess a deduction for each day the contractor overruns the I/D time. The agency specifies the time so as to minimize traffic inconvenience and delays. I/D provisions promote faster project completion and reductions in engineering inspection costs resulting from shorter construction schedules and faster completion. Disadvantages include increased cost and potential reduction in quality, and increased problems owing to utility conflicts, change orders, and contract adjustments.

Capping payments

It is normal for contract incentive payments to be capped at a maximum amount while disincentive payments are not normally capped. The transportation agency must evaluate and balance how much it is willing to pay to accelerate the work effort and the cost to do so. Is it cost effective to do so? Incentive capping provides the agency with a predictable budget and reduces the agency's overall risk of overspending for acceleration.[409]

Is disincentive a penalty?

Disincentive assessments are not penalties, but are compensation for road user delay costs. There are many methods available to estimate road user costs (RUC). According to FHWA, only one state case has invalidated an I/D specification since it was not based on RUCs and there was no language in the specification that described the disincentive as a means to recover RUCs resulting for the construction project. It appears likely that most I/D claims have been settled to avoid establishing precedent. In any event, to be successful in defending against any legal challenge asserting that disincentive is a "penalty," it would be critical that the RUC be based on reasonable estimates associated with the delay caused by the highway construction project. The RUC must be based on sound engineering practice, and should have a documented procedure for calculating RUC impacts due to construction.[410]

FHWA criteria for use

There is a clear distinction between I/D provisions and the purpose of liquidated damages. They have different functions. I/D provisions motivate the contractor to complete the work ahead of schedule and recover damages for late completion. Liquidated damages are intended to recover construction oversight costs and/or damage to the traveling public. In some states, liquidated damages are meant to cover only damage and inconvenience to the traveling public, while a separate assessment of "engineering charges" covers owner damages for late completion.

USDOT regulations (23 C..FR. §.635.127) require state transportation agencies to establish liquidated damages as a minimum to recover overruns in contract time. RUCs are more extensive, are used to justify I/D, and are not liquidated damages. Although they are similar, RUCs are significantly greater than liquidated damages and extended engineering costs caused by late completion sustained by the public agency.

Time adjustment issues

The use of I/D provisions create numerous time adjustment issues. Standard contract provisions used to evaluate requests for time extensions also apply to I/D provisions, unless other express provisions control. By way of example, Florida DOT's use of a "no excuse" provision and its effect on contract extensions is somewhat different, and will be discussed later in this section. Weather risks are managed in different ways by state transportation agencies. Some transfer them all to the

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[405] *Id.* at 20–21.

[406] FHWA, *supra* note 156, § IV, at 3, http://www.fhwa.dot.gov/programadmin/contracts/sep14tx2009.cfm, last accessed June 28, 2012.

[407] FHWA Web site SEP 14 Project listing, http://www.fhwa.dot.gov/programadmin/contracts/sep14list.cfm, last accessed Sept. 8, 2013.

[408] *Id*.

[409] FICK, CACKLER, TROST, & VANZLER, TIME-RELATED INCENTIVE AND DISINCENTIVE PROVISIONS IN HIGHWAY CONSTRUCTION CONTRACTS 31 (NCHRP Report 652, Transportation Research Board, 2010), available at http://onlinepubs.trb.org/onlinepubs/nchrp/nchrp_rpt_652.pdf, last accessed Sept. 8, 2013.

[410] *Id.* at 25–26.

contractor, while others share the risk by allowing time extensions for abnormal weather. Excusable delays such as plan errors, third party conflicts, and different and unforeseen site conditions are also treated in a variety of ways that warrant close examination of the contract risk allocation provisions.[411]

Types of I/D [412]

Types of I/D clauses include A + B bidding, lane rental, A + B without I/D provisions (no incentive is offered for early completion nor is a disincentive assessed for late completion other than liquidated damages), and A+ B with I/D provisions (incentive is paid for early completion and disincentive charged for late completions).

I/D provisions are not to be included in all transportation projects. Projects that have unknowns such as utility conflicts, right-of-way issues, sizable excavations with unknown soil conditions, and the mandated use of innovative construction techniques and materials are not good candidates for time-related I/D provisions.[413]

d. No Excuse Clauses—Florida [414]

Florida DOT has examined many methods to accelerate construction of transportation facilities. It has developed a "no excuse bonus" provision that gives contractors an incentive to complete the contract work on time. The contractor is given a "drop dead date" for completion of a certain phase of the project, or for completion of the entire contract. If the contractor completes in advance of this date, it will be given a bonus. There are no excuses for any delays, such as weather delays, for not achieving the completion date. In addition there are no disincentives other than liquidated damages for not meeting the contract completion date. The perceived advantages include project acceleration, faster project completion, reduced inspection costs, a proactive enhanced safety approach by the contractor, and contractors taking on more risk. Perceived disadvantages include increased cost, possible risks involved for owner, project claims, and quality.[415]

Time adjustments in no-excuse contracts are treated differently than traditional time extensions. Florida has utilized an "excusable no-excuse" clause, which provides that if excusable delays have a total impact greater than 15 percent of the time remaining, then they are considered for a time extension. This appears to be a compromise position, which permits the contractor to earn a no-excuse bonus if the contractor was delayed for reasons beyond the contractor's control. This approach does not recognize small delays that could have impact.[416]

e. Bidding Overhead [417]

Caltrans and the contracting community developed a unique way to provide more accurately for timely overhead compensation. Special provisions for time-related overhead are incorporated into the contract as a bid item on selected contracts over $5 million. Time-related overhead includes field and home office overhead for the time required to complete the work. In addition, the specification provides for increases in the time-related overhead bid item for suspension of work, and for the department granting an increase of contract time for a compensable delay. If the time-related bid item exceeds 149 percent of the bid quantity, the contractor is required to submit an audit examination and report by a certified public accountant. The California Department of Transportation (Caltrans) found that use of this provision limits the magnitude of time extensions and reduces the number of overhead compensation claims and use of other experts.[418]

Available state studies

Further information regarding the use and evaluation of alternate contracting methods can be found in Minnesota DOT's Innovative Contracting Guidelines (2005), Pennsylvania DOT's Innovative Bidding Tool Kit (2002), Ohio DOT's Innovative Contracting Manual (2006), Caltrans' Innovative Procurement Practices (2007), and Florida DOT's Alternative Contract Methods (2000).[419]

3. Alternative Contracting Methods

a. Introduction—Historical Background

New attention and focus have been placed on alternate methods to shorten project delivery time. State transportation agencies have implemented new methods with the goal of not only reducing time, but also of reducing overall costs and assuring that construction facilities meet quality and safety standards.

In determining which project delivery system approach is appropriate for a given project, it is advisable to analyze the varying systems that might be available. Some state transportation agencies have formed an innovative contracting advisory committee to provide a structured approach to assist the agency in making project delivery decisions. An excellent example is the approach taken by Colorado DOT for the I-70 Twin Tunnel Project. The process assisted the DOT in determining the dominant and obvious choice of project delivery methods. The process involved analyzing project goals, delivery schedule, level of design, initial project

[411] *Id*. at 31.

[412] *Id*. at 31.

[413] *Id*. at 33.

[414] *Id*.

[415] ANDERSON & DAMNJANOVIC, *supra* note 399, at 16–17.

[416] FICK, CACKLER, TROST & VANZLER, *supra* note 409, at 31.

[417] FICK, CACKLER, TROST & VANZLER, *supra* note 409, at 18; coverage of issues from ANDERSON & DAMNJANOVIC, *supra* note 399.

[418] ANDERSON & DAMNJANOVIC, *supra* note 399, at 19; Caltrans Standard Specification 9.1.11, Time Related Overhead.

[419] ANDERSON & DAMNJANOVIC, *supra* note 399, at 32–43.

risk assessment, cost, staff experience and availability (owner), level of oversight and control, competition, and contractor experience. The committee evaluated design-build, design-bid-build, and Construction Manager/General Contractor (CM/GC) and concluded that CM/GC was most appropriate under the factors considered.[420]

1. SEP-14

Beginning in 1988, FHWA developed SEP-14 to allow the states to evaluate promising contracting techniques that would not comply with normal and traditional statutory requirements. The objective of SEP-14 was to evaluate project specific innovative contracting practices undertaken by state transportation agencies that had the potential to reduce life-cycle costs while maintaining quality. The intent of SEP-14 was to provide the administrative flexibility to evaluate promising nontraditional contracting practices on selected FA projects.[421]

2. Cost plus time, lane rental, design-build, warranty clauses

Since FHWA's implementation of SEP-14 in 1990, many processes that were once considered experimental, including design-build, cost plus time bidding (A+ B bidding), lane rental, and the use of warranties, have become mainstream practices across the country. After permitting states to utilize design-build contracting for 10 years, the FHWA issued a Final Rule sanctioning design-build contracting as an allowable delivery method.

3. SEP-15

Further, in October 2004, FHWA established SEP-15 to encourage experimentation in the use of public–private partnerships, and to identify for trial evaluation new public–private partnership approaches to project delivery. It is anticipated that these new approaches will allow the efficient delivery of transportation projects without impairing FHWA's ability to carry out its stewardship responsibilities to protect the environment and taxpayer.[422] SEP-15 does not replace SEP-14, which is still available to evaluate experimental contract administration methods.

The objectives of the SEP-15 program are to encourage test and experimentation in the entire project development process, identify impediments of current law and regulations, and promote greater use of public–private partnerships and private investment in transportation improvements. The objectives also include development of processes and approaches to address impediments, and to evaluate and propose administrative and statutory recommendations to remove these impediments.[423] Further discussion of SEP-15 is contained in Section 4 of this study.

4. PPP—2007

In August 2007, FHWA issued revised design-build regulations to comply with Section 1503 of SAFETEA-LU, which permits agencies to issue RFPs and notices to proceed for preliminary design work before conclusion of the NEPA process. A further detailed discussion of SAFTEA-LU and PPP is contained in Section 1.C. of this study.[424]

b. The Design-Build Method

1. Advantages and Disadvantages

Under the design-build method of project delivery, design and construction are combined in one single contract, with a single point of contact responsible for both the design and construction. The design-build contractor, which may be one contractor or a consortium of design, construction, and management firms, assumes the design risk, and agrees to construct the project according to its design dawings.[425] The design-build method permits the contractor the maximum flexibility for innovation in the selection of design materials and construction methods. Industry survey information conducted for NCHRP Project 2005, Topic 38-12, indicates that the potential benefits and major advantages of design-build implementation include substantial time savings. Managers of design-build projects who were surveyed in a federal study estimated that project delivery reduced the overall duration of the project by 14 percent, and reduced the overall cost by 3 percent.[426] Other advantages include

[420] CDOT I-70 Tunnel Risk Assessment and Project Delivery Selection, available at http://www.coloradodot.info/projects/i70twintunnels/cmgc, last accessed on July 6, 2012. More generally, *see also* http://www.coloradodot.info/business/designsupport/innovative-contracting-and-design-build/documents/cmgc-cca, last accessed on July 6, 2012.

[421] See FHWA Initiative to Encourage Quality Through Innovative Contacting Practices, Special Experimental Projects No. 14 (SEP-14) on FHWA Web page, http://www.fhwa.dot.gov/programadmin/contracts/021390.cfm.

[422] See http://www.fhwa.dot.gov/ipd/p3tools_programs/sep15_procedures.htm, last accessed Mar. 21, 2011.

[423] FHWA Web information tools and programs on SEP-15, http://www.fhwa.dot.gov/ipd/p3/tools_programs/sep15_faqs.htm, last accessed Mar. 21, 2011.

[424] 23 C.F.R. 627 et al.

[425] EDWARD FISHMAN, MAJOR LEGAL ISSUES FOR HIGHWAY PUBLIC-PRIVATE PARTNERSHIPS 5 (NCHRP Legal Research Digest No. 51, Transportation Research Board, 2009), available at http://onlinepubs.trb.org/onlinepubs/nchrp/nchrp_lrd_51.pdf, last accessed on Sept. 8, 2013.

[426] Design-Build Effectiveness Study As Required by TEA Section 1307(f), Jan. 2006, executive summary and final report link available at http://www.fhwa.dot.gov/reports/designbuild/designbuild.htm. Last accessed Sept. 7, 2013.

reduced construction engineering and inspection costs, reduced change orders and claims, improved quality, inclusion of innovative ideas, and shortened design and construction duration. Perceived disadvantages include higher construction costs attributable to owners' increased risk exposure, owners' loss of control, fewer bidders, problems related to shifting quality control (QC) functions from the DOT to contractor, and difficult warranty enforcement.[427]

2. State Transportation Design-Build Authority

Many states have passed laws authorizing design-build procurement. To date 42 states, the District of Columbia, Puerto Rico and the Virgin Islands have the ability to deliver design-build transportation projects.[428] (See the Appendix H chart of states with design-build authority.) In December 2011, while preparation of the current update to this volume was under preparation, New York State enacted design-build legislation.

Design-build selection can lead to litigation. For example, after Ohio enacted design-build legislation, it then became the subject of litigation. In *Trumball Corporation v. Ohio Department of Transportation*, contractor TGR commenced a breach of contract suit and a declaratory judgment action, sought a temporary restraining order to stop a $200 million public improvement project known as I-71 - I-670. The Ohio Department of Transportation (ODOT) accepted technical proposals from three contractors. The technical proposals were reviewed by ODOT and, pursuant to a detailed scoring system, were given cumulative numerical grades. The short-listed contractors who survived the rigorous process were guaranteed to receive a $500,000.00 stipend from ODOT. Prior to opening the price proposals, TGR was notified that its Technical Proposal had been determined nonresponsive and was not given a numerical grade. TGR's proposal was not opened, and ODOT withheld the $500,000.00 stipend. The Court of Claims denied TGR's request for a restraining order, determined that TGR did not show by clear and convincing evidence that it would suffer irreparable harm if the project were not suspended, and found that TGR had an adequate remedy at law. The court noted that the Director of ODOT has broad discretion in making the determination regarding responsiveness.[429] Subsequently, after trial, the Court of Claims ruled in favor of TGR, determining that their technical proposal was responsive, and rendered a judgment in favor of TGR on their claim of breach of contract, damages to be determined after future audit, based upon the contract provisions that provided for payment of a $500,000 stipend after audit, whichever is lower.[430]

3. Federal Laws and Regulation

As previously mentioned, design-build is authorized by SAFTEA-LU and TEA-21, and federal regulations relating to design-build are contained in 23 U.S.C. Section 635.309 and 23 C.F.R. Part 627. The regulations provide that FHWA will not authorize final design and physical construction until the project confirms that 1) that the air quality non-attainment and maintenance areas meet all transportation conformity requirements of CFR Parts 51 and 93; 2) the NEPA review process has been concluded; 3) the RFP document has been approved; 4) FHWA receives a statement either that the right of way, utility and railroad work has been completed or that all necessary arrangements will be made; and 5) if railroad, utility, and right-of-way is included, the design-builder's scope of work must include a statement concerning the scope and current status of the required services and a statement about compliance with the Uniform Relocation Acquisition Policies Act of 1970.[431]

The regulations provide that state highway agencies are strongly encouraged to include provisions for suspension of work, differing site conditions, and significant changes to the work in the design-build agreement.[432]

4. Design-Build Methods

a. Selection—Request for Qualifications, RFP

Many state transportation agencies have obtained statutory authority to construct transportation projects using the design-build methodology. Many design-build authorizing statues permit a "best value" selection process allowing not only price, but other qualitative factors to be considered when selecting the design-builder, instead of a competitive selection process reliant solely upon the lowest bid price. Federal regulations define "best value" selection as any selection process in which proposals contain both price and qualitative components, and the award is made based upon a combination of price and analysis of qualitative factors.[433] The best value selection process allows the transportation agency to select the design–builder that best meets the combination of agency and stakeholder goals. The agency may consider important quality-related factors to include the following: the design-builder's organization of the work, experience and qualification of the

[427] ANDERSON & DAMNJANOVIC, SELECTION AND EVALUATION OF ALTERNATIVE CONTRACTING METHODS TO ACCELERATE PROJECT COMPLETION 15 (NCHRP Synthesis 379, Transportation Research Board, 2008).

[428] JEFFREY BUXBAUM & IRIS N. ORTIZ, PUBLIC SECTOR DECISION MAKING FOR PUBLIC-PRIVATE PARTNERSHIPS 9 (NCHRP Synthesis 391, Transportation Research Board, 2009), http://onlinepubs.trb.org/onlinepubs/nchrp/nchrp_syn_391.pdf.

[429] Trumball Corp. et al v. Ohio Dep't of Transp., Court of Claims of Ohio, Case No. 2011-06943, Nov. 15, 2011.

[430] *Id.*

[431] 23 C.F.R. 635.309

[432] 23 C.F.R. 635.109.

[433] 23 C.F.R. 636.103.

firm and personnel, proposed management scheme, design and construction technical solutions, past performance, backlog, and financial capacity. The manner in which these selection factors, including price as well as other factors, will be weighed must be determined early in the procurement process before issuing the RFP. Typical state statutes establish a two-step selection process in which the first step is a Request for Qualifications (RFQ), and the second step is an RFP. At the RFQ stage, the transportation agency selects the top qualified companies to submit a detailed proposal along with a cost proposal. Federal design-build regulations suggest that the following factors be considered in phase one of selection: scope of the work, and weighted factors including technical approach, technical qualifications such as specialized experience, technical competence, and past performance capability.[434] Phase two criteria include both technical and price proposals. The regulations provide that all factors and significant subfactors and their relative importance must be clearly stated and described in the solicitation.[435] Agencies may then be allowed further discussion in selecting the best proposal, and are not required to select the lowest cost proposal.

b. Contract risk identification and allocation

A systematic approach to risk identification and management can reduce the contract price and avoid future contract disputes.

Once risk is identified, the transportation agency can evaluate measures to mitigate possible impact and determine how to allocate risks amongst the various parties. In general terms, the risk should be allocated to the party that can best take steps to control and manage the effects of such risk. The federal design-build regulations divide risk into several categories, which include government risk, regulatory compliance risk, construction phase risk, post-construction risks, and right-of-way risks. Government risks include the potential for delays, scope changes, or additions and modifications. Regulatory compliance risks involve environmental issues and third-party issues such as permitting, railroad, and utilities. Construction-phase risks include differing site conditions, traffic control, public access, and weather and schedule. Post-construction risks include public liability and meeting specified performance standards. Right-of-way risks include acquisition costs, appraisals, relocation delays, and court costs.[436]

Other risks that should be allocated include security, financing, time/completions, force majeure, third-party litigation, community opposition, and destruction/casualty. The results of the risk analysis process should be used in preparing the design-build contract provisions and agreements with stakeholders and other third parties.[437] A further detailed discussion of risk allocation is contained in this volume's discussion of PPP, below.

c. Stipends

The cost of preparing proposals can constitute a considerable financial burden upon proposers. Providing a stipend helps cover a portion of the costs, and can provide an effective financial incentive that can increase competition. The stipend rarely covers the full cost of proposal preparation. Industry surveys show stipends range between 0.1 percent and .25 percent of the proposed cost, and thei availability and terms of use should be identified in the RFQ and RFP.[438]

In exchange for the stipend, however, the agency should become the owner of the work product prepared by the proposer, even if the proposal is not ultimately selected.

The stipend serves to encourage highly qualified proposers to participate in the procurement, increase the quality of proposers, compensate unsuccessful proposers for a portion of the cost of preparing, and encourage participation in future design-build procurement.[439]

d. Incentive/Disincentive

The use of incentives, either alone or in combination with disincentives, can be an effective tool for assuring project quality. The type and amount of incentive will depend on the nature of the project, and on the goals and concerns of the transportation owner. Some design-build contracts contain performance based incentives rewarding the design builder at certain intervals or milestones, or for meeting predetermined performance criteria for quality, safety, etc.[440] The Alaska Way Viaduct agreement, for example, provides incentives for completion prior to the completion deadline. The agreement provides that if the design builder achieves substantial completion before a 316-day calculated time period, it shall be entitled to an incentive of $100,000 per day up to a maximum amount of $25,000,000. The incentive payment would be added to the total compensation via a change order, would be payable at the time

[434] 23 C.F.R. 636.204.

[435] 23 C.F.R. 636.209.

[436] 23 C.F.R. 636.114.

[437] NYSDOT, Design-Build Procedures Manual Vol. 1, Sept. 2008, at 12–16. Practical experience and common sense also suggest that it might possibly be wise to consider, and to allocate contractually, the risk of criminal fraud by subcontractors or suppliers, the risk of such fraud passing initially undetected due to bribery of inspectors, and the potentially substantial costs of correcting belatedly discovered fraud-related noncompliance with technical specifications critical to the safety and durability of the completed structure or facility.

[438] Design Institute of America, DBIA Position Statement, Use of Stipends, http://www.dbia.org/resource-center/Documents/ps_stipends.pdf.

[439] NYSDOT, *supra* note 437, at 17.

[440] MICHAEL C. LOULAKIS, DESIGN-BUILD FOR THE PUBLIC SECTOR 252–53 (Aspen Publishers, New York, 2003).

of final payment, and would not affect the contractor's obligation to pay liquidated damages, which would be capped at $75,000.000.[441] Further discussion of I/D provisions is addressed in the Section 1.C., discussion of PPP

e. Insurance

Design-build contracts generally contain insurance requirements identical to those of traditional design-bid-build contracts. Transportation contracts require commercial general liability, commercial auto liability, worker's compensation, and, if applicable, professional liability and builders risk protection. A further discussion of insurance requirements is contained in Section 7 of this study.

In the traditional design-bid-build situation, insurance for projects is normally covered under the contractor's procured insurance policies. In the design-build arena, other forms of insurance should be considered, including Owners' Controlled Insurance Programs (OCIPs) or Contractor Controlled Insurance programs (CCIPs).

OCIPs can be an effective way to improve safety and reduce the costs of insurance for large projects. Basic features of an OCIP are: 1) the owner purchases the insurance coverage to cover all contractors and subcontractors;(2) there is an integrated owner-contractor managed safety program; and 3) claims are centrally processed. OCIPs are able to achieve savings through the use of lower bulk insurance rates, improved safety management, and reductions in disputes between contractors as to who is liable for loss.[442]

Wrap-up insurance, which includes OCIPs and CCIPs, may also provide savings and improve claim management and loss control. If an OCIP is used, the transportation agency is responsible for procurement of an insurance broker and the creation of the OCIP program. The OCIP program will include all the general and professional liability and other insurance for the project. All contractors and subcontractors would be contractually required to participate in the program, and to delete insurance costs from their overhead. If a CCIP is used, the design–builder is required to provide an insurance program that covers the design-builder and its subcontractors. The design–builder would be responsible for administration of the CCIP and insuring that all subcontractors do not include insurance costs in their overhead.

Professional liability requires special attention. If the standard insurance program is used, it is the design-builder that should obtain and maintain, for the full duration of the project, a professional liability policy in the name of the design-builder. It is not acceptable effort for the design-builder to rely on the insurance policy or policies of its designers to cover professional liability. The design-builder is the entity under contract with the owner, and the owner will look to the design-builder for responsibility.[443]

f. Warranties

Federal regulations provide that state highway agencies may include warranty provisions in projects on the NHS. Federal regulations exclude maintenance items from federal participation. They provide that no warranty will be approved if, in the judgment of the Division Administrator, it may place an undue obligation on the contractor for items over which the contractor has no control.[444]

The design-build contract may also contain general warranty provisions covering all work on a project and/or component-specific warranty (extended warranty) on selected items such as pavement or structures.

General warranty provisions have been limited to a maximum of 2 years,[445] and should be covered in the contract documents. Extended warranties may extend beyond the general 2-year warranty requirements and will be limited to the design-builder's ability to obtain bonds covering the extended warranty period. Warranty provisions may be difficult to enforce if the transportation agency is not able to substantiate that it has maintained the roadway within the specified standards or has permitted activities that have caused distress or damage.[446] Federal requirements for design-build warranties provide that warranties may not include items of routine maintenance that are not eligible for federal participation. FHWA regulations provide that warranties are short, generally 1 to 2 years; however, projects developed under PPP agreements may include warranties that are appropriate for the terms of the agreement. The regulations also permit alternate warranty proposals in best value selections, and the alternates must be in addition to the warranty in the base proposal.[447]

In design-build contracts where the design-builder has been given flexibility in determining means and methods, warranty specifications can provide a real quality incentive to the design-builder in addition to

[441] State of Washington DOT SR 099 Bored Tunnel Alternative Design Build Project, § 13.3.

[442] FHWA memorandum Oct. 7, 2002, Owner Controlled Insurance Program Policy, *see* http://www.fhwa.dot.gov/programadmin/contracts/100702.cfm, last accessed Sept. 8, 2013.

[443] NYSDOT, *supra* note 437, at 20–21.

[444] 23 C.F.R. 635.413.

[445] *See* 23 C.F.R. 635.413.

[446] NYSDOT, *supra* note 437, at 88–90. Note that one potential factor to consider in this regard is that a warranty may become meaningless if a contractor goes bankrupt and ceases doing business after the project has been completed, if any warranty bond has expired or has been suspended due to nonpayment of premiums, and if there are no significant remaining assets or closely affiliated business entities against which enforcement of the warranty may be pursued.

[447] 23 C.F.R. 413.

providing protection to the owner. If the transportation agency is overly prescriptive and provides the design solutions, however, and the design-builder constructs the project according to the means and methods specified by the agency, it may be difficult to enforce the warranty.[448]

g. QA/QC

QA/QC are controversial topics in the design-build arena. Design–builders are concerned that the "traditional" inspectors would not comprehend the differences between the design-build and traditional projects and would likely delay the project schedule. They have asserted that the contracting community is capable of providing this service. Design-build contracts often require that the contractor will provide QA/QC functions as a contract deliverable in accordance with the owner's approved program.

Project approaches to this issue vary. Some project owners are reluctant to depart from the traditional inspection approach and include extensive provisions regarding quality control and assurances as well as incentives and disincentives associated with quality issues. Some contracts require the QA functions to be performed by otherwise nonaffiliated firms not associated with the design-builder. Some contracts require the QA firm to report to senior management instead of to the project manager and/or project owner in addition to the design-builder.[449]

5. Significant Design-Build Projects

a. Highways

1. Maryland DOT, ICC Connector [450]

In the East, the Intercounty Connector (ICC) is an 18-mi, 6-lane design-build toll highway under construction in Maryland. Engineering News-Record selected the project as the region's best overall project in 2011, and an example of a high level of environmental stewardship demonstrated on a transportation project.[451] On Contract A, the DB team instituted a turtle management plan that saved and managed hundreds of turtles during the 4-year construction schedule . The roadway links the areas between the I-270/I -370 and I-95/U.S. 1 corridors with central and eastern Montgomery County and Prince George's County. The finished project will have variable fully electronic toll structures based upon peak and off-peak travel times. The funding sources include Maryland Transportation Authority revenue bonds, Treansportation Infrastructure Finance and Innovation Act (TFIA) loans, the Maryland Transportation Trust Fund, and the State of Maryland General Fund.[452]

The Maryland State Highway Administration conducted less quality assurance oversight than under a typical design-bid-build project, transferring more of the responsibility to the design-build team. The team used more than 35 full-time independent quality control professionals in planning and measuring quality as the work progressed.[453]

This $2.4-billion, 18-mi project also includes reconstruction of two major interchanges. This design-build project was greatly accelerated, and broke ground in July 2007. Four of the five design-build contracts have been completed and 17 of the 18 mi opened in November 2011.

2. I-15 Reconstruction, Utah

The use of design-build methodology was successfully demonstrated by the Utah Department of Transportation in the $1.63-billion construction of 17 mi of I-15 and associated facilities through Salt Lake City. The design-build method was selected for the project because of the immense public pressure to complete the project before the 2002 Winter Olympics. The I-15 project was Utah's first design-build project. Since the project was funded with federal funds, Utah obtained FHWA approval under SEP-14. The project included construction or reconstruction of more than 130 bridges, reconstruction of 7 urban interchanges, the reconstruction of 3 major Interstate junctions, and construction of an extensive region-wide advanced traffic management system. State procurement laws were amended to authorize the use of design-build clearly, and to permit award to a firm that provided the best value proposal to the State. Utah estimated it would take 10 years to complete the project under the traditional low-bid method approach; however, the design-builder completed the project in 5 years and $32 million under budget.[454] The use of performance specifications as opposed to prescriptive specifications encouraged innovation in design and construction, and Utah DOT also derived $30 million in savings by utilizing an OCIP.

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[448] NYSDOT, *supra* note 437, at 88.

[449] Nancy Smith, Getting It Right: How to Structure Complex Projects to Allocate Risks and Minimize Disputes, (Oct. 11, 2011). *See* http://www.nossaman.com/getting-right-how-structure-complex-projects-allocate, last accessed Sept. 8, 2013.

[450] FICK, ELLS, CACKLER, TROST, & VANZLER, *supra* note 409.

[451] Bruce Buckle, *Maryland Highway Takes the Eco Friendly High Road*, ENR, New York Regions Best Project 2011, Nov. 7, 2011, at 62–63.

[452] Case Studies Intercounty Connector, *see* http://environment.fhwa.dot.gov/projdev/travel_landUse/icc-case-study/icc-case-study.htm and http://www.iccproject.com/PDFs/2011 ICC Financial Plan S.pdf.

[453] Buckle, *supra* note 451, at 63.

[454] FISHMAN, *supra* note 425. *See also* FHWA Office of Innovative Program Delivery, Project Profiles Table: I-15 Corridor Reconstruction project, http://www.fhwa.dot.gov/ipd/project_delivery/resources/general/report_to_congress_2011_table.htm.

3. E-470

The E-470 design-build project for Denver's E-479 Public Highway Authority consisted of a 47-mi four-lane toll highway developed in four segments, which commenced in 1995. The project connects the E-470 at I-25 south of Denver, passes along the western edge of Denver International Airport, turns back towards the west, and terminates at I-25. The project cost $1.23 billion and is supported by revenue bonds backed by toll receipts and registration fees. The project was completed in 2003, and represents one of the first roads in the nation built under PPP. The roadway project was built under budget. The completed road contains many innovations including electronic toll collection.[455]

b. Transit Projects

1. Hudson-Bergen Light Rail (New Jersey)

This $ 2.3-billion project was to design-build, operate, and maintain a 20-mi light rail transit system in New Jersey for New Jersey Transit and the New Jersey DOT. Awarded in 1985, the project included 16 stations, several station extensions, and 45 light rail vehicles, and was completed in 2000. The Hudson-Bergen Light Rail is owned by New Jersey Transit and operated under a Design-Build Operate and Maintain contract with Washington Group International (formerly Raytheon Infrastructure). The contract provides for a 15-year operation and maintenance term. The project was successfully completed in January 2003, and several other expansions have since been completed. The initial segment was opened in 2000, nearly 5 years ahead of projections, and the project realized cost savings of over $300 million.[456]

2. Hiawatha Light Rail (Minnesota)

The Hiawatha Light Rail Transit was a $715 million design-build contract for an 11.6-mi light rail line serving 17 stations in Minneapolis, Minnesota, and linking downtown Minneapolis-St. Paul International Airport and the Mall of America. The corridor was 12 mi in length, with 17 stations, and required building 24 light rail vehicles. The design-build method was utilized for two separate design build-contracts, one for light rail vehicles and one to place rail, signal, and communication equipment along the alignment. The project entered revenue service in 2004 and carried 92,000 passengers in its first week of operation.[457]

6. Other Issues

a. Design Responsibility—Fru–Con Case

Controversy has arisen concerning the design-builder's design responsibility and the effect of agency reviews, tests, and approvals. Do such owner activities relieve the design-builder of liability? Many contracts contain provisions specifying that the contractor retains liability for any defects in the project notwithstanding the actions of the owner. Assuming the contract contains appropriate provisions, it should be sufficient to overcome the design-builder's argument that the owners' actions relieve it from liability. Transportation agencies and owners should avoid directing the contractor to design and construct the project in a particular way (providing design specifications), which would create an implied warranty, raising obstacles that might affect the holding that owners' actions do not relieve the design-builder from liability. [458]

A similar issue was addressed in *Fru–Con Construction v. United States*.[459] The contract documents assigned the Contractor the responsibility to design a detailed blasting plan. The court noted that the government's approval of the submittal did not relieve the contractor of its contractual duties. The court referenced the specific contract provision that specified that approval of submittals did not relieve the contractor of the responsibility for any error that may exist and the contractor as still responsible for the design of adequate connections and satisfactory completion of the work.

b. Limits of Liability

Some design-build agreements limit liability to a certain fixed amount specified in the agreement, while others contain no limits on liability. Design-build agreements often exempt from this liability limit criminal acts as determined in a court of law, intentional fraud, or misconduct. A more detailed discussion is contained in this volume's discussion of PPP, below.

7. Further Resources

AASHTO References

The AASHTO Guidance for Design Build Procurement, issued in January 2008, represents an excellent resource for design-build information.

[455] USDOT Report to Congress, App. D, at 144–45. *See* http://www.fhwa.dot.gov/ipd/project_profiles/co_e470.htm.

[456] USDOT Report to Congress on Public Private Partnerships, at 38; *see also* FHWA Project Profiles, Hudson-Bergen Light Rail, http://www.fhwa.dot.gov/ipd/project_profiles/nj_hudson_bergen.htm.

[457] USDOT, *supra* note 456, at 151–2. *See* http://fhwa.dot.gov/ipd/project_profiles/mn_hiawatha.htm, last accessed Sept. 8, 2013.

[458] Smith, *supra* note 449; Loulakis, *supra* note 440, at 258–59.

[459] 42 Fed. Cl. 94, 97 (1998).

Best Practice Studies

In September 2005, the NYSDOT issued a Design Build Procedures Manual consisting of five volumes of text, exhibits, and forms and templates that can be a useful resource for further inquiry into the design-build arena.

c. Public–Private Partnerships and Project Finance

1. Historical Basis of PPPs

The USDOT Report to Congress on Public–Private Partnerships, submitted to Congress in 2004, defines a PPP as a contractual agreement, formed between public and private sector partners, which allows more private sector participation than is traditional. The agreement usually involves a governmental agency contracting with a private company to renovate, construct, maintain, and/or manage a facility or system."[460]

PPPs are not new concepts for transportation infrastructure development. PPPs date back to 1792 with the development of the private Philadelphia and Lancaster Turnpike in Pennsylvania.[461]

In the late 1980s, states began to explore greater private sector participation in highway development with the legislative authorization of Virginia's Dulles Greenway project, followed by the Pocahontas Parkway in Virginia and the Southern Connector in South Carolina.

In 1990, FHWA created SEP-14 allowing, for states to experiment with innovative contracting options such as cost plus time, bidding lane rental, and the use of warranties.

In 1991, Congress passed ISTEA, landmark legislation that established new priorities while raising funding to a new level. ISTEA drew attention to environmental and community needs, established and funded CMAQ, and encouraged stakeholder participation. It also allowed for more flexibility in the comingling of FA funds, and allowed toll credits to apply toward the nonfederal match. Prior to this change, tolls were not allowed to be applied for the nonfederal match.[462]

In 1998, TEA-21 was passed to increase further flexibility in funding. It added new funding features, which included State Infrastructure Banks (SIBs) and TIFIA to provide credit assistance to major projects of national significance. It also expanded the toll credit to 100 percent cost of the project, and permitted toll facilities that could be operated by a private toll authority.[463]

In 2004, USDOT submitted a detailed report to Congress on the potential use of PPPs for the funding and construction of future surface transportation capital projects.[464]

In 2004, FHWA also created SEP-15 to identify for trial evaluation new PPP approaches to project delivery.[465]

The objectives of SEP-15 programs are to encourage experimentation in the entire project development process, identify impediments in current law and regulations, and proactively promote the greater use of PPPs and private investment in transportation improvements. SEP-15 also develops processes and approaches, addresses impediments, and evaluates and proposes administrative and statutory recommendations.[466] The objectives of SEP-15 are also to increase project delivery flexibility, encourage innovation, improve project delivery time, and promote PPPs. It permits FHWA to identify current FHWA regulations, laws, and practices that may inhibit greater use of PPPs, and allows the FHWA to develop approaches and procedures that address the impediments.[467]

Eligible projects are defined as projects that will advance the goals of the SEP program and that will test innovative delivery techniques prohibited by current provisions of Title 23 U.S.C. and FHWA rules and regulations.

The process requires project sponsors (which may include state agencies, localities, and public-private transportation ventures) to submit applications that provide a brief description of the project and the specific areas of experimentation, explain innovative techniques and their expected value, and identify proposed performance measures to evaluate success of the SEP-15 project.[468] If acceptable, the project sponsors will make a formal presentation of the SEP-15 application and address any questions. The FHWA will work with the public and private sponsors to draft an Early Development Agreement (EDA). The EDA should contain key elements of project planning and design, regulatory compliance, timelines, financing, construction, and operations. Upon completion of the major milestones, the public–private sponsors are required to submit a report that summarizes the lessons learned from the SEP-15 process, and includes recommended statutory and regulatory changes with an explanation of how the changes will improve the delivery of the FA highway program.[469]

The SEP-15 Steering Committee is responsible for overall management and oversight. The Steering Committee proposes SEP-15 project cofacilitators, provides recommendations regarding applications, manages development of documents and promotional materials,

[460] USDOT, *supra* note 456.

[461] *Id.* at 15.

[462] University Transportation Research Center, NYSDOT, Partnership for New York, Briefing Paper, Mar. 8, 2006, at 5.

[463] *Id.* at 6.

[464] USDOT, *supra* note 456.

[465] *See* http://www.fhwa.dot.gov/ipd/p3/tools_programs/sep15.htm, last accessed Sept. 8, 2013.

[466] See http://www.fhwa.dot.gov/ipd/p3/tools_programs/sep15_faqs.htm, last accessed Sept. 8, 2013.

[467] *Id*.

[468] *See* Frederick C. Wright, Jr., Action: SEP-15 Application Process, FHWA memorandum, Oct. 14, 2004, available at http://www.fhwa.dot.gov/programadmin/contracts/101404.cfm, last accessed Sept. 8, 2013.

[469] *Id*.

and develops training courses relevant to the administration of SEP-15 projects.

Evaluation and selection criteria include whether the proposed experimental feature is prohibited under current policies and procedures, and whether the parameters of the experimental feature extend beyond procurement issues of SEP-15. (See 69 *Federal Register* 59983, September 23, 2004.) Evaluations will also focus on whether the experimental features improve the delivery time, quality, or expense of the project, and could influence FA policy and procedure. In addition, a plan to evaluate how the experimental feature contributes to the overall success of the project will be reviewed.

If approved, the Early Development Agreement is developed jointly between the State DOT and FHWA, describing the parameters of the experimental features. The EDA will identify the specific role of the parties, define procedures, and establish time frames for each experimental feature.

It should be noted that SEP-15 may not be used to experiment outside Title 23, nor can it be used to experiment with state law. Other than areas governed by Title 23 of the U.S. Code, applicants must comply fully with State and Federal laws and regulations, such as NEPA and other environmental requirements.

In 2005, Congressional passage of SAFETEA-LU continued the progression of more flexibility for private sector involvement.[470] It included express provision, SAFETEA-LU Section 3011, for a Public-Private Partnership Pilot Program.[471] It provided expanded use of private activity bonds in which interest was not subject to federal income tax, thus reducing project financing costs, and further enhanced authority to use tolling to finance construction of Interstates. SAFETEA-LU amended the Internal Revenue Code to allow tax-exempt private activity bonds (PAB) for privately developed and operated highway and freight facilities, authorizing up to $14 billion through 2009. It also increased the flexibility for using design-build by eliminating the $50 million floor on the size of a design-build contract, and allowed PPPs to apply directly for TIFIA funds.[472]

These aforementioned laws encouraged states to pursue PPPs for transportation projects by establishing pilot programs and innovative finance mechanisms, and by adding tolling flexibility.[473]

As the 2014 update to this volume was in advanced draft form, Congress passed and President Obama signed into law MAP-21, discussed earlier in Section 1 of this volume. It appears that this legislation may require the Secretary of Transportation to take certain administrative actions in support of broader use of PPPs.

[470] SAFETEA-LU, Pub. L. No. 109-59, 119 Stat. 1144 (2005).

[471] SAFETEA-LU § 3011, 49 U.S.C. § 509 note, Pub. L. No. 109-59, 119 Stat. 1144, 1588.

[472] BUXBAUM & ORTIZ, *supra* note 428, at 6–7.

[473] *Id.* at 9.

2. Chart of States With PPP Legislation

There are 23 states that have enacted PPP authorizing legislation.[474]

3. Types of PPP Projects—Brownfield and Greenfield

There are two different types of transportation infrastructure suitable for PPP projects, which have been categorized as "brownfield "and "greenfield" projects. The development and construction of a new facility is generally referred to as a greenfield project, while the operation and maintenance of an existing facility is referred to as a brownfield project. Generally, greenfield projects will be more complex and expensive than brownfield projects, because of the need to plan, design, and build a new transportation facility.[475]

Today's transportation agencies use many different forms of PPPs, which include:

a. Design-Build

Under design-build (DB) contracting the design and construction are combined into a single point of contact. The DB contractor may be one company or a consortium of design, construction, and management firms. Innovation is encouraged by the use of performance specifications rather than traditional prescriptive specifications. Some DB contracts contain lengthy warranty provisions and shift the risk of project quality assurance to the private contractor.

b. Design-Build-Operate-Maintain

Under Design-Build-Operate-Maintain (DBOM), the private contractor is responsible for design and construction and also for operation and maintenance for a fixed period of time. The DBOM contractor agrees to meet owner-specified performance standards involving management of the asset's capacity and congestion management. Examples include the Hudson Bergen Light Rail project in New Jersey and the I-15 project in Utah.

c. Design-Build-Finance-Operate

The Design-Build-Finance-Operate (DBFO) contractor is a variation of the DBOM process that involves the DBOM operator in financing the design, construction, operation, and maintenance of the facility. Generally, the DBFO model uses tolls or other pricing mechanisms to repay the financing used to build the facility**.** Examples of DBFO include Las Vegas monorail SR-91 and SR-125 California.

d. Build-Operate-Transfer

[474] *See* App. I.

[475] Fishman, *supra* note 425, at 4.

The Build-Operate-Transfer (BOT) approach is similar to DBFO except that the contractor retains ownership of the transportation facility after the completion of the operating and maintenance phase of the contract**.**

4. Financing PPPs

There are several financing tools available to private sector groups desiring to provide debt or equity financing for transportation projects. In addition to a standard financing mechanism that includes lines of credit and loan guarantees, private-sector consideration can be given to the following:

a. TIFIA and GARVEE

The TIFIA program was enacted in 1998 as part of TEA-21. Notably, the TIFIA program has reportedly been continued and enhanced with additional funding and revisions to administrative eligibility criteria under MAP-21, enacted in 2012.[476] TIFIA allows USDOT to provide direct credit assistance to the sponsors of major transportation infrastructure projects. The TIFIA credit program provides direct loans, loan guarantees, and standby lines of credit. TIFIA assistance may be for public and private entities and can only support 33 percent of project costs for projects with cost of $100 million or 50 percent of the state's federal aid highway apportionment.[477] As of June 2004, $3.5 billion in TIFIA project assistance had been made to 11 projects, supporting $15 billion in project costs.

Grant Anticipation Revenue Vehicle (GARVEE) is a debt-financing mechanism authorized by 23 U.S.C. § 122. GARVEE allows a state or political subdivision or public authority to pledge future federal-aid highway funds to support debt financing costs. GARVEE enables debt-related expenses to be paid with future federal aid. The GARVEE financing mechanism enables states to generate, through the sale of GARVEE bonds, up-front capital for major highway projects earlier than it could using the traditional pay-as-you-go funding mechanism. Many states have participated in this program, including California, Idaho, Colorado, Ohio, Oklahoma, Arizona, New Mexico, Alabama, Alaska, and Arkansas.[478]

b. Private Activity Bonds

PABs are a form of tax-exempt bond financing that can be issued on behalf of a state or local government to provide financing for qualified projects. Currently there are $15 billion in tax-exempt PABs that are not subject to the state agency general cap on PABs.

c. 63-20 Public Benefit Corporations

63-20 public benefit corporations are nonprofit corporations created pursuant to Internal Revenue Service Rule 63-20 and Revenue Procedure 82-26, which are authorized to issue tax-exempt debt on behalf of private developers. The nonprofit must engage in activities that are "public" in nature, the state or political subdivision must have a "beneficial interest" in the corporation, and unencumbered legal title in the financed facilities must vest in the government until the bonds are paid.

d. State Infrastructure Bank Credit Assistance

SIBs are revolving funds that are administered by the states to support transportation projects. They provide low-interest loan and loan guarantees to public or private sponsors of federally aided highway projects. A SIB functions like a bank by offering loans and other credit products to private and public PPP sponsors, and has been expanded to 38 states and Puerto Rico. Since 2004, 32 states have entered into 373 SIB loan agreements with a dollar value of $4.8 billion.

e. Tolls

Direct tolls on highway users are another useful financing tool for PPP. Flat-fee tolling, variable pricing, and congestion pricing are all in the mix that can provide positive cash flow to invest in new capacity or reinvest in existing systems.

i. Availability payments and shadow tolls

Shadow tolls are another variation of tolling which support private financing of highway projects. In return for the "shadow toll," the contractor agrees to design, build, and operate or maintain the facility. The shadow toll is payment equal to the amount of toll that would have been imposed on the users of the facility if a direct user fee was implemented.

Another variation is the use of availability payments to compensate a private contractor for the cost of designing and building a transportation facility. The availability payment is a regular (monthly) payment made to the concessionaire contractor during the operation and maintenance phase in exchange for providing a project for public use of a predetermined level of capacity and quality. Availability payments do not depend on traffic volume, but are an agreed-upon regular payment during the operating and maintenance phase less any deductions assessed for failure to meet performance standards or quality or safety requirements. Availability payments start once the project is open, which provides an incentive for timely completion. The Port of Miami tunnel discussed later in this section is funded with availability payments

[476] For text of, and Conference Committee report on, MAP-21, see *supra* note 25. For link to news article reporting continuation of TIFIA under MAP-21, *see* Goad & Hurst, *supra* note 24.

[477] USDOT, *supra* note 456, at 30–31.

[478] *Id*. at 24–26.

5. Sample Projects

a. Long-Term Lease Concessions

i. Chicago Skyway

The $1.83 billion PPP for the Chicago Skyway, finalized in January 2005, focused intense media attention and sent shockwaves thought the international transportation community. The consortium of Cintra-Maquarie submitted the winning bid, entered into a 99-year lease, and, in exchange for the right to toll revenue, the concessionaire also agreed to perform certain capital improvements, install an electronic toll collection system, and improve the Skyway's traffic. The terms of the lease provided that tolls could be increased according to the consumer price index (CPI) or a negotiated rate schedule. The agreement also required the consortium to comply with City of Chicago hiring policies with respect to residency preference, minority contracting, etc.

The lease provided that the consortium would assume all legal liability for the operation and maintenance of the facility. Within the first 6 months, the electronic toll system, and newly hired toll collectors at lower hourly wages, cut operational costs, and dramatically increased traffic and transactions, and reduced congestion. The City of Chicago planned to use the $1.83 billion to repay general obligation debt, fund $100 million of visible programs, fill a budget shortfall, and fund $500 million in city reserves.[479]

ii. Indiana Toll Road

Following on the Skyway, a PPP was entered into on the 157-mi Indiana Toll Road operated by the Indiana DOT. The same consortium of Cintra-Maquarie submitted the $3.8-billion winning bid for the 75-year term. The long-term lease agreement required state legislative approval and was signed into law in March 2006. The final terms of the lease require the consortium to fund $700 million worth of capital improvements in the Indiana Toll Road including an electronic toll system. The agreement also contained a noncompete clause that prohibits the funding of a transportation improvement within a 10-mi radius of the Indiana Toll Road. The legislation also authorized step toll increases based upon a schedule approved by the legislature. Unlike the Skyway provisions, the $3.8 billion was required to be used for transportation-related activities. Indiana planned to retire toll road bonds, establish a trust fund for future Indiana DOT projects, and fund the "Major Moves" Construction Program.[480]

b. Availability Payments—DBFO (Case Studies)

iii. Port of Miami Tunnel, Florida

The Port of Miami Tunnel project involves the construction of a new direct access highway connection between I-395 and the Port of Miami. The main component of this $1.4-billion project is the construction of twin tunnels that will be bored under the shipping channel in downtown Miami. The project is a DBFOM project funded by "availability payments" instead of tolls. Construction began in May 2010 and is expected to be complete in 2014.

The availability payments of $33 million per year were to be distributed by Florida DOT over a 30-year term of the operating contract, unless performance standards relating to lane availability and service quality and safety were not met. This approach provided incentives for timely completion of the facility, since the payments did not start until construction was complete. The consortium was also to receive $100 million in progress payments during construction from 2010 to 2013 and $350 million from Florida DOT when the project was complete. At the conclusion of the term, the consortium would hand back the facility to Florida DOT, and at that time might be required to correct any deficiencies.[481]

iv. Pocahontas Parkway, Virginia, SR-895—63-20 Public Benefit Corporations

The Pocahontas Parkway is an 8.8-mi 4-lane toll road that connects I-95 with I-295, also known as SR-895, near the Richmond International Airport. This project was the first construction project implemented and completed under Virginia's innovative Public–Private Transportation Act of 1995 (PPTA).

The Pocahontas Parkway proved to be an object lesson in the risks both of overoptimistic traffic volume and toll revenue estimates, and of poor risk allocation in PPP contract drafting and negotiation.

It was completed in September 2002 for $314 million, $10 million below the original $324-million contract.[482] The Virginia DOT established a 63-20 public benefit corporation, the Pocahontas Parkway Association (PPA), to finance the development of this toll facility by using tax-exempt bonds, obtaining funding from Virginia's Infrastructure Bank, and obtaining federal funds for design costs. After completion, unfortunately, the PPA experienced serious financial difficulties during operations as traffic volumes were significantly lower than projected and toll revenues produced only half the forecast amount. In 2004, while the facility was producing $7 million in annual toll revenues, and the PPA had roughly $2.2 million from investment income

[479] Fishman, *supra* note 425, at 9–10.

[480] *Id*. at 10–11.

[481] *Id.* at 16–17. *See also* FHWA project profile, http://www.fhwa.dot.gov/ipd/project_profiles/fl_port_miami_tunnel.htm.

[482] USDOT, *supra* note 456, at 147–8.

on its reserve account, annual facility costs were on the order of $30 million—$25 million for debt-carrying costs, $2.8 million for amortization, $2 million for operating and maintenance costs, and $0.7 million for PPA administrative costs. The net shortfall was on the order of $21 million per year. While much of this fell on the PPA, Virginia DOT apparently absorbed on the order of $2 million per year in unanticipated operation and maintenance costs.[483] By 2006, the PPA reportedly had debts totaling $522 million—for the construction of a $314 million highway.[484]

In June 2006 the Virginia DOT negotiated an agreement with an Australian toll road operator, Transurban, under which Virginia DOT granted a 99-year lease concession for Transurban to acquire the PPA's rights to the Pocahontas Parkway through a special-purpose entity for the price of $458 million, and to manage, operate, and maintain the Parkway, and collect the tolls. (It is unclear how the PPA was able to pay off the remainder of its $522 million in debts.) In addition, Transurban agreed to construct a 1.58-mi extension to the Richmond International Airport conditioned on TIFIA financing. The agreement gave Transurban the right to set toll rates, but capped them at specified maximum amounts. Transurban took over maintenance responsibilities and costs from Virginia DOT, and agreed to give maintenance expenses priority over creditors. Under the new agreement, Transurban assumed the full risk for traffic volumes and toll revenues, and Virginia DOT made no guarantees. While the agreement involved a 99-year lease, the State of Virginia retained the right to terminate the concession after 40 years if it paid off Transurban's debts for the project and compensated Transurban for lost return on equity.[485]

While this project was a success in terms of successful completion, it serves as an example of the risk encountered by projects that issue bonds backed by projected toll revenues that are not achievable.

c. Comprehensive Development Agreements

i. Texas SH-130, TTC 335,[486] North Tarrant Express

The Texas DOT SH-130 project is a 92-mi toll highway, the largest element of the $3.6-billion Central Texas Turnpike System. Segment 1-4 of SH-130 was developed through an exclusive development agreement. Segments 5-6 were developed under a comprehensive development agreement (CDA). The CDA provides for design and construction to be conducted by the private consortium and gives Texas DOT the option for requiring the design-builder to provide maintenance, while Texas DOT is responsible for operating the toll facility. The initial phase of SH-130 opened nearly 1 year ahead of schedule and more than $400 million under budget.

The Trans Texas Corridor initiative was envisioned as a massive 4,000-mi multimodal super corridor that would contain toll roads and commuter rail in 1,200 ft corridors. Texas DOT expected the project to take place over 50 years, and costs were estimated to be $200 billion, to be funded with PPPs and tolling. The first segment of the massive project was the construction of TTC-35. Texas DOT has signed a CDA with Cintra-Zachary whereby Cintra-Zachary has agreed to develop the preliminary concept and financing plans for TTC-35 in exchange for $3.5 million.

The project was subject to intense community opposition over tolling and the appropriation of 500,000 acres of private property. In 2004, the Trans Texas Corridor project was scaled back. In 2009, Governor Perry stated that "the name Trans Texas Corridor is over with." The Texas legislature approved a measure to expunge the references to the Trans Texas Corridor from state statutes, which was signed into law by Governor Perry on June 17, 2011.[487]

6. State PPP Authority

a. Virginia

One of the first laws to enable the use of PPP in transportation was the Virginia PPTA of 1995. The Act, modified in 2005, allows PPPs for solicited and unsolicited proposals and contains guidelines to assist the Virginia DOT and other Virginia public entities in pursuing PPP agreements. The PPTA serves as an excellent model for state legislative initiatives.

The statute authorizes private entities to develop or operate qualifying projects promoting timelier or less costly completion while serving the public safety and welfare. The Act requires approval by a responsible public entity, and provides that the public entity may request proposals or invite bids. The statute establishes detailed guidelines for responsible public entities' action and submission requirements. It specifies PPP evaluation criteria, and provides for notification of affected local jurisdictions. It contains details of the powers and duties of the private entity, provisions for a detailed comprehensive agreement, interim default provisions, and provisions related to remedies, use of public entities' condemnation powers, and use of federal, state, and local financing. In addition, it provides details of

[483] Peter Samuel, *Pocahontas Parkway Revenues About Half Forecast*, TOLLROADS NEWS, Feb. 18, 2004, available at http://www.tollroadsnews.com/node/582, last accessed on Sept. 8, 2013.

[484] Peter Samuel, *Transurban has $522m Agreement to Take Over Pocahontas Parkway VA*, TOLLROADS NEWS, May 2, 2006, available at http://www.tollroadsnews.com/node/1516, last accessed on Sept. 8, 2013.

[485] *Id.*

[486] Fishman, *supra* note 425 at 14.

[487] Paul West, *Perry's Road Dream a Public Relations Nightmare*, SCHENECTADY GAZETTE, Nov. 24, 2011.

competitive negotiation, posting of conceptual proposals and comment periods.[488]

Under the statute, the public entity may grant or loan federal money and public funds and permit the use of TIFIA funds for PPP, and is not required to obtain legislative approval for individual PPPs. It permits all types of delivery systems, and exempts the PPP from the application of the state's general procurement laws. It permits the PPP to include local governments and regional authorities, and confers the power to develop and or operate qualifying transportation facilities. It also permits conversion of existing highways into toll roads.[489]

b. Florida

Similarly, Florida PPP legislation allows Florida to receive or solicit PPP proposals, but these must have the concurrence of the Florida DOT and be consistent with the Florida Transportation Plan. Chapter 334.30 of Florida Statutes provides that there is a public need for the rapid construction of safe and efficient transportation facilities for the purpose of traveling and that it is in the public's interest to provide for the construction of additional safe, convenient, and economical facilities. The statute provides local resources to fund and finance the project. It requires that the project be owned by the department upon completion or termination of the agreement. It provides evaluation criteria, and limits PPP agreements to 50 years, but allows them to be up to 75 years as approved by the Secretary of Transportation. In addition, the Florida statute permits the use of state resources to finance and fund the PPP. The statute allows solicited and unsolicited proposals, and permits TIFIA loans but requires prior legislative project approval as evidenced by the approval of the project in the department's work program. It permits all kind of procurement including use of DB, long-term lease, and exemptions from general procurement laws.[490]

c. California[491]

California in 2009 passed a PPP statute that authorizes the use of PPPs for transportation projects by Caltrans and regional transportation agencies. The statute authorizes the contracting entity to impose tolls and user fees and authorizes solicited and unsolicited proposals. If unsolicited, proposals are subject to a competitive bid process if the public sponsor wishes to proceed. The statute authorizes an RFQ and RFP procurement selection process and provides an unlimited number of projects. Selection is to be based on low bid or best value, and the statute sunsets and the PPP agreements must be signed by December 31, 2016.[492]

The statute established the California Transportation Commission to focus on PPP developments and education. The Commission must approve the project. To date, the Presidio Parkway PPP has been approved, in 2010, using TIFIA financing and availability payments.[493]

The validity of the California statute has survived judicial challenge in *Professional Engineers in California Government et al. v. Department of Transportation*. The plaintiff's professional engineers sought a permanent injunction to prohibit Caltrans from implementing the PPP for Phase II of the Presidio Parkway on the grounds that the project did not qualify as a PPP under the Streets and Highway Code. The Court of Appeals affirmed the lower court's denial of relief. The court rejected plaintiff's argument that although Caltrans was responsible for the performance of the work, it was not required to actually perform the engineering work, since the design was performed by a consultant. Also the court rejected plaintiff's argument that the statute required the project be funded by tolls and user fees, and concluded that the statute does not mandate but merely authorizes toll and user fees.

7. Common Legal Issues in PPP

State transportation officials should be aware of the following legal issues that merit analysis and attention in the PPP procurement process.[494]

a. Solicited and Unsolicited Proposals

A threshold issue that often arises involves what to do with unsolicited proposals. The USDOT Model Legislation provides for the receipt, evaluation, and acceptance of unsolicited proposals. If the unsolicited proposal meets the requirements, the public agency must advertise the proposal in general terms to solicit competing proposals for the same transportation facility, at which time the public agency may select the initial proposal or a competing proposal based upon its evaluation criteria. The Model Legislation provides that the agency may charge a reasonable fee to cover the costs of reviewing the unsolicited proposal. The Virginia PPTA serves as an excellent model and contains detailed guidelines and procedure on treatment of unsolicited proposals. Virginia has developed a QC process in which unsolicited proposals are analyzed to determine

[488] VA. CODE § 56.575.

[489] For a detailed discussion of suggested P3 legislation see FHWA Office of Innovative Program Delivery, http://www.fhwa.dot.gov/ipd/p3/state_legislation/.

[490] FLA. STAT. ANN. §§ 334.30, 337.251,338,165; 338.22–338.251, 339.55, and 348.0004; see FHWA project delivery Web site, n.455 *supra*.

[491] Smith, *supra* note 449.

[492] CAL. STS. & HIGH. CODE § 143 (SBX2 4).

[493] Nancy Smith, Public Private Partnerships, presentation, NCPPP Conference, Sacramento, California, Jan. 20, 2011.

[494] More detailed discussions of these issues are contained in BUXBAUM & ORTIZ, *supra* note 428, and NCHRP Legal Research Digest 51, Transportation Research Board, 2012.

if the project is in the public interest, and to then make a decision on whether the project should be pursued.[495]

b. Confidentiality vs. Transparency

PPP critics have often voiced concern over lack of transparency in the PPP process. PPP agreements are complicated, and are sometimes criticized for lack of transparency. The PPP selection process must be both transparent and confidential, which are important factors for the success of the PPP procurement. Any perceived unfairness and uncertainty in the procurement process will undermine public support for the PPP project, and may lead to litigation. The Virginia DOT has developed a process to review PPP submissions that incorporates public participation. In Virginia, PPPs are reviewed by an independent review panel comprised of various stakeholder groups. Evaluation criteria should be detailed in the enabling legislation and in the RFP and RFQ procurement process.

Protecting confidential information and trade secrets is also a concern. Protecting financial statements, trade secrets, and other commercially sensitive financial information from disclosure is an important issue. Considering a PPP proposal and subsequent negotiations often require revelation of information about corporate finances, strategic business plans, and unique design and technologies. Similar concerns exist under state open records laws. One of the nine exemptions under the Freedom of Information Act (FOIA) covers trade secrets and commercial or financial information, which are privileged and confidential. Under the USDOT Model Legislation, the private bidder designates as confidential or proprietary under the applicable open records law and, to the extent the agency agrees, it will take appropriate action to protect confidentiality. Virginia, Oregon, and Florida have taken specific legislative steps to protect PPP records from public disclosure.[496] Due to the numerous parties involved in these complex negotiations, all should be aware of the requirements of federal and state open record laws.

c. State Approval

Some jurisdictions require that the state legislature or some other public entity review and approve proposed PPP agreements after they have been negotiated and finalized by the various entities. The California statute requires approval by the California Transportation Commission. Such legislative veto powers create uncertainty in the process and discourage PPP development when entities have to incur substantial development costs.

d. Bonding

Performance bonding is an important element in a PPP since it provides the transportation agency with some assurance that a project will be completed if the concessionaire has difficulty. The size of the contracts may preclude or limit small contractor participation. Exorbitant bond premiums can limit bidder participation since only a few companies are able to obtain bonds. Billion-dollar PPP projects are unable to get 100 percent performance bonds. Such bonding, even if available, is very expensive and tends to reduce competition and limit the number of proposers. Accordingly, some public owners have reduced the bonding limit to 50 percent. Less costly letters of credit and other forms of security should be considered in addition to legislative changes to enhance PPP development. The Texas DOT has adopted letters of credit on some of its most recent PPP projects. It should be noted that use of letters of credit may provide the owner with performance protection but do little to protect unpaid subcontractors and suppliers who cannot make demands on the letter of credit.[497] The provisions of the Alaska Way Viaduct DB agreement require Performance and Payment bonds in the amount of $500 million.[498] Changes to state legislation should be considered. By way of example, Missouri passed revisions to its performance bond requirements in order to use design-build-finance-maintain (DBFM) contracts to repair and replace 800 of the state's worst bridges.[499] States need to review their performance and payment bond statutes to determine whether they allow sufficient flexibility so that the private sector can respond if the bonds are not available in the marketplace.[500]

One owner's use of letters of credit, instead of the traditional performance bond, has led to litigation in Ohio. The Ohio State University conducted a pilot program for a construction manager at-risk contract for a medical center expansion. In order to save $12 million in surety bond costs, it required the construction manager to furnish a $20-million irrevocable letter of credit. Several subcontractors' associations and national trade associations commenced suit, seeking to compel the university to require traditional bonding. The Ohio Supreme Court ruled that the surety association had standing to sue, but was not entitled to compel the owner to obtain a surety bond, and that the bond requirement was not applicable under the specific provision of Ohio bidding law.[501]

e. Risk Allocation

[495] BUXBAUM & ORTIZ, *supra* note 428, at 15.

[496] USDOT, *supra* note 456, at 182.

[497] Interview with Nancy Smith of Nossaman Guthner Knox Elliott LLP, Oct. 6, 2011.

[498] State of Washington DOT, SR 099 Bored Tunnel Alternative Design Build Project, § 13.3.

[499] Fishman, *supra* note 425, at 36.

[500] BUXBAUM & ORTIZ, *supra* note 428, at 23.

[501] Anna H. Oshiro & Michael S. Zicherman, *Subcontractor Default Insurance May be Used In Place of Surety Bond*, 31 CONSTRUCTION LAWYER 43, Hard Hat Case Notes (Fall 2011).

Risk allocation is well understood in the traditional procurement. In PPPs, close attention should be paid to risk assignment or transfer. In a traditional public sector design-bid-built project, the public sector makes all the decisions regarding production, financing, operation, and maintenance of the facility. As a result, very little opportunity exists for the private sector to assume project risk. In a PPP, the private sector has greater control over design, construction, operation, and maintenance of the facility and so is able to absorb risk. Some identified risks include: site risks, site preparation (environmental and archeological) risks, land use risks, technical risks, cost overruns, delays in completion, failure to meet performance criteria, and operating cost overruns. Additional potential risks include those involving delays and interruptions in operations, shortfalls in service quality, project acceptance risks, and risks arising from control of assets, political instability, demand/volume, construction costs, right-of-way costs, maintenance costs, transactional costs, currency/exchange, economic shifts, life-cycle costs, and changes of law.[502]

In a PPP, risk should be allocated to the party that can best manage it. Proper allocation of risk will result in lower overall risk for the entire project.

Some of the risks considered to be best handled by the public sector include environmental, right-of-way acquisition, statutory, regulatory, and public acceptance ones.[503] Risks of changes in applicable public law that could have deleterious effects on the private partner's revenues are also often allocated to the public sector partner.

Risks typically transferred to the private sector partner include construction/schedule risks and traffic/revenue risks. It is also common to allocate construction, financial, traffic, revenue, and various other risks to the private sector because they are often in a better position to manage such risks. To the extent that the private entity agrees to finance the construction, or agrees to operate and maintain the facility, his risks include financing risk, traffic risk, and revenue risks.

The parties often share environmental and force majeure risks that are outside the control of either party. The parties also share the opportunity for excess revenue upon the return of total investment.[504]

State DOTs should note that PPPs for major projects are not based on simple, standard form contracts incorporating "boilerplate" language. Instead, they generally require lengthy, complex, project-specific agreements. The drafting and negotiation of such contracts requires specialized legal expertise, cannot be handled by agency non-attorney contracts or administrative staff, and may place heavy demands on agency lawyers put in the position of negotiating with private sector lawyers for commercial toll road operators who have acquired specialized expertise in how to maximize profits while minimizing risks. This may prove especially problematic in states where DOTs do not have their own full-time in-house counsel specializing in transportation issues, but instead depend upon a State Attorney General's Office to provide generalized legal advice and assistance on an as-needed basis.

f. Tort Liability

The potential for unlimited tort liability in the absence of sovereign immunity and other protections available to public agencies is a serious issue and concern to private entities. The Congressional Budget Office noted in 1997 that potential tort liability poses a significant risk to private investors in road projects.[505] Accidents involving deaths, injuries, and environmental damage may result in financial loss to private partners. The public partner may be subject to claims for damages related to design flaws and operation problems. Public partners are often, but not always, protected by sovereign immunity or liability caps imposed by state tort claim statutes.[506] Some private partners mitigate these risks by turning over the operation and ownership to the state once the project is completed, while others rely on insurance coverage, which can be expensive.[507]

Some states have attempted to get the private sector to assume third-party tort liability as part of a PPP agreement road project. However, transferring the risk of tort liability to the private sector may increase the overall risk of the PPP, and may increase its cost and result in a less than optimal deal for the taxpayers.[508]

In Missouri, the legislation for the Mississippi River Bridge PPP project limited tort claims to the sovereign immunity tort caps of the state.[509] Another solution is to avoid the problem by transferring the operation and maintenance of a facility back to the public authority after construction.[510]

g. Noncompete Clauses—SR-91, California

Noncompete clauses provide for protection of future revenue streams when tolls are the finance mechanism. Noncompete clauses limit the public entity's ability to make construction improvements to nearby facilities so as not to erode the demand for the PPP facility.[511] The

[502] BUXBAUM & ORTIZ, *supra* note 428, at 16–17; and USDOT Report to Congress, *supra* note 460, at 60–61.

[503] BUXBAUM & ORTIZ, *supra* note 428, at 18.

[504] FISHMAN, *supra* note 428, at 33.

[505] USDOT Report to Congress, *supra* note 459, at 88.

[506] Notably, while New York State has waived sovereign immunity and allows highway tort claims to be adjudicated by its Court of Claims, it has not imposed any cap upon liability and is exposed to unlimited liability in such cases. Damages awards in individual New York State Court of Claims highway tort claims cases have occasionally exceeded $40 million.

[507] *Id.* at 89.

[508] *Id*. at 62.

[509] FISHMAN, *supra* note 426, at 33.

[510] *Id*.

[511] BUXBAUM & ORTIZ, *supra* note 428, at 32.

classic example most cited is SR-91 in California, wherein the PPP agreement provided that Caltrans agreed not to make improvements within a 1.5 mi "protection zone" of the HOT lanes on SR-91 without consulting the private operator. Later, for safety reasons, Caltrans merged the lanes over the objections of the operator, which led to litigation over the noncompete clause. In 2003 the toll lanes were purchased by Orange County Transportation Authority and the noncompete provision was eliminated.[512]

h. Labor Issues

Labor issues are often topics in PPP agreements. In brownfield projects, labor issues range from displacement of existing workers to concerns about wages, health insurance, and pension and other benefits.

In greenfield projects, the concern relates to the private sector paying prevailing wages. To address such concerns, the Chicago Skyway PPP agreement provided for all contracts to contain prevailing wage language and required the concessionaire to retain all unionized employees.[513]

i. Limits of Liability, Liability, and I/D

Agreements should contain and define liability, indemnification obligations, and insurance requirements for both the public and private entity, and prudent State DOT attorneys should pay close attention to such provisions. Typical agreements also provide for limits of liability to exclude liability for indirect, consequential, or incidental damages whether arising in contract, tort (including negligence), or other legal theory.[514]

These issues are, for example, addressed in the Chicago Skyway agreement. The FHWA Web site describes some of the provisions that are being used.[515]

The Dulles Corridor Metrorail Project agreement limits liability to $500 million from all causes and damages, which include liquidated damages. However the contract excludes from the cap liability for intentional fraud, misconduct, or criminal acts as determined in a court of law.[516] The Dulles Metrorail agreement also contains detailed procedure and indemnification provisions for negligence, recklessness, and willful misconduct; infringement of patented or copyrighted materials; fraud; or intentional misrepresentation, etc.[517] State DOT attorneys may well wish to include consideration of such provisions in PPP agreements.

The PPP for the North Tarrant Express Project in Texas, by contrast, does not include any cap on liability.

The DB agreement for the Alaska Way Viaduct provides for a cap on liability of $5,000,000 with respect to breach of the design-builder's obligation to complete the project and perform warranty work: $500,000.00 with respect to the design-builder's obligation to make payments to all laborers, mechanics, subcontractors, and suppliers; and $100,000.000 with respect to any other cause. In general terms, the cap excludes liability for damage or loss to the extent it is covered by insurance, or any liability for damages arising from fraud, willful misconduct by a DB-related entity, and/or criminal acts by the design-builder.

j. Termination Clauses

Typical termination provisions provide for termination for default and termination for convenience, and contain detailed notice requirements.

PPPs should have clear provisions addressing terminations and hand-back provisions that define the role of all parties to the agreement, as well as protect the public interest. Termination provisions specify how the PPP contractor will be compensated for completed work depending on the reasons for termination.[518]

The PPP agreement should address what happens at the end of the term or upon material default by one of the parties.

With respect to a material default, the public sector needs to ensure it can take prompt and adequate steps to keep the highway facility available and in proper condition for the traveling public in event of material breach or default,[519] while the private entity needs to ensure it has a reasonable opportunity to cure any breach or default. Consideration should be given to providing a dispute avoidance mechanism such as dispute resolution boards in the basic contract to minimize the difficulties that might arise in such potentially contentious situations.

k. Maintenance Standards

Maintenance standards are often incorporated into PPP agreements. The goal of the public sector is to ensure that the leased facility meets or exceeds its maintenance standards. The Chicago Skyway contains 300 pages of detailed extensive terms and maintenance compliance requirements developed by the City of Chicago.[520] In addition to such standards, State DOT attorneys should consider inclusion in PPP agreements of provisions for monitoring, enforcing, and funding future maintenance obligations.

l. Perception of Foreign Control of Local Contractor

[512] *Id*. at 32.

[513] *Id*. at 36.

[514] Amended and Restated Comprehensive Agreement Relating to Route 495 HOT Lanes, Dec. 19, 2007, Virginia Department of Transportation and Capital Beltway LLC, at 122.

[515] *Id*. at 38.

[516] Design Build Contract, Dulles Metrorail Project, Metropolitan Washington Airport Authority and Dulles Transit Partners LLC, May 31, 2007, at 100–103.

[517] *Id*. at 80–83.

[518] BUXBAUM & ORTIZ, *supra* note 428, at 37–38.

[519] FISHMAN, *supra* note 425, at 37.

[520] *Id*. at 10.

Perceptions of foreign control of public assets may lead to national security issues. Many foreign companies have past experience with operating toll roads throughout the world, and they have a strong presence in many PPP agreements, which include the Chicago Skyway, Indiana Toll Road, Trans Texas Corridor, and Pocahontas Parkway in Virginia. As the nation focuses on national security issues, these perceptions of foreign control should be examined to avoid potential problems in the PPP procurement process, particularly where PPP project agreements include long-term leases turning virtually all control over critical state transportation facilities to foreign corporate entities.

m. Use of Proceeds

How the proceeds from a PPP are used is subject to much debate, ranging from use of funds dedicated to future transportation projects, to retiring existing transportation debt (Indiana Toll Road), to addressing general government shortfalls and other government functions (Chicago Skyway).

n. Hand-Back Provisions

At the end of the term the facility, along with the right to collect tolls, reverts back to the public entity. It is the public interest that the facility is in good condition, requiring no more than minimal public investment. The PPP should provide terms and specify the condition for the return, and may include penalties for not meeting these requirements.[521] The detailed hand-back requirements for the Port of Miami Tunnel Project require the concessionaire, at the expiration of the term, to transfer the project to FDOT. The agreement provides for FDOT inspection of the project and requires the concessionaire to diligently perform and complete "renewal work" prior to turn over to FDOT. The agreement establishes a hand-back requirements reserve account or letter of credit, which are anticipated to be used to fund the renewal work required to meet the hand-back requirements.[522]

o. Environmental Liability, Including Preexisting Conditions

Generally in PPP agreements the owner remains responsible for preexisting environmental hazards. The owner becomes the "generator" and has the liability for future hazards. Generally liability for risk of known conditions is given to the private party, while unforeseen and unknown conditions are eligible for some level of compensation, which may involve the concessionaire retaining an initial amount.[523] However the cost of remediation performed by the concessionaire is generally the concessionaire's responsibility and not the owner's.[524] The DB agreement for the Alaska Way Viaduct provides for the owner, the Washington State DOT, to indemnify, protect, and defend the DB-related entities from all third-party claims from the presence of any hazardous materials within the project right-of-way, except for the hazardous material the design builder is responsible for as described in other sections of the agreement. The design-builder shall not be required to execute any hazardous waste manifest as a "generator."[525]

p. Specific Performance as a Remedy

Specific performance is an equitable remedy that could be adopted, but research into specific performance as a remedy for default has shown neither reported cases nor any contract provisions in PPP agreements that refer to this issue.

d. Construction Manager at Risk and CM/GC

The Construction Manager at Risk (CMR) method of construction, also known by FHWA and some states as CM/GC or Construction Manager as Contractor (CMC), is a method of construction procurement and management that seeks to use a team approach among owners, designers, and contractors to optimize the balance between the various objectives of transportation construction projects during planning, design, and construction.[526] This method can be used by public agencies that have statutory authority to contract with a general contractor who then not only acts as the prime contractor but also manages the construction project on behalf of the agency.[527] This type of contract generally includes

[521] BUXBAUM & ORTIZ, *supra* note 428, at 34.

[522] Port of Miami Tunnel and Access Improvement Project, § 6.9-6.10.

[523] Telephone conversation with Patrick Harder, Nossaman Guthner Knox Elliott LLP, Dec. 19, 2011.

[524] Interview with Nancy Smith, Nossaman Guthner Knox Elliott LLP, Oct. 6, 2011.

[525] State of Washington DOT, SR 099 Bored Tunnel Alternative Design Build Project § 18.2.

[526] DOUGLAS D. GRANSBERG & JENNIFER S. SHANE, CONSTRUCTION MANAGER-AT-RISK PROJECT DELIVERY FOR HIGHWAY PROGRAMS, A SYNTHESIS OF HIGHWAY PRACTICE 5 (NCHRP Synthesis 402, Transportation Research Board, 2010); available at http://onlinepubs.trb.org/onlinepubs/nchrp/nchrp_syn_402.pdf, last accessed on Oct. 12, 2011; hereinafter cited as "NCHRP Synthesis 402." This synthesis provides a detailed review of the reasons, procedures, selection methods, preconstruction services, guaranteed maximum prices, quality management procedures, and barriers to implementation associated with CMR, and is a valuable resource for any state DOT evaluating the possibility of trying CMR as a project delivery method. Please note also that NCHRP has undertaken a project, NCHRP 10-85, to develop a Guidebook for Construction Manager-at-Risk Contracting for Highway Projects, initiated in 2011 and scheduled to be completed in 2013, which may provide significant additional information about CMR for state DOTs; *see* http://144.171.11.40/cmsfeed/TRBNetProjectDisplay.asp?ProjectID=2963, last accessed on Sept. 8, 2013.

[527] *See, e.g.*, UTAH STAT. § 63-56-36(2) (2002).

either a fixed price for the construction or a guaranteed maximum price (GMP). In order to contract in this manner, an agency needs express statutory authority to deviate from competitive bidding rules. Such a statute generally authorizes the agency to solicit proposals and select the best proposal, similar to the manner in which it contracts with architects and engineers.

CMR uses somewhat different procurement, design, and construction procedures than the other main methods of construction: DBB, the traditional method required by law in many states and used by the majority of state DOTs, and DB, an innovative method that handles design and construction through a consolidated procurement process and places design and construction under the control of a single firm. CMR appears to offer state DOTs a potentially beneficial choice compared with the existing DBB method or the newer DB method. To explain why, it is necessary to consider some of the principal goals, tradeoffs, and risks involved in transportation construction projects, and the different ways in which the DBB, DB, and CMR methods address these goals, tradeoffs, and risks.

All transportation construction projects have goals involving the speed, quality, and cost of construction.[528] Building projects quickly minimizes the duration of traffic delays and other construction inconveniences to the traveling public and delivers transportation benefits sooner. Building projects to high standards of quality helps to assure the long-term safety, reliability and maintainability of the completed facility or structure. Controlling construction costs helps to keep projects affordable, a particularly significant factor when an agency's fiscal resources are limited.

These three basic goals conflict with each other. As one timeworn aphorism among design engineers has it: "fast, good, cheap—pick any two." Owners and designers face difficult tradeoffs. Emphasizing speed of construction may force a choice between obtaining good quality but incurring high costs, or controlling costs but sacrificing quality. Emphasizing quality may force a choice between building quickly but incurring high costs, or controlling costs but building slowly. Emphasizing cost control may force a choice between building quickly but sacrificing quality, or building well but slowly.

DBB, the traditional method of highway construction used by most state DOTs, seeks to assure quality by having design decisions made by in-house design engineers or highly qualified design consultants, independent of the profit motivations of construction contractors, and to control costs through competitive bidding of the construction work after the design is completed.[529] While supported by clear statutory authority in most states, familiar, and time-honored, this method of construction has a variety of drawbacks. By requiring that the project design be fully completed before the construction work can be bid and the construction work begun, DBB prevents state DOTs from delivering projects more quickly through overlapping the design and construction processes. By maintaining separation between the design engineers and the design process on the one hand and construction contractors and the construction process on the other, DBB may prevent design decisions from giving adequate consideration to factors such as constructability.[530] Design engineers, without access to the practical expertise of construction contractors, sometimes produce designs that are more difficult, expensive, or slow for contractors to build than alternative and equally valid methods which contractors might be aware of. DBB may produce the lowest apparent initial prices through competitive bidding, but this method may give contractors no incentives to keep construction costs under control, and in fact may encourage contractors to maximize profits by seeking change orders (design changes through contract amendments) that will increase their compensation after the initial contract award.[531] By making contractor selection dependent upon the lowest bid, DBB may also tend to award contracts to contractors who aim to meet the minimum contractually required standards, rather than contractors who may do better quality work at the cost of somewhat higher prices.

DB, a widely considered alternative method, seeks to accelerate project completion and control project costs by combining the procurement of design and construction services into a single contract under the control of a single firm. The perceived advantages of the DB method are that it streamlines procurement, allows joint management of and close coordination between designers and builders, speeds project completion through coordinated overlapping of design and construction, and helps to control costs. DB may also involve a variety of disadvantages, however, which are not as widely recognized. DB may require the owner to surrender design control over the project to the DB contractor.[532] DB may also subject decisions by design engineers to financial pressures, although it does not relieve design engineers from exposure to potential legal liability for design decisions. As a result, DB may have the potential to favor speed of project completion, and

[528] GRANSBERG & SHANE, *supra* note 526, at 13, fig. 5, citing D.D. GRANSBERG, J.E. KOCH & K.R. MOLENAAR, PREPARING FOR DESIGN-BUILD PROJECTS: A PRIMER FOR OWNERS, ENGINEERS AND CONTRACTORS (ASCE Press, 2006).

[529] While FHWA does not currently have regulations on CMR, FHWA does require that state DOTs obtain Special Experimental Projects Number 14—Innovative Contracting approval in order to obtain federal-aid funding for projects or programs using CMR; *see* FHWA Construction Program Guide Web page on Construction Manager/General Contractor Project Delivery, http://www.fhwa.dot.gov/construction/cqit/cm.cfm, last accessed on Sept. 8, 2013, which includes a link to information on the SEP-14 approval process. *See also* GRANSBERG & SHANE, *supra* note 526, at 7.

[530] GRANSBERG & SHANE, *supra* note 526, at 7.

[531] *Id*.

[532] *Id*. at 5, 8–9.

control over project costs, over design considerations and construction quality.

1. The Goals of CMR and GC/CM

The CMR method, also known as the General Contractor/Construction Manager (GC/CM) method, while requiring FHWA approval for use on federal-aid transportation projects,[533] seeks to provide the advantages and avoid the disadvantages of DBB and DB through a team approach. The goals and advantages of CMR include the following:

Owner Retention of Design Control—As discussed below, while CMR takes advantage of construction contractors' expertise, it leaves control over design decisions in the hands of the owner and the owner's in-house or consultant design engineers.[534] Design decisions are made for engineering reasons, and not because a construction manager pressured engineers to compromise their judgment and design quality in order to increase the contractor's profits.

Qualification-Based Selection—CMR allows the owner to select the designer and contractor on the basis of qualifications rather than lowest price, while still controlling costs by making use of competitive bidding for selection of trade subcontractors.[535]

Teamwork—CMR seeks to promote teamwork on projects by aligning the interests and goals of the owner, engineering design consultant, and construction contractor to the greatest extent possible, from early in the project through to project completion.[536]

Constructability—CMR enhances project constructability by selecting and retaining a construction contractor early in the project, to provide design engineers with input based on construction expertise from early in the design process, well prior to construction, when design adjustments are quicker, easier, and less expensive to make.[537] This is preferable to waiting until after the project design has been completed to conduct a constructability review, and then offering recommendations requiring extensive, time-consuming, and expensive revisions to project plans. The purpose is to improve the quality of project design, and reduce owners' costs, while also improving contractors' profitability. Through a preconstruction services contract, the owner and designer can also obtain the construction contractor's assistance with scheduling, cost estimating, value analysis, and communications with project stakeholders.[538]

Control of Risks—CMR focuses on identifying and addressing the foreseeable risks of large, complex, and expensive projects; doing so early enough to allow such risks to be controlled through cost-effective methods; and improving predictability by allocating among the parties those risks which cannot be fully avoided. In particular, once design has advanced far enough, the contractor provides the owner with a GMP for construction, including contingencies.[539]

Faster Project Delivery—CMR accelerates project delivery by making it possible to overlap design and construction in a planned and controlled manner, initiating construction of early stages of the project as soon as designs for those stages are complete, and allowing the contractor to lock in favorable prices for materials and equipment as early as possible, even while work on design of later stages of the project continues.[540] As an added benefit, this allows risks to be managed one stage at a time, rather than presenting all parties with the full range of risk from the outset of the project.

Minimization of Disputes—By affording the construction contractor input to the design process from early in the project, CMR allows the contractor to flag potential problems for avoidance or resolution early on, and encourages the contractor to consider the resulting project design a joint effort.[541] CMR also seeks to manage ongoing risks through a collaborative process, rather than pitting the owner and designers against the contractor in an adversarial process. The purpose is not only to anticipate and avoid problems at the design stage, but also to promote teamwork in solving problems encountered in the field in order to reduce disruption, delay, and cost increases during construction.[542]

2. Advantages of CMR Over Design-Build

For owners, CMR offers significant potential advantages over DB.[543] Perhaps the most important of these is that under CMR, the owner retains control over the detailed design of the project, while still achieving cost savings, rather than surrendering control over the design to the design-builder as required under DB.[544] Typically, the owner has separate contracts with a design firm and the contractor, and the contracts require them to consult and cooperate with each other regarding constructability and comparable issues.[545] Like DB, CMR provides the owner with an opportunity to accelerate project delivery through overlapping the design and construction stages of the project.[546] Another advantage for owners is that participation in the design of the project through a CMR preconstruction services agreement encourages the contractor to have a sense of ownership of the resulting design, which may help to minimize disputes between the contractor and the

[533] *Id.* at 1.

[534] *Id*. at 1, 9, 12, 13.

[535] *Id*. at 1, 34–50.

[536] *Id*. at 14–15.

[537] *Id*. at 2, 13–14.

[538] *Id.* at 26, 51–64.

[539] *Id*. at 1, 5, 12, 65–76.

[540] *Id*. at 3, 12, 15, 24.

[541] *Id.* at 16.

[542] *Id*. at 5.

[543] *Id*.at 11.

[544] *Id*. at 5, 9, 12, 13.

[545] *Id*. at 7, 15.

[546] *Id*. at 12, 15.

owner and designer during construction, and make any disputes that do occur easier to resolve.[547] It is possible that owners may find sufficient flexibility under state statutes to implement CMR in states whose statutes do not authorize the use of DB.[548] It also appears possible that consultant engineering design firms may prefer working under CMR to DB, due to their ability to preserve the independence of their professional judgment under CMR rather than being subjected to direct control by contractors' project managers who may not be engineers under DB. For all of the parties involved, owners, designers, and contractors, CMR appears to represent a more incremental change and less of a radical shift from the traditional DBB approach than DB does.[549] This may make it somewhat easier for owners to transition from the traditional DBB approach.

3. State Experience with CMR Procedures

There is considerable variation between states in whether existing statutory authority for transportation construction projects authorizes state DOTs to use CMR as a construction method, and state DOTs considering the possible use of CMR would be well advised to research the scope of their existing statutory authority before undertaking CMR projects.[550] State DOTs having experience with complex and sophisticated construction projects, and having adequate resources, may wish to consider CMR, particularly for large, complex, high-risk, and time-sensitive projects that require complex phasing, and on which value engineering may result in significant cost reductions.[551]

Utah DOT appears to have more experience with use of CMR than most other state DOTs. Utah has a statute authorizing CM/GC projects, and has adopted regulations governing contracting for CM/GC projects.[552] Utah's statute requires that those rules must require competitive selection of the GC/CM, and also that where an additional subcontractor is procured by the GC/CM, it must be publicly bid in the same manner as if the agency were managing the construction.[553] Utah DOT has a CM/GC Web page, has posted sample CM/GC documents on line, and has also posted annual CM/GC reports for 2007 through 2009.[554]

Several other states have at least some experience with CMR. Florida DOT has a CMR Web page, and has posted sample CMR documents online.[555] Oregon DOT performs CMR projects under a state statute authorizing exemptions from competitive bidding requirements under specified circumstances, and a specific exemption issued under that statute for CMR projects.[556] Oregon DOT has constructed a bridge on an Interstate highway using the CM/GC method, and has a Web page for the project on which it has posted various documents used in the RFP process used to select the CM/GC firm for that project.[557] Arizona has enacted a statute governing CMR contracting.[558] In Arizona, the City of Glendale has posted online copies of sample contracts for CMR design-phase services and construction-phase services.[559] Other state DOTs, including Michigan and Rhode Island, have some experience with CMR involving aviation or port facilities rather than highway projects. Alaska DOT reportedly also has some limited experience with CMR.

Two state DOTs, in Nevada and Washington State, have obtained statutory authority to use CMR[560] and are reportedly considering the possibility of CMR pilot projects, but do not yet appear to have any experience

[547] *Id*. at 1, 2, 5, 16.

[548] *Id*. at 6.

[549] *Id*. at 3.

[550] *Id*. at 27.

[551] *Id.* at 27–30.

[552] UTAH STAT. § 63-56-36(2) (2002); UTAH ADMIN. CODE RULE R916-4, Construction Manager/General Contractor Contracts, effective Sept. 1, 2011; available at http://www.rules.utah.gov/publicat/code/r916/r916-004.htm, last accessed on Sept. 8, 2013; as referenced by http://www.fhwa.dot.gov/construction/contracts/cmgc_statutes.cfm, last accessed on Sept. 8, 2013.

[553] UTAH STAT. § 63-56-36(2) (2002).

[554] *See* http://www.udot.utah.gov/main/f?p=100:pg:0:::V,T:,1869; http://www.udot.utah.gov/main/f?p=100:pg:0:::1:T,V:1871,; http://www.udot.utah.gov/main/uconowner.gf?n=113504002204 9311030; and http://www.fhwa.dot.gov/programadmin/contracts/sep14_ut.cfm; last accessed on Sept. 8, 2013; as referenced by http://www.fhwa.dot.gov/construction/cqit/cm.cfm, last accessed on Sept. 8, 2013.

[555] *See* http://www.dot.state.fl.us/construction /CONSTADM/CMatRisk/CMatRisk.shtm, last accessed on Sept. 8, 2013; as referenced by http://www.fhwa.dot.gov/construction/cqit/cm.cfm, last accessed Sept. 8, 2013.

[556] *See* OR. REV. STAT. ORS279C.335, available at http://www.leg.state.or.us/ors/279c.html, last accessed on Sept. 8, 2013. Oregon DOT conducts CMR projects under Exemption No. 2007-51; *see* http://www.fhwa.dot.gov/construction/contracts/cmgc_statutes.cfm, last accessed on Sept. 8, 2013.

[557] *See* http://www.oregon.gov/ODOT/HWY/MPB/WRB.shtml#CM_GC_Procurement_Documents, last accessed on Sept. 8, 2013; as referenced by http://www.fhwa.dot.gov/construction/cqit/cm.cfm, last accessed on Sept. 8, 2013.

[558] ARIZ. REV. STAT. § 28-7366, available at http://www.azleg.gov/FormatDocument.asp?inDoc=/ars/28/07366.htm&Title=28&DocType=ARS, last accessed on Sept. 8, 2013.

[559] *See* http://www.glendaleaz.com/engineering/documents/SampleCMARDesignPhaseServicesContract.pdf, and http://www.glendaleaz.com/engineering/documents/SampleGMPContract.pdf, last accessed on Sept. 8, 2013; as referenced by http://www.fhwa.dot.gov/construction/cqit/cm.cfm, last accessed on Sept. 8, 2013.

[560] The State of Washington statute is Revised Code of Washington (RCW) 39.10.340 through 39.10.410, available at http://apps.leg.wa.gov/rcw/default.aspx?cite=39.10, last accessed on Sept. 8, 2013.

with CMR projects that have gone all the way from inception to completion.[561]

The Washington State statute, originally enacted in 2002, authorizes agencies to use the GC/CM method when implementation of the project involves complex scheduling requirements; the project involves construction at an existing facility that must continue to operate during construction; or the involvement of the GC/CM during the design stage is critical to the success of the project.[562] The statute defines a GC/CM as

> a firm with which a public body has selected and negotiated a maximum allowable construction cost to be guaranteed by the firm, after competitive selection through formal advertisement and competitive bids, to provide services during the design phase that may include life-cycle cost design considerations, value engineering, scheduling, cost estimating, constructibility, alternative construction options for cost savings, and sequencing of work, and to act as the construction manager and general contractor during the construction phase.[563]

Although the statute refers to "formal advertisement and competitive bids," it contemplates an RFP process rather than the traditional invitation for bids and submission of unit price bids. Proposers must compete on the relative superiority of their proposals based on the factors set out in the statute. Evaluation factors include, but are not limited to, the ability of professional personnel, past performance in negotiated and complex projects, and ability to meet time and budget requirements; the scope of work the GC/CM proposes to self-perform and its ability to perform it; location; recent, current, and projected workloads of the firm; and the concept of its proposal.[564] Because the criteria to be evaluated are subjective, a committee process is used to evaluate the proposals. The committee selects the most qualified finalists, which then submit final proposals. The committee selects the firm submitting the highest scored final proposal using the evaluation factors and the relative weight of factors published in the RFP.[565]

Other state transportation agencies are using the CMR approach. For example, the Miami Intermodal Center comprises a multiyear program of ground access to and with Miami International Airport. It incorporates the construction of a new rental car facility comprising space for 10,000 cars, an automated airport people mover, and various roadway improvements to improve airport access. It is being financed by Miami-Dade Expressway Authority toll revenue, TIFIA loans, and federal grants. It is being constructed under the CMR delivery system. The CMR project delivery system provides the opportunity to begin construction, centralize risk and responsibility under one contract, and guarantee completion of the project at a GMP.[566]

State DOTs considering whether to undertake projects on a CMR basis might wish to review the Utah, Florida, and Oregon DOT Web pages on CMR and CM/GC and the sample documents posted on them, and contact those DOTs or other states having CMR experience to benefit from the lessons they have learned through undertaking such projects.

NCHRP Synthesis 402 provides a more detailed examination of models for CMR delivery, which state DOTs considering use of the CMR method should review in considering what approach they might wish to take.[567]

The Associated General Contractors of America (AGC), the national trade association of construction contractors, also offers a CMR Web page[568], which includes a link allowing public owners to purchase the AGC's CM/GC Guidelines for Public Owners,[569] a PowerPoint presentation that includes coverage of CMR,[570] and a map providing information concerning which states currently authorize the use of CMR for horizontal (i.e., highway) construction.[571]

4. CMR Selection Methods

Since an essential element of CMR is the identification, selection, and retention of a construction contractor to perform preconstruction services during the design phase of the project, the use of a "lowest responsible bidder" approach to the selection of the contractor is not suitable for selection of such a contractor. While open public competition through an RFP or comparable process is appropriate, selection of a CMR contractor needs to focus more on the contractor's past project experience, the qualifications of the contractor's personnel, and a demonstrated ability to perform construction projects in a manner reflecting timely, high-quality work delivered within fiscal constraints, rather than merely obtaining the lowest price.[572] NCHRP Synthesis 402 examines CMR contractor selection methods,

[561] GRANSBERG & SHANE, *supra* note 526, at 17–18; for further discussion of state DOT experience with CMR projects, *see* pp. 18 to 26.

[562] WASH. REV. CODE § 39.10.340 (2013).

[563] WASH. REV. CODE § 39.10.210 (2013).

[564] WASH. REV. CODE § 39.10.360 (2013).

[565] *Id.*

[566] *See* FHWA project profile, http://www.fhwa.dot.gov/ipd/project_profiles/fl_95_express.htm.

[567] GRANSBERG & SHANE, *supra* note 526, at 27–33.

[568] *See* http://www.agc.org/cs/cm_atrisk, last accessed on Sept. 8, 2013; as referenced by http://www.fhwa.dot.gov/construction/cqit/cm.cfm, last accessed on Sept. 8, 2013.

[569] http://store.agc.org/Construction-Delivery.

[570] Michael J. Ladino, Esq., Kenneth A. Reedy, P.E., & John E, Carlson, DBIA, Alternate Project Delivery in Horizontal Construction; http://www.agc.org/galleries/projectd/APDM%20in%20Horizontal%20Construction.pdf, last accessed on Sept. 8, 2013.

[571] *See* http://www.agc.org/cs/industry_topics/project_delivery/cmatrisk, last accessed on Sept. 8, 2013.

[572] GRANSBERG & SHANE, *supra* note 526, at 7.

and state DOTs considering use of the CMR method would benefit from evaluation of its findings.[573]

5. CMR Preconstruction Services

Under the CMR method, in addition to assigning in-house design staff or retaining a consulting engineering design firm, the owner typically enters into a preconstruction services agreement with the selected contractor prior to either the completion of design or the commencement of construction, which will be handled under a separate construction contract with the contractor. This allows the owner and the designer to involve the construction contractor during the design phase, take advantage of the contractor's field experience and expertise, and reduce overall design costs through cooperation and collaboration between the owner, designer, and contractor.[574] One of the most important aspects of such collaboration involves drawing on the contractor's input to take considerations of constructability into account and incorporate such considerations into major design decisions as early as possible in the design of the project, avoiding or at least reducing the need to make major design changes later in the project when they would be more disruptive and expensive.[575] NCHRP Synthesis 402 includes detailed discussion of CMR preconstruction services, which state DOTs considering use of the CMR method would benefit from reviewing.[576]

6. CMR Procedures for Setting Maximum Price

Another significant benefit of CMR for owners is that it allows them to protect against cost risks by getting the contractor to make a contractual commitment to a GMP for construction once the design of the project is sufficiently advanced.[577] While this may sometimes be done on a one-time, lump sum basis for construction of the project as a whole, one of the advantages of CMR is that it affords both owners and contractors the flexibility to use progressive rather than lump sum procedures for setting GMP. Basically, the project can be broken into phases, with construction of early phases commenced as soon as designs are completed for those phases, in order to accelerate project completion by allowing construction to begin while work on designing the later phases of the project continues. The construction of each phase can be handled by a separate agreement, or by supplemental agreements to a master agreement, with the owner and contractor agreeing upon a GMP for each individual phase before construction of that phase begins. This allows both the owner and the contractor to use more current information, and affords greater flexibility in managing construction costs as the project progresses, rather than being constrained by a single lump-sum figure determined before any construction has taken place.[578] An additional advantage of the progressive approach to setting GMPs for each phase of the project is that it allows the contractor to lock in current prices for construction materials and services, which can be a significant advantage during periods when prices and costs are rising.[579] NCHRP Synthesis 402 includes an examination of CMR procedures for setting GMPs, which state DOTs considering use of the CMR method should review.[580]

7. CMR Quality Management Procedures

One of the objectives of CMR is to improve project design quality, and avoid or minimize later construction problems, through contractor involvement and collaboration with designers beginning relatively early in the design process.[581] During the construction phase, QC can be handled, under the construction phase contract, in a manner familiar from the traditional DBB process, using DOT in-house or consultant inspectors to perform field inspections and quality assurance (QA) functions and documentation.[582] NCHRP Synthesis 402 includes an evaluation of CMR quality management procedures, which state DOTs contemplating use of the CMR method should consider.[583]

8. Case Law

The CMR or GC/CM method of construction has been the subject of litigation in California, Oregon, and Indiana.

In *City of Inglewood—Los Angeles Civic Center Authority v. Superior Court*, the agency had entered into a contract that was similar to a GC/CM contract. In addition to requiring that the contractor coordinate the solicitation and acceptance of bids and supervise the construction, it also required the contractor to guarantee a maximum price for the entire project.[584] The court held that the contract was not valid. By requiring that the contractor guarantee a maximum price, the agency went beyond the normal responsibilities of a professional such as an engineer or architect. The contract was more in the nature of a prime contract, which had to be competitively bid and could not be negotiated.

However, in cases in which the construction manager's role does not include guaranteeing a maximum price, these arrangements have generally been upheld as legitimate exceptions to the requirements of competi-

[573] *Id.* at 34–50.

[574] *Id*. at 2, 8, 12, 14, 26.

[575] *Id*. at 15, 26.

[576] GRANSBERG & SHANE, *supra* note 528, at 51–64.

[577] *Id*. at 1.

[578] *Id*. at 2, 10, 16, 24.

[579] *Id*. at 3, 12.

[580] *Id*. at 65–76.

[581] *Id* at 77–79.

[582] *Id*. at 79–80.

[583] *Id*. at 77–81.

[584] City of Inglewood - Los Angeles Civic Center Authority v. Superior Court, 7 Cal. 3d 861, 103 Cal. Rptr. 689, 500 P.2d 601 (1980).

tive bidding without specific statutory authority. These arrangements are similar to the GC/CM contract, in that the rationale for the contract appears to be factors similar to those set out in the Washington State GC/CM statute. They are distinct from the GC/CM contract, however, in that the construction manager does not also act as a general contractor and they do not include a fixed price guaranteed by the construction manager.

For example, in *Mongiovi v. Doerner*, the contract was let to a construction manager in a project using a "fast track" method of construction contracting.[585] There was to be no prime contractor; rather, the construction manager was to supervise the solicitation and acceptance of bids and then share supervisory authority over the construction with the architect. The construction manager did not perform any construction work nor did it supply materials. Because the contract involved only professional, personal services, it could be evaluated only by subjective criteria and was therefore held to be exempt from public bidding.

In another case, the hiring of a construction manager was found to be authorized by a school district's statutory authority to hire an architect or engineer to prepare plans, specifications, and estimates and to supervise construction.[586] The district had no statutory authority to employ the GC/CM method, but rather contracted with a construction manager rather than a prime contractor. The construction manager then coordinated the solicitation and acceptance of bids for 27 different school addition projects. The construction manager shared general supervisory authority with the architect during construction. The unsuccessful bidder did not contend that the district could not hire architects and engineers to act as construction managers, but argued that the exception for architects and engineers did not allow the construction management contract to be let without bids. The court held that although the statute allowing the employment of architects and engineers was silent on construction managers, the district had general authority to hire "such other personnel or services, all as the governing board considers necessary for school purposes."[587] The construction manager function was consistent with the authority to hire architects and engineers, and was authorized by this catch-all provision.

4. New Concepts

Other new concepts potentially affecting project delivery are on the horizon, including Integrated Project Delivery, Building Information Modeling, and Design Sequencing.

a. Best-Value Procurement

1. Definition and Process

Best-value procurement can be defined as a process where price and other key factors are considered for evaluation in the selection process, to minimize impacts and enhance the long-term performance and value of the construction. Best-value procurement may encompass many of the concepts from other current procurement methods, which include pre and post qualifications, A+ B bidding, and extended warranties. Best-value procurement is commonly used in DB procurement. The Army Source Selection Guide (Army 2001) defines best value as "the expected outcome of an acquisition that in the Government's estimation provides the greatest overall benefit in response to the requirements."

2. Best-Value Selection for Construction Projects

Shortcomings of the traditional low-bid system have led to increased focus on best-value procurement. The development of best-value procurement borrows ideas and approaches form the private sector. Private sector construction owners have often used best-value selection to obtain the best value for the dollars expended. Best-value selection in negotiated procurement is generally based on numerous factors, which include cost, schedule, quality, safety, and technical ability. Best-value procurement practices are increasingly being adopted by the public sector through legislation.

3. Best-Value Selection in Transportation Projects

FAR Part 15, contracting by negotiation, establishes the best-value source selection process for federal contracts. The process, known as "competitive negotiation," requires the source selection decision to be based on a determination that the selected proposer has offered the best value to the government. For many years, 23 U.S.C. § 112 (b) (3) has required low-bid procurement for most construction projects. With the implementation of the SEP-14 initiative, however, many projects authorized have used the best-value concepts and added to the public-sector body of knowledge. In 1998, Congress acknowledged the need for such alternate procurement and enacted revisions to 43 U.S.C. § 112(b)(3), allowing best-value procurement to be used for DB projects. The American Bar Association (ABA) has published Model Legislation for state and local legislatures to incorporate best-value concepts into the competitive bid process. The Model Code provides a prototype of legislation that allows best value to be considered in awarding construction projects. The ABA model is intended for DB projects, but does permit its use on other projects for which competitive sealed bidding is determined to be impractical and not advantageous to the owner. States that permit consideration of best value in construction procurement currently include Delaware, Colorado, and Kentucky. Legislation in various states is moving towards allowing the use of best-value selection. Many

[585] Mongiovi v. Doerner, 24 Or. App. 639, 546 P.2d 1110 (1976).

[586] Attlin Constr., Inc. v. Muncie Community Schools, 413 N.E.2d 281, 287 (Ind. App. 1980).

[587] *Id*. at 290.

states have passed best-value selection for DB selection. However, beyond DB, other best value statutes have been passed in Colorado, Delaware, and Kentucky. The Colorado and Kentucky laws do not appear to be applicable to DOT projects. The Delaware code allows best-value procurement for large public work projects, with best value determination based on objective criteria outlined in the invitation for bid. The Delaware statute assigns 70 to 90 percent weight to price and 10 to 30 percent to schedule in its evaluation. The agency must rank the bidders according to this criteria and award to the highest ranked bidder. Apart from DB selection, the best-value evaluation and selection process for construction projects has been a topic of several projects that have received SEP-14 approval. The Michigan DOT is using the best-value selection process for the M-39 (Southfield Freeway), wherein the contract will be awarded to the bidder who proposes the best value as determined by a formula that weighs technical score as 40 percent and price as 60 percent. In addition, best-value selection is being implemented for the City of Colorado Springs Woodman Road Widening Project.

4. Best-Value Bid Protests

In certain instances, best-value selections have led to bid protests. By way of example:

Butt Construction—A best value bid protest was commenced by Butt Construction Company, Inc. for renovation work at Wright-Patterson Air Force Base. Butt had submitted a lower cost proposal for the project than Monarch, the firm awarded the contract. The government determined that the proposal submitted by Monarch was technically superior, and that Monarch's experience was sufficient to justify the higher price. The Comptroller General rejected the protest, and noted that the source selection officials had broad discretion to determine the manner and extent of technical and price evaluation.

White Construction—A public owner's decision to award to a bidder other than the lowest bidder has also caused problems in Massachusetts. In September 2000, White Construction, the low bidder on one alternate bid, challenged the award to DeMatteo for renovation of the Tobin Memorial Bridge. Mass. Ann. Laws. ch. 30, § 39M (2000) requires award to the lowest bidder and eligible bidder on the basis of competitive bids publicly opened and read. The public agency in Massport provided for alternate bids and awarded the project to higher bidder DeMatteo, who was the low bidder on the *silica fume concrete alternate.* The Appeals court rejected the protest since White was not the low bidder on all alternates and the owner had the discretion toaward to DeMatteo, who was the lowest bidder on the *silica fume concrete alternative.* The case provides a clear example of giving the owner the discretion to determine that a higher cost alternative is more advantageous than the lowest-priced bid without having to justify its decision with a cost benefit analysis of the alternates.

Minnesota I-35—An important best value selection bid protest decision was handed down in the DB selection for the I-35 Bridge construction project in Minneapolis, Minnesota. In 2007, the Minnesota Legislature enacted DB best value for certain construction projects. On August 1, 2007, the Mississippi River Bridge collapsed, killing 13 people and injuring many others. In recognition of the critical nature for the acquisition of a permanent replacement, the Minnesota DOT conducted DB procurement. The Minnesota DOT utilized a two-step process (RFQ followed by RFP) for selection, adhering to the statutory framework. Flatiron-Manson J.V. (Flatiron) received the highest score, based upon the evaluation by the Minnesota DOT Technical Committee. Plaintiffs commenced a bid protest, which was denied by the agency decision, and the contract was later awarded to Flatiron. Litigation for injunctive relief was commenced on October 16, 2007, but the requested injunction was denied on October 31, 2007. Flatiron then proceeded with the construction of the new bridge. Plaintiffs appealed the order to the Court of Appeals on November 7, 2007, which was ultimately dismissed December 11, 2007. The litigation returned to the District level. On July 16, 2008, Plaintiffs filed a motion for a temporary injunction against seeking to enjoin the reconstruction of the I-35 Bridge by Flatiron, asserting that the Flatiron contract was illegal since it was not responsive to the RFP in that it proposed work outside the right-of-way and did not comply with the two webs-per-girder requirement. The District Court on August 26, 2008, recognized that the project had a substantial completion date of September 24, 2008, and was nearly complete. The District Court rejected appellants' argument that the winning bid was not responsive. The Court of Appeals affirmed the District Court decision, holding that the common law definition of "responsiveness" does not apply to DB best-value procurement process and that the Minnesota DOT Technical Committee acted within its discretion when it determined Flatiron was responsive. The court affirmed the best-value selection that was at greater cost based on the exercise of discretion by the construction agency.

b. Integrated Project Delivery (IPD)

1. Definition—Enhanced Collaboration.—Integrated Project Delivery (IPD) is a collaborative approach to project delivery. It is a major paradigm shift under which multiple parties, including the owner, designer, contractors, and major suppliers, enter into one contract. The principles behind this approach require the parties to provide inputs at all stages of construction, and to share the risks and rewards of their collaborative efforts. IPD is founded on principles of trust, mutual respect, and mutual benefit and reward. The principles of IPD include collaborative decision-making, early involvement of key project participants, early goal definition, and intensified planning.[588] IPD principles

[588] NATIONAL ASSOCIATION OF STATE FACILITIES ADMINISTRATORS (NASFA), CONSTRUCTION OWNERS

also include key participants bound together as equals, shared risk and reward based upon project outcome, liability waivers between key participants, fiscal transparency, intensified design, jointly developed project target criteria, collaborative decision-making and open communication.

IPD envisions a contractual model under which the owner, constructor, designer, and potentially others enter into a single multi-party contract. The multi-party agreement also provides for management of the project to be governed by a committee that strives for unanimous decision-making. The parties may adopt some of the IPD principles without formally adopting a multi-party contract. "Lean" construction principles, multi-party agreements, and building information modeling (BIM) are often incorporated into the IPD arrangement.

The "lean" construction movement is based on applying principles of lean manufacturing in the design, engineering, and construction of capital projects. "Lean" provides planning tools and mechanisms to maximize value and minimize waste throughout the life cycle of the project. Tools and techniques involve target value design, setting base design, and a detailed planning structure such as the "Last Planner System," which brings together design team leaders and trade foremen for frequent collaborative meetings wherein each group makes reliable promises regarding future work efforts.[589]

The principles of the multi-party contract require full and open communication; an incentive compensation structure; active collaboration among the owner, constructor, and designer; and appropriate limitation of liability for the design and construction team. The IPD concept has been adopted in hospital construction and is being given active consideration and analysis by public owners such as Massachusetts DOT. IPD principles are also being given attention by the Division of Capital Asset Management of the Commonwealth of Massachusetts.[590]

2. BIM.—Digital technology has changed many aspects of today's design and construction process. Digital drawing and models serve as shared resources for information about a facility, forming a reliable basis for decisions from inception through award and final construction. BIM software permits collaboration by various stakeholders at different phases of the life cycle of the facility to insert, extract, update, and modify information in the building information model. BIM is a tool, not a delivery method, and is quite powerful when the entire project team can see the impact of decisions instantly and comprehensively upon constructability and schedule. BIM has become an essential element of collaborative project delivery.[591]

c. Design Sequencing —Caltrans

In California, Caltrans experimented with design sequencing in several projects before the advent of DB authority. Design sequencing may be an option for those transportation agencies that lack DB authority.

In Design sequencing, the agency prepares the design in phases that will allow the start of construction when the design phase is complete. The agency delivers the remaining phases of design at predetermined dates after construction has started. The bid documents contain all necessary items, but do not contain completed estimates since the design has not been completed.[592]

The advantages include faster project delivery. Disadvantages include agency retention of the risk, and potential for construction inefficiency owing to conflicting or overlapping work between the initial sequence and subsequent sequences, unforeseen site conditions, and third-party conflicts during construction.[593]

C. ELEMENTS OF THE PUBLIC CONSTRUCTION CONTRACT

1. Agency's Responsibility for Contract Plans, Specifications, and Technical Information

a. Requirement for Detailed Plans and Specifications

A common feature of state competitive bidding requirements is that contracting agencies prepare plans and specifications for their construction projects.[594] In addition, they must make these documents available to prospective bidders, along with other documentation to assist bidders in preparing and submitting proposals.[595] Even without being specifically required by legislation, the agency's obligation to furnish detailed plans and specifications arises as a necessary implication of the requirement for competitive bidding. The objective of this policy cannot be achieved unless bidders are sufficiently well informed of the plans and specifications of the job to permit them to prepare their proposals intelligently and correctly. Whether based on statutory language or implications, the duty to provide definite plans, specifications, and technical information is

ASSOCIATION OF AMERICA (COAA), ASSOCIATION OF HIGHER EDUCATION FACILITIES OFFICERS, ASSOCIATED GENERAL CONTRACTORS OF AMERICA (AGC), and AMERICAN INSTITUTE OF ARCHITECTS (AIA), INTEGRATED PROJECT DELIVERY FOR PUBLIC AND PRIVATE OWNERS 3 (2010).

[589] 2011 Construction Law Update, Aspen Publishers, at 20–23.

[590] INTEGRATED PROJECT DELIVERY, *supra* note 588, at 31.

[591] *Id*. at 18–19.

[592] ANDERSON & DAMNJANOVIC, *supra* note 399, at 20.

[593] *Id*. at 21.

[594] Portions of this section are derived from *Competitive Bidding and Award of Highway Construction Contracts* by Dr. Ross D. Netherton, published by the Transportation Research Board in 1976 and included in the first edition of SELECTED STUDIES IN HIGHWAY LAW, vol. 3, p. 1125: supplemental, *Id*. at 1214–51.

[595] *See*, *e.g.*, WASH. REV. CODE § 47.28.040 (2002).

strongly rooted in public policy and is consistently enforced by the courts.[596]

Standard specifications published by the various state transportation agencies show a similar pattern of statements relating to the interpretation of plans, specifications, and technical information, in some instances going so far as to require bidders to examine the site of the proposed work as well as the technical documents describing the work required. Notwithstanding these disclaimers, state statutes emphasize the goal of opening up the bidding process to competition among all bidders on equal terms, including information about the job.

When courts have been called on to determine whether this duty has been met, they have adopted the same pragmatic approach. When the situation did not readily permit more precision or detail, they have found that the duty has been met by "substantial compliance."[597] In one case, the Minnesota court was concerned with the actual effect of the language on the bidder's ability to write its proposal:

> The court has found that the plans and specifications were sufficiently definite and precise to afford a basis for competitive bidding. Witnesses for the respective parties differed as to the range above the minimum of 1200 horsepower that would be reasonable. They all admitted that some range would be reasonable. The question was one of fact, and the evidence sustains the court's finding.[598]

Specifications that do not suffer from vagueness could, at the other extreme, become so restrictive as to preclude effective competition among bidders. However, the discretion of the contracting agency in drafting specifications for work normally will not be overruled unless it is shown to be arbitrary, oppressive, or fraudulent.[599]

The form and style in which plans, specifications, and technical information are prepared are influenced more by industry customs and agency practices than by conventions and case law. In many projects, each phase of the construction—such as earthwork, concrete, structural steel, masonry, and carpentry—is treated in a separate section of the bid documents. Likewise, equipment and machinery used in the work will be described separately, and each category of basic materials will have its own section. Although no fixed rules prescribe the organization of these elements, there is a preference for arranging them as closely as practicable to the sequence of the construction operations. In all cases the drafter should bear in mind that the method used must present the plans and specifications in a manner that enables any bidder relying on them to determine what is required in all-important details of the work.

In preparing project plans and specifications, the drafter must also consider how the description of materials and methods will facilitate the inspection and testing that is required during the construction and prior to acceptance of the finished work. For projects involving major highways or structures, there is no practical way to determine by a single test or series of tests of the finished work whether it will perform its intended function throughout its expected service life. Therefore, it is customary to control the quality of materials and workmanship by testing components as they are assembled and installed. For most types of materials and construction, contracting agencies use standard specifications and test procedures. In this published form, they are incorporated by reference into project plans and specifications, subject to the special provisions or modifications for the project.

Where contracts do not involve subject matter that is unusual or complex, and advertisements for bids omit pertinent features or descriptive information, courts tend to take a pragmatic approach and accept substantial compliance where the defective specification does not result in any practical disadvantage in preparing or evaluating bids.[600] A similar standard was applied in a case in which a document was identified as "plans," even though it did not meet the technical definition of plans. The court found that the information included in the document provided boundaries, contents, and test results of borrow pits, and was provided to bidders to provide foundation material for the preparation of bids. It was thus considered part of the agency's "plans and specifications" on which the bidders were entitled to rely, even though it did not meet the definition of "plans" in the standard specifications.[601] However, in another case, where an agency specifically stated in the bid documents that pit test data was provided for information only and was not a special provision, the court held that the agency did not provide any warranty with the information. Rather, the contractor was required to determine for itself the nature of the material in the gravel pits and was not entitled to rely on the information.[602]

The same applies where bidders charge that a contracting agency has failed to furnish the latest and best technical information available. The limits of a contracting agency's duty in this regard are illustrated

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[596] Sullivan v. State through Dep't of Transp. and Dev., 623 So. 2d 28, 30 (La. App. 1 Cir. 1993).

[597] Scanlan v. Gulf Bitulithic Co., 44 S.W.2d 967, 970 (Tex. Comm'n App. 1932) (in order for specifications to be invalid, must be more than "deficient in the most trivial respect").

[598] Otter Tail Power Co. v. Village of Elbow Lake, 234 Minn. 419, 425, 49 N.W.2d 197, 202 (1951).

[599] *See infra* note 758 and accompanying text.

[600] Publantation on the Green, Inc. v. Gamble, 441 So. 2d 299, 304 (La. App. 1983) (description of land by address and location within a larger public facility approved); Platt Electr. Supply, Inc. v. City of Seattle, Div. of Purchasing, 16 Wash. App. 265, 555 P.2d 421, 430 (1976) (failure to describe warranty or method of implementing warranty).

[601] Jack B. Parson Constr. Co. v. State, by and Through Dep't of Transp., 725 P.2d 614, 616 (Utah 1986).

[602] Mooney's, Inc. v. South Dakota Dep't of Transp., 482 N.W.2d 43, 46 (S.D. 1992).

where a union that had members who would have been hired by a bidder complained that the agency did not notify bidders of a forthcoming change in the official wage determination so that it could be reflected in bidding on a federally funded construction project. The court dismissed the complaint with the following observation:

> The plaintiff would expand [the highway] administrator's duty…compelling him to keep one ear pressed on the walls of the Department of Labor's Wages and Hours Division, straining to hear of prevailing wage modifications…as yet unborn, but which might issue within days or hours of an opening of bids. No such burden is imposed by [the law] as presently written, and none shall be manufactured by this court.[603]

Where the technical information in question is in the form of governmental actions, prospective bidders must, along with the rest of the public, monitor the official newspapers or publications where the information is announced.

An agency has no duty to disclose to bidders on a construction project facts in its possession when its superior knowledge or silence would convey a false impression, where the agency has made no affirmative misrepresentation.[604] The agency has a duty only to provide bidders with information that will not mislead them.

Where a bid item is left out of the bid specifications, the agency may be found to have failed to provide sufficiently definite plans and specifications for the contract.[605] In such a case, the agency will be liable for any additional costs incurred by the contractor in providing that item of work.

In addition to bidders, subbidders are entitled to rely on the plans, specifications, and other bid documents that are in existence at the time that their subbids are prepared.[606]

b. Responsibility for Accuracy of Specifications

When the agency sets out detailed plans and specifications for the construction of a public project, it warrants that those plans and specifications are adequate. The agency will thus bear the loss resulting from inadequate or inaccurate plans or specifications. The leading federal case on this issue is *United States v. Spearin*, a 1918 case that involved construction of a dry dock at the Brooklyn Naval Shipyard.[607] The dry dock construction necessitated relocation of a sewer line, which the contractor completed. A subsequent storm event caused failure of the sewer line due to the presence in the line of a dam that was not shown on the government's plans, and resulted in flooding of the area excavated for the dry dock. The contractor refused to rebuild the sewer, and it was unsafe to continue working in the area without doing so. The government then terminated the contract. The contractor sued for and recovered its lost profits. The United States Supreme Court held that the government was responsible for the accuracy of its specifications: "I[f] the contractor is bound to build according to plans and specifications prepared by the owner, the contractor will not be responsible for the consequences of defects in the plans and specifications."[608]

Further, the Court held that this responsibility was not overcome by the contractor's duty to inspect the site and to check the plans.

> [T]he insertion of the articles prescribing the character, dimensions, and location of the sewer imported a warranty that, if the specifications were complied with, the sewer would be adequate. This implied warranty is not overcome by the general clauses requiring the contractor, to examine the site, to check up the plans, and to assume responsibility for the work until completion and acceptance.[609]

In other words, the duty to inspect the site did not include a responsibility to check it in such detail, including a review of the history of the site, so as to determine the presence of the dam located inside the sewer. The contractor was entitled to rely on the government's plans as being accurate and complete and as giving it sufficient information to build what was contemplated. The government was required to bear the loss for its plans being insufficient, as it was considered to have misrepresented the site conditions.

The contractor is not liable for any defects in the project built if the defects resulted from the plans and specifications furnished to the contractor.[610] This rule, known as the doctrine of constructibility, or the implied warranty of constructibility, is not negated by the provision of a changes clause that allows for alterations in the plans and specifications.[611]

A Florida court applied the doctrine of constructibility, or the *Spearin* doctrine, in a case that involved

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[603] Operating Eng'rs Local Union No. 3, Int'l Union of Operating Eng'rs v. Hurley, 546 F. Supp. 387, 390 (D. Utah 1982).

[604] Hendry Corp. v. Metropolitan Dade County, 648 So. 2d 140, 142 (Fla. App. 3 Dist. 1994) (DSC clause will be triggered only where there has been an inaccurate representation that is relied on, not where there has been no representation).

[605] Sullivan v. State, Through Dep't of Transp. and Dev., 623 So. 2d 28 (La. App. Cer. 1993) *writ denied*, 629 So. 2d 1179 (La. 1993).

[606] J.F. White Contracting Co. v. Department of Public Works, 24 Mass. App. Ct. 932, 508 N.E.2d 637, 639, *review denied*, 400 Mass. 1104, 511 N.E.2d 620 (1987).

[607] 248 U.S. 132, 39 S. Ct. 59, 63 L. Ed. 166 (1918); *see also* K. Golden and J. Thomas, *The Spearin Doctrine: The False Dichotomy Between Design and Performance Specifications*, 25 PUB. CONT. L.J. 47–68 (1992).

[608] *Spearin*, 248 U.S. at 136 (citations omitted).

[609] *Id*. at 137 (footnotes omitted).

[610] O&M Constr., Inc. v. State, Division of Admin., 576 So. 2d 1030, 1039–40 (La. App. 1 Cir. 1991), *writ denied*, 581 So. 2d 691 (1991).

[611] Gilbert Pacific Corp. v. State by and Through Dep't of Transp., Comm'n., 110 Or. App. 171, 822 P.2d 729, 732 (Or. App. 1991), *review denied*, 830 P.2d 596.

fence construction along an Interstate highway, *Phillips & Jordan, Inc. v. State, Department of Transportation*.[612] The court held that the rule that the agency is liable for unanticipated construction costs due to a latent defect in the plans and specifications did not apply. The plans and specifications had provided for clearing and grubbing of a 10-ft wide strip along the highway. They did not specify what equipment should be used. The contractor found that the brush in the area was so dense that it needed to use heavier equipment for the clearing, and that equipment used 12-ft wide blades. The result was that the contractor ended up clearing a larger area than called for in the contract, and the Florida Department of Transportation refused to pay for the extra area.

The court held that there was not a latent defect in the plans. The contractor was aware of the site conditions, and knew that its equipment of choice would clear an area more than 10-ft wide. It submitted its bid with full knowledge of these facts, and could not later claim that there was a latent defect.[613]

i. Duty to Inquire Re Patent Defects or Ambiguities.— An exception to the general rule that the awarding agency warrants the adequacy of its design specifications is the principle that a contractor has a duty of inquiry with respect to a patent defect or ambiguity in the contract.[614] This duty of inquiry is created regardless of the reasonableness of the nondrafting party's interpretation of the contract.[615] A bidder has the duty to scrutinize the bid solicitation for potential problems prior to bidding.[616] Upon finding an ambiguity, the contractor is charged with asking the contracting officer the true meaning of the contract. However, the contractor must inquire only as to major discrepancies, obvious omissions, or manifest conflicts in the contract provisions.[617] If the contractor fails to seek clarification of a patent ambiguity prior to submitting its bid, then it bears the risk of misinterpretation.[618]

One court has explained the reason for the doctrine of patent ambiguity as follows:

> If a patent ambiguity is found in a contract, the contractor has a duty to inquire of the contracting officer the true meaning of the contract before submitting a bid. This prevents contractors from taking advantage of the Government; it protects other bidders by ensuring that all bidders bid on the same specifications; and it materially aids the administration of Government contracts by requiring that ambiguities be raised before the contract is bid on, thus avoiding costly litigation after the fact....[619]

If different interpretations of a contract are plausible, then the court will inquire as to whether the discrepancy would be apparent to the reasonably prudent contractor. It is not the contractor's actual knowledge but rather the obviousness of the inconsistency under an objective standard that imposes the duty to make inquiry.[620] The contractor's failure to notice an obvious ambiguity does not excuse the duty of inquiry.[621] However, the contractor's actual knowledge of an ambiguity is sufficient to create the duty of inquiry.[622]

The purpose of allocating to contractors the burden to inquire about patent ambiguities is to allow the agency to correct any errors before contract award, and to ensure that all contractors bid on the basis of identical specifications.[623] In providing an interpretation to the inquiring contractor, the response would be sent to all holders of bid packages so that all bidders have the benefit of the agency's interpretation. An essential element of public bidding is a common standard of competition among bidders. All conditions and specifications must apply equally to all prospective bidders, thus permitting contractors to prepare bids on the same basis.

> It is to assure a level playing field that contractors are urged in bid documents to examine the documents thoroughly, make site visits, attend prebid conferences, and raise questions about the drawings, specifications and conditions of bidding and performing the work. To every extent possible, such questions should be addressed before bid opening.[624]

Where the contract contains an order of precedence clause, the contractor is entitled to rely on the representation in the document that has higher precedence, and is not required to resolve a patent discrepancy between that document and one of lower precedence.[625] Generally, specifications will be identified in an order of precedence clause as governing over drawings where there is a discrepancy between the two. The clause is designed to excuse reporting of a patent ambiguity. It automatically removes the conflict *between* specifications and drawings by assigning precedence to the specifications.[626] However, discrepancies *within* either specifications or drawings must still be reported.

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[612] 602 So. 2d 1310 (Fla. App. 1 Dist. 1992).

[613] *Id*. at 1313.

[614] Department of Transp. v. IA Constr. Corp., 138 Pa. Commw. 587, 588 A.2d 1327, 1330 (1991).

[615] International Transducer Corp. v. United States, 30 Fed. Cl. 522, 527 (1994), *aff'd*, 48 F.3d 1235 (1995).

[616] Avedon Corp. v. United States, 15 Cl. Ct. 771, 777 (1988).

[617] *Id*.

[618] Delcon Constr. Corp. v. United States, 27 Fed. Cl. 634, 638 (1993).

[619] Newsome v. United States, 230 Ct. Cl. 301, 676 F.2d 647, 649 (1982) (footnotes omitted).

[620] Maintenance Eng'rs, Inc. v. United States, 21 Cl. Ct. 553, 560 (1990).

[621] *Id*.; *see also* Troise v. United States, 21 Cl. Ct. 48, 58 (1990).

[622] D'Annunzio Bros., Inc. v. N.J. Transit Corp., 245 N.J. Super. 527, 586 A.2d 301, 303–04 (1991).

[623] *Id.* at 304.

[624] *Id.* at 304 (citing Collins Int'l Serv. Co. v. United States, 744 F.2d 812, 814 (Fed. Cir. 1984)).

[625] Hensel Phelps Constr. Co. v. United States, 886 F.2d 1296, 1299 (Fed. Cir. 1989).

[626] *Id*. at 1298.

Whether the implied warranty of constructibility applies to specifications depends on whether they are design specifications or performance specifications. In making this determination, one must consider the language of the contract as a whole; the nature and degree of the contractor's involvement in the specification process; the degree to which the contractor is allowed discretion in carrying out performance of the contract; and the parties' usage and course of performance of the contract.[627]

ii. Design Specifications.—The contractor's claim of defective design specifications is based on the *Spearin* principle that there is an implied warranty that design specifications, if followed, will lead to a successful product. A design specification is one that sets out in precise detail the materials to be used and the manner in which the work is to be performed.[628] The contractor has no discretion to deviate from a design specification.[629] The contractor bears the burden of proving that a design specification is defective and that the defect cause the contractor's difficulties.[630] Design specifications contain the implied warranty under *Spearin* that if they are followed an acceptable product will result.[631]

iii. Performance Specifications.—Performance specifications set forth objectives to be achieved, and the successful bidder is expected to exercise its ingenuity in achieving that objective, selecting the means and methods of accomplishing it, and assuming responsibility for that selection.[632] Performance specifications do not contain any implied warranty of constructibility.[633] Only an objective or standard of performance is set out in the contract.[634] Along with control over the choice of design, methods, and materials, there is a corresponding responsibility to ensure that the end product performs as the agency desires. The contractual risk of nonperformance is thus on the contractor.

For highway and bridge construction undertaken directly by the federal government and by state agencies under federal-aid funding programs, standard specifications for materials and workmanship provide accepted criteria for preparation of bids and, subsequently, evaluation of results. However, specifications expressed in terms of overall performance may still be used for certain items of equipment or machinery that may readily be tested prior to use by the contractor. Various types of heavy equipment, pumps, motors, generators, and other accessories may be considered as being necessary to qualify a contractor for particular work. In such cases, performance specifications for these items are frequently used, sometimes in conjunction with the additional requirement that the equipment or other items be warranted by the contractor or manufacturer to perform as proposed.

c. Use of Requests for Proposals

Statutes allowing the use of a request for proposals may allow more latitude to the agency in setting the requirements for bidding.[635] For example, a county was found not to have violated the competitive bidding requirement for a performance bond where it used a request for proposals and limited participation to only those firms that had substantial financial resources, thereby providing reasonable assurance to the county to secure performance.[636] Whether such deviations from basic public works project requirements will be allowed will depend on how broadly those requirements are written and on whether the authority allowing the use of requests for proposals allows those deviations.

Many states' transportation agencies have obtained statutory authority to use DB contracting, in which the contractor assumes responsibility for both design and construction. These statutes allow the use of requests for proposals as an alternative to competitive bidding, recognizing the need to evaluate the qualifications of the DB team in the same manner that other engineering contracts are evaluated.[637]

2. Required Federal Clauses

Any state DOT undertaking federal-aid highway and bridge construction contracts should become familiar with the provisions of 49 C.F.R. § 18.36, a USDOT regulation establishing detailed requirements governing procurement methods and procedures that state DOTs must comply with on federal-aid projects, or risk losing federal-aid funding for those projects.

One of that regulation's subsections, 49 C.F.R. § 18.36(i), sets forth provisions that federal-aid contracts must contain. As of 2011, these mandatory contract provisions include:

- All contracts above the simplified acquisition threshold must include administrative, contractual, or legal remedies in instances where contractors violate or breach contract terms, and provide for such sanctions and penalties as may be appropriate.

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[627] Fruin-Colnon Corp. v. Niagara Frontier Transp. Auth., 180 A.D. 2d 222, 585 N.Y.S.2d 248, 253–54 (1992).

[628] Fla. Board of Regents v. Mycon Corp., 651 So. 2d 149, 153, *rehearing denied* (Fla. App. 1 Dist. 1995).

[629] Blake Constr. Co. v. United States, 987 F.2d 743, 745, *rehearing denied* (Fed. Cir. 1993), *cert. denied*, 510 U.S. 963, 114 S. Ct. 438 (1993); John Massman Contracting Co. v. United States, 23 Cl. Ct. 24, 32 (1991).

[630] Edward M. Crough, Inc. v. Department of General Services of District of Columbia, 572 A.2d 457, 468 (1990).

[631] *Blake Constr. Co.*, 987 F.2d at 745.

[632] *Id.*

[633] John Massman Contracting Co. v. United States, 23 Cl. Ct. 24, 32 (1991).

[634] Fruin-Colnon Corp., Traylor Bros, Inc. and Onyx Constr. & Equipment, Inc. v. Niagara Frontier Transp. Auth., 180 A.D. 2d 222, 585 N.Y.S.2d 248, 253 (1992).

[635] *See* ABA Model Code, *supra* note 60, at § 3-203.

[636] Stapleton v. Berks County, 140 Pa. Commw. 523, 593 A.2d 1323, 1331, *appeal denied*, 604 A.2d 251, 529 Pa. 660 (1991).

[637] *See* notes 311 through 318 and accompanying text.

• All contracts in excess of $10,000 must include provisions for termination for cause and for convenience by the grantee or subgrantee, including the manner by which termination will be effected and the basis for settlement.

• All construction contracts in excess of $10,000, including all subcontracts in excess of $10,000 issued under such contracts, must include Equal Employment Opportunity (EEO) provisions in compliance with Executive Order 11246 of September 24, 1965, entitled "Equal Employment Opportunity," as amended by Executive Order 11375 of October 13, 1967, and as supplemented in Department of Labor regulations (41 C.F.R. Chapter 60).

• All contracts and subcontracts for construction or repair must include provisions in compliance with the Copeland "Anti-Kickback" Act (18 U.S.C. 874) as supplemented in Department of Labor regulations (29 C.F.R. Part 3).

When required by federal grant program legislation, all contracts for construction in excess of $2,000 must include federal prevailing rate provisions in compliance with the Davis-Bacon Act (40 U.S.C. 276a to 276a–7) and U.S. Department of Labor regulations (29 C.F.R. Part 5).

• All construction contracts in excess of $2,000, and any other contracts involving the employment of mechanics or laborers in excess of $2,500, must include provisions in compliance with Sections 103 and 107 of the Contract Work Hours and Safety Standards Act (40 U.S.C. 327–330) as supplemented by Department of Labor regulations (29 C.F.R. Part 5).

• All contracts must include notice of awarding agency requirements and regulations pertaining to reporting.

• All contracts must include notice of awarding agency requirements and regulations pertaining to patent rights with respect to any discovery or invention that arises or is developed in the course of or under such contract.

• All contracts must include awarding agency requirements and regulations pertaining to copyrights and rights in data.

• All contracts must include provisions requiring access by the grantee, the subgrantee, the federal grantor agency, the Comptroller General of the United States, or any of their duly authorized representatives to any books, documents, papers, and records of the contractor that are directly pertinent to that specific contract for the purpose of making audit, examination, excerpts, and transcriptions.

• All contracts must require retention of all required records for 3 years after grantees or subgrantees make final payments and all other pending matters are closed.

• All contracts and subcontracts in excess of $100,000 must include environmental provisions requiring compliance with all applicable standards, orders, or requirements issued under Section 306 of the Clean Air Act (42 U.S.C. 1857(h)), Section 508 of the Clean Water Act (33 U.S.C. 1368), Executive Order 11738, and Environmental Protection Agency regulations (40 C.F.R. Part 15).

• All contracts must include provisions on mandatory standards and policies relating to energy efficiency, which are contained in the state energy conservation plan issued in compliance with the Energy Policy and Conservation Act (Pub. No. L. 94–163, 89 Stat. 871).

In addition to the above, 23 U.S.C. § 112(e) and 49 C.F.R. § 18.36(r) require that all highway and bridge construction contracts include standardized contract clauses concerning site conditions, suspension of work, and material changes in the scope of work for highway construction contracts. These requirements are discussed further below.

The latest information regarding the impact of the 2012 enactment of the new MAP-21 federal surface transportation funding legislation, applicable by its terms to projects from July 2012 through the end of FY 2014 in September 2014, upon the above requirements for inclusion of specified clauses in federal-aid projects, or adding any new required clauses, can be found on FHWA's Web site.[638]

a. Clauses Required in Form FHWA-1273

Since 1994, FHWA has also had a standard form document, form FHWA-1273, "Required Contract Provisions Federal-Aid Construction Contracts," which it requires state DOTs to incorporate into federal-aid state highway and bridge construction and reconstruction projects, and to physically include in every federal-aid transportation project construction contract. While the 2014 update to this current volume was in preparation, FHWA undertook a federal rulemaking proceeding to revise form FHWA-1273. Commenced in January 2012, this was concluded with a June 2012 notice of final action, adopting the revised form to be effective on a mandatory basis on and after August 9, 2012.[639] As this form may be revised again from time to time in the future, practitioners are advised to check FHWA's Web site periodically for any further revisions.

This form is viewable on FHWA's Web site, and can also be downloaded as a PDF file.[640] The form requires that its provisions must be set out in full and cannot be incorporated by reference, and that breach of any of the

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[638] FHWA, Moving Ahead for Progress in the 21st Century Act (MAP-21), A Summary of Highway Provisions, July 17, 2012, http://www.fhwa.dot.gov/map21/summaryinfo.cfm, last accessed on July 25, 2012.

[639] FHWA Docket No. FHWA-2011-0122, Revision of Form FHWA-1273; NPRM 77 Fed. Reg. 4880 (Jan. 31, 2012); Notice of Final Action, 77 Fed. Reg. 37954 (June 25, 2012); mandatory effective date of new form, Aug. 9, 2012. For links to the NPRM, Notice of Final Action, and other related materials, see http://www.fhwa.dot.gov/programadmin/contracts/1273/, last accessed on July 25, 2012.

[640] http://www.fhwa.dot.gov/programadmin/contracts/1273/1273.pdf, last accessed on July 25, 2012.

requirements may be grounds for termination of the contract.[641] Further, breach of specific sections may be considered grounds for federal debarment. Since the form is lengthy and its provisions are detailed, they will not be summarized here in any detail. In general terms, they cover the following, but state DOTs should review the form itself, including any updates on FHWA's Web site, for the details:

- General provisions, including requirements governing subcontracts as well as contracts.
- Nondiscrimination provisions, including lengthy and detailed EEO and DBE provisions. Part II of Form FHWA-1273 covers in detail the nondiscrimination requirements applicable to all federal-aid contracts, including equal employment opportunity, DBE requirements, and record keeping requirements. This is discussed in more detail in Section 4.
- Provisions requiring nonsegregated facilities and prohibiting segregated facilities. Part III contains strict requirements for nonsegregated facilities, one of which is that the contractor and its subcontractors certify to FHWA that they do not utilize segregated facilities. A breach of this certification will be considered a violation of the EEO provisions.
- Labor standards that must be addressed include the agreement to refrain from discrimination against labor from other states and not to employ convict labor, with the exception of convicts on parole, probation, or work release.[642]
- Provisions on payment of predetermined minimum wages, in accordance with the Davis-Bacon Act and U.S. Department of Labor regulations, including maintenance of payroll records so that prevailing wages may be verified.[643] Part VIII requires adherence to applicable federal, state, and local laws governing health, safety, and sanitation.
- Provisions requiring submission of statements of compliance and maintenance of payroll records, including compliance with the Copeland Act and U.S. Department of Labor regulations, 29 C.F.R. Part 3, implementing that Act.
- Provisions on records of materials, supplies, and labor, requiring that contractors maintain records in accordance with form FHWA-47, "Statement of Materials and Labor Used by Contractor of Highway Construction Involving Federal Funds," which apply to all federal-aid projects except projects costing less than $1 million or those involving rail crossing protective devices, highway beautification, or force-account contracts.
- Provisions in Part VII of the form on the conditions under which the contractor will be allowed to subcontract work or assign the contract which, among other things, require the contractor to perform at least 30 percent of the work of the project with its own forces, excluding specialty items, and prohibit the subcontracting of any portion of the project without the written approval of the state DOT administering the contract.
- Provisions on safety and accident prevention implementing the Contract Work Hours and Safety Standards Act, 40 U.S.C. § 333; requiring compliance with all applicable federal, state, and local laws governing safety, health, and sanitation, per 23 C.F.R. Part 635; and making OSHA regulations, 26 C.F.R. Part 1926, applicable to federal-aid construction sites.
- Provisions on false statements concerning highway projects requiring the posting of the full text of 18 U.S.C. § 1020 in a location readily available to all personnel on a federal-aid construction site.
- Provisions concerning implementation of the Clean Air Act and the Federal Water Pollution Control Act. Part X of the Form requires compliance with provisions of the Federal Clean Air Act[644] and the Federal Water Pollution Control Act (the Clean Water Act).[645] This particular section is presented as a stipulation that the contractor or subcontractor is in compliance with these provisions, the violation of which is grounds for termination under Part I of the form.
- Provisions, in accordance with 49 C.F.R. Part 29, regarding debarment, suspension, ineligibility, and voluntary exclusion. Contractors and subcontractors are required under Part XI of the form to certify that they are not presently debarred, suspended, or otherwise ineligible from participating in a federally funded contract by any federal agency; that they have not within the previous 3 years been convicted or had a civil judgment imposed against them for offenses such as fraud, embezzlement, or false statements; and that they have not within the previous 3 years had a contract terminated for default.
- Provisions, in accordance with 31 U.S.C. § 1352 and 49 C.F.R. Part 20, regarding the use of contract funds for lobbying. Part XII of the form requires contractors to certify that no contract funds have been or will be used for lobbying elected officials or public employees.
- In the case of Appalachian contracts only, provisions concerning employment preference for Appalachian contracts.

While some of the required clauses in form FHWA-1273 cover the same matters as the requirements set forth in 49 C.F.R. § 18.36(i), form FHWA-1273 does not cover all of the matters addressed in 49 C.F.R. § 18.36(i), and 49 C.F.R. §1 8.36(i) does not cover all of the requirements set forth in form FHWA-—they are partially overlapping, rather than identical. So while state DOTs must incorporate form FHWA-1273 in all their federal-aid highway and bridge construction and reconstruction contracts, that is not alone sufficient to comply with all USDOT requirements for contract clauses. In addition to using form FHWA-1273, they

[641] Form FHWA-1273, pt. 1.

[642] 23 C.F.R. § 635.117(a) (2001).

[643] 23 C.F.R. § 635.118; Form FHWA-1273, pts. IV and V.

[644] 42 U.S.C. § 7401 *et seq*.

[645] 33 U.S.C. § 1251 *et seq*.

must also review the standard contract documents used for their federal-aid projects to ensure that those standard documents include provisions addressing all of the requirements in 49 C.F.R. § 18.36(i).

Where procurement regulations require that a contract contain a particular clause, the contract will be read as though it contained that clause, even if it is omitted.[646] Federal regulations have the force and effect of law and must be deemed to be terms of the contract even if not set forth in the contract; the contractor is charged with knowledge of the regulations.[647] Further, the regulations will apply even if inconsistent with a contract provision.[648]

However, where statutes, regulations, or policies of the contracting agency require that certain provisions must be included in all of the agency's construction contracts, they generally are incorporated into standard forms that all bidders must use. Typically, some of these provisions are concerned with procedures to be followed during performance of the contract so that administrative processing will be facilitated. Others impose positive duties on the contractor in the performance of the contract that may affect its methods of operation, and therefore must be reflected in the contractor's bid.

Examples of both types occur in the required provisions for federal-aid highway construction contracts. Requirements for keeping records and making reports on acquisition of materials, supplies, and labor illustrate the type of provisions dealing with contract administration.[649] Requirements that contractors comply with provisions of federal environmental protection laws and federal labor standards illustrate factors that must be considered in calculating bid prices.[650] Contracts for direct federal construction projects require compliance with the Buy American Act and the Walsh-Healey Act.[651]

The federal regulations require that the required clauses be included in all prime contracts for federal-aid funded construction, and that the contractor be similarly required to include the clauses expressly in its subcontracts.[652] It is not sufficient to incorporate the clauses by reference.[653]

[646] District of Columbia v. Org. for Envtl. Growth, Inc. (OFEGRO), 700 A.2d 185, 198–99 (D.C. App. 1997).

[647] Century Marine, Inc. v. United States, 153 F.3d 225, 228 n.1 (5th Cir. 1998); General Eng'g & Mach. Works v. O'Keefe, 991 F.2d 775, 780 (Fed. Cir. 1993).

[648] *OFEGRO*, 700 A.2d at 199.

[649] Form FHWA-1273, Part VI, available on FHWA's Web page at http://wwwcf.fhwa.dot.gov/programadmin/contracts/1273.htm.

[650] *Id.* pts. IV and X.

[651] 41 U.S.C. §§ 10a and 35 (1999).

[652] 23 C.F.R. § 633.102(d), (e) (1999).

[653] *Id*.

b. Standardized Changed Conditions Clauses

In addition to the required clauses set out in Form FHWA-1273, the regulations contain additional required clauses regarding changed conditions.

i. Differing Site Conditions.—One of the longest utilized required federal clauses is the Differing Site Conditions (DSC) clause. It was preceded by a similarly worded provision that was known as the Changed Conditions clause. Cases interpreting these clauses date back almost half a century.[654] The contractor generally accepts the risk that subsurface or other latent physical conditions may be difficult to determine prior to construction and that they may be adverse.[655] The Supreme Court noted in that case that: "Where one agrees to do, for a fixed sum, a thing possible to be performed, he will not be excused or become entitled to additional compensation, because unforeseen difficulties are encountered…."[656]

The federal government has been concerned that because of this rule, contractors will have to price into their bids the risk that "unforeseen difficulties" such as adverse subsurface conditions will cause the project costs to exceed the bid price. In addition, contractors will have to factor into their bid prices the cost of investigating subsurface soil conditions.

> The purpose of the changed conditions clause is thus to take at least some of the gamble on subsurface conditions out of bidding. Bidders need not weigh the cost and ease of making their own borings against the risk of encountering an adverse subsurface, and they need not consider how large a contingency should be added to the bid to cover the risk. They will have no windfalls and no disasters. The government benefits from more accurate bidding, without inflation for risks that may not eventuate. It pays for difficult subsurface work only when it is encountered and was not indicated in the logs.[657]

The use of the DSC clause shifts the risk of adverse subsurface or other latent physical conditions from the contractor to the government. Otherwise, if the contract is silent about the risk of unforeseen conditions, the contractor would bear the risk even though those conditions might significantly increase the cost of the project.[658] Preventing contractors from bidding on a "worst-case scenario" basis is the goal of inclusion of the DSC clause.[659] The clause imposes on the government the risks for conditions that the contract documents fail to disclose, but leaves upon the contractor the costs of en-

[654] *See*, *e.g.,* United States v. Rice, 317 U.S. 61, 66–68, 63 S. Ct. 120, 123–23, 87 L. Ed. 53 (1942) (interpreting Changed Conditions clause).

[655] *See Spearin*, *supra* note 7.

[656] *Id.* at 136.

[657] Olympus Corp. v. United States, 98 F.3d 1314, 1317 (Fed. Cir. 1996) (quoting from Foster Constr. C.A. & Williams Bros. Co. v. United States, 193 Ct. Cl. 587, 435 F.2d 873, 887 (Ct. Cl. 1970)).

[658] Iacobelli Constr., Inc. v. County of Monroe, 32 F.3d 19, 23 (2d Cir. 1994).

[659] *Id*.

countering conditions described in the contract.[660] The result is that the government should as a rule get lower bids, and only pay for DSCs when they actually occur, rather than funding a contingency in each contract.

The DSC clause applies only to those conditions that exist at the time of contract execution. It does not apply to conditions that develop during performance of the contract.[661] This is true even if this time limitation is not expressed in the clause itself or elsewhere in the contract.[662] The DSC clause is addressed in greater detail in Section 5.

ii. Suspension of Work. — This clause allows the project engineer to adjust the compensation and/or schedule to account for delays that are ordered by the engineer and that are "an unreasonable period of time," which is defined as "not originally anticipated, customary, or inherent to the construction industry."[663]

iii. Significant Changes in Character of Work.—This clause defines "significant change" as:

> (A) When the character of the work as altered differs materially in kind or nature from that involved or included in the original proposed construction; or
>
> (B) When a major item of work, as defined elsewhere in the contract, is increased in excess of 125 percent or decreased below 75 percent of the original contract quantity.[664]

This clause reserves to the engineer the right "to make, in writing, at any time during the work, such changes in quantities and such alterations in the work as are necessary to satisfactorily complete the project."[665] It further provides that such changes "shall not invalidate the contract nor release the surety."[666] The contractor is entitled to an adjustment, including anticipated profit, in the event of a significant change.[667] Change provisions are intended to compensate the contractor for burdens not contemplated by the contract.[668] To qualify for an adjustment under a changes provision, the contractor must prove that any increased costs arose from conditions differing materially from those indicated in the bid documents, and also that the changes were reasonably unforeseeable in light of the information available to the contractor.[669]

c. Noncollusion

The federal regulations require that the state agency provide a form to be executed by each bidder, and included in the contract, stating that the bidder has not engaged in collusive behavior:

Each bidder shall file a statement executed by, or on behalf of the person, firm, association, or corporation submitting the bid certifying that such person, firm, association or corporation has not, either directly or indirectly, entered into any agreement, participated in any collusion, or otherwise taken any action, in restraint of free competitive bidding in connection with the submitted bid. Failure to submit the executed statement as part of the bidding documents will make the bid nonresponsive and not eligible for award consideration.[670]

d. Nondiscrimination

All contracts with participation by any branch of the U.S. Department of Transportation are required to comply with the nondiscrimination provisions of 49 C.F.R. Section 21, which implements Title VI of the Civil Rights Act of 1964 in federal transportation programs. Appendix C to this section provides illustrations of how this section applies to the various operations of the Federal Aviation Administration, FHWA, and the Federal Transit Administration (formerly the Urban Mass Transit Administration).

e. Prompt Payment

The 1999 FHWA Disadvantaged Business Enterprise (DBE) regulations were written to address the constitutional deficiencies identified in the program in *Adarand Constructors, Inc. v. Pena*.[671] Chief among these was the requirement that the program be "narrowly tailored" to address a compelling governmental interest. As part of the "narrow tailoring" requirement, FHWA included a number of "race-neutral" measures that are intended to benefit all small or new businesses, not just those owned by minorities or women. Among these is a requirement for prompt payment of subcontractors by prime contractors.[672] FHWA specifically found: "It is clear that DBE subcontractors are significantly—and, to the extent that they tend to be smaller than non-DBEs, disproportionately—affected by late payments from prime contractors. Lack of prompt payment constitutes a very real barrier to the ability of DBEs to compete in the marketplace…."[673]

The regulation requires that federal-aid recipient agencies include in their DBE programs a requirement for a prompt payment clause to be included in every prime contract in which there are subcontracting possibilities.[674] Federal regulations in 49 C.F.R. 26.29, Par-

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[660] *Id*.

[661] *See* Olympus Corp. v. United States, 98 F.3d 1314, 1317 (Fed. Cir. 1996); John McShain, Inc. v. United States, 179 Ct. Cl. 632, 375 F.2d 829 (1967).

[662] *Olympus*, 98 F. 3d 1314.

[663] 23 C.F.R. § 635.109(a)(2) (1999).

[664] 23 C.F.R. § 635.109(a)(3)(iv) (1999). Changes are addressed in more detail in Section 5.

[665] 23 C.F.R. § 635.109(a)(3)(i) (1999).

[666] *Id*.

[667] 23 C.F.R. § 635.109(a)(3)(ii) (1999).

[668] Willamette Crushing Co. v. State By and Through Dep't of Transp., 188 Ariz. 79 932 P.2d 1350, 1352 (1997).

[669] *Id*.

[670] 23 C.F.R. § 635.112(f) (1999).

[671] 515 U.S. 200, 115 S. Ct. 2097, 132 L. Ed. 2d, 158 (1995).

[672] 49 C.F.R. § 26.29 (2000).

[673] 64 Fed. Reg. 5096, at 5105–06 (Feb. 2, 1999).

[674] *Id*.; 49 C.F.R. § 26.29(a) (2000).

ticipation by Disadvantaged Business Enterprises, require that state highway agencies have a contract clause that requires prime contractors to pay subcontractors for satisfactory performance of work within 30 days from receipt of payment from the public agency. FHWA mandates inclusion of these provisions in all subcontracts. The regulations also provide for full payment of retainages within 30 days after the subcontract work is satisfactorily completed.

State transportation agencies have three options:

1. Declining to hold retainages from prime contractors and prohibiting prime contractors from doing so.
2. Declining to hold retainages from prime contractors, and instead mandating a contract clause that obligates the prime contractor to make prompt and full payment to subcontractors of any held retainages within 30 days after the subcontractor‘s work is satisfactorily completed.
3. Continuing to hold retainages from the prime, providing for prompt and regular incremental payment acceptance of portions of the prime contract, paying retainages to prime contractors upon acceptance, and requiring a contract provision that obligates the prime contractor to pay any owed retainages to subcontractors for satisfactory completion of the affected work within 30 days after the prime's receipt of payment.

In addition, the regulation provides for *suggested* contract provisions that include reference to appropriate alternate dispute resolution provisions to resolve payment disputes, and a contract clause providing that the prime will not be entitled for reimbursement for subcontractor work until the prime ensures that the subs are promptly paid for the work they have performed, and other mechanisms to ensure that DBEs are fully and promptly paid. States have generally opted to release retainages for all contractors to comply with the above requirements.

It should be noted that economic recovery legislative proposals may possibly lead to enactment of a general federal prohibition against states with holding any retainages from contractors on any federal-aid projects.

The regulation requires that agencies include in their prime contracts an enforcement mechanism for prompt payment of subcontractors. This may be either an alternative dispute resolution process for the resolution of payment disputes, or a provision stating that the prime contractor will not be paid for its work unless it ensures that subcontractors are promptly paid for their work, or any other mechanism consistent with the regulation and with state law.[675]

A prompt pay clause does not preclude the prime contractor from withholding payments from the subcontractor based on identifiable claims.[676]

i. “Pay when paid.”—The prompt-pay requirement would appear not to interfere with the prime contractor’s use of a “pay when paid” clause in its subcontracts, since it does not apply until the prime contractor has been paid by the agency. The “pay when paid” clause, or “pay if paid,” allows the prime contractor to condition its payment to the subcontractor on its prior receipt of payment from the agency.[677] Most jurisdictions that have considered these clauses do not construe them to release the prime contractor from its obligation to pay the subcontractor if the owner fails to perform. Rather the clause merely affects the timing of payments, regardless of whether the owner performs.[678] Courts will not shift the risk of the owner’s nonperformance, or failure to pay, to the subcontractor unless the language of the clause clearly indicates that the parties intended to do so.[679] On the other hand, where the language expressly states that receipt of payment from the owner or the agency is a condition precedent to payment being owed to the subcontractor, the court will treat it as a condition precedent.[680] But because condition precedents are not favored, there must be clear contract language to create them.

f. Termination of Contract

The FHWA regulations require that state highway construction contracts using federal funds contain some provision for termination of the contract, both for default and for public convenience:

All contracts exceeding $2,500 shall contain suitable provisions for termination by the State, including the manner in which the termination will be effected and the basis for settlement. In addition, such contracts shall describe conditions under which the contract may be terminated for default as well as conditions where the contract may be terminated because of circumstances beyond the control of the contractor.[681]

g. “Buy America” Requirements

A federal statute and FHWA regulations adopted in 1983 imposed Buy America requirements for federal-aid projects.[682] As FHWA's Web site indicates, these regula-

[675] 49 C.F.R. § 26.29(b) (2000).

[676] Pottstown Fabricators, Inc. v. Manshul Constr. Corp., 927 F. Supp. 756, 757 (S.D.N.Y. 1996) (applying state prompt pay statute allowed prime contractor to withhold payments to satisfy claims, liens, or judgments against subcontractor where those had not been discharged).

[677] *See* Urban Masonry Corp. v. N&N Contractors, Inc., 676 A.2d 26, 36 n.19 (D.C. App. 1996) (example of “pay when paid” clause).

[678] Koch v. Construction Technology, Inc., 924 S.W.2d 68, 71 and n.1 (Tenn. 1996).

[679] *Id*; *see also* Thomas J. Dyer Co. v. Bishop Int’l Eng’g Co., 303 F.2d 655, 660–61 (6th Cir. 1962).

[680] *See Urban Masonry*, note 677 *supra*, at 36.

[681] 23 C.F.R. § 633.210 (1999).

[682] 23 U.S.C. § 313; 23 C.F.R. § 635.410; and see FHWA's Nov. 25, 1983, Final Rule, available at http://www.fhwa.dot.gov/programadmin/contracts/112583.cfm, last accessed on Sept. 8, 2013. The "Buy America" program must be distinguished from “Buy American,” which applies to federal direct procurements. 41 U.S.C. 10a-10c.

tions require that a state's specifications require the use of domestic steel and iron products, and also requires that all manufacturing of these products (including protective coatings) have occurred in the United States.[683] The 2012 enactment of the Federal MAP-21 surface transportation funding legislation reportedly includes certain provisions amending previously existing Buy America provisions, including one that would end a project segmentation loophole that had sometimes been used to avoid requiring the use of American-made steel, iron, and manufactured items in highway and bridge projects. Practitioners should refer to FHWA's Web site for the latest available information concerning current Buy America requirements.

A state may obtain a waiver of this requirement from the FHWA Regional Administrator if the state can show that the product is not produced in the United States in sufficient and reasonably available quantities that are of a satisfactory quality. Pursuant to federal legislation enacted in 2008 and 2010, however, the U.S. Secretary of Transportation is required to provide informal public notice and an opportunity for comment at least 15 days prior to granting any such waiver, and must submit an annual report to the Congressional Appropriation Committees on any waivers granted to Buy America Requirements.[684] Due to that new requirement, FHWA now requires that any state DOT seeking such a waiver submit its request to the Office of FHWA's Director of Program Administration for review and consideration.[685] FHWA has also set up an Web page concerning the requirements for submission, public notice, comment, and FHWA review of such waiver requests.[686]

There are also minimum usage criteria for nondomestic products,[687] and nationwide waivers for ferryboat equipment and machinery[688] and pig iron and processed, pelletized, and reduced iron ore.[689] The requirement for Buy America is not affected by the United States' participation in international trade agreements such as the World Trade Organization Government Procurement Agreement or the North American Free Trade Agreement, as Congress noted an exception for this requirement in its approval of these agreements.[690] This includes the U.S.– Canada Agreement on Government Procurement of February 16, 2010.[691]

In addition to the statute and regulations, FHWA headquarters has issued at least five policy memoranda between 1989 and 2011 providing policy guidance to state DOTs concerning FHWA's interpretation of "Buy America" requirements, all of which are accessible via FHWA's Web site.[692] State DOTs should check those memoranda for details on FHWA's interpretation of these requirements.

FHWA's Web site also includes a Web page, "FHWA's Buy America Q and A for Federal-aid Program," which provides answers to 49 frequently asked questions about Buy America requirements.[693]

h. ARRA Requirements

During 2009, Congress enacted and the President approved major federal economic stimulus legislation,

[683] 23 C.F.R. § 635.410(b)(1); *see also* FHWA's Web site for a summary of Buy America requirements at http://www.fhwa.dot.gov/construction/cqit/buyam.cfm. The regulations were amended to extended Buy America requirements to protective coatings in 1993, pursuant to ISTEA § 1041(a); *see* 58 Fed. Reg. 38972 (July 21, 1993), amending 23 C.F.R. pt. 635.

[684] *See* Consolidated Appropriations Act of 2008, Pub. L. No. 110-161, 121 Stat. 1844, Division K, § 130; the SAFETEA-LU Technical Corrections Act of 2008, P.L. No. 110-244, 122 Stat. 1572, § 117; and Consolidated Appropriations Act of 2010, Pub. L. No. 111-117, 123 Stat. 3034, Division A, § 123.

[685] *See* FHWA Memorandum dated March 13, 2008, available at http://www.fhwa.dot.gov/construction/contracts/080313.cfm, last accessed on September 8, 2013.

[686] http://www.fhwa.dot.gov/construction/contracts/waivers.cfm, last accessed on September 8, 2013.

[687] *See* http://www.fhwa.dot.gov/construction/cqit/buyam.cfm, last accessed on Sept. 8, 2013.

[688] *See* FHWA's Feb. 9, 1994, Federal Register Notice, available at http://www.fhwa.dot.gov/programadmin/contracts/020994.cfm, last accessed on Sept. 8, 2013.

[689] *See* FHWA's Mar. 24, 1995, Federal Register Notice, available at http://www.fhwa.dot.gov/programadmin/contracts/032495.cfm, last accessed on Sept. 8, 2013.

[690] *See* C.F. Corr and K. Zissis, *Convergence and Opportunity: The WTO Government Procurement Agreement and U.S. Procurement Reform*, 18 N.Y. L. SCH. J. INT'L & COMP. LAW at 303 (1999), for a discussion of how the Buy American requirements applicable to direct federal procurement apply in light of international trade agreements.

[691] For the text of that Agreement, *see* http://www.ustr.gov/trade-topics/government-procurement/us-canada-agreement-government-procurement, last accessed on Sept. 8, 2013. FHWA's Web site indicates that "The Agreement identifies specific programs for coverage, however, it does not include the highway program. Thus, all Federal-aid highway projects, including those funded under the Recovery Act (excluding TIGER grants, which are subject to section 1605 of the Recovery Act), administered by FHWA will continue to be subject to the Buy America provisions in Title 23 U.S.C. 313." *See* http://www.fhwa.dot.gov/construction/cqit/buyam.cfm, last accessed on Oct. 16, 2010.

[692] *See* http://www.fhwa.dot.gov/construction/cqit/buyam.cfm; and *see* FHWA's July 6, 1989, memorandum at http://www.fhwa.dot.gov/programadmin/contracts/070689.cfm; FHWA's Dec. 22, 1997, memorandum at http://www.fhwa.dot.gov/programadmin/contracts/122297.cfm; FHWA's Oct. 5, 2005, memorandum at http://www.fhwa.dot.gov/construction/cqit/100405.cfm; FHWA's Mar. 13, 2008, memorandum at http://www.fhwa.dot.gov/construction/contracts/080313.cfm; and FHWA's June 11, 2011, memorandum at http://www.fhwa.dot.gov/construction/contracts/110613.cfm; all last accessed on Sept. 8, 2013.

[693] http://www.fhwa.dot.gov/construction/contracts/buyam_qa.cfm, last accessed on Aug. 2, 2012.

known as ARRA, which included $30.8 billion in federal-aid funding for transportation projects.[694]

ARRA made $27.5 billion in federal General Fund appropriations available to FHWA for supplemental formula grants, of which roughly $840 million was set aside for specific purposes, and an additional $1.5 billion for discretionary grants.[695] FHWA and state DOTs obligated $26.6 billion in funding to more than 12,000 highway and bridge projects across the United States by March 1, 2010, and also awarded 51 Surface Transportation Discretionary Grants (TIGER grants) to support other transportation projects, including highway safety, intermodal centers, commuter rail, and regional bicycle networks.[696] FHWA apportioned the ARRA Highway Infrastructure Investment Funds among a variety of existing, statutorily authorized FHWA highway programs.[697] In order to provide for effective use of the funds, FHWA required its Division Administrators to develop Risk Management Plans for their divisions.[698]

ARRA included a number of provisions applicable to the FHWA highway funding. Among other things:

- The ARRA funds were to be in addition to previously existing funds for the fiscal years involved.[699]
- At least half of the funds had to be used for projects that could start within 120 days of enactment of the legislation.[700]
- ARRA-funded projects were required to use American iron, steel, and manufactured goods.[701]
- Laborers and mechanics on ARRA-funded project were to be paid prevailing wages.[702]
- The Governors of states receiving ARRA highway funding were required to certify that the states would maintain their own funding for highway projects, and to identify the amounts of funds that the states planned to expend from nonfederal sources between the date of enactment and September 30, 2010.[703]
- Contracting procedures for ARRA projects were to include ESSA provisions for individuals with disabilities.[704]
- The performance of ARRA projects was to comply with NEPA requirements.[705] and
- Contracts for ARRA projects were to comply with the Federal Property and Administrative Services Act and the FAR.[706] FHWA paid particular attention to promoting highway work zone safety precautions for ARRA-funded projects, in coordination with FHWA's Work Zone Safety and Mobility Rule.[707]

FHWA also established a bonding assistance program DBEs under ARRA.[708] Further, FHWA sought to use the availability of ARRA funding to increase projects incorporating On-the-Job Training and Supportive Services (OJT/SS) elements.[709]

ARRA also included broader accountability requirements as a condition of funding. It created a Recovery Accountability and Transparency Board, composed of a Presidentially-appointed Chair and the Inspectors General from 12 federal agencies; the Inspector General of USDOT was named the Vice Chairman of the board.[710] The board was empowered to audit and review the expenditure of ARRA funds; to make recommendations to federal agencies for prevention of fraud, waste, and mismanagement; to refer instances of fraud, waste and mismanagement to Federal Inspectors General; to submit quarterly and annual reports to the President and Congress; and to take various other actions intended to assure accountability and transparency in the expenditure of stimulus funding.[711] OMB also issued administrative guidance to federal agencies concerning expenditure of ARRA funds.[712]

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[694] American Recovery and Reinvestment Act (ARRA) of 2009, Pub. L. No. 111-5, 123 Stat. 114; text of bill available at http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=111_cong_bills&docid=f:h1enr.pdf, last accessed on Sept. 8, 2013. For the $30.8 billion figure for transportation projects, see http://www.recovery.gov/Transparency/fundingoverview/Pages/fundingbreakdown.aspx#ContractsGrantsLoans, last accessed on Sept. 8, 2013.

[695] *See* http://www.fhwa.dot.gov/economicrecovery/summary.htm, last accessed on Sept. 8, 2013.

[696] *See* http://www.fhwa.dot.gov/economicrecovery/, last accessed on Sept. 8, 2013.

[697] *See* http://www.fhwa.dot.gov/legsregs/directives/notices/n4510705.htm, last accessed Sept. 8, 2013.

[698] *See* http://www.fhwa.dot.gov/economicrecovery/memo20090304.htm, last accessed on Sept. 8, 2013.

[699] ARRA § 1601; *see* http://www.fhwa.dot.gov/economicrecovery/summary.htm, last accessed Sept. 8, 2013.

[700] ARRA § 1602.

[701] ARRA § 1605.

[702] ARRA § 1606; and ARRA §§ 1201 and 1511, *see* http://www.dot.gov/recovery/certifications.html, last accessed on Sept. 8, 2013.

[703] ARRA § 1607.

[704] ARRA § 1608.

[705] ARRA § 1609.

[706] ARRA § 1610.

[707] 23 C.F.R. pt. 630 subpt. J; and *see* http://www.fhwa.dot.gov/economicrecovery/workzones.htm, last accessed on Sept. 8, 2013.

[708] *See* ARRA § 1512; and http://www.fta.dot.gov/grants/13948.html.

[709] *See* http://www.fhwa.dot.gov/economicrecovery/memo20090427.htm, last accessed on Sept. 8, 2013.

[710] For the Board's Web site, *see* http://www.recovery.gov/About/board/Pages/TheBoard.aspx; for information on the members of the Board, including the Vice Chairman, *see* http://www.recovery.gov/About/board/Pages/BoardMembers.aspx; both last accessed on Sept. 8, 2013. The Web site includes links to additional information regarding the Board's powers, functions, guidelines, reports, and other information.

[711] *See* http://www.recovery.gov/About/board/Pages/Powers_Functions.aspx, last accessed on Sept. 8, 2013.

[712] *See* text and links to OMB materials at http://www.recovery.gov/About/Pages/The_Act.aspx, last accessed on Sept. 8, 2013.

3. Examples of Required State Clauses

Many states' public works or transportation construction statutes set out required clauses for inclusion in construction contracts, such as clauses for termination for convenience, liquidated damages, DSCs, suspension of work, and dispute resolution.[713] Some of these are the same as or very similar to the required federal clauses. A few of these typical state clauses are examined here, along with some newer and more unusual requirements such as value engineering clauses.

a. Liquidated Damages

Time is an essential element of the transportation contract. The costs to the public owner for administration of the contract include engineering inspection and supervision. These costs increase as the contract time increases. Similarly, road user costs increase in the same manner if the completion date is extended. Liquidated damages provide a means to recover these costs if the project is extended.[714]

There are clear functional distinctions between I/D provisions and the purpose of liquidated damages. I/D provisions motivate the contractor to complete the work ahead of schedule and provide disincentives for late completion. Liquidated damages, by contrast, are intended to recover construction oversight costs and/or damage to the traveling public. In some states, such as New York, liquidated damages are meant to cover only damage and inconvenience to the traveling public, while a separate assessment of "engineering charges" covers state damages for late completion.

USDOT regulations (23 C.F.R. § 635.127) require state transportation agencies to establish liquidated damages as a minimum to recover overruns in contract time. RUCs are more extensive, are used to justify I/D, and are not liquidated damages. Although they are similar, RUCs are significantly greater than liquidated damages and the extended engineering costs sustained by the public agency caused by late completion.

For any highway project using any of the I/D or lane rental fees provisions (including road user fees), the calculation of RUCs is necessary. It is a measurement of the impact the transportation facility has on the traveling public. RUCs may include costs associated with travel time, vehicle operation accidents, or air quality. The need for defensible I/D provisions mandate that RUCs be based upon reasonable estimates. FHWA has provided numerous studies and references that can provide guidance on developing RUCs.[715]

Liquidated damages clauses are generally favored by the courts. They save the time and expense of litigating the issue of damages by fixing in advance the amount to be paid in the event of a breach. Liquidated damages clauses serve a particularly useful function "when damages are uncertain in nature or amount or are unmeasurable."[716] An example of this type of damages might be costs to "public convenience" or losses suffered by the traveling public where traffic patterns are interrupted beyond the time called for in the contract.

The test for the validity of a liquidated damages clause is whether it fairly compensates the party benefiting from it for actual damages, or whether it constitutes a penalty. A clause that results in a penalty will not be enforced. Liquidated damages may be used as a disincentive for late completion; however, they must fairly relate to the actual loss suffered by the agency.[717] The challenger has the burden of proving that a liquidated damages clause creates an unenforceable penalty.[718] If the liquidated damages clause is stricken as a penalty, actual damages may still be awarded.[719]

A liquidated damages clause need not be specially tailored to a particular contract.[720] The clause will be enforced as long as the amount is not disproportionate to the loss, so as to prove that compensation was not the object, but rather that a penalty was intended.

An example of a liquidated damages clause that was found to be unenforceable as a penalty is in *Kingston Constructors v. Washington Metro Area Transportation Authority*.[721] In that case, the Washington Metropolitan Area Transportation Authority (WMATA) was replacing transformers that contained PCB, a hazardous substance whose use is now prohibited. The contract included a liquidated damages clause charging $1,000 per day to the contractor for late completion. WMATA had included this amount as a contingency against possible penalties that could have been imposed by the Environmental Protection Agency (EPA), even though WMATA knew that EPA did not plan to assess any penalties. The court found this to be a penalty.[722]

However, an agency may be obligated in a consent decree with EPA or another regulatory agency to see that particular work is completed, and may choose or be required by its public bidding statutes to do that work by contract. If the consent decree includes a penalty for late completion of the work to be assessed by EPA against the agency, then it would appear to be reasonable to include that amount in the contract between the agency and the contractor as liquidated damages. The amount will be fixed in the consent decree and is certainly a liquidated amount from the agency's standpoint. Even though it is intended to be a "penalty" from EPA's standpoint, it would appear to be an item of

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[713] *See, e.g.*, D.C. CODE § 2-305.07 (2002); HAW. REV. STAT. § 103D.501 (1999).

[714] *See* FHWA, *supra* note 401 § III, at 41–42.

[715] *Id.* at 9.

[716] DJ Mfg. Corp. v. United States, 86 F.3d 1130, 1133 (Fed. Cir. 1996) (quoting Priebe & Sons v. United States, 332 U.S. 407, 411, 68 S. Ct. 123, 92 L. Ed. 2d 32 (1947)).

[717] State of Ala. Highway Dep't v. Milton Constr. Co., 586 So. 2d 872, 874 (1991).

[718] *DJ Mfg.*, *supra* note 716, at 1134.

[719] *See* Kingston Constructors v. Washington Metro. Area Transit Auth. (WMATA), 930 F. Supp. 651, 656 (D.D.C. 1996).

[720] *DJ Mfg.*, *supra* note 716, at 1133.

[721] 930 F. Supp. 651 (D.D.C. 1996).

[722] *Id*. at 656.

damage from the transportation agency's standpoint in that the agency only has to pay the penalty if the contractor is late in completing the work. Thus the result in *WMATA* should not preclude an agency from passing along such stipulated penalties to a contractor as liquidated damages.

b. Dispute Resolution

A disputes resolution clause generally establishes one or more procedures for resolving disputes. These may include disputes review boards, typically composed of engineers or architects; mediation; arbitration, both mandatory and nonmandatory; and litigation. The clause will generally set time limits for each type of dispute resolution to be invoked, and the manner in which it is invoked. It will also establish what individual or group of individuals has jurisdiction at each particular stage of a dispute.[723] In the absence of such a clause, a party cannot be compelled to arbitrate or to utilize other alternative dispute resolution methods.[724]

Parties may be held to have waived the right to compel arbitration by initiating litigation. A "no waiver" provision in the arbitration or dispute resolution clause will preserve the right to utilize arbitration where litigation is initiated to obtain interim relief, such as attachment or injunction.[725] But protracted litigation of an arbitrable dispute will waive the parties' right to compel arbitration.

The authority to enter into binding arbitration pursuant to a disputes resolution clause will be implied in the agency's authority to contract. It need not be set out expressly in statute as it will be "necessarily or fairly implied."[726]

c. Value Engineering / Life-Cycle Costs

Hawaii's public works statute requires the inclusion of a value engineering clause in contracts over $250,000.[727] The clause is required to provide:

> (1) That cost reduction proposals submitted by contractors:
>
> (A) Must require, in order to be applied to the contract, a change order thereto; and
>
> (B) Must result in savings to the State or county, as the case may be, by providing less costly items than those specified in the contract without impairing any of their essential functions and characteristics such as service life, reliability, substitutability, economy of operation, ease of maintenance, and necessary standardized features; and
>
> (2) That accepted cost reduction proposals shall result in an equitable adjustment of the contract price so that the contractor will share a portion of the realized cost reduction.[728]

d. Audit Rights

Illinois' public procurement statutes require that all contracts include the requirements for the contractor's recordkeeping that will facilitate audit of the contractor's books and records. Further, it requires the following:

Every contract and subcontract shall provide that all books and records required to be maintained under subsection (a) shall be available for review and audit by the Auditor General and the purchasing agency. Every contract and subcontract shall require the contractor and subcontractor, as applicable, to cooperate fully with any audit.[729]

e. Use of State Products; Local Preference

A federal statute, 23 U.S.C. § 112, establishes FHWA's requirements for competitive bidding for construction contracts.[730] USDOT regulations, 49 C.F.R. § 18.36(c)(2), provide as follows:

> Grantees and subgrantees will conduct procurements in a manner that prohibits the use of statutorily or administratively imposed in-State or local geographical preferences in the evaluation of bids or proposals, except in those cases where applicable Federal statutes expressly mandate or encourage geographic preference. Nothing in this section preempts State licensing laws. When contracting for architectural and engineering (A/E) services, geographic location may be a selection criteria provided its application leaves an appropriate number of qualified firms, given the nature and size of the project, to compete for the contract.[731]

FHWA has also issued a regulation, 23 C.F.R. § 635.409, "Restrictions on Materials," addressing the issue of whether states may impose state or local preferences for use of products or materials produced within the state on federal-aid highway or bridge projects.[732] The regulation prohibits state highway agencies from

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[723] *See* Washington Metro. Area Transit Auth. v. Buchart-Horn, Inc., 886 F.2d 733, 735 (4th Cir. 1989).

[724] AJM Packaging Corp. v. Crossland Constr. Co., 962 S.W.2d 906, 911 (Mo. App. 1998). An exception will be if a statute required arbitration of claims within a certain dollar limit.

[725] S & R Co. of Kingston v. Latona Trucking, Inc., 159 F.3d 80, 85 (2d Cir. 1998).

[726] Carteret County v. United Contractors of Kinston, Inc., 120 N.C. App. 336, 462 S.E.2d 816, 820 (1995).

[727] HAW. REV. STAT. § 103D-409 (1999).

[728] *Id*.

[729] ILL. COMP. STAT. 30 500/20-65 (b) (1999).

[730] 23 U.S.C. § 112 is available at http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=browse_usc&docid=Cite:+23USC112, last accessed on Sept. 8, 2013.

[731] 49 C.F.R. § 18.36(c)(2) is available at http://eC.F.R..gpoaccess.gov/cgi/t/text/text-idx?c=eC.F.R.&sid=3d50ad5e260841b86bd171f32d35b9d6&rgn=div5&view=text&node=49:1.0.1.1.12&idno=49#49:1.0.1.1.12.3.5.14 , last accessed on Sept. 8, 2013.

[732] 23 C.F.R. § 635.409 is available at http://frwebgate.access.gpo.gov/cgi-bin/get-C.F.R..cgi?TITLE=23&PART=635&SECTION=409&YEAR=2001&TYPE=TEXT, last accessed on Sept. 8, 2013.

imposing any requirement or enforcing any procedure in connection with a project that would establish a price differential in favor of articles or materials produced within the state, or prohibit, restrict, or discriminate against articles or materials produced in or shipped from any other state.[733] It also prohibits state highway agencies from prohibiting, restricting, or discriminating against articles or materials of foreign origin to any greater extent than permissible under USDOT and FHWA requirements, the apparent reference being to "Buy America" requirements.[734]

FHWA's Web site states as follows: "FHWA policy prohibits contractual provisions that provide a preference for in-State materials to the exclusion of comparable materials produced outside of the State. Such provisions may give particular advantage to a designated source and thus restrict competition."[735]

The reasons for the enactment of the federal statute, and the adoption of the USDOT and FHWA regulations and policy statement, become more apparent when one considers historical case law, which in some cases has upheld the validity of state-preference statutes in the face of constitutional challenges.

State statutes may require the use of products produced in a particular location, similar to the Federal "Buy America" requirements. These statutes have been subject to the same constitutional challenges as state-preference statutes. For example, the Pennsylvania Steel Products Procurement Act requires that any Pennsylvania public works construction contract require the use of steel that is produced in the United States.[736] The statute was challenged as being preempted by international trade agreements as well as by federal law, and as being violative of the Commerce Clause.[737] The federal court held that the statute was valid because the State of Pennsylvania was acting as a market participant rather than as a regulator, and that the statute was not preempted.[738]

State legislation has occasionally imposed limitations on the preparation of bids that raise questions regarding unconstitutional interference with Interstate commerce. Early consideration of state laws requiring contractors to give preference to local construction material usually took the view that such laws were discriminatory against material produced outside the state, and therefore a restraint of trade. The New York Court of Appeals explained this view:

> It is a regulation of commerce between the states, which the legislature had no power to make. The citizens of other states have the right to resort to the markets of this state for the sale of their products, whether it be cut stone, or any other article which is the subject of commerce…Under the Constitution of the United States, business or commercial transactions cannot be hampered or circumscribed by state boundary lines, and that is the effect of the statute in question….[739]

The cases that have raised this issue have presented a wide range of situations, and factual differences have distinguished permissible preferences from prohibited practices. Arizona's law relating to award of public works contracts illustrates a type of preference that has been upheld. With respect to contractors, it provides:

> [B]ids of contractors who have not been found unsatisfactorily in prior public contracts, and who have paid state and county taxes within the state of Arizona for not less than two successive years immediately prior to the making of said bid…shall be deemed a better bid than the bid of a competing contractor who has not paid such taxes, whenever the bid of the competing contractor is less than five (5) per cent lower, and the contractor making such bid, as herein provided, to be deemed the better bid, shall be awarded the contract.… Ariz. Stats. § 56-109, A.C.A. 1939.

The constitutionality of this act was upheld in *Schrey v. Allison Steel Manufacturing Co.*,[740] with the Arizona Supreme Court speaking as follows:

> All discrimination or inequality is not forbidden. Certain privileges may be granted some and denied others under some circumstances, if they be granted or denied upon the same terms, and if there exists a reasonable basis therefor…The principle involved is not that legislation may not impose special burdens or grant special privileges not imposed on or granted to others; it is that no law may do so without good reason…[A] statute may be allowed to operate unequally between classes if it operates uniformly upon all members of a class, provided the classification is founded upon reason and is not whimsical, capricious, or arbitrary.[741]

States are allowed to regulate public construction contracts so as to protect or promote legitimate public interests, provided constitutional standards of reasonableness and equal treatment are satisfied. In the *Schrey* case, the question of unreasonable burdens on Interstate commerce appeared to be secondary to the question of whether the state law could be reconciled with constitutional requirements that public contracts must be awarded to the lowest responsible bidder.

4. Required Use of Exclusive Sources and "or Equal" Clauses

The contracting agency may also designate certain materials, products, or processes by standard brand names. Such designation is feasible where the items are obtainable on the open market and have been standardized by commercial use. In these cases, however, speci-

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[733] 23 C.F.R. § 635.409(a).

[734] 23 C.F.R. § 635.409(b).

[735] *See* http://www.fhwa.dot.gov/construction/cqit/stprefer.cfm, last accessed on Sept. 8, 2013.

[736] 73 P.S. §§ 1881-1887.

[737] Trojan Technologies, Inc. v. Commw. of Pennsylvania, 916 F.2d 903 (3d Cir. 1990).

[738] *Id*. at 910 (citing White Mass. Council of Constrs. Employees, Inc., 460 U.S. 204 at 210, 103 § 1042, 75 L. Ed. 2d (1983).

[739] People *ex rel.* Treat v. Coler, 166 N.Y. 144, 150, 59 N.E. 776, 777 (1901).

[740] 75 Ariz. 282, 255 P.2d 604 (1953).

[741] *Id.* 255 P.2d at 606 (citation omitted).

fications must be drafted carefully because of the competitive aspects of patented or proprietary products and processes.

The agency must exercise care to assure that clear reference points are provided in the description of materials and workmanship. Then project specifications are not weakened by authorizing a measure of discretion by the contractor in selection of materials and performance of construction. This generally is done by use of the term "or equal" when describing quality or specifying materials or methods. It may also be done by stating "or other methods satisfactory to the Engineer," or "…commercial grades shown on the plans…and acceptable to the Engineer." Such terms introduce elements of discretion or negotiation into the standards of performance. However, they are controlled by the context of the language and the nature of the tasks involved.

The "or equal" clause may be phrased in terms of a "substantial equivalent." One court has held this term to mean a product that is equal in value in essential and material requirements. For competitive bidding purposes, equivalency is determined by whether the item bid is both functionally and qualitatively equal or identical to the specific product in the specification to which the equivalency standard applies.[742] Such a specification is often used when a description of the technical construction of the component is not available. The practice is in effect a "shorthand" method of describing the type of product desired rather than spelling out the engineering specifications of the product.[743]

The principles of fair competition are subjected to further tension where contracting agencies specify in their bid invitations that the work must be performed with certain designated materials or processes. Where specifications require use of materials or processes that are patented or otherwise obtainable only from exclusive sources, it is arguable that monopolistic control over one element of the contract's specifications could easily lead to bid rigging.

Early state court decisions generally aligned with the "Wisconsin view" or the "Michigan view" of this question. The difference in these two approaches was explained thus:

> The keystone of the argument in support of the Wisconsin line of cases is that where the statute requires competitive bidding, after advertising, as a condition precedent to the power of the municipality to contract for street improvement, the statute is violated when the…contract specifications require the use of a patented or monopolized article, because there can be no real competition when the bidding is practically restricted to the individual or corporation controlling the patent; on the other hand, the fundamental reason supporting the Michigan line of cases is that, even where the statute requires competitive bidding, it…does not apply, when all the competition is allowed which the situation permits; that a municipality should not be denied the right, for the benefit of its citizens, to avail itself of useful inventions and discoveries, even though protected by patents; and that when a city exercising its power to make the public improvements in good faith decides to contract for the use of patented articles, there is created no monopoly and no abatement in competition beyond what necessarily results from the rights and privileges given the patentee by the federal government….[744]

In highway construction, contracts for paving and procurement of paving supplies have furnished a large proportion of the examples of patent and monopoly problems. The period 1920 to 1960 was one of noteworthy progress in this aspect of engineering; numerous patentable improvements were developed, and highway agencies naturally sought to obtain the benefits of their use. The weight of authority gradually swung to a position of approving the specification of patented or exclusive source items or their equal, provided there is no intent thereby to restrict the competition among bidders.[745] In addition, practical safeguards against hardships in preparing bids often are provided by the contracting agency through advance agreements with owners of patented products or exclusive sources to allow their use by all bidders on equal terms. The question of whether contractors' offers of materials are equal has been the subject of much litigation.

a. Warranty of Commercial Availability

This is an important consideration, as by including a brand name product or component in its specifications, the agency warrants the commercial availability of that product or component.[746] This warranty does not, however, relieve the contractor of the usual risks of nonperformance that result from the contractor's relationship with its subcontractors and suppliers, or the willingness of the supplier to provide the product within the time period specified by the contract.[747] The agency warrants only that the sole source supplier will provide the product.

The warranty of commercial availability, in which the government warrants the commercial availability of brand name components, and the limits of the warranty, were discussed in *Edward M. Crough, Inc. v. Department of General Services of District of Columbia*.[748] That case involved a specification for a particular type of roofing material, for which there were only two known suppliers and only one local supplier. In addition to requiring the particular roofing material, the District required a 5-year guarantee. Therefore, there was not a realistic option for the contractor to deal with anyone

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[742] State *ex. rel.* Polaroid Corp. v. Denihan, 34 Ohio App. 3d 204, 517 N.E.2d 1021, 1026 (1986).

[743] Edward M. Crough, Inc. v. Department of General Services of D.C., 572 A.2d 457, 461 (D.C. App. 1990).

[744] Dillingham v. Mayor, et al., of City of Spartanburg, 75 S.C. 549, 56 S.E. 381, 384 (1907).

[745] Hoffman v. City of Muscatine, 212 Iowa 867, 232 N.W. 430 (1931).

[746] Edward M. Crough, Inc. v. Department of General Services of D.C., 572 A.2d 457 (D.C. App. 1990).

[747] *Id*. at 463.

[748] 572 A.2d 457 (D.C. App. 1990).

other than the one local supplier. The specification was thus considered to be a sole-source specification. Initially, the supplier agreed to supply the product, but would not provide the 5-year guarantee because it believed that the roof design was inadequate. The District then agreed to redesign the roof to accommodate the supplier's concerns, and the supplier agreed to provide the guarantee.

The contractor attempted to argue that the warranty of commercial availability had been breached. However, where there was one supplier willing to meet the terms of the specification—providing the required material and the 5-year guarantee—commercial unavailability was not shown.[749]

The court contrasted this contractor's situation with the facts of *Aerodex, Inc. v. United States*, in which the contract called for a particular brand name component "or approved substantial equal."[750] The contractor found that the sole supplier of the required part refused to sell the part to the contractor or to make its specifications available to the contractor so that they could be fabricated elsewhere. There was no way to obtain either the brand name or a "substantial equal." In that case, the court found that the government had the obligation either to ascertain the availability of the component, or to provide specifications so that the component could be duplicated by the bidder or other suppliers.

b. Challenging Sole-Source Specifications

A party challenging the award of a contract who did not submit a bid will be found to have standing if it can prove that it would have submitted a bid but for the sole-source specification, that its equipment was equivalent to that specified in the bid specifications, and that the restrictions of the sole-source specification undermined the integrity of the competitive bidding process.[751] A sole-source specification may be found invalid and contrary to public bidding requirements if it can be shown that comparable products or systems were available.[752]

Generally, an agency should be able to advertise for bids for and ultimately purchase the type of products that they desire, within the confines of public bidding requirements. Public bidding laws do not require that specifications be so general in description that every supplier of a product can bid on the contract, thereby denying the agency of the type and quality of goods or services that it is accustomed to. Specifications are not illegal merely because they may be met only by one vendor. They may, however, be objectionable if they are drawn to the advantage of only one manufacturer, not for satisfying the public interest but to ensure award to that particular vendor.[753]

Specifications cannot be so precise as to knowingly exclude all but one prospective bidder.[754] If the agency should reasonably know that only one bidder can satisfy its specifications, then the agency should seek bids for a brand name or the equivalent of that product.[755] The "or equal" or "or equivalent" clause may serve to eliminate a challenge to specifications that the specification is proprietary or that the agency is seeking a sole source without adequate justification.

Where the choice of materials in a contract is not for a particular brand name but rather for a particular type of material over another, the agency is given greater latitude to choose the type of material that it wishes to be used in its project. Thus, there was no valid claim for an equal protection violation by a gravel supplier challenging bid specifications that called for the use of crushed stone rather than crushed gravel.[756] The Vermont DOT had rewritten its standard specifications to require the use of crushed stone rather than gravel where crushed stone was available, finding that crushed stone provided a stronger road base.[757] There was no evidence in the case that the State's exercise of choice between competing products as a consumer denied the supplier equal protection. There was no allegation in that case that there was only one available supplier of crushed stone, and there was not an argument that the specification called out a particular brand or supplier.

The agency has broad discretion to draft terms for a contract, and courts will not substitute their judgment for that of the agency in the absence of fraud or bad faith.[758] This is particularly so where the agency shows that the particular provision calling for a specific product is reasonably required in order to meet the desired performance requirements and is free from any intent to restrict or eliminate competitive bidding. The test is whether the specification is drawn to the improper advantage of any particular member or group of the relevant industry or occupation and is not for any reason that is in the public interest, but is rather intended to ensure the award of the contract to that particular member or group.[759]

Whether the use of sole-source specifications is allowed at all depends on state law. New Jersey has a

[749] *Id.* at 461–62.

[750] Aerodex, Inc. v. United States, 189 Ct. Cl. 344, 417 F.2d 1361 (1969).

[751] Unisys Corp. v. Department of Labor, 220 Conn. 689, 600 A.2d 1018, 1022–23 (1991).

[752] *In re 1985 Washington County Annual Financial Report Surcharge*, 529 Pa. 81, 601, A.2d 1223, 1226–27 (1992).

[753] *Unisys Corp.*, *supra* note 7511, 600 A.2d at 1023.

[754] Utilimatic, Inc. v. Brick Township. M.U.A., 267 N.J. Super. 139, 630 A.2d 862, 865–66 (1993).

[755] *Id.* at 866.

[756] Hinesburg Sand & Gravel Co., Inc. v. State, 166 Vt. 377, 693 A.2d 1048, 1049 (1997).

[757] *Id.* at 1046–47.

[758] Construction Contractors Ass'n of Hudson Valley v. Board of Trustees, Orange Community College, 149 Misc. 440, 565 N.Y.S.2d 997, 1000 (1991); *see also* Nev. State Purchasing Div. v. George's Equipment Co., 105 Nev. 798, 783 P.2d 949, 953 (1989).

[759] *Construction Contractors*, *supra* note 758, at 1000.

statute that specifically prohibits the use of a particular manufacturer's brand in bid documents.[760] The purpose of the statute is to maintain the policies underlying competitive bidding, which is guarding against favoritism and corruption.[761] Each agency must determine whether its own state contracting statutes allow the use of brand names and "or equal" clauses.

c. Warranty of Specifications

Where an agency specifies a particular brand name product in its specifications, the contractor has no discretion but to use that product in order to comply with the contract. In such a situation, the brand name provision is considered a design specification that contains an implied warranty that satisfactory performance will result from adherence to the specification.[762] However, if the contract provision contains an "or equal" clause, it is not considered a proprietary or design specification, but is rather a performance specification that does not contain an implied warranty of constructibility.[763]

5. Risk Allocation through Exculpatory Clauses

Clauses in construction contracts that limit damages are considered to be in the public interest, such as those that protect the agency from claims that the agency has caused unreasonable delay.[764] A party may exculpate itself prospectively for its own conduct, whether intentional or unintentional. Exculpatory clauses contained in public contracts are subject to the general rules of contract law regarding exculpatory clauses. Clauses such as "no damages for delay" or "no pay for delay" are considered exculpatory clauses. One of the requirements for exculpatory clauses is that the clause must be conspicuous and cannot be buried in the middle of other contract language. A Texas court found that a "no damages for delay" clause was invalid because it violated the requirement that an exculpatory clause be conspicuous.[765] Whether a clause is conspicuous and meets the requirements for fair notice is a question of law. A clause is considered conspicuous if a reasonable person, against whom the clause is to operate, ought to have notice of it. The court found that a "no damages for delay" clause was inconspicuous where it was contained "in the midst of a multi-page, single-spaced contract."[766] The clause contained no heading or warning, nor was it typed in a conspicuous form such as larger or bolder typeface. Another problem with conspicuousness was found in a contract in which the exculpatory clause was printed on the back of the contract.[767]

a. No Damages for Delay

Contracting agencies may include provisions for shifting to the contractor the risk of costs caused by delay. Typically, these clauses allow only for a time extension in the event of delay. Where a no-damages-for-delay clause is enforced, the contractor will not be entitled to any damages attributable to the delay, including increased labor costs, project overhead, idle equipment, and additional bond premiums.[768]

Also, as an exculpatory clause, the clause will not be enforced against the nondrafting party if it is ambiguous. Thus, where a no-damages-for-delay clause included in a subcontract provided for "only" a time extension, it did not bar damages for delay since it was ambiguous as to whether the "only" applied to time extensions or to damages.[769]

Another court has held that another exception to the enforceability of a no-damages-for-delay clause is when the delay is caused by the "active interference" of the agency or the agency's bad faith.[770] "Active interference" is defined as something more than mere negligence, and contemplates "reprehensible behavior" beyond a simple mistake, error in judgment, lack of total effort, or lack of complete diligence. The public agency must commit some affirmative willful act, in bad faith, that unreasonably interferes with the contractor's compliance with the contract schedule.[771] Unless one of these exceptions applies, the clause will be strictly construed and enforced.[772]

The application of a no-damages-for-delay clause also may be limited if the arbitrary and capricious actions of the agency result in the delay.[773] This is particularly true where the agency declines even to grant a time extension to compensate for the delay; such a refusal may be interpreted as active interference in the contract or as bad faith.[774] The Connecticut court held in *White Oak Corp. v. Department of Transportation*[775]

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[760] Morie Energy Management, Inc. v. Badame, 241 N.J. Super. 572, 575 A.2d 885, 887 (1990); N.J.S.A. 40A:11-13(d).

[761] *Id*. at 888.

[762] Florida Board of Regents v. Mycon Corp., 651 So. 2d 149, 153 (Fla. App. 1995). Note, however, that the specification may be challenged as proprietary if it does not allow "or equal."

[763] *Id*. at 153–54.

[764] Calumet Constr. Corp. v. Metropolitan Sanitary Dist. of Greater Chicago, 163 Ill. Dec. 255, 581 N.E.2d 206, 209–10, 222 Ill. App. 3d 374 (Ill. App. 1 Dist. 1991), *appeal denied*, 587 N.E.2d 1012.

[765] Argee Corp. v. Solis, 932 S.W.2d 39, 61 (Tex. App. 1995).

[766] *Id*. at 61.

[767] Advance Elevator Co. v. Four State Supply Co., 572 N.W.2d 186, 188–89 (Iowa App. 1997).

[768] White Oak Corp. v. Department of Transp., 217 Conn. 281, 585 A.2d 1199, 1202–03 (1991).

[769] Ragan Enters. v. L & B Constr. Co., 221 Ga. App. 543, 472 S.E.2d 88, 89–90 (1996).

[770] Edwin J. Dobson, Jr., Inc. v. State, 218 N.J. Super. 123, 526 A.2d 1150 (1987).

[771] *Id*. at 526, A.2d at 1153.

[772] United States for Use of Wallace v. Flintco, Inc., 143 F.3d 955, 964 (5th Cir. 1998).

[773] Findlen v. Winchendon Housing Auth., 28 Mass. App. Ct. 977, 553 N.E.2d 554, 555 (1990).

[774] Miss. Transp. Comm'n v. SCI, Inc., 717 So. 2d 332, 339 (Miss. 1998).

[775] 217 Conn. 281, 585 A.2d 1199 (1991); *see also* United States *ex rel.* Evergreen Pipeline Constr. Co. v. Merritt Merid-

that while a no-damages-for-delay clause is generally enforceable and not contrary to public policy, it will not be enforced if (1) the delays were caused by the agency's bad faith or willful, malicious, or grossly negligent conduct; (2) the delay was uncontemplated at the time of contracting; (3) the delay was so unreasonable that it amounted to an abandonment of the contract and the project by the agency; and (4) the delay resulted from a breach of a fundamental obligation by the agency.[776]

Other states' courts have found the clause to cover both anticipated and unanticipated delays.[777] All appear to agree on the other three exceptions. A Maryland court in *State Highway Administration v. Griener Engineering Sciences, Inc.* considered the differences between these two lines of decisions, and found that the Maryland clause did apply to delays not contemplated by the parties at the time of contracting.[778] The court analyzed the "New York" line of cases, which follow *Corrino Civetta Construction Corp. v. City of New York*.[779] This case sets out the exceptions noted in the *White Oak* case above, including delays uncontemplated by the parties at the time of contracting. The New York court in *Corrino Civetta* based its conclusion on the concept of mutual assent, that a party could not be held to have bargained away a right to assert a claim resulting from delay that the parties did not contemplate.[780]

The court then considered the "literal" approach, under which all delays are covered by the no-damages-for-delay clause, whether they were contemplated by the parties or not. Relying on a Wisconsin case, *John E. Gregory & Son, Inc. v. A. Guenther & Sons Co.*, 147 Wrs. 2d 298, 432 N.W.2d 584 (1988) the court concluded that parties can mutually assent to such a clause without contemplating in particularity all potential causes of delay. The clause is included because parties realize that some delays cannot be contemplated.[781] Indeed, one could argue that if a delay was contemplated it could be worked into the project schedule and a cost attached to it in the bid.

Other states have enforced similar clauses. A North Carolina court found a no-damages-for-delay clause to be valid and enforceable.[782] The clause was unambiguous and provided that no contract provision would be construed as entitling the contractor to compensation for delays.[783] A Georgia court found in *Holloway Construction Co. v. Department of Transportation* that the contract did not contain an implied warranty for the department to sequence the work of prime contractors, and that a no-damages-for-delay clause applied to bar claims for damages attributable to delays by other contractors.[784] In a similar case, the Georgia court held that the grading contractor could not recover damages from the State resulting from the delay attributable to the bridge contractor's performance.[785] The contract expressed the mutual intent that the State would not assume vicarious liability for delay caused by another contractor, and that a contractor's sole remedy in the event of delay was an extension of time.[786] An agency may be found to have waived the benefits of a no-damages-for-delay clause by agreeing to pay delay claims of the prime contractor, and thereby subject itself to the delay claims of subcontractors.[787]

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ian Constr. Corp., 95 F.3d 153, 167 (2d Cir. 1996); Miss. Transp. Comm'n v. SCI, Inc., 717 So. 2d 332, 338 (Miss. 1998).

[776] White Oak Corp. v. Department of Transp., 217 Conn. 281, 585 A.2d 1199, 1203 (1991); *see also* Jensen Constr. Co. v. Dallas County, 920 S.W.2d 761, 770 (Tex. App. 1996); United States *ex rel.* Evergreen Pipeline Constr. Co. v. Merritt Meridian Constr. *Corp.*, 95 F.3d 153, 167 (2d Cir. 1996); *Miss. Transp. Comm'n v. SCI, Inc.*, 717 So. 2d 332, 338 (Miss. 1998).

[777] *Compare* State Highway Admin. v Griener Eng'g Sciences, Inc., 321 Md. 164, 577 A.2d 363, 370 (1990) (applies whether particular delay contemplated by parties or not) *with* Department of Transp. v. Arapaho Constr., Inc., 257 Ga. 269, 357 S.E.2d 593, 594 (1987) (applies only to those types of delay contemplated by the parties).

[778] *Greiner Eng'g*, *supra* note 777, 577 A.2d at 368–71.

[779] 67 N.Y.2d 297, 502 N.Y.S.2d 681, 493 N.E.2d 905 (1986).

[780] *Greiner*, 577 A.2d at 368–69.

[781] *Id*. at 370.

[782] APAC-Carolina, Inc. v. Greensboro-High Point Airport Auth., 110 N.C. App. 664, 431 S.E.2d 508, 516, *review denied*, 438 S.E.2d 197 (1993).

[783] *Id.*

[784] 218 Ga. App. 243, 461 S.E.2d 257, 260 (1995).

[785] Department of Transp. v. Fru-Con Constr. Corp., 207 Ga. App. 180, 427 S.E.2d 513 (1993).

[786] *Id*. at 514.

[787] Findlen v. Winchendon Housing Auth., 28 Mass. App. Ct. 977, 553 N.E.2d 554, 556 (1990).

i. Effect of Suspension of Work Clause.—A suspension of work clause generally allows some compensation to the contractor where the work has been delayed. Where the contract incorporates the federally-required suspension of work clause, however, this does not necessarily operate to negate or to prohibit a no-damages-for-delay clause. The federal clause specifically provides that no equitable adjustment will be made for delays if they are excluded under any other provision of the contract.[788]

ii. Delay For Environmental Testing.—Where an agency knows that construction is occurring in an area that is or likely is contaminated and where environmental testing may need to be done to determine the method of disposal of excavated material, it may include a special provision addressing the potential for delay for testing. For example, the Washington State DOT has included such a provision for construction located in the vicinity of the Commencement Bay Nearshore/Tideflats site, which is an EPA-listed hazardous site. Washington State DOT's contract included work for environmental cleanup, and provided that delays of up to 60 days could occur while the agency waited for test results in order to determine how to handle certain materials. In using such a clause, the agency should take into account the reasonable time needed to accomplish sampling, receipt of results, and determination of how to proceed in light of the results. The agency should be able to document the time needed for the delay.

iii. Prohibition of No-Pay-for-Delay Clauses.—States may prohibit the use of no-pay-for-delay clauses by statute. For example, Oregon forbids the use of such a clause in a statute that states that such a waiver is against public policy:

Any clause in a public contract for a public improvement that purports to waive, release or extinguish the rights of a contractor to damages or an equitable adjustment arising out of unreasonable delay in performing the contract, if the delay is caused by acts or omissions of the public contracting agency or persons acting therefor, is against public policy and is void and unenforceable.[789]

b. Termination for Convenience

A provision in a highway construction contract allowing the state to terminate under certain specified conditions, such as for public convenience, with payment to be made only for work actually completed at the time of termination, is considered an exculpatory clause. As such, it is required to meet the requirements for such clauses.[790]

Standard termination for convenience clauses in public transportation contracts provide for termination caused by conditions that are beyond the control of the contractor. Grounds for termination for convenience include restraining orders or injunctions obtained by third parties: Executive Orders of the President for war, national defense, or national emergency; or acts of God. In addition, circumstances justifying termination for convenience could include loss of funding, or other circumstances that would make it in the best interest of the public agency to terminate the contract.

Termination for convenience contract provisions provide for written notice to the contractor, and should clearly set forth the contractor's obligations upon receipt of the written notice. Most state transportation standard contract documents provide for termination for convenience, but provide few details of the process or what is compensable. Strong termination for convenience provisions provide for contractors to stop work as specified, terminate all subcontracts, place no further orders for materials or services, transfer title and deliver to the agency fabricated or partially fabricated parts, return unused material to stock, develop and submit to the owner a material inventory, and to make the project site safe for the traveling public. State provisions typically include provision for the payment of completed and uncompleted work, items that are compensable and noncompensable, and a process to resolve the termination of convenience claim which include submission of claim within 60 days of termination date.[791]

A clearly drafted and explicit termination for convenience provision can minimize time-consuming termination disputes. Failure to list what items are compensable can lead to disputes.

In *Quality Asphalt Paving, Inc. v. State of Alaska Department of Transportation and Public Facilities,*[792] the contractor was seeking idle equipment damages for the period following the termination of convenience. The existing termination for convenience clause was silent on this issue. In *Quality Asphalt*, *supra*, the court affirmed the award of a limited 2-month time period after the termination for idle equipment costs based on Blue Book rates until the contractor was able to go back to work in full force. In addition, the court affirmed the award of unabsorbed overhead based upon the decision in *Nolan Brothers, Inc. v. United States.*[793]

In the *Nolan* case, the U.S. Court of Claims awarded Blue Book idle equipment damages after termination for convenience for 1.6 months, but denied recovery of post-termination overhead. Alaska DOT subsequently redrafted its termination for convenience provisions to clarify and eliminate these damage issues from future contracts.

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[788] 23 C.F.R. § 635.109(a)(2) (1999); Calumet Constr. Corp. v. Metropolitan Sanitary Dist. of Greater Chicago, 222 Ill. App. 3d 374, 581 N.E.2d 206, 209, 163 Ill. Dec. 255 (1991).

[789] OR. STAT. 279.063 (1) (1999).

[790] Department of Transp. v. Arapaho Constr., Inc., 180 Ga. App. 341, 349 S.E.2d 196, 198 (1981) *aff'd*, 257 Ga. 269, 357 S.E.2d 593 (1987).

[791] American Association of State Highway and Transportation Officials (AASHTO) Guide Specification, Division 100, at 48–49.

[792] 71 P.3d 865 (Alaska 2003).

[793] 437 F.2d 1371 (1971).

In Vermont, a major construction contract was terminated for convenience due to court injunctions resulting from lack of environmental approvals. The contractor asserted a claim for idle equipment and underabsorbed overhead, and the applicable Vermont provisions were silent on those issues. Subsequent settlement discussions were successful, and Vermont modified its termination provision to address idle equipment and loss of overhead. [794]

Ordinarily, a contract is considered to be irrevocable unless it contains terms allowing the parties to terminate the contract.[795] Clauses such as those allowing for termination for convenience must be explicitly set out in a contract between two private parties, and in the absence of such a clause the contract is presumed to be irrevocable.[796]

However, the doctrine of termination for convenience is an exception to the common-law requirement of mutuality of contract; the government is permitted to terminate the contract without being found to have breached the contract, if doing so is in the public interest. The United States Supreme Court has held that absent some contractual, statutory, or constitutional provision to the contrary, the government is entitled to terminate a contractor for any reason.[797]

This is easier to accomplish both in terms of authority and determination of compensation if the agency includes in its specifications a provision for termination of the contract for public convenience.

In addition to setting out the fact that the contract may be terminated for public convenience, the clause should also establish how the contractor is to be compensated in the event of such a termination. Examples of such clauses may be found in the standard specifications of state transportation agencies and in the federal standard specifications.

The owner is best served by having an explicit termination for convenience provision to limit exposure and liability. A standard termination for convenience clause provides the agency with broad rights to terminate the contract whenever the agency deems termination to be in the public interest.[798] The termination clause should be explicit as to damages, to avoid any surprise, limit contractor recovery to defined damage elements, and eliminate speculative claims of unreimbursed overhead and profit. Special attention should be devoted to idle equipment and overhead to prevent compensation arguments for equipment damages that are incurred after the termination, and to preventing the recovery of anticipated profits on work not performed. Some agencies permit recovery of reasonable settlement costs (including legal, clerical, and accounting costs) to prepare the termination for convenience claim, and storage and transportation costs to dispose of and protect termination inventory. Further, it limits the contractor's recovery to costs incurred as a result of the termination, payment for completed work, and costs of preparing the termination settlement proposal.[799] The contractor is not entitled to anticipatory profits as damages for breach of contract unless the agency acted in bad faith or abused its discretion.[800] In terminating the contract for convenience, the government limits its potential liability to the contractor to the value of the work completed at the time of the termination. The terminated contractor is entitled to its quantum merit performance under the contract, but not to its anticipated profits for work not yet performed.[801] Some termination of convenience provisions prohibit compensation of any absorbed overhead, loss of anticipated profits on work not performed, or idle equipment. The major impact of a termination for convenience clause is that it relieves the agency from the obligation of paying the contractor's anticipated profits for unperformed work.[802]

In *Department of Transportation v. Arapaho Construction, Inc.*, the court found that a termination clause was an exculpatory clause, and was unenforceable where the contract failed to incorporate any language explicitly referencing the clause's application to breach of contract cases.[803] Rather, the termination clause referred only to injunctions, and did not cover the agency's failure to provide required rights-of-way. Thus, the contractor was entitled to its lost profits.

A termination clause allowing the agency to terminate the contract in the event conditions arose that could prevent the contractor from proceeding with or completing the work was not considered to be the equivalent to the common law doctrine of impossibility of performance in *W.C. English, Inc. v. Commonwealth, Department of Transportation*.[804] Rather, the court held that the department properly terminated the contract under that clause when the contractor's cost overruns depleted the funds available to complete the project.

An ambiguity in a termination clause will ordinarily be construed against the drafter.[805] Thus where a contract contained two clauses, one a general termination for convenience clause and one a more specific clause

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[794] *Id.*

[795] Ham Marine, Inc. v. Dresser Indus., 72 F.3d 454, 460 (5th Cir. 1995).

[796] *Id.*

[797] Board of County Comm'rs, Wabaunsee County, Kansas v. Umbehr, 518 U.S. 668, 673–74, 116 S. Ct. 2342, 135 L. Ed. 2d 843 (1996).

[798] A.J. Temple Marble & Tile, Inc. v. Long Island R.R., 172 Misc. 2d 422, 659 N.Y.S.2d 412, 414 (1997).

[799] *Id.*

[800] *Id.* at 414–15; *see also* Century Marine, Inc. v. United States, 153 F.3d 225 (5th Cir. 1998).

[801] Hancock Electronics Corp. v. Washington Metro. Area Transit Auth., 81 F.3d 451 (4th Cir. 1996), *cert. denied*, 117 S. Ct. 299.

[802] D.C. v. Organization for Envtl. Growth, Inc., 700 A.2d 185, 199–200 (D.C. App. 1997).

[803] 180 Ga. App. 341, 349 S.E.2d 196, 198–99, (1986).

[804] 14 Va. App. 951, 420 S.E.2d 252, 254–55 (1992).

[805] Commonwealth of Pa. DOT v. Brozzetti, 684 A.2d 658, 665 n.14 (Pa. Commw. 1996).

that stated that the contract would be terminated only for failure to perform, inadequate performance, or lack of funding, the more specific clause controlled.[806]

c. Shortened Claim Filing Periods

Washington State has a statute pertaining to state highway construction that requires that any claims against the department arising out of a construction contract be filed in state court within 180 days of final acceptance of the contract by the state.[807] This provision is also included in the state's standard specifications.[808] A court reviewing the validity of the standard specification found that the provision was not unenforceable on the grounds that it was unreasonable.[809] Rather, the court found that legislative appropriations, budgetary constraints, federal funding concerns, the state's volume of public works contracts, and the overall highway funding scheme made the shorter limitation period reasonable.[810]

6. Other Requirements

a. Subcontractor Listing Requirements

Unless a statute or the bid specifications require listing of subcontractors, none will be required.[811] However, some states have enacted statutes that require bidders to list in their bids the subcontractors that they will contract with for the work if they are awarded the contract. An example is California's Subletting and Subcontracting Fair Practices Act. The purpose of the statute has been set out within the act as follows:

> The Legislature finds that the practices of bid shopping and bid peddling in connection with the construction, alteration, and repair of public improvements often result in poor quality of material and workmanship to the detriment of the public, deprive the public of the full benefits of fair competition among prime contractors and subcontractors, and lead to insolvencies, loss of wages to employees, and other evils.[812]

A case interpreting a similar statute describes "bid shopping" as the bidder's use of a low subcontract bid already received to pressure potential subcontractors into submitting lower bids.[813] "Bid peddling" is an attempt by a subcontractor to undercut a known bid that has already been submitted to the bidder on the prime contract.[814] Proof of actual bid shopping is not necessary to show a violation of a subcontractor listing requirement.[815] However, where bid shopping is shown, it will be considered to have prevented formation of the subcontract.[816]

The California statute requires that when a bidder on a street, highway, or bridge contract intends to subcontract to a particular subcontractor an amount "in excess of one-half of 1 percent of the prime contractor's total bid or…in excess of ten thousand dollars ($10,000), whichever is greater," then the bidder must list the name and place of business of that subcontractor.[817] It also requires that the agency must include the requirement for subcontractor listing either in its bid specifications or in its general conditions or standard specifications.[818]

New Mexico has a similar statute, the Subcontractors Fair Practices Act, modeled after the California statute.[819] It has the notable difference, however, of exempting highway construction work from its scope.[820] A case interpreting this statute is still instructive to the interpretation of similar statutes. In *Romero Excavation & Trucking, Inc. v. Bradley Construction*, a case that involved construction at a state university, the contractor was found to have violated the Act when it substituted itself for a subcontractor listed in its bid.[821] The subcontractor listing statute required that the bidder list only one subcontractor per category of work. If none was listed, then the bidder was required to perform that category of work itself. The statute essentially required the bidder to commit when it submitted its bid to either using a specified subcontractor to do a category of work or to doing that work itself.

The statute provided for circumstances when a substitution of a listed subcontractor was allowed; however, none applied in this case. The court concluded that even though the statute was directed at preventing substitution of another subcontractor, that allowing the prime contractor to substitute itself for a listed subcontractor was contrary to the purpose of the Act and was a violation.[822]

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[806] *Id*.

[807] WASH. REV. STAT. §47.28.120 (2002).

[808] WASHINGTON, STANDARD SPECIFICATIONS FOR ROAD, BRIDGE, AND MUNICIPAL CONSTRUCTION, § 1-09.11(3) (2000).

[809] Yakima Asphalt Paving Co. v. Wash. State Dep't of Transp., 45 Wash. App. 663, 726 P.2d 1021, 1024 (1986).

[810] *Id*.

[811] *See* Williams Bros. Constr. v. Public Building Comm'n of Kane County, 243 Ill. App. 3d 949, 612 N.E.2d 890, 895, 184 Ill. Dec. 14 (1993), *appeal denied*, 152 Ill. 2d 582, 622 N.E.2d 1229, 190 Ill. Dec. 912 (1993) (Illinois Public Building Commission Act did not require subcontractor listing); Pittman Constr. Co. v. Parish of East Baton Rouge, 493 So. 2d 178, 181 (1986), *writ denied*, 493 So. 2d 1206 (La. App. 1 Cir. 1986).

[812] CAL. PUB. CONT. CODE § 4101 (2002).

[813] Romero Excavation & Trucking, Inc. v. Bradley Constr., 121 N.M. 471, 913 P.2d 659, 662 (1996).

[814] *Id*. at 662; *see also* R.J. Land & Assocs. Constr. Co. v. Kiewit-Shea, 69 Cal. App. 4th 416, 81 Cal. Rptr. 2d 615, 617 (1999).

[815] Ray Bell Constr. Co. v. School Dist. of Greenville County, 331 S.C. 19, 501 S.E.2d 725, 731–32 and n.12 (1998).

[816] Pavel Enterprises, Inc. v. A.S. Johnson Co., 342 Md. 143, 674 A.2d 521, 531 (Md. App. 1996).

[817] CAL. PUB. CONT. CODE § 4104(a)(1) (2002).

[818] CAL. PUB. CONT. CODE § 4104 (2002).

[819] N.M.S.A. § 13-4-31 *et seq*. (1999).

[820] N.M.S.A. § 13-4-35 (1999).

[821] 121 N.M. 471, 913 P.2d 659 (1996).

[822] *Id.* at 663.

Similarly, a prime contractor in California was not allowed to substitute a subcontractor listed for one category of work for a subcontractor listed for another category of work. The bid did not divide that category of work between two subcontractors, and therefore the only listed subcontractor for that category was entitled to the subcontract.[823]

The California statute confers a right on the listed subcontractor that it will be awarded the subcontract, even though no subcontract exists at the time of bidding.[824] Unless statutory grounds for substitution are met, the prime contractor has no right to substitute another subcontractor for the one listed. The subcontractor's right to the subcontract may be enforced in an action against the prime contractor to recover the benefit of its bargain.[825] California's statute also provides for substantial penalties in the event that a violation is found. The awarding authority may, in its discretion, cancel the contract or assess a penalty against the contractor in an amount not exceeding 10 percent of the subcontract.[826] In addition, a violation may be grounds for discipline by the state contractors' licensing board.[827]

A federal district court has interpreted the Nevada subcontractor listing requirement as creating "pseudo-contractual" obligations on the part of the prime contractor, even though the subcontractor and prime contractor have no contract with each other at bid opening.[828] However, the statute makes them bound to one another in such a way as they may "disengage" only on specific statutory grounds. Under the statute, the subcontractor may obtain damages from the prime contractor for wrongful substitution.[829] It may also be entitled to injunctive relief against the prime contractor and the awarding agency, if it meets the standard for an injunction by showing that damages are insufficient relief. The subcontractor may meet this requirement by demonstrating that by not getting the subcontract, it will lose an opportunity to gain experience and enhance its reputation in the community. Damages cannot compensate for this loss.[830]

Where a statutory subcontractor listing requirement exists, it will be enforced even if not included in the bid specifications. A city was not estopped from enforcing the subcontractor listing requirement even though the bid package did not mention it, and even though the specifications referred to an American Institute of Architects provision requiring the identification of subcontractors following the contract award.[831]

b. Incorporation of Statutory Requirements

Any applicable statutory requirements in place at the time of contracting will be implied, even if not fully set out in the contract. The law existing at the time and place of the contract execution is part of the contract; this applies to public contracts as well as private.[832]

Statutory requirements may take the form of requiring a specific clause be included in a public contract, or may simply create an obligation for the contractor to comply with a particular legal requirement. Where valid regulations require the inclusion of a specific clause in a public contract, it will be deemed incorporated by operation of law even if it is omitted from the written contract.[833] This is true only where the required clause is consistent with the governing statute under which the contract is entered into; an inconsistent clause will not be incorporated by operation of law.[834]

c. Implied Terms and Warranties

All construction contracts have an implied warranty that they will be performed in a workmanlike manner.[835] However, where the contract contains an express provision setting out the degree of competence required for the work, such an implied warranty is considered redundant, and the warranty will not be implied.[836]

Like all contracts, public contracts contain an implied warranty of good faith and fair dealing.[837] The covenant is implied by law and "'obligates the parties to cooperate with each other so that each may obtain the full benefit of performance.'"[838]

d. Contracts Must Be in Writing

Because most transportation construction contracts are large transactions whose performance will span more than a year's time, an oral contract would likely violate the statute of frauds. Also, each agency's authority to contract is limited by the statutory language granting that authority. State and local agencies are creatures of statute, and have only those powers that the legislature grants to them. Generally, they do not

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[823] R.J. Land & Assocs. Constr. Co. v. Kiewit-Shea, 69 Cal. App. 4th 416, 81 Cal. Rptr. 2d 615 (1999).

[824] *Id*. at 618.

[825] *Id*.; CAL. PUB. CONT. CODE § 4103 (2001).

[826] CAL. PUB. CONT. CODE § 4110 (2002).

[827] CAL. PUB. CONT. CODE § 4111 (2001).

[828] Clark Pacific v. Krump, Constr., Inc., 942 F. Supp. 1324 (D. Nev. 1996).

[829] *Id*. at 1346.

[830] *Id*.

[831] Gaglioti Contracting, Inc. v. City of Hoboken, 307 N.J. Super. 421, 704 A.2d 1301, 1304–05 (1997).

[832] City of North Charleston v. North Charleston Dist., 289 S.C. 438, 346 S.E.2d 712, 715 (1986).

[833] United States v. Bills, 822 F.2d 373, 377 (3d Cir. 1987).

[834] *Id*.

[835] Korte Constr. Co. v. Deaconess Manor Assoc., 927 S.W.2d 395, 404 (Mo. App. 1996).

[836] *Id*. at 404.

[837] A.C. Shaw Constr., Inc. v. Washoe County, 105 Nev. 913, 784 P.2d 9 (1989).

[838] Record Steel & Constr., Inc. v. Martel Constr., 129 Idaho 288, 923 P.2d 995, 999 (Idaho App. 1996) (quoting Badgett v. Security State Bank, 116 Wash. 2d 563, 569, 807 P.2d 356, 360 (1991)).

have authority to make oral contracts. In addition, where a bid was lacking the bidder's signature, acceptance of that bid and making it part of a contract would have violated the statute of frauds.[839]

In *Scheckel v. Jackson County, Iowa*, the bidder and an assistant county engineer had a telephone conversation in which the assistant engineer informed the bidder that it was the low bidder and would get the award.[840] Ultimately, that bidder did not receive the award. The court held that the conversation between the assistant engineer and the bidder did not give rise to a contract. Under the statute, the contract required approval of the county board of supervisors, and neither the county engineer nor the assistant had authority to make an oral contract that would bind the county.[841]

Where there is a legal requirement that the contract be in writing and that it be approved by a particular individual or body, that requirement will be strictly enforced. In *Davis, Murphy, Niemiec and Smith v. McNett*, the court found that a county code section that provided that only county commissioners could enter into contracts for the county and required that the contracts be in writing was intended to prevent fraud against the county, and thus strict compliance was required.[842]

Modifications to the contract also must be in writing, and courts will strictly enforce prohibitions on oral modifications.[843] Likewise, any efforts to extend a contract by oral agreement will be found to not be binding on the agency.[844]

An exception to this requirement is found in *PacOrd, Inc. v. United States*.[845] In that case, the court found that the subcontractor was entitled to maintain an action against the United States in the absence of a written contract, because it was able to establish the existence of an implied-in-fact contract beyond the mere oral contract.

However, a North Dakota court did enforce an oral contract between a prime contractor and its subcontractor. In *Triton Corp. v. Hardrives, Inc.*, the street repair contractor who was interested in bidding on a city contract could not do so as it could not get a performance bond required by the city.[846] It then entered into an oral agreement with another company that could qualify for the performance bond. Its arrangement was that the street repair contractor would prepare the bid, and the second company would obtain the performance bond and submit the bid to the city. In return, the second company would be paid 10 percent of the contract price. This company was awarded the contract, but then decided that because the street repair company could not get a bond, that it would subcontract the work to someone else. The street repair company sued to recover its lost profits. The court found that a valid oral contract existed between the two contractors, and awarded the lost profits.[847]

Authority to contract must be express; apparent authority cannot serve as a means of holding a governmental entity to a contract.[848] A contractor relying on an individual's statement has no claim of entitlement to a contract. Further, the contractor has no claim of having been deprived of due process, as a legitimate claim of entitlement to the contract is necessary to establish a property interest.[849]

e. Specifications Are Not Rules

In *Alabama Department of Transportation v. Blue Ridge Sand & Gravel*, the aggrieved bidder challenged the department's standard specifications as "rules" that should have been adopted pursuant to the state Administrative Procedure Act.[850] The court found legislative intent to support its conclusion that the standard specifications were not "agency regulation, standard or statement of general applicability that implements, interprets, or prescribes law or policy."[851] Each standard specification was found to be a term that may be incorporated into a contract between the department and another party. Competitive bidding laws in Alabama allow a prospective bidder to challenge the inclusion of a specification; this is inconsistent with the specifications being rules.

Similarly, a Florida court held in *Department of Transportation v. Blackhawk Quarry Co. of Florida* that the department's standard specifications for road and bridge construction were not rules and did not need to be promulgated under the state Administrative Procedure Act.[852] Rather, the standard specifications set out standards for acceptance of materials, and were contract terms between the department and the agency.

Likewise, another court has held that the instructions to bidders included in the bid documents were not agency rules.[853] The court noted that the legislature had directed the agency in its statute to develop "policy and procedure guidelines" for contract documents. This was

[839] A.A.B. Electr., Inc. v. Stevenson Public Sch. Dist., 5 Wash. App. 887, 491 P.2d 684, 686–7 (1971).

[840] 467 N.W.2d 286, 288 (Iowa App. 1991).

[841] *Id*. at 289.

[842] 665 A.2d 1322, 1325 (Pa. Commw. 1995).

[843] Greater Johnstown School Dist. v. Frontier Ins. Co., 252 A.D. 2d 617, 675 N.Y.S.2d 212, 215 (1998).

[844] Alco Parking Corp. v. Public Parking Auth. of Pittsburgh, 706 A.2d 343, 348 (Pa. Super. 1998) (oral agreement to renew contract not binding on board where all contracts were required to be in writing and signed by the chairman).

[845] 139 F.3d 1320, 1323 (9th Cir. 1998) (applying Federal Acquisition Regulations, 48 C.F.R. § 2.101).

[846] 85 F.3d 343 (8th Cir. 1996).

[847] *Id*. at 346.

[848] Hutchison v. City of Huntington, 479 S.E.2d 649, 664 n.20 (W. Va. 1996).

[849] *Id*. at 664–5

[850] 718 So. 2d 27, 29–31 (Ala. 1998).

[851] *Id*. (quoting ALA. ADMIN. CODE, ch. 450-1-1 *et seq*.).

[852] 528 So. 2d 447, 450 (Fla. App. 1988).

[853] Cleveland Constr., Inc. v. Ohio Dep't of Admin. Services, 121 Ohio App. 3d 372, 700 N.E.2d 54, 68 (Ohio App. 1997).

found to be different from the situations in which agencies adopt "policies" that are in effect rules. The legislature used the specific terms "policy" and "guideline" where it could have used "rule."

The Florida court in the *Blackhawk Quarry* case did, however, find that the standard operating procedure adopted by the DOT for evaluating, approving, and controlling mineral aggregate sources was an administrative rule that had to be duly adopted under the Administrative Procedure Act. The operating procedure was an "agency statement of general applicability that implements, interprets or prescribes laws or policy."[854] Where such a policy is adopted as a rule, the agency has broad discretion in drafting and the rule will be upheld unless arbitrary and capricious.[855] Where administrative standards are adopted by the agency to govern construction projects and do not conflict with statutes, they will be considered to have the force of law.[856]

Cases from two states—Oklahoma and Oregon—note that the transportation agency's standard specifications in those states are actually adopted as agency rules.[857]

f. On-Call Contracts

In *Faulk v. Twiggs County*, the agency awarded a competitively bid contract to a contractor for on-call paving work.[858] Although the contract was indefinite as to the ultimate quantity, it contained a unit item bid price for the paving. The agency wanted to be able to pave in designated areas as funds to pay for the work became available, without letting a new contract each time. The court held that it was sufficient if the key for determination of the sum to be paid—the unit price—and the service to be rendered were contained in the contract.[859]

g. Express Warranties, Extended Warranties, and Related Federal Requirements

For many years, FHWA had a longstanding policy against the use of warranty clauses on federal-aid transportation projects. However in 1995, FHWA changed its views and allowed states to include warranty provisions for construction products. Federal regulations now provide that state highway agencies may include warranty provisions for projects on the National Highway System. Federal regulations exclude maintenance items from federal participation. They provide that no warranty will be approved if, in the judgment of the FHWA Division Administrator, it may place an undue obligation upon the contractor for items over which the contractor has no control.[860]

General warranty provisions have been limited to a maximum of 2 years (see 23 C.F.R. 635.413) and should be covered in the contract documents. FHWA regulations provide that warranties are short, generally 1 to 2 years. Projects developed under PPP agreements, however, may include warranties that are appropriate for the terms of the agreement. The regulations also permit alternate warranty proposals in best-value selections, and the alternates must be in addition to the warranty in the base proposal.[861]

A general warranty is permitted for specific construction project features, but not for the entire project since the contractor does not control the design process. Warranties may not cover maintenance, and contractors cannot warrant items over which they have no control. This has led to the use of concrete pavement warranties where the contractor can warrant the smoothness of the pavement. Warranties experience indicates that duration is from 2 to 5 years. Warranties beyond 5 years may not be cost-effective due to bonding or surety concerns. States have used warranty items for concrete pavement, bridge pavement, traffic striping, and expansion joints. If the work or project is not part of the NHS system, then warranties are covered under individual state or local laws and procedures.[862]

Pavement warranties are now in widespread use by many transportation agencies. Warranties are used to specify desired performance characteristics of a particular product over a specified period of time. Pavement warranties are intended to increase pavement performance by addressing quality during the construction process, and are not intended as maintenance agreements to cover undesirable work. There are two types of warranties in use: materials and workmanship warranties and performance warranties. Material and workmanship warranties generally involve preventive maintenance operations such as crack sealing, chipping, and micro sealing. Performance warranties relate to new roadway reconstruction, and have warranty periods from 5 to 20 years in duration.[863]

One practical consideration that public agencies may wish to consider in connection with the drafting and negotiation of warranty provisions, particularly in connection with long-term PPP project agreements, is appropriate provision for the enforcement of warranties in the event that the original contractor is no longer in business.

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[854] Blackhawk Quarry, 121 Ohio App. 3rd, at 450.

[855] Dravo Basic Materials Co. v. State, Dep't of Transp., 602 So. 2d 632 (Fla. App. 1992).

[856] Hoar v. Aetna Casualty and Surety Co., 968 P.2d 1219, 1221 (Okla. 1998).

[857] Anderson's Erosion Control, Inc. v. Oregon, *ex rel* Dep't of Transp., 141 Ore. App. 221, 917 P.2d 537 (Ore. App. 1996); Hoar v. Aetna Casualty and Surety Co., 968 P.2d 1219, 1221 (Okla. 1998).

[858] 269 Ga. 809, 504 S.E.2d 668, 670 (Ga. 1998).

[859] *Id*.

[860] 23 C.F.R. 635.413.

[861] 23 C.F.R. 635.413.

[862] FHWA, *supra* note 401, § IV, at 6–7; *see* http:/www.fhwa.dot.gov/programadmin/contracts/core04.cfm, last accessed Aug. 2, 2012; and FHWA Construction Program Guide, Warranties, at http://www.fhwa.dot.gov/construction/cqit/warranty.cfm.

[863] http://www.fhwa.dot.gov/pavement/warranty/.

h. Agency May Not Contract Away Essential Governmental Powers

An agency may not contract away any of the essential powers of government, including the police power, the power of eminent domain, and the power to tax.[864] Any contract provision that purports to do so will be considered void and unenforceable.[865]

[864] State Street Bank & Trust Co. v. Commw. of Pa., Treasury Dep't, 712 A.2d 811, 813 (Pa. Commw. 1998).

[865] State *ex rel.* Devonshire v. Superior Court, 70 Wash. 2d 630, 424 P.2d 913, 917–18 (1967) (city could not contract away power of eminent domain or bind itself to a restricted exercise thereof).

SECTION 2

CONTRACTOR LICENSING, QUALIFICATION, AND BOND REQUIREMENTS

A. LICENSING AND PREQUALIFICATION OF CONTRACTORS

1. Licensing and Prequalification Requirements

Where eligibility requirements are imposed on bidders by state law, they generally involve compliance with contractor licensing and prequalification rules.[1] Many states have requirements that all bidders must be licensed by the state and prequalified by the contracting agency as a condition to submission of a bid and award of a contract. These requirements have a direct relationship to determination of the lowest responsible bid. Application of these rules may vary depending on whether state or federal funding is involved. Licensing and prequalification requirements may apply to subcontractors as well as prime contractors.[2]

a. Public Policy Concerning Qualification of Bidders

Contractor qualification requirements are an important part of how transportation agencies carry out their statutory obligations to award construction contracts to the "lowest responsible bidder" in competitive bidding.[3] The term "lowest responsible bidder" means the bidder whose price is the lowest and whose offer adequately demonstrates the quality, fitness, and capacity to perform the work.[4] Determination of bidder qualifications and responsibility is largely a judgmental process.[5] Thus, the contracting officer's determination of responsibility is reviewed only for arbitrary and capricious action.[6]

Cases provide varying definitions of responsibility. One definition is "the bidder's apparent ability and capacity to perform the contract's requirements."[7] Another states that responsibility addresses "performance, capability of bidder including financial resources, experience, management, past performance, place of performance, and integrity."[8] Responsibility is considered to be a qualitative term, and includes trustworthiness, quality, fitness, and capacity to perform the contract satisfactorily.[9] Another court has allowed the consideration of financial ability, skill, integrity, business judgment, experience, reputation, and quality of previous work on public contracts.[10]

States may also define responsibility by statute. Oregon's public works statute provides that in determining if a prospective bidder has met the standards of responsibility, the public contracting agency shall consider whether a prospective bidder has:

> (i) Available the appropriate financial, material, equipment, facility and personnel resources and expertise, or ability to obtain the resources and expertise, necessary to indicate the capability of the prospective bidder to meet all contractual responsibilities;
>
> (ii) A satisfactory record of performance. The public contracting agency shall document the record of performance of a prospective bidder if the public contracting agency finds the prospective bidder not to be responsible under this sub-subparagraph;
>
> (iii) A satisfactory record of integrity. The public contracting agency shall document the record of integrity of a prospective bidder if the public contracting agency finds the prospective bidder not to be responsible under this sub-subparagraph;
>
> (iv) Qualified legally to contract with the public contracting agency; and
>
> (v) Supplied all necessary information in connection with the inquiry concerning responsibility. If a prospective bidder fails to promptly supply information requested by the public contracting agency concerning responsibility, the public contracting agency shall base the determination of responsibility upon any available information, or may find the prospective bidder not to be responsible[.][11]

Determination of these qualifications must be made by the contracting officer on a case-by-case basis. Historically, contracting officers have resorted to four basic methods, or combinations of methods, in carrying out this function. The earliest practice relied on the contracting officer's acknowledged authority to reject any (or all) bids if he or she deems it to be in the public in-

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[1] Portions of this section are derived from *Licensing and Qualification of Bidders* by Dr. Ross D. Netherton, published by the Transportation Research Board in 1976 and included in the first edition of SELECTED STUDIES IN HIGHWAY LAW.

[2] *See* 30 DEL. CODE §§ 2502 (1997); PG Constr. Co. v. George & Lynch, Inc., 834 F. Supp. 645 (D. Del. 1997).

[3] At least one court has held that even in the absence of a statutory requirement for doing so, public policy and economical conduct of government business require that contracts be awarded to the lowest responsible bidder. City of Phila. v. Com., Dep't of Envtl. Resources, 133 Pa. Commw. 565 577 A.2d 225, 228 (1990).

[4] *See* 30 ILL. COMP. STAT. 500/1-15.80 (2001) for a statutory definition of responsible bidder.

[5] W. Va. Medical Institute v. W. Va. Public Employees Ins. Bd., 180 W. Va. 697 379 S.E.2d 501, 503–04 (1989) (statute requiring award to lowest responsible bidder required subjective evaluation of quality, service, and compatibility with other programs in addition to price).

[6] *See, e.g.*, Advance Tank and Constr. Co. v. Arab Works, 910 F.2d 761, 765 (11th Cir. 1990) (applying Alabama law); State of Nev., State Purchasing Div. v. George's Equip. Co., 105 Nev. 798, 783 P.2d 949, 954 (1989); Grand Canyon Pipelines, Inc. v. City of Tempe, 816 P.2d 247, 250 (Ariz. 1991) (agency's decision regarding a determination of responsibility must not be arbitrary).

[7] Applications Research Corp. v. Naval Air Dev. Center, 752 F. Supp. 660, 682 (E.D. Pa. 1990).

[8] Bean Dredging Corp. v. United States, 22 Cl. Ct. 519, 522 (1991).

[9] Stacy and Witbec, Inc. v. City and County of S. F., 44 Cal. Rptr. 2d 472, 483, 36 Cal. App. 4th 1074, *modified on denial of rehearing, review denied* (1995).

[10] La. Associated General Contractors, Inc. v. Calcasieu Parish Sch. Bd., 586 So. 2d 1354, 1363 (1991).

[11] OR. REV. STAT. § 279.029(6)(a)(B) (2002).

terest to do so. Under this authority, a bidder's qualifications may be investigated and evaluated to the extent necessary. Courts have generally upheld the authority of contracting officers to investigate prospective contractors. They have also upheld the substantive determination of the administrative agency in the absence of any evidence of fraud, collusion, bad faith, or arbitrary and capricious conduct.[12]

A second method relies on the requirement that contractors must furnish performance bonds and other security for the protection of the general public and of individuals dealing with the contractors. Its rationale is that if a contractor can furnish the necessary bonds and sureties, the contracting officer may rely on the surety's investigation to verify the contractor's fitness.

A third method includes requirements that persons desiring to engage in general construction contracting or any of the various specialized branches of contracting must first obtain a license for this purpose. Licensing procedures normally call for a duly authorized public agency to examine the applicant and determine whether it is competent in its knowledge of engineering, construction, business administration, and laws applying to contracting, and has a good business reputation.[13] The contracting officer may wish to rely on this license, reasoning that if an applicant is considered "responsible" enough to obtain a contractor's license, it is responsible enough to bid on and receive the award of a public works contract.

Because both surety bonding and licensing have their limitations, a fourth method—prequalification—is widely used by states to evaluate contractors' qualifications. Under this procedure, contractors wishing to bid on public works contracts must previously be determined by the contracting agency to be qualified for the category of work involved and for undertaking a project of the size advertised.

Each of these four methods, or any combination of them, may serve as the basis for a valid administrative determination that a particular low bidder is also the lowest responsible bidder. The choice of method to be used may be made by the legislature, or may be delegated to the governing body or chief administrative officer of the contracting agency.

Procedures for evaluating contractors' qualifications serve three major public interests, namely preventing or minimizing adverse consequences of contractor default or delay; maximizing the benefits of the competitive bidding system; and improving the quality of public construction work.

i. Prevention of Contractor Default or Delay.—Legislatures have sought to protect public investments in public works by requiring suretyship and indemnification provisions in all public works contracts. However, these efforts may not be enough to cover the costs that the public must bear. Bonding requirements generally protect public agencies from loss of funds invested directly in costs of preparation and construction of a project. But the indirect costs of the agency's added overhead expense and the public's added period of inconvenience cannot be recovered from the contractor's surety.

To some extent, public works agencies can minimize risks that contractors will overextend themselves by subdividing large contracts into segments, no one of which is likely to overtax the contractor to which it is awarded. However, in such situations a default or inexcusable delay inevitably affects not only the contractor directly involved, but also other contractors whose work schedules are planned with reference to the schedules of that contractor.

Public safety is also an important reason for insisting that construction contractors be qualified to perform according to contract standards and schedules. Moral, legal, and professional obligations call for transportation construction programs to provide safe and convenient facilities for public travel. Court decisions and statutes have eliminated or restricted some states' sovereign immunity from suits based on defects in design and workmanship. At the same time, statutory standards for safe working conditions in federal law apply to contractors on state construction projects using federal funds, and similar state laws apply to state-funded projects. Thus, competence to adhere to standards that protect the safety of the traveling public and of workers employed in construction activity is an important aspect of contractor qualification.

ii. Improvement of Competitive Bidding.—The competitive bidding system is intended to secure the highest quality work for the least cost. But it can do this only if individual bidders realistically analyze the requirements of a construction plan and make their proposals fully responsive to these requirements and to prevailing market conditions.

Reliance on market forces alone to eliminate those contractors who engage in irresponsible bidding is not practical. Mandatory qualification procedures are viewed by all segments of the construction industry as a means by which responsible contractors can promote the stability of the bidding process by assuring that bids will maintain a realistic relationship to sound engineering practices and market conditions.

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[12] Marvec Constr. Co. v. Township of Belleville, 254 N.J. Super. 282 603 A.2d 184, 187 (1992); City of Cape Coral v. Water Services of America, Inc., 567 So. 2d 510, 513, *review denied*, 577 So. 2d 1330 (Fla. App. 2 Dist. 1990); Tasco Dev. & Building Corp. v. Long, 212 Tenn. 96, 368 S.W.2d 65 (1963).

[13] *See, e.g.,* IDAHO CODE § 54-1910(a) (2001).

iii. Improvement of the Quality of Public Construction.—Early proponents of contractor licensing and prequalification systems argued that such a system would result in higher quality highway construction. Contractors would be required to submit to examination of their qualifications prior to announcement of contracts. Also, the system included classification of contractors for certain types of work that they had demonstrated the ability to handle. Bidding would then be confined to those contractors whose competence was established.[14]

New or out-of-state contractors interested in doing work for transportation agencies may be allowed to bid only on small and less complex projects until they acquire the experience and financial resources to assure successful performance on larger projects. However, most states allow contractors wide latitude in the types of contracting work for which they may qualify. States assign capacity ratings to contractors according to fixed formulas that are applied uniformly to all applicants.

b. The Legal Basis of Contractor Qualification Systems

Many states require that persons engaging in general or specialized engineering or construction work must obtain licenses based on satisfactory demonstration of their professional competence. In addition, contractors intending to compete for public contracts for highway construction must, in most states, establish their qualifications for performing such work prior to being allowed to file their bids. In states that do not require prequalification, contractors who are low bidders on public projects must be certified as responsible and qualified to receive the contract award under a "postqualification" procedure. In both pre- and postqualification, the applicant is required to submit records of finances, management, and past relevant experience. Qualification is then based on a rating derived from evaluation of this evidence.

> A distinction must be made between the mechanism of licensing and the various forms of bidder qualification. Licensing is required to authorize individuals or corporations to engage in the business of construction contracting within a particular state. In contrast, prequalification and postqualification are methods of establishing a bidder's eligibility to bid on a public contract managed by a particular public agency, or to receive a particular contract as a result of competitive bidding. Licensing of contractors and certification under various qualification procedures must also be distinguished from that form of licensing that is in the nature of an occupational or privilege tax, which is chiefly for the production of tax revenue.[15]

i. Limits On State Police Power Applied To Contractor Qualification.—As in the regulation of businesses, trades, and occupations generally, the authority for licensing and qualification of contractors dealing with the public is based on the state's police power. The states must, however, respect the supremacy of federal law where it applies, and refrain from imposing any limitations on Interstate commerce. Accordingly, federal regulations applying to federally-assisted highway projects declare that state procedures for qualification of contractors will not be approved by the Federal Highway Administrator if in his or her judgment they may operate to restrict competitive bidding.[16] In addition to respecting the supremacy of federal laws, state contractor qualification requirements must avoid unfair discrimination among contractors, and must employ standards that are reasonably related to the legitimate objectives of the law.

Much of the early concern over possible discrimination is reflected in two Pennsylvania cases—*Harris v. Philadelphia*[17] in 1930 and *Corcoran v. Philadelphia* in 1950.[18] Both were taxpayers' suits to enjoin the application of municipal ordinances requiring prequalification of bidders on city public works projects. In *Harris*, the prequalification procedure was declared to be discriminatory; in *Corcoran*, the ordinance was sustained.

In *Harris*, the prequalification questionnaires were filed with the head of the municipal department that would supervise the performance of the contract, and if he was satisfied the prospective bidder's name was placed on a "white list" of "responsible bidders" entitled to submit bids without further inquiry. Others who were rejected by the department head were entitled to appeal his decision to a special board. In enjoining enforcement of this ordinance, the Supreme Court of Pennsylvania declared:

> It is obvious that, even if this plan is, in some respects, an advance on the previous method, it nevertheless opens wide the door to possible favoritism. The awarding director can place upon the white list the name of any intending bidder whom he chooses to approve, however irresponsible in fact, and that decision is not reviewable. On the other hand, he may compel all bidders, who are not favorites of his, to go to the expense of an appeal to the board, which will have before it only the answers to the questionnaire by those the awarding director has excluded from bidding, with no way of knowing whether or not their plant, equipment, experience and financial standing are superior or inferior to those of the bidders whose names the director has placed on the white list.[19]

Suggesting a way out of this danger, the court stated that prequalification might not be objectionable if all bidders' questionnaires were submitted to an independent committee having the expertise to properly analyze the evidence and advise on the classification and quali-

[14] *See* NETHERTON, *supra* note 1, at 1047.

[15] *See, e.g.*, WASH. REV. CODE § 18.27.030 (1999, 2003 Supp.)

[16] 23 C.F.R. § 635.110(b) (Apr. 2002).

[17] 299 Pa. 473, 149 A.722 (1930).

[18] 363 Pa. 606, 70 A.2d 621 (1950).

[19] 149 A. at 723–24.

fications of the applicants. It insisted, however, that all bidders must be treated equally in order to comply with the law.

Twenty years later, the Pennsylvania Supreme Court was asked to pass on another ordinance by which Philadelphia sought to require prequalification of bidders on municipal contracts.[20] The court held that the city's prequalification requirements were entirely reasonable, and were applicable to all potential bidders without discrimination. Moreover, the court found no fault with the manner in which the system had been applied to the project advertised in this instance, and denied plaintiff's charge that the city had circumscribed the advertised project in such a way as to place it outside the scope of the work classification for which the plaintiff was certified.

c. Qualification of Contractors on Federal-Aid Highway Projects

A policy of protecting and encouraging competitive bidding for contracts to construct federal-aid highways is reflected in federal statutes and FHWA regulations. The basic mandate is the statutory requirement that federal-aid highway projects shall be performed by contracts awarded through competitive bidding, unless the Secretary of Transportation makes an affirmative finding that some other method better serves the public interest. Contracts shall be awarded only on the basis of the "lowest responsive bid submitted by a bidder meeting established criteria of responsibility."[21] At the same time, the statute states:

> No requirement or obligation shall be imposed as a condition precedent to the award of a contract to such bidder for a project, or to the Secretary's concurrence in the award of a contract to such bidder, unless such requirement or obligation is otherwise lawful and is specifically set forth in the advertised specifications.[22]

The FHWA regulations require federal approval of any state prequalification requirements that will be applied in a federal-aid project.[23] The regulations further provide that there shall be no approval of qualification procedures that operate to restrict competition or prevent submission or consideration of bids by any responsible contractor.[24] "No contractor shall be required by law, regulation, or practice to obtain a license" before it may submit in a federal-aid project bid or have that bid considered.[25] As a result, some states exempt federally-funded transportation construction contracts from their state licensing requirement.[26] However, this prohibition does not prevent states from requiring the successful bidder to obtain a business or professional license upon the award of a contract.[27] This rule is based in part on the constitutional doctrine that states may not subject nonresident contractors to requirements that impede their bidding and so create a barrier to Interstate commerce. However, it also reflects the practical consideration that licensing serves no purpose in the bidding phase of a public works project. Federal regulations permit states to apply this requirement to both resident and nonresident contractors bidding on federal-aid highway projects.[28]

Federal regulations also require that states must allow sufficient time between the call for bids and the opening of bids.[29] This allows all potential bidders an opportunity to be prequalified after a full and appropriate evaluation of the contractor's experience, personnel, equipment, financial resources, and performance record.

In recognition of federal regulations designed to foster competition, and of the fact that contractors on federal-aid highway construction projects are everywhere subject to prequalification or postqualification requirements, states may accord special status to federal-aid highway contracts under their licensing laws. Idaho's Public Works Contractors License Act, for example, states:

> It shall be unlawful for any person to engage in the business or act in the capacity of a public works contractor within the state without first obtaining and having a license. . . . No contractor shall be required to have a license under this act in order to submit a bid or proposal for contracts for public works financed in whole or in part by federal aid funds, but at or prior to the award and execution of any such contract by the state of Idaho, or any other contracting authority mentioned in this act, the successful bidder shall secure a license as provided in this act.[30]

Although federal policy thus encourages the fullest possible competition for federal-aid contracts and prohibits states from imposing licensing or prequalification requirements that might serve to exclude responsible contractors from out of state, federal policy also expects contractors on federal-aid projects to be responsible firms and seeks to keep federal-aid funding from going to non-responsible firms that have engaged in serious criminal conduct or other non-responsible actions.[31]

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[20] 70 A.2d at 623.

[21] 23 U.S.C. § 112 (2001).

[22] 23 U.S.C. § 112(b)(1) (2001).

[23] 23 C.F.R. § 635.110(a) (Apr. 1, 2002).

[24] *Id*.

[25] 23 C.F.R. § 635.110(c).

[26] MISS. CODE § 31-3-1(c) (2000).

[27] 23 C.F.R. § 635.110(c); *see also* 29 DEL. CODE § 6923(d) (contractor is required to have Delaware business license prior to execution of public works contract); Thompson Elects. Co. v. Easter Owens/Integrated Systems, Inc., 702 N.E.2d 1016, 1020, 301 Ill. App. 3d 203, 234 Ill. Dec. 362 (Ill. App. 1998) (county did not abuse its discretion in accepting lowest bid even though bidder was not licensed in the state; decision was based on bidder's experience, its prequalification approval, and the fact that the bid specifications did not require a license prior to contract execution).

[28] 23 C.F.R. § 635.110(a) (Apr. 1, 2002).

[29] 23 C.F.R. § 635.110(c) (Apr. 1, 2002).

[30] IDAHO CODE § 54-1902 (2000, 2002 Supp.).

[31] This portion of this volume is drawn from a publication prepared by the authors of the 2011 update to this current

Accordingly, the qualification of contractors for federal-aid highway projects is subject to federal legislation and to federal regulations revised significantly in 2008, which concern the suspension and debarment of contractors and subcontractors from federal-aid transportation projects by the USDOT, as discussed in Section 2(B)(1) of this volume.[32]

The enactment of the ARRA,[33] and the Fraud Enforcement and Recovery Act of 2009 (FERA),[34] has had a significant impact in this area. ARRA provided approximately $50 billion in funding for transportation capital projects, as part of a broader $500-billion economic stimulus package, and provided certain safeguards to protect that funding as described below. In addition to amending the Federal False Claims Act, FERA strengthened certain other safeguards in federal law, and provided $245 million in additional funding to support investigative and enforcement efforts.

ARRA established a Recovery Accountability and Transparency Board to oversee the use of federal stimulus funding. It reviews and audits ARRA-funded programs and projects, refers potential abuses to the Inspectors General of USDOT and other federal agencies for investigation, and offers recommendations to agencies, the President and Congress on measures to prevent waste, fraud, and abuse. ARRA also provides whistleblower protection for employees of state and local governments and contractors.

The enactment of ARRA and FERA also led the USDOT Office of Inspector General (OIG) to conduct a further review of USDOT's suspension and debarment program beyond the revisions to that program made by the rulemaking in 2008. In May 2009, OIG issued an ARRA Advisory concerning the suspension and debarment program,[35] and in January 2010 OIG issued a more detailed audit report on that program.[36] These reviews considered ways to strengthen the program's effectiveness, as discussed further in Section 2(B)(1) of this volume.

While state DOTs operate under their own state statutory authority to award state contracts, the award of a federal-aid highway or bridge contract requires FHWA concurrence in order to maintain continued eligibility for the federal-aid funding for such a contract. If a state DOT selects a contractor for a federal-aid contract who has been suspended or debarred by USDOT, the state DOT may not be able to obtain FHWA concurrence in the award of the contract or if it obtains such concurrence without FHWA officials being aware of the involvement of a suspended or debarred firm, it may later face FHWA withdrawal of federal-aid funding after the project is already underway. This gives state DOT officials strong reasons for ensuring that their state processes for contractor qualification take USDOT suspensions and debarments into account.

The USDOT OIG has played, and continues to play, an important role in the implementation of other fraud-prevention measures under ARRA and FERA. The OIG works with FHWA, other USDOT units, and with state and local stakeholders to combat fraud, waste, and abuse affecting federal-aid highway and bridge programs. The OIG is mandated by law to conduct audits and investigations to prevent and detect waste, fraud, and abuse affecting USDOT programs.[37] USDOT's Inspector General is one of the members of the Federal Recovery Accountability and Transparency Board established pursuant to ARRA.[38] The USDOT OIG has also been strengthened by FERA, which significantly strengthened the Federal False Claims Act (FCA) and also gave federal investigators and prosecutors "significant new criminal and civil tools to assist in holding accountable those who have committed financial fraud."[39]

Acting in coordination with FHWA and other agencies as appropriate, the USDOT OIG embarked on a series of initiatives flowing from ARRA and FERA. The OIG's goals focused on maintaining oversight over USDOT's implementation of ARRA programs, including new tracking and reporting requirements; conducting proactive and reactive grant fraud investigations involving ARRA-funded programs and projects; conducting investigations of collusive price fixing, of false

volume; ERIC KERNESS & PETER SHAWHAN, IDENTIFICATION, PREVENTION, AND REMEDIES FOR FALSE CLAIMS IN HIGHWAY IMPROVEMENT CONTRACTING (NCHRP Legal Research Digest 55, Transportation Research Board, 2011); available at http://onlinepubs.trb.org/onlinepubs/nchrp/nchrp_lrd_55.pdf, last accessed on Nov. 26, 2011.

[32] *See* 31 U.S.C. § 6101 Note; *see also* 73 Fed. Reg. 24,139 (May 2, 2008), repealing 49 C.F.R. pt. 29 and adopting a new 2 C.F.R. pt. 1200.

[33] American Recovery and Reinvestment Act of 2008, Pub. L. No. 111-5, 123 Stat. 115 (2009).

[34] Fraud Enforcement and Recovery Act of 2009, Pub. L. No. 111-21, 123 Stat 1617 (2009) (FERA); text available at http://www.gpo.gov/fdsys/pkg/PLAW-111publ21/pdf/PLAW-111publ21.pdf (last accessed July 26, 2012).

[35] USDOT OIG, Advisory No. AA-2009-01, ARRA Advisory–DOT's Suspension and Debarment Program, May 18, 2009, available at http://www.oig.dot.gov/sites/dot/files/pdfdocs/Final_DOT_ARRA_Advisory_05-18-09_.pdf (last accessed on July 26, 2012).

[36] *See* USDOT OIG Report No. ZA-2010-034, *Final Report on the Department of Transportation's Suspension and Debarment Program*, Jan. 7, 2010, available at http://www.oig.dot.gov/library-item/5255 (last accessed on June 11, 2010).

[37] Inspector Generals Act of 1978 as amended by the Inspector General Reform Act of 2008, Pub. L. No. 110-409, 122 Stat. 4302 (2008); available at http://www.ignet.gov/pande/leg/pl110-409.htm (last accessed June 12, 2010).

[38] *See* The Recovery Accountability and Transparency Board, http://www.recovery.gov/About/board/Pages/TheBoard.aspx and related links (last accessed on June 11, 2010).

[39] Press Release, White House Office of Communications, Statement of the President, May 20, 2009; available at http://www.whitehouse.gov/the-press-office/reforms-american-homeowners-and-consumers-president-obama-signs-helping-families-sa (last accessed June 12, 2010).

claims involving labor and materials, and of bribery of public officials; and promoting joint efforts with USDOT units and state and local stakeholders to combat fraud, waste, and abuse.[40]

The OIG also conducted fraud prevention awareness training and other outreach activities to inform USDOT staff, state DOTs, and others at all levels of government about how to recognize, prevent, and report suspected fraud.[41] The USDOT OIG has, among other things, prepared a training video on False Statements and Claims to provide government officials and members of the public with an understanding of common fraud schemes and to strengthen collaborative efforts aimed at prevention and detection of such schemes. This video is potentially useful for any federal, state, or municipal transportation officials.[42] As of January 31, 2010, the OIG had provided 168 training sessions for more than 11,000 individuals nationwide, including officials from FHWA regional offices, state DOTs, and other public agencies. As of January 31, 2010, OIG had also received 184 complaints and accepted 16 for prosecution.[43] The OIG continues to monitor fraudulent schemes in the contracting process and to issue audit reports concerning various administrative practices, develop work plans, and conduct outreach to various state DOTs and public authorities.[44]

In addition, the USDOT OIG, the Federal Recovery Accountability and Transparency Board, the Antitrust Division of the U.S. Department of Justice (DOJ), and the U.S. Government Accountability Office (GAO) have undertaken initiatives to combat waste, fraud, and abuse potentially affecting federal-aid highway and bridge projects following the enactment of ARRA and FERA. Such measures go beyond the scope of a discussion of qualification of bidders for federal-aid contracts, but are discussed in other publications.[45]

Beyond the statutory safeguards provided by ARRA and FERA and agency initiatives undertaken pursuant to them, the FARs were amended in 2008 to add new requirements for contractors and consultants dealing with federal agencies.[46] *It should be noted that the 2008 FAR amendments apply only to direct contracting by federal agencies, and do not apply to grant recipients. Thus, they do not apply to federally-funded state highway contracts on federal-aid projects.* They are instructive, however, with regard to ethics and disclosure requirements which the DOJ and Congress consider necessary to protect federal contracting from fraud.

The impetus for the FAR amendments came both from DOJ and from enactment of federal legislation, the Close the Contractor Fraud Loophole Act.[47] The 2008 FCA amendments require that every covered federal contractor adopt a written Code of Business Ethics and Awareness within 30 days after receiving the award of a federal agency contract and make that Code available to each of their employees. The 2008 FCA amendments also require that every contractor receiving a federal agency contract of more than $5 million, and major subcontractors on such contracts, make timely disclosure to the agency OIG, in connection with the award, performance, or closeout of a government contract by the contractor or subcontractor, whenever the contractor has credible evidence that a principal, employee, agent, or subcontractor has committed a violation of federal criminal law involving fraud, conflict of interest, bribery or gratuity, criminal or civil violation of the FCA, or receipt of a significant overpayment on the contract. The disclosure requirement includes an ongoing obligation to disclose any newly discovered information up to 3 years after the closeout of the contract. Note that a conviction, indictment, investigation, or conclusive proof is not required to trigger the disclosure requirement. The firm merely has to have "credible evidence" indicating that an associated person or firm has committed criminal conduct.[48] Under the 2008 FCA amendments, failure to make such mandatory disclosures contitutes grounds for federal suspension and/or debarment.

2. Prequalification of Contractors for Performance-Based Construction

The traditional process of developing and performing highway and bridge projects is usually conceived of as having three main phases. A state or municipal DOT or other public owner identifies a need for a transportation project, obtains public funding for the project, and conducts a planning and environmental review process,

[40] *See* the USDOT OIG's Strategic Plan dated Sept. 2009, available at http://www.oig.dot.gov/sites/dot/files/OIG_Strategic_Plan_2009_508.pdf (last accessed June 10, 2010).

[41] *See, e.g.*, http://www.oig.dot.gov/oig-recovery-training (last accessed on June 10, 2010), including a detailed USDOT OIG PowerPoint training presentation, Fraud Awareness and Prevention, available at http://www.oig.dot.gov/sites/dot/files/Website_2009_ARRA_OIG_General_Presentation.pdf (last accessed on June 10, 2010).

[42] USDOT OIG, False Statements and Claims Video, available at http://www.preventtransportationfraud.org/falsestatementvideo.html (last accessed on June 22, 2010).

[43] *See* USDOT OIG Recovery Act Monthly Report for January 2010, available online at http://www.oig.dot.gov/sites/dot/files/DOT%20OIG%20Monthly%20Report%20Num%2011%20January%202010%2002-05-10.pdf.

[44] *Id.* The USDOT OIG and the American Association of State Highway and Transportation Officials (AASHTO) held a Sixth Annual National Fraud Awareness Conference on Transportation Infrastructure Programs in Arlington, Va., from July 26 through 29, 2010; for further information, see http://www.preventtransportationfraud.org/ (last accessed on June 22, 2010).

[45] *See* KERNESS & SHAWHAN, *supra* note 31.

[46] 48 C.F.R. § 52.203.13

[47] Pub. L. No. 110-252, tit. VI, ch. 1, 122 Stat. 2323 (2008).

[48] 48 C.F.R. §§ 3.1003, 9.406-2(b)(vi), 9.407-2(a)(8), and 52.203.13.

which identifies a preferred alternative approach to the project. The DOT then either assigns in-house engineering staff, or retains an engineering firm as a consultant, to prepare detailed engineering designs for the project, with the personnel preparing, reviewing, and approving the engineering design for the project having to meet state licensing requirements for the practice of engineering as a profession. Finally, when the engineering plans are complete and funding is in place, the DOT lets a construction contract to the lowest responsible bidder, with bidders either being reviewed in advance before being allowed to bid (prequalification) or being reviewed after bidding and rejected only if they are determined non-responsible (postqualification). The DOT then inspects the construction work on an ongoing basis, either through in-house construction inspectors or construction inspection consultants, to assure that the contractor complies with the minimum quality standards established by the DOT's standard specifications.

While the traditional system has advantages, it also has disadvantages that become increasingly evident over time. It is relatively slow to deliver a completed project, because no construction work can be undertaken until all engineering design work has been completed. It does not, for example, allow for fast-tracking projects by allowing construction to begin while later stages of the project are still being designed. It does little, if anything, to foster teamwork between designers and construction contractors, because they are generally entirely separate businesses engaged in different lines of work and performing their respective functions at different times during the life cycle of a project.

One consequence of this is that design engineers often fail to obtain sufficient information about constructability issues from interacting with contractors who have field experience. As a result, some designers may on occasion produce designs that look good on paper and in theory, but prove to be more difficult, time-consuming, and expensive than necessary for contractors to build in the field.

Another consequence of this is that, if contractors encounter unanticipated site conditions, advanced deterioration of existing structures, or constructability problems, construction work may need to stop for weeks at a time while a team of design engineers, who had previously completed their work designing the project and had moved on to other things, are reassembled in order to analyze the problem and design a solution, with the public forced to cope with traffic congestion, the parties potentially incurring financial losses, and the DOT facing a number of dissatisfied parties in the meantime.

In addition, the authors note that although the prequalification and postqualification systems may weed out firms that have been convicted of criminal conduct or lack sufficient financial capacity or technical capability to perform the project, they do little beyond that to improve the quality of construction beyond meeting the specifications set by owners. Aside from contracts that may include incentive/disincentive clauses, cost-plus-time bidding, or quality incentives, they do little to identify or reward construction contractors who demonstrate quality in performance by building projects on time, within budget, safely, and with a cooperative attitude toward the public owner and members of the public affected by the project. If anything, the traditional prequalification and postqualification systems may involve a risk of generating perverse incentives, in which firms could gain cost advantages by cutting corners on quality of materials and equipment, employing inexperienced personnel willing to work for lower wages, not meeting contract specifications, and disregarding construction safety practices, and use cost advantages obtained through such practices to underbid higher-quality construction firms. Such contractors might increase administrative costs for public owners by requiring closer supervision through construction inspection. There might also be a risk that the projects built by such contractors might have higher maintenance costs following completion as problems resulting from inferior work practices develop over time.

The current trend toward innovative forms of project management, such as design-build (DB) and construction manager at risk (CMR), basically represents efforts to devise structural solutions to some of these difficulties. Both DB and CMR are intended to allow for fast-tracking of projects by allowing construction to begin while the design of later stages of the projects is still underway. Both DB and CMR are intended to provide for closer cooperation and teamwork between design engineers and construction contractors, so that project designs take constructability considerations into account and engineers remain part of the project team and available on an ongoing basis to help devise prompt solutions to unanticipated problems encountered by construction contractors in the field, thus minimizing construction downtime and project delays. Both DB and CMR are, in theory at least, also intended to help DOTs and other public owners reduce administrative costs by having DB or CMR firms take on greater responsibility for quality control and warranty commitments so that DOTs can reduce costs associated with construction inspection.

Unless DOTs and other public owners can select DB or CMR firms with an established record of proven performance and high quality, however, the DB and CMR approaches involve increased risks. If a DOT entrusts quality-control functions to a DB or CMR firm and reduces or eliminates construction inspection efforts in reliance upon expectations of quality, and if the DB or CMR firm abuses that trust, then both the DOT and the traveling public may face consequences in terms of poor-quality transportation facilities, growing maintenance problems, and lack of adequate means to hold contractors accountable for dealing with postconstruction problems. The traditional prequalification and postqualification approaches do not focus on selecting contractors who deliver the highest-quality results.

Solving such problems necessarily involves developing a system for evaluation and selection of contractors that identifies and places a value on contractors capable

of performing quality work without constant and close supervision, and capable of performing a project on time, within budget, and with minimal delays resulting from problems encountered in the field. This type of system will involve ongoing evaluation and rating of the quality of contractors' work over time, and will factor the rated quality of contractors' performance into the weighting of bids or the evaluation of proposals submitted through a competitive RFP process. Such a system can no longer continue to rely on the existing postqualification or prequalification systems without significant change.

The Transportation Research Board (TRB) and NCHRP have devoted attention to this issue. In 2009, TRB published a synthesis, *Performance-Based Construction Contractor Prequalification*,[49] which evaluates this issue through a detailed examination of contractor prequalification policies and procedures, contractor performance evaluations, barriers to implementation, and prequalification case studies, and offers both conclusions and recommendations for further research. It focuses on identifying contractor performance-based prequalification practices based on construction quality, timely performance, safety record, and other criteria, with an effort to identify systems that effectively furnish incentives for good contractor performance.[50] The study indicates that two guiding principles for evaluating such systems is whether such systems add value to projects by reducing performance risk and whether the elements of such systems are justifiable and defensible.[51]

The study defines performance-based prequalification as:

> A set of practices and backup documents that must be followed by a construction contractor to qualify to submit a bid on a construction project based on quality, past performance, safety, specialized technical capability, project-specific work experience, key personnel, and other factors. This information may be provided on a project-by-project basis or on a specified periodic basis.

It would go beyond the scope of the current volume to discuss in detail the research findings and syntheses of practice offered in the study. For state and municipal DOT officials responsible for efforts to develop improved project delivery systems for the future, careful and thorough consideration of this study and its findings would appear to be warranted. A few of the study's conclusions may be summarized briefly, however.

a. Dependence Upon Selection of Well-Qualified Contractors

The authors of *NCHRP Synthesis 390* recommend that highway construction agencies begin the process of transitioning to performance-based prequalification rather than continuing to rely on existing administrative prequalification or postqualification systems. They take the view that the bonding of construction contractors is associated more with administrative prequalification than with performance-based prequalification, and question what value performance-bonding adds to construction projects. They recommend that DOTs simplify the performance-based prequalification process, focusing on major rather than minor performance evaluation criteria, and seek to develop nationwide standardization of the information required by DOTs for performance-based prequalification. They suggest that both bidding and bonding capacity could be adjusted through a performance-based prequalification system, with performance-bonding requirements lowered for contractors with proven track records of high-quality performance. They suggest the use of a three-tier performance-based prequalification system, with the first tier including evaluation of the contractor's bonding capacity, the second tier involving a contractor performance-evaluation system based on specified factors, and the third tier involving project-specific prequalification of contractors for selected projects, in which agencies concluded that this would add value to the contractor-selection process for a given project.[52]

b. Contractor Prequalification Policies and Procedures

The authors of the NCHRP study examined state DOT approaches to contractor prequalification policies and procedures.[53] The authors found that 35 state DOTs had prequalification requirements. Of those, 29 required prequalification for all projects, and 6 required it only for selected projects. In addition, 21 applied the same prequalification criteria to all projects, whereas 14 applied prequalification criteria, which differed according to the monetary size, technical complexity, delivery method, technical content, or other characteristics of the contracts involved. Those figures changed somewhat when the prequalification requirements were performance-based. Of the states having performance-based prequalification procedures, 7 required prequalification for all projects while 11 required it for selected projects only. Four applied the same prequalification criteria to all projects, while 9 applied criteria that differed depending on the characteristics of the projects and contracts involved.[54] Analyzing the various prequalification forms in use by state DOTs, the authors of the NCHRP study identified 10 factors, falling into

[49] Douglas D. Gransberg and Caleb Riemer, *Performance-Based Construction Contractor Prequalification, A Synthesis of Highway Practice,* NCHRP Synthesis 390, TRB, The National Academies, Washington, D.C., 2009; available at http://onlinepubs.trb.org/onlinepubs/nchrp/nchrp_syn_390.pdf, last accessed on January 3, 2012.

[50] *Id.* at 3.

[51] *Id.* at 5.

[52] *Id.* at 54 to 60.

[53] *Id.* at Chapter Two, pp. 15 et seq.

[54] *Id.* at 16-17; see esp. table 5 and figures 6 and 7.

three broad categories, included in the majority of such forms. These were:[55]

- Financial criteria—type of business (publicly or privately owned), and financial statement.
- Managerial criteria—key personnel experience, major convictions for bidding or contract crimes or fraud, business connections, and any prior project defaults or other failures.
- Performance criteria—work classifications, construction experience, major project experience, and available equipment.

More than half of the state DOTs using performance-based prequalification procedures focused on eight particular criteria when making their prequalification determinations. The three most frequently cited factors were major project experience, technical ability, and past illegal behavior. The other five common factors included key personnel experience, available equipment, quality and workmanship, managerial ability, and financial capability.[56]

c. Contractor Performance Evaluations vs. Bonding and Bonding Capacity

Going beyond general prequalification criteria, the authors of the NCHRP study examined more closely what things state DOTs considered important in establishing credible contractor performance evaluation processes, and what particular criteria agencies focused on in rating contractor performance. The study found that, to establish credible processes, agencies focused on assuring the accuracy, fairness, and consistency of evaluations of contractor performance, and on establishing a retention period for such evaluations that was sufficiently long to be useful, but that still allowed marginal contractors who worked on improving their performance to have the opportunity for such improvements to be reflected in their current evaluations.[57] The study's authors reviewed the factors considered by agencies in rating performance, and identified 17 factors typically considered by the state evaluation systems. The 10 factors most frequently used by DOTs in such evaluations were:[58]

- Timely project completion.
- Coordination and cooperation with the agency.
- Timely and complete submittals of documentation.
- Environmental compliance.
- Conformance with contract documents.
- QA program effectiveness.
- Proper maintenance and protection of traffic.
- Safety program effectiveness.
- Impacts to the traveling public.
- DBE utilization.

Additional factors often considered in performance evaluations included coordination and cooperation with property owners, level of effort displayed on the job, coordination and cooperation with third-party stakeholders, timely punchlist completion; mitigation of time overruns, mitigation of cost overruns, and responsiveness to warranty call-backs.

d. State DOT Experiences

To consider how difficult it might be for state DOTs or other agencies to implement performance-based prequalification and how performance-based prequalification was working out in actual practice for those agencies that had already implemented it, the authors of the NCHRP study considered actual and potential barriers to implementation[59] and selected three agencies for case studies. [60] Of barriers to implementation, those considered to have the greatest significance included ensuring that agency evaluators were qualified, assuring that agency rules governing the process were transparent and logical, the potential impact of agency performance ratings on contractors' bonding capacity, and the legal implications of performance evaluations. A variety of other barriers were, however, also noted by state DOTs and contractors, and discussed by the authors of the study.[61] In selecting agencies for case studies, the authors sought agencies that had adopted objective contractor performance evaluation systems that supported their prequalification processes in a meaningful way and had adopted specific processes that not only used the performance evaluation output to reward contractors with a good record, but also encouraged contractors with a poor record to improve. Based on these considerations, the authors chose Michigan DOT, FDOT, and the Ontario Ministry of Transportation for case studies. Although these agencies' procedures and experiences varied somewhat, the case studies revealed that all three agencies included consideration of the following factors in their systems:[62]

- Contractors' financial capability.
- Contractors' calculated capacity factors from their financials.
- Detailed financial analyses.
- Contractors' equipment and plant resources.
- Performance evaluations.
- Past project experience.

Those interested in a closer examination of how these three agencies approached evaluating the performance of contractors, and what experiences they had in doing so, will find detailed case study evaluations of each in the NCHRP study.[63]

[55] *Id.* at 17–19.

[56] *Id.* at 21–23; see esp. figure 12.

[57] *Id.* at 26–28.

[58] *Id.* at 29–30, see esp. figure 19.

[59] *Id.* at ch. 4, at 37–40.

[60] *Id.* at ch. 5, at 41–53.

[61] *Id.* at 37–40.

[62] *Id.* at 41–43.

[63] *Id.* at 43–44 (Michigan DOT), 44–48 (Florida DOT), and 48–51 (Ontario MOT).

3. State Laws and Regulations Relating to Licensing of Public Works Contractors

By requiring persons who engage in public works construction to first obtain a license for this business, public agencies have an opportunity to screen applicants to assure that they have professional competence and other characteristics that favor high standards of workmanship and business integrity. Generally, these laws are completely separate in their operation from highway agencies' contractor qualification procedures, but in several states the licensing of contractors operates as part of the qualification process. A listing of state contractor licensing laws is included in Appendix D.

Some states' statutes make the undertaking or overseeing of construction work in violation of a contractor's licensing law a misdemeanor.[64] Penalties for such violations generally consist of fines, although some states specifically authorize injunctions to restrain unlicensed persons from engaging in public works contracting.[65]

Contractor licensing laws and rules are necessary parts of the public's defense against unreliable, fraudulent, and incompetent work.[66] Accomplishment of this objective has been held to require that the regulatory penalties apply as consistently to licensed contractors who undertake work beyond the scope of their licenses as to those who are unlicensed for any type of construction work.[67] Conditions of the license must be met regardless of any inconsistent arrangements made between private parties, even though the convenience of the construction process may be served by them.[68] While recognizing that strict adherence to licensing requirements limits the flexibility often desired by contractors to improvise responses to unforeseen construction problems, courts are very reluctant to relax compliance standards.[69]

Although licensing laws may provide that intentional failure to comply is punishable as a misdemeanor, a parallel deterrent is the doctrine that courts will not enforce claims of contractors who do not comply with licensing laws.[70] This rule may be applied to defeat the entire contract as being illegal where entered into by an unlicensed contractor.[71] It may also be applied to limit the right of recovery by a licensed contractor to the dollar limit of the work that the license authorizes it to undertake. Application of contractor licensing laws to bar an unlicensed contractor's action against a state has been held not to constitute a taking of property without due process of law.[72] The failure of the contractor to obtain the required license prior to the start of the work cannot be cured; a subsequently obtained license does not validate the contract.[73] However, where an individual corporate officer was licensed, even if the corporation was not, a state court did enforce the contract rather than create a windfall to the owner for the completed but uncompensated work.[74] Most states require that the contractor be licensed at the time of contract execution, but do not require that it be licensed at the time of bid submission, opening, or award.[75]

Parties may choose to voluntarily comply with the terms of a contract with an unlicensed contractor. A court may enforce an arbitration award in favor of an unlicensed contractor.[76] Also, an unlicensed contractor may be able to recover actual documented expenses in a court of equity, upon a showing of clear and convincing proof of those expenses, even though the court will not allow recovery in quantum meruit.[77]

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[64] IDAHO CODE § 54-1920 (2000; 2002 Supp.), FLA. STAT. 489.127(2) (2001).

[65] State v. Summerlot, 711 So. 2d 589, 592 (Fla. App. 1998) (contractor was criminally liable for contracting without a license).

[66] Northwest Cascade Constr. Inc. v. Custom Component Structures, 8 Wash. App. 581, 508 P.2d 623, 626 (1973), *modified*, 83 Wash. 2d 453, 519 P.2d 1 (1974); Scientific Cages, Inc. v. Banks, 81 Cal. App. 3d 885, 146 Cal. Rptr. 780, 781 (1978).

[67] Alan S. Meade Assoc. v. McGarry, 315 S.E.2d 69, 71–72 (N.C. App. 1984).

[68] Hagberg v. John Bailey Contractor, 435 So. 2d 580 (La. App. 1983) (where a contractor who was duly licensed to do business in his own name undertook to assist a street paving contractor by acting under the latter's name, court held that he acted as an unlicensed contractor, because the licensing law required him to do business only under the name by which he was licensed).

[69] Scientific Cages, Inc. v. Banks, 81 Cal. App. 3d 885, 146 Cal. Rptr. 780, 781 (1975).

[70] Brady v. Fulghum, 308 S.E.2d 327, 330 (N.C. 1983); White v. Miller, 718 So. 2d 88 (Ala. App. 1998) (unlicensed contractor could not recover under contract or quasi-contract, nor could it file a mechanics lien for work that required a contractor's license because contracts entered into by unlicensed contractor, whether express and implied, are void); Fisher Mechanical Corp. v. Gateway Demolition Corp., 669 N.Y.S.2d 347, 247 A.D. 2d 579 (N.Y. App. 1998) (an unlicensed plumbing subcontractor could not recover in breach of contract action against general contractor on transit project even though the general contractor knew that the subcontractor was not licensed); Cevern, Inc. v. Ferbish, 666 A.2d 17, 22 (D.C. App. 1995) (no recovery in quantum meruit for unlicensed contractor); *see also* FLA. STAT. § 489.128 (2001).

[71] *See* White v. Miller, 718 So. 2d 88 (Ala. App. 1998).

[72] Cameron v. State, 15 Wash. App. 250, 548 P.2d 555, 557 (1976) (contractor sought recovery of bid bond and cost of parking lot construction).

[73] Jenco v. Signature Homes, Inc., 468 S.E.2d 533 (N.C. 1996).

[74] Berkman v. Foley, 709 So. 2d 628 (Fla. App. 1998).

[75] Thompson Elects. Co. v. Easter Owens/Integrated Systems, Inc., 301 Ill. App. 3d 203, 234 Ill. Dec. 362, 702 N.E.2d 1016 (1998).

[76] Davidson v. Hensen, 135 Wash. 2d 112, 954 P.2d 1327, 1331 (1998).

[77] Roberts v. Houston, 970 S.W.2d 488 (Tenn. App. 1997); *see also* Covern, Inc. v. Forbish, 666 A.2d 17 (D.C. App. 1995) (no recovery in quantum meruit even where contractor had complied with all licensing requirements except paying for the license).

With only a few exceptions, contractor license fees are set at levels needed to defray, at least in part, the expenses of administering the regulatory features of the law.[78] Principles of tax equity apply, and have been tested in cases where licensees pay differing rates according to classifications described in the law. Delaware's law provides that nonresident contractors must pay fees for each job performed, while resident contractors pay only a single annual license fee. A court held that this rate structure was not unconstitutional, despite the fact that nonresidents might pay considerably more fees annually than residents would.[79]

a. Comparison of State Legislation

The structure and much of the content of state laws for licensing of public works contractors reflect general agreement on what these laws should try to accomplish, and how this can best be done. A comparative summary of these laws is given in Appendix C.

Some state legislatures have chosen to establish special bodies or boards to administer licensing requirements, and have delegated to them substantial rulemaking authority for working out procedures and standards to assure that applicants have professional competence and other requisites. The separate status of these boards provides a degree of independence, which is considered important for impartial processing of license applications and administering disciplinary actions. As a result, little or no suggestion of favoritism or abuse of discretion in the issuance of licenses has occurred in the history of these laws. Coupled with provisions for formal review and appeal to the courts when rulings of the board are disputed, these laws have not been challenged on the constitutional sufficiency of their structure.[80]

b. Scope of the Licensing Requirement

Statutory definitions of contracting agree in substance that a contractor is one who, for a fixed fee, commission, or other form of compensation except wages, undertakes, oversees, or bids to undertake the construction, alteration, repair, improvement, removal, or demolition of a building, highway, bridge, road, street, railroad, or other structure.[81] The licensing requirement may be limited to instances of this activity where the monetary value of the contract exceeds a stated minimum figure.[82]

A number of other exemptions also appear in state contractor licensing laws. Typically, no contractor's license is required for the following:

- Public utilities engaged in construction, repair, or alteration of their own facilities.[83]
- Duly licensed engineers and architects acting solely in their professional capacity.[84]
- Persons engaged in building, altering, or repairing residential structures on their own property.[85]
- Construction, alteration, or repair of structures on land owned by the federal government.[86]
- Installation of products that are not actually fabricated into and become permanent parts of a structure.[87]
- Mowing and litter removal on highways.[88]

Judicial interpretation has also refined the legislative definition of the scope of these laws. Thus, where a person furnished equipment and labor on a day-to-day basis for construction of an industrial structure, he was not regarded as a contractor under the state's licensing act.[89] In the court's view, the statute's purpose was to insure the quality of contractors' work. For the license requirement to apply to a contractor, its role in a project must be a substantial one, both in terms of its size and its influence on the work performed.[90] Also, where the two entities that made up a joint venture were each licensed, no separate license was needed for the joint venture.[91]

Consistent with their purpose to protect the public against unreliable, incompetent, or fraudulent construction practices generally, statutes requiring licensing of construction contractors describe the objects of their regulation in broad and inclusive terms. As a result, much of the litigation involving these laws is concerned with interpreting statutory definitions of the term "contractor." This has called for making distinctions between contractors and their employees. It also requires distinctions between general contractors and others performing the functions of subcontractors, ma-

[78] *See* Lite House, Inc. v. North River Ins. Co., 471 S.E.2d 166 (S.C. 1996) (license bond was intended to apply toward health and safety concerns and not to cover supplier for nonpayment of materials).

[79] American Paving Co. v. Director of Revenue, 377 A.2d 379 (Del. Super. 1977).

[80] *See* NETHERTON, *supra* note 1, at 1057.

[81] *See, e.g.*, FLA. STAT. § 489.105(3) (2001).

[82] *See* IDAHO CODE § 54-1903(i) (2000).

[83] Westinghouse Elec. Corp. v. Rhodes, 97 Ariz. 81, 397 P.2d 61 (1964).

[84] FLA. STAT. § 489.103(11) (2001).

[85] *But see* City of Seattle v. State of Wash., 965 P.2d 619, 136 Wash. 2d 693 (1998) (city program that used unemployed homeless adults to upgrade lighting fixtures in low income housing units violated state requirement for electrical contractor's license).

[86] IDAHO CODE § 54-1903(f) (2000).

[87] IDAHO CODE § 54-1903(d) (2000).

[88] Clancy's Lawn Care and Landscaping v. Miss. State Board of Contractors, 707 So. 2d 1080 (Miss. 1997).

[89] Messina v. Koch Indus., 267 So. 2d 221*, writ issued*, 263 La. 620, 268 So. 2d 678 (1972).

[90] *See* Vallejo Dev. Co. v. Beck Dev. Co., 24 Cal. App. 4th 929 (Cal. App. 1994) (execution of contract and exercising administrative and oversight functions is acting in the capacity of a contractor, thus licensing requirement applied); Interstate Commercial Building Services, Inc. v. Bank of America, 23 F. Supp. 2d 1166 (D. Nev. 1998).

[91] J. Caldarera & Co. v. Hospital Service District, 707 So. 2d 1023 (La. App. 1998).

terial men, lessors of equipment, and fabricators of manufactured products used as fixtures.[92]

In their interpretation of contractor licensing laws, the courts have distinguished between contractors and their employees according to the extent to which they share in 1) determining the nature of the work to be done, 2) deciding on methods to be used, and 3) supervising the work. Therefore, in considering whether one who furnished a backhoe and operator must obtain a contractor's license, the court was persuaded he should not, because he was told by others where to dig, when to come to work, and what degree of care was needed, and the work was supervised by representatives of other contractors at the work site.[93]

In contrast, where one has control over the manner in which details of the work are accomplished, purchases materials and equipment, hires labor, and supervises the construction process, one is subject to the licensing requirement. This is true notwithstanding that he or she is called an employee, and that the employer makes suggestions as to these matters and coordinates various parts of the total project.[94]

Where decision-making authority is divided, or is exercised jointly, the criterion of control must be applied cautiously. Even when the decisions of one are limited chiefly to accepting construction plans and specifications that another has been hired to prepare and supervise, both may be regarded as general contractors so as to require them to obtain licenses.[95]

By the same criterion of control, one who undertakes to supply labor and materials to a general contractor may also be treated as a contractor. Where an entity was engaged in supplying temporary laborers to licensed contractors, retaining all payroll functions and ability to determine wages, that company was subject to contractor licensing requirements.[96] In another case, Arkansas' contractor licensing law was applied to a materials and labor subcontractor on the grounds that it had agreed to 1) do work to the owner's satisfaction, 2) indemnify the owner and general contractor for any claim resulting from the subcontractor's fault, 3) do work according to the owner's plans and specifications and be responsible for work and materials, and 4) restore damaged work.[97]

Where employee status is not at issue, liability under construction contractor licensing laws may turn on how directly and substantially one's work contributes to the construction process and project result. One who merely supplies goods for others to install, or whose products are not permanently attached to a structure, has regularly been held not to be a contractor within the terms of the licensing law. The same applies to lessors of construction equipment.

The distinction between contractors and manufacturers of fabricated items used in highway construction or operations has been presented in various situations involving on-site assembly and installation of fixtures. The California court's approach to this problem is illustrated in *Walker v. Thornsberry*, where a general contractor purchased prefabricated metal restrooms from a manufacturer, to be delivered to the construction site and bolted to a concrete foundation furnished for them by the purchaser.[98] Plumbing, electrical hook-ups, roofing, and painting were to be done by the general contractor or other subcontractors. On these facts, the court held that the manufacturer was not engaged in construction that required obtaining a contractor's license. Its contribution to the finished construction project was "at most minor and incidental," and not sufficient to make the items installed a fixed part of the structure being built.

The test used by the California court in *Walker v. Thornsberry* may have different results in other circumstances. For example, where a sprinkler system and mounting for a sign were buried in the ground, and there was excavation and construction of concrete dugouts, the court held that these actions constituted construction within the purview of the contractor licensing law.[99]

Painting must always be considered carefully according to its particular circumstances. Often it is entirely incidental to the construction process, where in other cases it adds something necessary to the structure. Moreover, painters frequently have almost complete control over the way their work is done. In such cases, painters may be considered contractors for licensing purposes.[100]

Contractor licensing laws may restrict their scope only to certain types of construction contracting. In the case of a contract to excavate and dispose of earth and rock, and to reclaim land at a sanitary landfill site, an Idaho court applying the state's licensing statute held that the work could be regarded as public works construction within the purview of the statute, even though no structures were involved in the project.[101]

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[92] *See* Farwest Steel Corp. v. Mainline Metal Works, Inc., 48 Wash. App. 719, 741 P.2d 58, 60, *review denied*, 109 Wash. 2d 1009 (1987) ("subcontractor" is one who takes from the prime contractor a specific part of the work, distinguished from materialman).

[93] Dahl-Beck Electric Co. v. Rogge, 275 Cal. App. 2d 893, 80 Cal. Rptr. 440 (1969).

[94] Campbell v. Smith, 68 N.M. 373, 362 P.2d 523 (1961).

[95] Harrell v. Clarke, 325 S.E.2d 33 (N.C. App. 1985).

[96] Personnel Temp. Services v. W. Va. Division of Labor, Contractor Licensing Bd., 197 W. Va. 149, 475 S.E.2d 149, 153–54, 197 W. Va. 149 (W. Va. 1996).

[97] Bird v. Pan Western Corp, 261 Ark. 56, 546 S.W.2d 417 (1977).

[98] 97 Cal. App. 3d 842, 158 Cal. Rptr. 862 (1979).

[99] E.A. Davis Co. v. Richards, 120 Cal. App. 2d 238, 260 P.2d 805 (1953).

[100] 19 A.L.R. 3d 1407, 1418

[101] McKay Constr. Co. v. Ada County Bd. of County Comm'rs, 99 Idaho 235, 580 P.2d 412 (1978).

c. Examinations and Criteria for Licensing

State contractor licensing laws generally require applicants to submit statements regarding their qualifications with their license applications. Thereafter, applicants may be required to take oral and/or written examinations, or submit to a background investigation by the licensing board, in order to fully establish compliance with licensing criteria.

Statements of criteria for licensing vary considerably in their details. Essentially they focus on the question of whether a contractor appears to have the ability to make practical applications of its knowledge of general contracting, and whether it has a good reputation for conducting business. Technical competence as a contractor must be shown in such matters as ability to read plans and specifications, estimate costs, and apply construction methods. Professionalism generally is also tested by reference to an applicant's knowledge of construction ethics and of the state's laws and regulations relating to construction, health, safety and liens, and the applicant's record in the business community.[102]

d. Impact of Licensing on the Design-Build Method of Contracting

When state licensing of contractors developed, the DBB or "lowest responsible bidder" method of contracting was the main, and indeed almost the only, method of public works contracting. As newer approaches to contracting have developed, such as the DB and CMR approaches, it has become apparent both that the state licensing process was not, in general, set up to accommodate DB or CMR contracting; and that the different approaches to licensing taken by different states have varying impacts on attempts to pursue DB or CMR contracting in different states.

Although it is now several years old, one of the best considerations of this issue is a legal memorandum, available online, prepared by two partners in a law firm with a significant practice in the area of infrastructure.[103] The article points out that before deciding how to organize a DB contractor to perform work in a particular state, it is first necessary to evaluate state licensing laws and any DB specific laws in that state. All 50 states and the District of Columbia require professional licenses for the performance of architectural or engineering (A/E) services, but the states' approaches to such regulation vary considerably. Beyond pointing out the ways in which differing statutory provisions can require those organizing DB firms to take different approaches, the memorandum provides a state-by-state survey of relevant statutes in all 50 states plus the District of Columbia, as those statutes stood when the memorandum was prepared, together with an assessment of how each state's laws affect the structure of DB entities. The memorandum also includes a page of summary observations on special issues relating to DB firms.

4. State Practice Regarding Prequalification of Bidders

The process and standards for a state's contractor qualification system may not be fully set forth in its statutes. Some of the law relating to prequalification is in the form of administrative regulations and the related policy directives of the state transportation agency's governing body.[104] See Appendix E for statutes and regulations relating to qualification of bidders for state transportation agencies.

The question of whether specific enabling legislation is necessary to authorize and guide such administrative action arose relatively early in the history of prequalification. Generally this was satisfactorily resolved by reference to the language of the state transportation agency's authority for awarding construction contracts. There was considerable support for the view that the power to impose prequalification requirements may be implied in performing the statutory duty to select the lowest responsible bidder.[105]

However, the earliest court decisions on prequalification dealt with this matter in a way that inspired most public officials to desire some statutory authority for their system even though it might not be absolutely necessary. Statutory authority for a local school board to require prequalification was at issue in *J. Weinstein Building Corp. v. Scoville*.[106] On its own resolution, the board required prospective bidders on its construction contracts to submit evidence of their qualifications before receiving copies of the project plans. The only state statute involved required that the contract be awarded to "the lowest responsible bidder furnishing security as required by the board." The court held that this did not authorize the prequalification requirement, saying that it required legislative authority.[107]

The critical issue for legislation is that it provide all the elements that courts have suggested are essential to assure fairness among bidders and promote competition. In this regard, seven main elements comprise the

[102] *See, e.g.,* IDAHO CODE § 54-1910 (2000, 2002 Supp.).

[103] Nancy C. Smith & Linda N. Cunningham, Memorandum, Impact of Licensing Rules on Legal Structure of D-B Contractors, Nossaman Guthner Knox & Elliott LLP, Apr. 11, 2005; available at http://nossaman.com/impact-licensing-rules-legal-structure-db-contractors, last accessed on Nov. 26, 2011.

[104] Pursuant to the requirements of the Administrative Procedure Act (APA) in most states, prequalification requirements are rules of general applications that should be adopted in compliance with the APA, rather than being merely included in standard specifications or statements of agency policy. *See* Department of Transp., State of Fla. v. Blackhawk Quarry of Florida, Inc., 528 So. 2d 447, *review denied*, 536 So. 2d 243 (1988), for a discussion of what type of procedure must be adopted as a rule under the APA rather than included as a contract specification that is not subject to the APA's procedures.

[105] *See* Netherton, *supra* note 1, at 1050, 1055.

[106] 254 N.Y.S. 384, 388, 141 Misc. 902 (Sup. Ct. 1931).

[107] *Id*.

prequalification systems that typically apply to the states' transportation construction contracts.

1. Authority for establishment of prequalification requirements.
2. Definition of the scope of application of the requirements.
3. Designation of the agency responsible for certifying contractor qualification.
4. Description of the evidence of qualification to be submitted to the certifying agency, and procedure therefor.
5. Description of the criteria for evaluating contractor qualification.
6. Establishment of a system of classification for contractors, and methods for rating contractor qualifications.
7. Establishment of bases for revocation or disqualification of contractors' certification, and procedures for review or appeal of such actions.

a. Designation of Responsible Agency

Except where it is part of licensing public contractors, prequalification for highway construction contracts is the responsibility of the state agency that awards those contracts. In those states that combine prequalification with licensing, the licensing agency examines and certifies bidder applicants for the particular classes of work and assigns the capacity ratings it deems them qualified for.

In the majority of states, enabling statutes provide merely that the prequalifying agency shall be the state transportation agency. Taken literally, this may be open to the objection that possible favoritism may exist because the contract-awarding agency is in a position to control who may bid. Therefore, the regulations governing prequalification may specify that certification shall be by or on the recommendation of a separate committee or board appointed for this purpose by the chief administrative officer or governing body of the highway agency. Judicial approval of the use of these advisory bodies to evaluate contractor qualifications has encouraged the adoption of this approach as an alternative to spelling out standards and procedures in excessive detail in enabling legislation.[108]

b. Scope of Requirements

Where limits are placed on the requirements for prequalification of contractors, they generally are stated in terms of minimum amounts of the contracts involved. Also, the prequalification requirement may be impliedly removed for emergency construction work where that work is statutorily exempt from competitive bidding.

Previous qualification in another state generally is considered in evaluating an applicant's experience and past record of performance, but with the single exception of the District of Columbia, out-of-state qualification is not accepted as an alternative to compliance with prequalification requirements.[109]

State laws and policies on prequalification of subcontractors vary. Those that favor subcontractor prequalification point out that the need to assure competency and responsibility in construction work is as great in regard to subcontractors as for prime contractors.[110] One benefit is that prequalification of subcontractors may assist prime contractors in locating potential subcontractors whose work record and financial condition have been documented and evaluated by the agency. Also, where specialty work is contracted for separately, the same specialty contractor may bid as a prime contractor on one project and appear as a subcontractor in another.

These benefits have a practical price for the public works agency that must process the additional volume of subcontractor applications, annual reports, and other paperwork. Specialty contractors include a high proportion of small businesses, of which a certain number may have only minimal experience and capitalization. Transportation agencies may conclude that they cannot effectively monitor the number or range of specialty businesses that may wish to be prequalified, and may prefer instead to let the public interest be protected by the diligence of the prime contractor, backed up by its surety bonding company, each of which has a direct interest in seeing that the contract is performed satisfactorily.

Administration of prequalification programs, regardless of their scope, needs good working definitions of subcontractors for the variety of situations in which it may be necessary to distinguish them from other parties in the construction process. The distinction between subcontractors and employees is one that must be made frequently. This was an issue in *Ro-Med Construction Company v. Clyde M. Bartly Co*. [111] Under Pennsylvania's regulations, contractors on state highway projects were required to use only subcontractors currently prequalified and classified by the DOT. The subcontractor had arranged to have its payroll carried by the prime contractor, and its key personnel listed with nonexistent job titles on the prime contractor's employee list. The genuineness of this apparent employee relationship was further brought into question by evidence of how labor actually was hired and supervised for the project in question. The court concluded that the doubtful employee-subcontractor relations precluded sum-

[108] *See* Harris v. City of Phila., 299 Pa. 473, 149 A. 722 (1930).

[109] While acknowledging savings of time and effort in processing certifications, the Department of Transportation noted that if certification by one state must be accepted by others on full faith and credit, it would be possible for fronts and firms of marginal eligibility to seek certification in states with the least effective programs for screening out ineligible businesses. This type of "forum-shopping" is not consistent with the objectives of the program. *See* 49 C.F.R. §§ 23.51, 23.53, and comments in 48 F.R. 33440 (July 21, 1983).

[110] *See* 30 DEL. CODE ANN. §§ 2502(a) (2001); PG Constr. Co. v. George & Lynch, Inc., 834 F. Supp. 645 (D. Del. 1993).

[111] 411 A.2d 790 (Pa. Super. 1979).

mary judgment on the legality of the contract under the department's prequalification regulations.

Distinctions may also have to be made between subcontractors and fabricators or suppliers of materials and structural units at work sites. Such cases generally turn on whether the party in question performs a substantial part of the contract as a "distinct part of the work" in such a way that it does not contemplate merely furnishing materials or supplying personal service.[112]

When legislation specifies standards to be applied in prequalification, strict construction of the statutory language may limit what a contracting agency can do to modify or change its procedures. Even where emergencies occur, courts are wary of allowing any administrative modification of standards or procedures that may exceed delegated authority. This was the result where the WSDOT attempted to direct the manner in which temporary measures would be taken while a major bridge was being replaced, and included this in the standards for prequalification of bidders on the project.[113] WSDOT decided that a temporary floating structure should be installed to allow traffic operations to be maintained on a state highway while a permanent bridge for the highway was being built at a nearby location. WSDOT had had success with the design and methods used by a particular contractor, and when it published its notice for bids, it modified its usual prequalification criteria to require bidders to show "necessary experience, organization and technical qualifications to design and construct floating structures," and to provide "evidence of previous successful use…of the proposed floating bridge configuration."[114] The proposed configuration, as set forth in the bid specifications, essentially described the methods used by a particular contractor who had done previous work on floating bridges. Under the published criteria, that contractor was the only one qualified to bid, and other interested bidders appealed WSDOT's denial of their prequalification.

The court viewed WSDOT's action as inconsistent with the policy that public contracts must be awarded through competitive bidding. The court held that this policy already was limited by the prequalification standards contained in the state law, and that any attempt to introduce further limitations administratively must be solidly based on legislative authority.[115] Admittedly, this put WSDOT in a difficult position, since its need to replace a major bridge destroyed by storm was both critical and immediate. Under the circumstances, WSDOT concluded that it did not have time to prepare a detailed bridge design and perform the customary engineering analysis before putting it into operational use. Therefore, it selected a solution that already had been demonstrated as safe for public use, and made the previous successful use of that design a requirement for prequalification of bidders. Notwithstanding this rationale, the court held that WSDOT lacked statutory authority to include an additional prequalification requirement, noting that "[b]y choosing to eliminate competent bidders at the prequalification stage, the salutory effect of truly competitive bidding was lost."[116]

c. Evidence of Qualification

Current practice has achieved a substantial degree of standardization regarding the types of evidence contractors must submit to show their qualifications, and the format for their presentation. This result is due mainly to early efforts of the American Association of State Highway and Transportation Officials (AASHTO) and the Associated General Contractors (AGC) to develop uniform definitions for the items of information that were considered to be the minimum necessary to permit reliable contractor prequalification.[117] While most states adhere to a standard request for financial information and history of other projects, some states do have additional information requirements.

Practice varies regarding the necessity for an applicant's financial statement to be prepared by a certified public accountant. Regardless of this requirement, the evidence submitted by an applicant to document its qualifications is subject to verification by the state.[118] However, the agency is not necessarily required to do its own investigation of the contractor's financial status if its submission is incomplete.[119]

Contractor prequalification statements, questionnaires, and related documents may be treated as confidential information by the state officials who receive and handle such documents, so long as disclosure is not required under public disclosure laws.[120]

Once they are determined to be prequalified bidders by the highway agency, contractors are periodically required to give evidence of their continuing eligibility for this status. Generally, this is done annually by submitting information on work performed during the previous year, an updated financial statement, and a description of current personnel and equipment. In addition, transportation agency regulations customarily require prequalified contractors to promptly notify the agency of any significant changes in their circumstances that might affect their capacity to perform work

[112] *See*, *e.g.*, Druml Co. v. Knapp, 6 Wis. 2d 418, 94 N.W.2d 615 (1959).

[113] Manson Constr. and Eng'g Co. v. State, 24 Wash. App. 185, 600 P.2d 643 (1979).

[114] 600 P.2d at 645.

[115] *Id*. at 646.

[116] 600 P.2d at 647.

[117] *See* NETHERTON, *supra* note 1.

[118] Dep't of Labor and Indus. v. Union Paving & Constr. Co., 168 N.J. Super. 19, 401 A.2d 698 (1979).

[119] Kimmel v. Lower Paxton Township, 633 A.2d 1271 (Pa. Commw. 1993) (contractor's failure to include "assets page" was legally disqualifying error that could not be cured after bid opening).

[120] For example, Washington's Public Disclosure Act specifically exempts financial records submitted to the Department of Transportation for the purpose of prequalification. WASH. REV. CODE 42.17.310(1)(m).

for which they have been prequalified. This requirement may be in general terms, or it may be particularized by referring to information called for in the agency's prequalification questionnaire.[121]

Where joint venture bids are planned, the general rule is that all the joint venturers must be prequalified separately, although the combined current capacity of all may be used to determine whether the joint bid will be accepted and considered.[122] In this matter the desires of the joint venturers regarding the percentage of a contract to be charged to the capacity of each of the parties are normally carried out in determining qualification. On the other hand, where two or more firms under the same ownership are combined for purposes of bidding, they are treated as a single entity for qualification and bidding.

The possibility that information obtained and relied on for prequalification of bidders may have secondary legal significance was raised in a Michigan court in *E.F. Solomon v. Department of State Highways and Transportation*.[123] This suit sought to recover liquidated damages withheld from a prime contractor for a work delay resulting from the insolvency of a subcontractor during the course of construction. Under the department's regulations, subcontractors as well as prime contractors were required to be prequalified and to submit evidence of their ability to carry out the work. The prime contractor had selected a paving subcontractor from the department's list of prequalified bidders.

Referring to these prequalification procedures, the plaintiff argued that a warranty of accuracy accompanied prequalification approval and listing by the department, and the plaintiff had reasonably relied on this implied warranty to his detriment. The plaintiff cited cases in which contractor claims were allowed because of reliance on erroneous information supplied by the agency.

While the court might have distinguished these cases, because in each case the state knew the unreliability of the information given to its contractor, it elected instead to meet the issue of an implied warranty of accuracy squarely. It stated that prequalification procedures were "simply a mechanism by which defendant determined who would be allowed to bid on state highway projects," and emphasized that recovery of claims based on misrepresentation of information generally depended on the state having previous knowledge of the prequalified bidders' erroneous character, or else having failed to take appropriate precautions that would have revealed the error in time to avoid it or the consequences of relying on it. The court also cited the state constitutional prohibition against using the credit of the state as a guarantee or surety in favor of a private individual and declared that the contractor's attempt to find an implied warranty of accuracy in the prequalification process would accomplish precisely what the constitution prohibited.

d. Classification of Contractors

The certifying agency generally has a twofold responsibility. First, it must determine what type of construction work each particular contractor is qualified to perform. Second, it must assign to the contractor a maximum limit on the amount of work it has the apparent capacity to perform successfully at one time. The former is generally referred to as a contractor's "classification," and the latter as its "rating." Customarily, the prequalification statute or regulations establish a list of classes of work, and instruct applicants to indicate those classes for which they wish to be certified.

The validity of classification lists, whether statutory or administrative, is likely to depend on their having a reasonably close relationship to the way the transportation agency organizes and advertises work to be performed through contract. Classification lists vary in detail, but generally reflect agreement on certain broad categories of construction, such as excavation and grading, paving, structures, and specialty work of all types. Classification systems that use these categories are readily defensible against possible charges that the certifying agency may arbitrarily and unfairly exclude contractors from bidding on work they desire. Among the categories of work listed, valid distinctions generally can be made on the basis of the types and amounts of equipment needed, the amount of working capital involved in acquiring and processing materials, technical and managerial skills, and organization required. In addition, contractors are not restricted from requesting that they be qualified for new classes of work.

e. Contractor Capacity Ratings

Certification of a contractor's eligibility to bid on public construction work normally includes an evaluation of its capacity to perform such work, and designation of its maximum limit in terms of the total dollar amount of work that the contractor may have underway for the contracting agency at any one time. Capacity ratings are individual, and are based on analysis of the contractor's disclosures regarding its current financial circumstances and other business information. Review of state laws and practices reveals several approaches to this analysis.

In some states, the entire function of rating contractors' capacity is treated as a matter of judgment by the contracting agency. Evaluation of contractors' capacity is based on statements of financial resources, experience, and organization. But inevitably, heavy reliance is placed on the contractor's record of past performance with the agency, and on the safeguard that it must furnish various bonds to indemnify the agency for any default in performance.

A contrasting practice is illustrated in those states where legislation or administrative regulations set forth mandatory formulas for establishing maximum capacity ratings for prospective bidders. Coupled with standard

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[121] E. Smalis Painting Co. v. Commonwealth, Dep't of Transp., 452 A.2d 601 (Pa. Commw. 1982).

[122] *See* OHIO REV. CODE § 5525.03.

[123] 131 Mich. App. 479, 345 N.W.2d 717 (1984).

definitions and uniform accounting procedures, these formulas promote systematic, uniform comparison of contractors' financial resources and other performance factors with a minimum of personal judgment by the rating officer.

Most states determine capacity ratings in a two-stage process. Typically, an applicant contractor's financial resources are initially rated to reflect its presumed ability to finance the construction work called for. Adoption of uniform accounting definitions and procedures permit formulas for financial ratings to become quite precise. But regardless of form, ratings are designed to measure financial responsibility by standards that have practical acceptance in the market place, where the contractor must compete for labor, materials, and technical skill.

Once financial resources are rated, an applicant's maximum capacity rating is established by evaluating its financial condition in conjunction with other relevant factors: (1) the types and amounts of equipment available, (2) the background of key personnel and structure of the organization, (3) previous experience, and (4) record of performance. Application of these factors to the applicant's current financial base may be through use of a multiplier number, or a percentage of a hypothetical perfect standard. Selection of a multiplier or other modifying factor may be based almost entirely on the judgment of the certifying officer, or upon judgment channeled to a prescribed set of factors.[124]

f. Rating First-Time Bidders and Out-of-State Contractors

Because the rating systems described above cannot entirely avoid using judgment based on an applicant's past performance, special problems arise in the evaluation of the capacity of new businesses bidding for the first time and of contractors whose base of operations and work record are outside the state. Because neither type of contractor has established any record of performance with the certifying agency, they may be given ratings of limited capacity until they demonstrate the capacity and reliability of their work.

In the case of out-of-state contractors, the normal practice is to relate their rating to their previous out-of-state experience. For example, the policy of the WSDOT is to award out-of-state contractors an initial prequalification rating of 2.5 times the highest value of the work the contractor has completed within that work class during the past 3 years.[125]

Where the state does not have a formula for rating out-of-state contractors and first time bidders, it must rely on administrative judgment based on information obtained from other agencies. These may be found objectionable because they depend so largely on judgment rather than on objective methods of measuring capacity and competency. Agency judgments may restrict competition or deal unequally with segments of the construction contracting industry. There is no history of litigation challenging these limitations on bidding capacity, and the apparent acceptance of prequalification practice under these rating formulas is largely attributable to a combination of careful initial handling of applications and effective use of administrative appeal procedures in the resolution of disputed ratings.

g. Conclusiveness of Prequalification

Courts are divided on the question of whether an agency may give further consideration to a prequalified contractor's responsibility when it submits a bid. The Alabama Supreme Court has held that the fact that a contractor is prequalified does not necessarily represent a finding of responsibility when a bid is submitted.[126] An Indiana appellate court has held that a bidder is a "responsible bidder" if it is capable of performing the contract fully, has integrity and reliability, and is qualified under the Indiana statute.[127]

5. State Practice Regarding Postqualification of Bidders

The practices of Minnesota, New York, and Rhode Island are based on a policy that favors examining a bidder's competence, financial responsibility, and other qualifications only if it is the low bidder on a public works contract. The proponents of this practice argue that it serves the general objective of encouraging as many contractors as possible to bid on a given project, and assures that the lowest responsible and competent bidder is awarded the contract. They assert that postqualification is more advantageous because it renders judgment on contractor capacity as near to the award of the contract as possible. Events can and do sometimes change a bidder's qualifications within a short time. If an apparent low bidder is postqualified, the most recent developments and current circumstances may be considered, and will assure the best evaluation. Also, for smaller agencies that do less construction, it may be more efficient to evaluate only the low bidder rather than all potential bidders.

Prequalification systems recognize the necessity of evaluating bidders in the light of their current circumstances and prospects. In many states prequalification procedures provide for updating information filed earlier. Advocates of postqualification point to this, however, as a case of duplicating the effort of both the bidder and the contracting agency.

In a New Jersey case, the court considered whether the New Jersey Highway Authority had discretion to use a postqualification process in a contract for towing services on state highways. In *Sevell's Auto Body Company, Inc. v. New Jersey Highway Authority,* [128] the

[124] *See* NETHERTON, *supra* note 1.

[125] WASH. ADMIN. CODE § 469-16-120(5).

[126] Crest Constr. Corp. v. Shelby County Bd. of Educ., 612 So. 2d 425 (Ala. 1992) (citing ALA. CODE § 41-16-50).

[127] Koester Contracting, Inc. v. Board of Comm'rs of Warrick County, 619 N.E.2d 587 (Ind. App. 1993) (citing A.I.C. 36-1-12-4(b)(8)).

[128] 703 A.2d 948 (N.J. Super. 1997).

state sought to enter into a contract for towing services on state highways. The provision in the specifications allowing postqualification of bidders was challenged. The court held that the specification did not conflict with the principle that a bidder may not agree to supply an essential element of its bid after bids are opened. Bidders were required to meet detailed standards on the bid submission date, and were required to submit with their bids a certification stating that they were in full compliance with those standards as of that date.

After low bidders for each zone were identified, they were asked to submit evidence of qualification. The court held that the agency's decision to use this method was an appropriate exercise of its discretion, in that it sought to minimize the administrative burden for itself and bidders while at the same time assuring that all bidders were competing on an equal basis.

6. Disadvantages Faced by Postqualification States

While postqualification provides for open access to participation in competitive bidding by the largest possible selection of firms and avoids the necessity of investigating the responsibility of construction firms unless and until a firm is the lowest bidder for a government construction contract, this approach to determining contractor responsibility also involves some significant potential disadvantages for the state DOTs or other public owners involved.

The postqualification approach appears to be implicitly based on the assumption that the need for competition, considerations of justice, and other factors involving the public interest require that agencies open contract lettings to the broadest possible group of potential bidders and give any firm consideration on a *de novo* basis any time it submits a low bid, even if it has significant legal, financial, or other responsibility problems.

A criminal conviction, for example, does not automatically dictate that a contractor must be found nonresponsible. Bidders for contracts, even those whose records include a criminal conviction, are entitled to due process before a DOT in a postqualification state determines whether to accept or reject their low bid. The state DOT may be able to resolve concerns about a firm's responsibility by imposing conditions on a contract award, such as requirements that all convicted officers or directors place their stock in a blind trust and remove themselves from management of the company, or that the company retain at its own expense an IPSIG or Monitor to prevent or deter any further misconduct. In addition, the public agency in its discretion, after giving due consideration to a conviction, may award the contract for other specific reasons. Various state DOTs have had experience, and some successes, with this approach.

There are, however, some significant potential disadvantages to this postqualification system. State DOTs operating solely under "lowest responsible bidder" contract award statutes, without the benefit of prequalification authority, cannot automatically comply with USDOT suspensions and debarments, even for firms that have been indicted or convicted for serious criminal offenses directly involving government contracting, and even when the state DOT concludes that the nature and severity of the criminal conduct, and the degree of moral turpitude involved, would make any award to such a firm against the public interest. Instead, each time they let contracts, they must receive and open bids from such firms, make an initial announcement that such a contractor is the apparent low bidder for a government construction contract, and then afford the contractor notice and an opportunity to be heard on the issue of whether the contractor is "responsible" within the meaning of the state's "lowest responsible bidder" statute. To comport with constitutional due process requirements, a federal debarment cannot be considered to be conclusive and automatically dispositive evidence in such a matter; it must be treated as merely evidence to be considered in the application of state law. On federal-aid projects, this forces the state DOT to go beyond merely reciting a prior history of a criminal conviction and federal debarment and build an administrative record that will withstand state judicial review before rejecting the bidder as non-responsible; or, in the alternative, face the near certainty that FHWA will withdraw the federal-aid funding from the project if the state fails to find the low bidder non-responsible and reject the firm's bid in favor of another firm that has submitted a higher bid.

The issue is not simply that state DOTs or other public owners lacking debarment authority must handle such a situation on a case-by-case basis. Even a firm from which a state DOT has previously rejected bids as nonresponsible can continue to bid on further projects. This gives nonresponsible contractors and their attorneys multiple ongoing opportunities to change organizational arrangements, to test and challenge the state DOT's stated rationale for finding the firm nonresponsible, and then to initiate legal proceedings in an effort to persuade not just the state DOT, but the state courts reviewing their actions, that the state DOT lacks sufficient evidence in the record to justify depriving contractors of major contracts. Aside from the risk of losing a court ruling in such a case, state DOTs or other public owners engaged in such litigation face a considerable administrative burden in working with their litigation attorneys to justify their decisions in court repeatedly on an ongoing basis.

7. Subcontractor Responsibility, State Review, and Approval of Subcontractors

State transportation agencies focus significant attention on contractor qualification, capacity, and responsibility. Attention should also be focused on subcontractors. Federal regulations (23 C.F.R. § 635.116) require that before any contract work is to be performed under a subcontract, it must be authorized in writing by the state highway agency. The regulations also mandate that the state highway agency assure that each subcontract contains all the pertinent provisions and require-

ments for the prime contract, such as the form FHWA-1273. Other regulations (23 C.F.R. 625.116 (a)) specify that not less than 30 percent of the total original contract must be performed by the prime contractor, exclusive of identified specialty items. Aside from these provisions, there are no regulations (aside from DBE regulations) that relate to subcontractor approval.

Disclosure of subcontractor approval often occurs after the contract has been signed and awarded. However, the Oregon Department of Transportation requires that the name of the subcontractor be disclosed within 2 working hours after the advertised bid closing time. Failure to submit the form by the disclosure deadline will result in a nonresponsive bid which will not be considered for award.[129]

Our research has found no uniform state subcontractor approval process. Each state adheres to its own individual statutory requirements and state processes.

Many states, prior to approving the prime contractor's request to subcontract, review the Excluded Parties List maintained by GSA to determine whether the proposed subcontractor is federally debarred or under suspension so as to avoid jeopardizing federal funding for the project. Some state agencies require the subcontractor to be prequalified using their state's prequalification process, while postqualification states review their internal records to ascertain if there is a cause for any concern. One postqualification state agency, NYSDOT, will check the GSA's Exluded Parties List and will also review corporate status, debarment, and willful violation lists maintained by the New York State Department of Labor and records of Occupational Safety and Health Administration (OSHA) violations. In addition, NYSDOT ascertains if the subcontractor resides in a discriminatory jurisdiction, which may require additional approvals. Further, NYSDOT will also review its own internal list of firms with known responsibility issues to determine whether there is any cause for concern. If the review raises any concerns, the contractor and the proposed subcontractor will be informed and given an opportunity to address and respond to these concerns and issues prior to NYSDOT's determining whether to approve or disapprove the request for permission to subcontract.

B. SUSPENSION AND DEBARMENT OF CONSTRUCTION CONTRACTORS; LICENSE REVOCATION; DISQUALIFICATION

1. USDOT Suspension and Debarment from Federal-Aid Programs

In reviewing potential contract awards and/or subcontractor approvals on federal-aid highway and bridge projects, state DOT officials must determine whether the apparent low bidder, chosen RFP responder, or proposed subcontractor is subject to a USDOT suspension or debarment from participation in federal-aid construction programs. Since USDOT suspensions and debarments have uniform nationwide application, USDOT suspensions and debarments have much broader impacts on firms that engage in business in more than one state than on any license revocation, disqualification, revocation of prequalification, or suspension or debarment actions undertaken by the officials of any individual state.

a. USDOT Suspension and Debarment Regulations: 2 C.F.R. Part 1200

USDOT undertakes the suspension or debarment of contractors, subcontractors, and other firms from federal-aid construction programs pursuant to USDOT's debarment regulations. USDOT has had suspension and debarment regulations in effect since 1984.[130] Since 2008, these have been codified as 2 C.F.R. Part 1200.[131]

USDOT does not suspend or debar contractors in a vacuum. Federal suspensions and debarments are subject to Executive Order 12549 of 1986 and Executive Order 12689 of 1989 and also to regulations of OMB, 2 C.F.R. Part 180. USDOT has adopted the OMB regulations, 2 C.F.R. Part 180 Subparts A through I as the USDOT policies and procedures governing USDOT suspensions and debarments.[132] USDOT suspensions and debarments apply to all contracts and subcontracts, regardless of tier, funded by USDOT and expected to equal or exceed $25,000 and also to all contracts governed by 2 C.F.R. §180.220(b) of the OMB regulations.[133] The USDOT regulations apply not only to contractors and subcontractors, but also to any participant in a covered transaction as defined by the OMB regulations, apparently including state DOT officials involved in the funding, award, and administration of federal-aid state contracts.[134]

The USDOT regulations require state DOTs, prime contractors, and subcontractors to pass the USDOT suspension and debarment requirements down to all contractors, subcontractors, and lower-tier subcontractors, by including in all contracts and subcontracts provisions requiring such participants to comply with 2 C.F.R. Part 180 Subpart C, and requiring such participants to include a similar term or condition in lower-tier covered transactions.[135]

It may be possible for a state DOT that is so inclined to obtain from USDOT an exception permitting an excluded contractor or subcontractor to participate in a

[129] OAR § 279C.370, First Tier Subcontractor Disclosure.

[130] *See* former 49 C.F.R. pt. 29, adopted in 1984; 49 Fed. Reg. 15,197 (Apr. 18, 1984).

[131] *See* 2 C.F.R. pt. 1200. For statutory authority, see 31 U.S.C. § 6101 Note, Pub. L. No. 103-355 § 2455, 108 Stat. 3243, 3327 (1994). For rulemaking adopting 2 C.F.R. pt. 1200 and repealing former 49 C.F.R. pt. 29, *see* 73 Fed. Reg. 24139 (May 2, 2008).

[132] 2 C.F.R. §§ 1200.10 and 1200.30.

[133] 2 C.F.R. § 1200.220.

[134] 2 C.F.R. § 1200.20.

[135] See 2 C.F.R. §§ 180.435, 1200.332, and 1200.437.

particular federal-aid project. The USDOT regulations authorize such exceptions to be granted by the heads of USDOT's various operating administrations, which include FHWA, and other persons to whom the heads of such operating administrations may delegate such authority.[136] As a practical matter, any state DOT seeking such an exception will probably need to do so not only through the appropriate FHWA Division Office, but also through those officials of the USDOT Office of Inspector General (OIG) handling FHWA matters.

b. Issues Addressed During 2008 Rulemaking

During 2008, USDOT undertook a rulemaking to repeal and replace its former 49 C.F.R. Part 29 suspension and debarment regulations with the current 2 C.F.R. Part 1200 suspension and debarment regulations.[137] In the course of doing so, USDOT addressed a variety of specific issues. These issues included, among other things, a government-wide federal initiative to consolidate all federal agencies' formerly separate suspension and debarment regulations into 2 C.F.R.; the adoption of OMB's regulations, 2 C.F.R. Part 180, as governing the policies and procedures to be followed in suspension and debarment proceedings; the availability of a procedure for seeking exceptions from USDOT; the applicability of USDOT's suspension and debarment requirements to all subcontracts, regardless of tier, over $25,000; the responsibility of all participants, including state DOTs, prime contractors, and subcontractors, to notify lower-tier participants of USDOT's suspension and debarment requirements; and the responsibility of state DOTs to inform prime contractors of the requirements of 2 C.F.R. §180.435.

c. Implementation Issues [138]

Any state DOT attempt to award a federal-aid contract to a firm under USDOT suspension or debarment, absent the grant of an FHWA exception expressly authorizing such an action, would involve substantial risks. FHWA could not only withhold the FHWA consent required to award such a contract, but it could also withdraw federal-aid funding from a project even if such funding had previously been approved. Even were such a situation not to come to FHWA's attention until after a state DOT had awarded the contract and the contractor had already commenced work, FHWA could retroactively withdraw all remaining federal-aid funding for the project and potentially seek to recover any federal-aid funds previously paid out under the contract, leaving both the state DOT and the contractor without the federal funding necessary to pay for any work already performed or to continue the project.

USDOT and FHWA take the suspension and debarment program quite seriously, and this program has received concerted attention from USDOT and FHWA management in recent years. The enactment of ARRA[139] and FERA[140] led the USDOT OIG to conduct a further review of USDOT's suspension and debarment program, beyond the revisions to that program made by the rulemaking in 2008. In May 2009, OIG issued an ARRA Advisory concerning the suspension and debarment program,[141] and in January 2010 OIG issued a more detailed audit report on that program.[142] These reviews considered ways to strengthen the program's effectiveness.

OIG's May 18, 2009, ARRA Advisory concerning the suspension and debarment program noted deficiencies that could leave USDOT potentially vulnerable to doing business with irresponsible businesses and individuals.[143] This Advisory noted a lack of adherence to USDOT policy time frames and a lack of oversight. OIG's more detailed audit report, issued in 2010, focused on increased risks that USDOT and other agencies might award contracts and grants to parties that USDOT would ultimately suspend and debar and on other weaknesses in USDOT's policies and procedures and internal controls.[144]

The 2010 audit report referred, for example, to a case in which the Commonwealth of Kentucky had awarded a $24-million contract in ARRA funds to a company that could have been suspended based upon indictments under USDOT's policy and Code of Federal Regulations. FHWA commented that the available evidence was not legally sufficient. The report and the authors noted that the FHWA's Chief Counsel had cited recent action to improve the processing of suspension and debarment cases, which included developing an action plan and dedication of more staff to this effort, steps to expedite cases, and efforts to reduce the backlog to meet the 45-day contract award time period.[145]

2. State Suspension and Debarment

Where prequalification statutes permit consideration of factors bearing on bidder responsibility as well as ability and capacity, prequalification and debarment

[136] 2 C.F.R. § 1200.137.

[137] 73 Fed. Reg. 24,139 (May 2, 2008).

[138] FHWA memorandum, Relocation and Amendment of Nonprocurement Suspension/Debarment Regulations, June 12, 2008, http://www.fhwa.dot.gov/construction/contracts/080612.pdf.

[139] American Recovery and Reinvestment Act of 2008, Pub. L. No. 111-5, 123 Stat. 115 (2009).

[140] FERA, Pub. L. No. 111-21, 123 Stat 1617 (2009); text available at http://www.gpo.gov/fdsys/pkg/PLAW-111publ21/pdf/PLAW-111publ21.pdf (last accessed June 12, 2010).

[141] USDOT OIG, *supra* note 35.

[142] *See* USDOT OIG Report No. ZA-2010-034, *Final Report on the Department of Transportation's Suspension and Debarment Program*, Jan. 7, 2010, available at http://www.oig.dot.gov/library-item/5255 (last accessed on June 11, 2010).

[143] USDOT OIG, *supra* note 35.

[144] *See* USDOT OIG, *supra* note 36.

[145] *Id.*; and address of Tom Holian, FHWA Chief Counsel, to TRB Annual Meeting, Jan. 12, 2010.

tend to be used as complementary processes. Contractors' efforts to assert a right to do business with public agencies have succeeded in some states, and have resulted in some procedural limits on agency discretion in debarment actions.[146]

Legislative authority for prequalification of bidders normally includes authority for the certifying agency to suspend or revoke a contractor's certification for various enumerated causes and "for other good cause."[147] Consistent with their basic approach to review of administrative actions, courts generally are not inclined to second-guess the decision of an executive agency on its merits in the absence of a showing of fraud, bad faith, or arbitrary action. Yet because prequalification directly affects the right to have one's bid considered for a contract award, disciplinary action that results in suspension or revocation of a bidder's eligibility is taken seriously by all interested parties. Recognizing that the right to engage in business has important economic consequences, courts have insisted that disciplinary actions against qualified bidders must be handled in accordance with rules that assure fairness and equal treatment. Actions must be taken in strict compliance with applicable statutes and administrative regulations.

This is illustrated in *White Construction Company, Inc. v. Division of Administration, State Department of Transportation*.[148] In that case the prequalifying agency notified a contractor of its temporary suspension by letter from the agency's Director of Road Operations, citing apparent failures to follow certain procedures on the work site and relying on statutory authority to suspend for good cause. In an action for mandamus to restore the contractor's bidding status, the Florida Supreme Court found that the agency's intended suspension was not effective because it was not issued by the Secretary of Transportation, as required by the statute.[149]

The court in *White Construction Company* made it clear that where prequalification authority is conferred by statute, and the certifying agency promulgates rules, the agency must fully comply with those rules.[150] Similarly, contractors must comply with these rules in order to protect their rights. For example, failure to make timely application for administrative review of a suspension order has resulted in a holding that the right to such a hearing was waived.[151] Likewise, a contractor was found to have not timely filed exceptions to the administrative law judge's decision where it mailed them on the last day of the applicable time period.[152]

a. Failure to Update Prequalification Records

Agencies may require the contractor to update or supplement its prequalification questionnaire or to notify the agency of significant changes in its status. For either type of requirement, however, interpretations of their scope differ. This is illustrated in *E. Smalis Painting Company v. Commonwealth, Department of Transportation.*[153] Department prequalification regulations required contractors to submit a statement of any felony convictions of its directors, principal officers, or key personnel, and also to notify the department of any changes in that information. Based on these requirements, and acting on information from a local prosecuting attorney's office that the petitioner's president had been convicted of a felony and was awaiting sentencing, the department suspended the contractor.

In contesting the suspension, the petitioner argued that the duty to submit a report of the conviction did not arise until sentencing was completed. The court disagreed. While conceding that the term "conviction" had both a popular usage and a technical usage, and that the technical usage should be used unless it would defeat the apparent intent of the law, the court felt that in this instance "conviction" was to be understood as meaning a verdict of guilty or a plea of guilty.[154]

b. Debarment for Failure to Pay Prevailing Wages

In the mid-1930s, the Davis-Bacon Act was amended to provide that where a firm was found to have disregarded its obligation to pay prevailing wages to employees, no contract would be awarded to that firm for 3 years from the date of publication of the list containing the name of the firm.[155] Several courts have held that failure to pay prevailing wages is grounds for debarment. In *Electrical Contractors v. Tianti*, the contractor was debarred for 3 years for failure to pay prevailing wages, even though the failure was found to be negligent rather than intentional.[156] In other cases, the violation of the prevailing wage requirement was found to be willful and therefore a basis for debarment.[157] In considering a claim that the bidder had violated overtime provisions, however, a court found that where the

[146] Sameena, Inc. v. United States Air Force, 147 F.3d 1148 (9th Cir. 1998) (contractor was entitled to notice and a hearing before being debarred).

[147] *See, e.g.,* Lawrence Aviation Indus. v. Reich, 28 F. Supp. 2d 728 (E.D. N.Y. 1998) (failure to promptly pay award of backpay and prejudgment interest to victims of sexual discrimination in hiring was grounds for debarment).

[148] 281 So. 2d 194 (Fla. 1973).

[149] 281 So. 2d at 197.

[150] 281 So. 2d at 197.

[151] Dickerson, Inc. v. Rose, 398 So. 2d 922 (Fla. App. 1981); Latrobe Road Constr. Inc. v. Com. Dep't of Transp., 107 Pa. Commw. 54, 527 A.2d 214, *appeal denied*, 536 A.2d 1335 (1987) (failure to raise issue of whether prequalification provisions violated due process was waived when not raised before agency review board).

[152] State Board of Registration v. Brinker, 948 P.2d 96 (Colo. App. 1997).

[153] 452 A.2d 601 (Pa. Commw. 1982).

[154] *Id*. at 602.

[155] 40 U.S.C.A. § 3144 (6 (2003); 29 C.F.R. pt. 5 (2000)).

[156] 613 A.2d 281, 223 Conn. 573 (1992).

[157] Hull Corp. v. Hartnett, 568 N.Y.S.2d 884, 77 N.Y.2d 475, 571 N.E.2d 54 (1991).

violation was not willful it did not render the contractor ineligible to bid.[158]

In *Copper Plumbing & Heating Company v. Campbell*, the Secretary of Labor's power to debar for wage law violations was challenged.[159] The court found that the regulations were not "penal" in nature and were necessary for effectuating compliance with and furtherance of the public policy represented by the labor acts. *Janik Paving & Construction v. Brock* also discussed the power of the Secretary of Labor to debar and cause such debarment to be listed with the Comptroller General.[160]

c. Other Grounds for Suspension and Debarment

Several other statutory grounds for debarments relating to misconduct, such as bribery of public officials, fraud in the procurement of public contracts, or violation of the Buy America Act, were enacted at the federal and state levels starting in the 1930s and continuing up to the present.[161] Additional statutes did not specify suspension or debarment for violation, but such powers were found to be inherent within the powers to establish a program or the regulations to effectuate a program. For example, *L.P. Stewart & Bro., Inc. v. Bowles* dealt with presidential power under the Second War Powers Act.[162] The court determined that the President had the power to allocate materials or facilities, of which requirements for national defense created a shortage, in such manner, upon such conditions, and to such extent as he deemed necessary or appropriate in the public interest. This included the power to issue suspension orders against those who did not comply with the program.

i. Antitrust.—If the contractor has been found to have violated the antitrust laws, a suspension or debarment proceeding may be undertaken at the federal level and possibly at the state level. However, the following situations may result in nonresponsibility determinations prior to the actual suspension or debarment:

1. The antitrust matter predated the practice of having suspension or debarment proceedings at the federal level following conviction for antitrust violations;

2. There is or was insufficient evidence for criminal conviction, but there is sufficient evidence to find a contractor to be "nonresponsible";

3. The prosecutors strike a deal with the contractor, in exchange for plea bargaining or testimony, that suspension or debarment will not take place at the federal level;

4. The contractor is named as an unindicted coconspirator and there is no recovery for antitrust based on a civil action;

5. An antitrust indictment has been rendered against the contractor;

6. Principals of a firm were convicted of antitrust violations while they were with another firm and no suspension or debarment proceeding was undertaken against those principals on an individual basis;[163]

7. The parent or the holding company of the contractor has been found guilty of antitrust violations somewhere else in the country.[164]

ii. Collusive Bidding.—Public policy favoring award of public contracts through competitive bidding serves the interest of the contracting agency by assuring that it obtains needed goods and services at fair prices, and serves the interest of contractors by assuring that all bidders will have equal opportunity to bid and receive equal treatment in consideration of their proposals. This policy is implicit in statutes and regulations directing that competitive bidding be used, and is explicitly implemented in legislation prohibiting fraud and combinations in restraint of trade and competition. All these interests are endangered when there is collusion among bidders to submit noncompetitive or rigged proposals, or otherwise restrict competition and thereafter conceal the fact that such an unfair advantage exists.

Collusion of this sort may take the form of agreements among bidders to submit proposals that are artificially high, or to submit identical bids, or for some bidders to withhold or withdraw their bids in favor of others. The damaging effects of contractor combinations may sometimes be less direct and obvious.

Instances of unpermitted collusion in bidding are usually thought of in terms of restricting competition by secret arrangements among bidders. However, the issue may arise through arrangements between contractors and public agencies. Collusive contracting was charged where a municipality leased a parking lot from an attorney who did work for the city, where it obtained insurance from a company in which the mayor owned stock and was employed, and where it deposited funds in banks where city officials served as director. Under these circumstances, it was held that the purchase of insurance from a company employing the mayor was the only act that violated the state's competitive bidding requirement. The other actions were held to not constitute prohibited forms of collusion in public bidding.[165]

Where there is evidence of a conspiracy to subvert a statutory requirement for award to the lowest responsible bidder through competitive bidding, the criminal nature and consequences of the conspiracy cannot be

[158] Hull-Hazard, Inc. v. Roberts, 517 N.Y.S.2d 824, 129 A.D. 2d 348, *aff'd*, 532 N.Y.S.2d 748, 72 N.Y.2d 900, 528 N.E.2d 1221(1988).

[159] 290 F.2d 368 (D.C. Cir. 1961).

[160] 828 F.2d 84 (2d Cir. 1987).

[161] *See, e.g.,* 41 U.S.C. § 106.

[162] 322 U.S. 398, 64 S. Ct. 1097, 88 L. Ed. 1350 (1944).

[163] State of N.Y. v. Hendrickson Bros., 840 F.2d 1065 (2d Cir. 1988), *cert. denied*, 488 U.S. 848, 102 L. Ed. 2d 101, 109 S. Ct. 129 (1988).

[164] *See* HARP, *supra* note 1, at 1124-N-22, 23.

[165] McCloud v. City of Cadiz, 548 S.W.2d 158 (Ky. App. 1977).

avoided by reliance on the contracting authority's statutory right to reject any or all bids "if it is in the public interest to do so."[166]

iii. Improper or Unethical Conduct.—In connection with the DBE program, many situations arise where the contractor has transactions with a DBE firm that is later decertified or otherwise loses its status for fraud or illegal conduct. Some states have tried to undertake corrective action against the contractors who have transacted business with these DBE firms by finding the contractor "nonresponsible," entering into corrective action agreements, or attempting to suspend or debar the contractor. Such situations include:

1. The contractor has set up a DBE firm with which it deals exclusively (a front for the contractor).
2. The contractor has dealt with a DBE that it should reasonably know is a front based on the manner in which the DBE conducts its business.
3. The contractor has dealt with a DBE that it should reasonably know is not rendering a "commercially useful purpose."
4. The contractor has performed the DBE's work and given the DBE a percentage of the contract price.

Among the types of misconduct to which federal debarment regulations apply are fraud, deceit, or other actions indicating serious lack of business integrity or honesty with respect to the eligibility of firms to participate in the DBE, WBE, or MBE programs. For example, a firm may be suspended or debarred if it acts as or knowingly makes use of a "front" company (i.e., a firm that is not really owned and controlled by minority or disadvantaged individuals or women, but poses as such to participate as a DBE in a federally assisted contract). Even in the absence of a specific false statement that would subject a party to criminal liability under 18 U.S.C. § 1001 (the federal "false statements" statute), a firm that acts as or uses a front may justifiably be viewed by acting so as to indicate a serious lack of business integrity or honesty.[167]

USDOT's DBE regulations indicate that DBE violations may result in USDOT suspension and debarment proceedings, or in a referral to the U.S. Department of Justice for a criminal investigation.[168] When the DBE rules were rewritten in 1999, the provisions for possible suspension and debarment were retained.[169]

Violations may also result in potential criminal action and/or debarment by the state involved. However, if the violation pertains to the federal DBE program, it is more likely to involve only a federal debarment unless the state has by statute also adopted or duplicated the federal program. To the extent that DBE violations also transgress state criminal statutes, independent or concurrent remedies could exist.

d. Right to Due Process in the Suspension, Debarment, or Disqualification Process

The law does not recognize that a contractor has a legally protected right to bid and be awarded a public contract merely because its qualifications as a potential bidder have been certified. However, revocation of a certificate of qualification is in the nature of a license revocation and is subject to due process requirements.[170] Thus, a certificate holder is entitled to notice and a hearing at which its representatives may explain or rebut the evidence giving rise to the agency's action.

Because the bidding and award process is based entirely on statutory authority, departmental administrative proceedings leading to suspension or debarment must adhere strictly to statutory requirements. Thus, statutes have been construed to require that contractors may be disqualified for unintentional violations of the law as well as for intentional actions.[171] Also, jurisdiction and authority for debarment by a contracting agency has had to be specifically authorized in applicable statutes.[172] Administrative proceedings must include the keeping of records showing that all jurisdictional elements of the case were addressed and sustained by factual findings developed in accordance with statutes and regulations.[173]

Under USDOT's new regulations, 2 C.F.R. Part 1200, suspension and debarment of highway construction contractors and subcontractors on federal projects are governed by the Governmentwide Debarment and Suspension (Nonprocurement) process, adopted in accordance with the rule-making provisions of the federal Administrative Procedure Act.[174] With respect to debarments, suspensions, or disqualifications at the federal level, when the appropriate processes provided for within the rules are followed, due process challenges to

[166] Commonwealth v. Gill, 5 Mass. App. 337, 363 N.E.2d 267 (1977).

[167] 50 F.R. 18493 (May 1, 1985).

[168] *Id*.

[169] 49 C.F.R. § 26.107 (2000).

[170] Capeletti Bros. v. State Dep't of Transp., 362 So. 2d 346 (Fla. App. 1978) (delinquency on prior state contract); North Central Util. v. Walker Community Water Systems, Inc., 437 So. 2d 922 (La. App. 1983) (failure to comply with public bid law); Seacoast Constr. Corp. v. Lockport Urban Renewal Agency, 339 N.Y.S.2d 188 (1972) (lack of qualification and experience record); Couch Constr. Co. v. Dep't of Transp., 361 So. 2d 172 (Fla. App. 1978) (failure to attend pre-bid conference).

[171] Dep't of Labor and Indus., Div. of Workplace Standards v. Union Paving and Constr. Co., 168 N.J. Super. 19, 401 A.2d 698 (1979) (repeated violations of prevailing wage laws).

[172] Dep't of Labor v. Berlanti, 196 N.J. Super. 122, 481 A.2d 830 (1984).

[173] Dep't of Labor v. Berlanti, 196 N.J. Super. 122, 481 A.2d 830 (1984); Seacoast Contr. Corp. v. Lockport Urban Renewal Agency, 339 N.Y.S.2d 188 (1972); Dep't of Labor and Indus., Div. of Workplace Standards v. Union Paving and Constr. Co., 168 N.J. Super. 19, 401 A.2d 698 (1979); Capeletti Bros. v. State Dep't of Transp., 362 So. 2d 346 (Fla. App. 1978).

[174] 5 U.S.C. § 700 *et seq*.

the validity of such actions have relatively little chance of succeeding.

The USDOT's suspensions or debarments of highway construction contractors undertaken pursuant to 2 C.F.R. Part 1200 are serious actions. In order to be eligible to receive federal aid for transportation projects, the states must abide by the federal actions or lose the federal aid.[175] In addition, consistent action by the states complements and effectuates the federal action. Federal suspension or debarment regulations also require that the General Services Administration (GSA) "shall compile, maintain, and distribute a list of all persons who have been debarred, suspended, or voluntarily excluded by agencies under Executive Order 12549 and these regulations, and those who have been determined to be ineligible."[176]

However, state action of suspension or debarment cannot be undertaken by relying solely on federal suspension or debarment when states are administering projects with federal-aid, as doing so would violate the contractor's right to a hearing before the state agency. State agencies should not use the Federal Government's consolidated lists of suspensions, debarments, or disqualifications without considering the matter at the state level in an appropriate due process fashion. A violation of the contractor's rights may be found where one agency uses a clearinghouse or consolidated list of agency determinations to take a new adverse action against the contractor or subcontractor, without giving the contractor any hearing or opportunity to rebut. Unless there are clear statutory authorizations that permit or authorize the list to be used to suspend, debar, or disqualify a contractor or subcontractor, clearinghouse lists should be used only to alert governmental agencies at the state level that there is some question of the contractor's or subcontractor's status. There must then be a review that complies with due process before a deprivation of rights takes place.

i. De Facto Debarment.—When responsibility determinations are made in case-by-case reviews, contractors have claimed that they were subjected to de facto debarment. However, the courts have upheld determinations of nonresponsibility even where such decisions were repeated several times based on the same facts, as long as an opportunity was given to the contractor each time to show corrective action. This issue was addressed in *Callanan Industries v. White*, [177] where the court stated:

> The ability of the Department to reject bids of irresponsible bidders is not frustrated by its inability to debar future bids. Once the Department finds a bidder to be irresponsible for a particular reason, assuming that such a finding was not arbitrary or capricious, it could proceed to reject each of that bidder's future bids, in effect creating the sort of debarment accomplished in the instant case. However, this would force the Department to consider anew the bidder's responsibility upon each bid and presumably, change its position when and if the bidder remedies the cause of the finding of irresponsibility.

ii. Compliance with Rule-Making.—Callanan addressed both the authorization to debar or suspend at the state level and the requirements of a rule-making process under a state Administrative Procedure Act. The New York State Department of Transportation was concerned about Callanan's business relationship with two DBE firms. These firms, one of which Callanan had established, were found to be frauds and guilty of misconduct in the DBE program and were decertified. The next time Callanan was the lower bidder, the Department challenged the firm's honesty, integrity, good faith, and fair dealings and indicated that the firm should show good cause why the award should be made to it for that project. The Department also declared its intention to suspend or debar the firm for up to 3 years for its past conduct. The Department set forth in its Manual of Administrative Procedures (MAP), a copy of which was given to Callanan with the notice, the notice requirements and the criteria that should be applied in any suspension or debarment decision. The MAP also established a Contract Review Unit (CRU) to effectuate the MAP process relative to contract awards and approvals. Prior to the meeting between the CRU and Callanan, the firm submitted the apparent low bid on another project and that too was reviewed by the CRU.

At the meeting, Callanan's attorney did not address the contractor's misconduct but, instead, challenged the authority of the CRU. After the meeting, the CRU determined on January 3, 1986, that Callanan should be debarred from receiving awards of future projects and from participating as a subcontractor, supplier, or provider of labor on future contracts for a period of 30 months.[178]

The MAP was not promulgated as a rule under the State Administrative Procedure Act. The Department considered the procedures to be internal guidelines to assist the CRU's decision-making process. The procedures did not dictate a particular result, but rather set out what should be considered by the CRU. The Department also did not have express legislative authority to suspend or debar contractors, but assumed it had such power from the legislative direction to award contracts only to the lowest responsible contractor as would best promote the public interest.[179]

The court considered the main issue to be "whether the Department had the authority to provide for a means of debarring or suspending bidders on the ground of irresponsibility."[180]

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[175] *See* Required Contract Provisions, Federal-Aid Construction Contracts, Form FHWA-1273 Part XI, Certification Regarding Debarment, Suspension, Ineligibility and Voluntary Exclusion (modified June 22, 1999).

[176] 49 C.F.R. § 29.500 (2001).

[177] 118 A.D. 2d 167, 503 N.Y.S.2d 930, 933, *motion to modify denied*, 123 A.D. 2d 462, 506 N.Y.S.2D 287, *appeal denied*, 69 N.Y.2d 601 (1987).

[178] *Id.* 503 N.Y.S.2d at 932.

[179] *Id*.

[180] *Id*.

> [T]he authority given the Department with regard to awarding of contracts is in terms of rejecting or accepting bids. Certainly, the Department can and should consider past conduct by a bidder in making its decision as to whether the bidder on a particular contract is responsible…
>
> However, in no statute has the Legislature granted the Department the authority to commence any sort of proceeding for the purpose of punishing an irresponsible bidder or debarring such a bidder from submitting bids in the future.
>
> The power to investigate violations of a statute and to punish violators is a significant power and is penal in nature.[181]

The court found that debarment was a punishment and, therefore, must be based on specific and express legislative terms with appropriate procedural safeguards before debarment can be undertaken. The court also concluded, "Nor can the power to debar bidders be necessarily implied from the authority to reject bids made by irresponsible bidders."[182]

The court also held that the debarment provisions were invalid because they were not adopted pursuant to the state Administrative Procedure Act. Where an administrator is undertaking some action relative to suspension, debarment, or disqualification of a contractor, the right affected will be deemed to be either a "property right" or a "liberty right," or both. Therefore, the process must be subjected to appropriate rule-making.[183] Where the rules have been properly adopted, the suspension or debarment will be upheld if it is supported by substantial evidence.[184]

Due process requirements relative to suspension, debarment, or disqualification of highway construction contractors at both the federal and state levels are now well established. The deprivation of a right, even on a temporary basis, must meet the constitutional requirement of notice and a meaningful opportunity to respond before the deprivation takes effect. At a minimum, this involves the right to be informed of the nature of the charges and of the relevant supporting evidence. In determining the adequacy of the deprivation procedures, there must be consideration of the government's interest in imposing the deprivation, the private interests of those affected by the deprivation, the risk of erroneous deprivations through the challenged procedures, and the probable value of additional or substitute procedural safeguards.

Some cases state that depending on the circumstances and the interests at stake, an evidentiary hearing may be required before a legitimate entitlement may be terminated or suspended.[185] In more recent cases, the Supreme Court has held that procedures will be sufficient, even though they provide for less than a full evidentiary hearing, as long as they do provide for some kind of a hearing or meeting that ensures an effective initial check against mistaken decisions before the deprivation occurs, in addition to a prompt opportunity for complete administrative and possibly judicial review after the deprivation.[186]

Brock v. Roadway Express[187] brought much of the prior law on the requirements of due process in connection with deprivation of a right into focus. That case involved the temporary reinstatement with back pay of a truck driver who claimed that he was discharged in retaliation for complaining about safety violations. The Secretary of Transportation, pursuant to Section 405 of the Surface Transportation Assistance Act of 1982, ordered the reinstatement of the truck driver with back pay pending a final determination on his complaint.[188] The central issue of the case was whether the Secretary of Transportation had provided Roadway appropriate due process when the driver's reinstatement and back pay were imposed on Roadway by the Secretary. Roadway was notified of the driver's charge and given an opportunity to meet with personnel in the Secretary's office, and was permitted to submit statements. However, it was not permitted access to the relevant evidence supporting the driver's complaint or to other information on which the reinstatement order was based. The Supreme Court stated:

> We conclude that minimum due process for the employer in this context requires notice of the employee's allegations, notice of the substance of the relevant supporting evidence, an opportunity to submit a written response, and an opportunity to meet with the investigator and present statements from rebuttal witnesses. The presentation of the employer's witnesses need not be formal, and cross-examination of the employee's witnesses need not be afforded at this stage of the proceeding.[189]

Due process thus does not require a full evidentiary hearing prior to invoking a deprivation, provided there is an adequate post-determination hearing at a meaningful time intended to resolve the disputes. Further, due process requires access to information upon which the deprivation of rights order was based.

The result in *Callanan Industries v. City of Schenectady* is consistent.[190] In that case, Callanan Industries had submitted the low bid, but the City of Schenectady awarded the contract to the second bidder,

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[181] *Id*. at 932, 933.

[182] *Id*.

[183] *Id*. at 933, 934.

[184] Adonizio Brothers v. Pa. Dep't of Transp., Bd. of Review, 529 A.2d 59 (1987).

[185] *See, e.g.*, Goldberg v. Kelly, 397 U.S. 254, 90 S. Ct. 1011, 25 L. Ed. 2d 287 (1970).

[186] *See, e.g.*, Cleveland Board of Educ. v. Loudermill, 470 U.S. 532, 105 S. Ct. 1487, 84 L. Ed. 2d 494 (1985) (public employee had property right in continued employment, was entitled to notice and opportunity for pre-termination hearing); O'Hare Truck Service v. Northlake, 518 U.S. 712, 116 S. Ct. 2353, 135 L. Ed. 2d 874 (1996) (public contractor entitled to same property right as public employee in continued performance of contract).

[187] 481 U.S. 252, 107 S. Ct. 1740, 95 L. Ed. 2d 239 (1987).

[188] *Id*. at 256.

[189] *Id*. at 264.

[190] 116 A.D. 2d 883, 498 N.Y.S.2d 490 (1986).

who was determined to be the lowest responsible bidder. Prior to the award, Callanan discussed its past performance with City officials in view of the City's claim that in the prior year a rehabilitation contract had been performed by Callanan in a seriously deficient manner, and further that the corrections by Callanan were unsatisfactory to the City officials. Callanan claimed that the City's failure to provide it with a hearing prior to the rejection of the bid denied it due process. The court determined that Callanan's informal conferences with the City Council and other City officials as well as judicial review satisfied Callanan's due process rights.

This issue was also considered in *Inglewood Los Angeles County Civic Center Authority v. Superior Court of Los Angeles County*, in which the award was made to the second lower bidder on the basis of qualifications, but where the low bidder was not found to be nonresponsible.[191] The court found in that case that due process required giving the low bidder the evidence reflecting on its responsibility and affording it the opportunity to rebut adverse evidence and present evidence that it was qualified to perform the contract.

In *DeFoe Corporation v. Larocca*, the New York State Department of Transportation had rejected all bids for a project due to bidding irregularities.[192] In the second bidding for the project, the joint venture of Schiavone and North Star Contracting Company was the apparent low bidder. Schiavone had been part of a different joint venture that had been the apparent low bidder the first time the project had been advertised. Between the time of the first bid and the second bid, several officials in the Schiavone firm were indicted for MBE fraud. Because of the indictment, as well as the possible inability of the top officials of the corporation to perform the project while defending against the criminal charges, the Department found the Schiavone firm to be nonresponsible and awarded to the second low bidder.[193]

Prior to the second bid letting on that project, the Schiavone firm was also the apparent low bidder on another large project in New York City, but was found to be nonresponsible for the same reasons given above. The matters were considered together in the State's Appellate Division in *Schiavone Construction v. Larocca*.[194] Upholding the State's decision, the Appellate Division made several important points relative to due process. First, it noted that Schiavone did not acquire a property right to the contracts.[195] Second, however, the court held that since the refusal to award the contracts to Schiavone "had a drastic effect upon their ability to carry on their business," Schiavone had a "cognizable liberty interest."[196] Lastly, the court noted that

> [T]he procedures afforded petitioners [Schiavone and the joint venture of Schiavone and North Star] were adequate. Due process is flexible and is determined by a weighing of the interests at stake, the risk of erroneous deprivation, the probable value of additional safeguards and the cost of substitute procedures. In cases such as the one at bar, a formal trial-type hearing is not necessary. Here, petitioners were given notice of the [Contract Review] Unit's concern over their responsibility and the reasons for that concern. Petitioners were afforded an opportunity to rebut the charges both in writing and at informal hearings. They were informed of the reasons for denial of their contract bids and were afforded this review pursuant to CPLR article 78. We find that these procedures were adequate under the circumstances of this case.[197]

Whether the contractor succeeds in challenging a suspension or debarment might depend upon whether it asserts a property or a liberty interest in its ability to bid on public contracts. *Polyvend, Inc. v. Puckorius* demonstrates what a difficult time a contractor can have when it asserts a denial of due process in connection with a property interest.[198] In that case, a license plate manufacturer had its bid for a license plate contract rejected pursuant to a state statute, which prohibited award of a government contract to a person or business that had been involved in the bribery of a state official or employee. The Circuit Court granted the state summary judgment. The Appellate Court reversed with a finding that the state statute was unconstitutional on due process grounds. The Supreme Court of Illinois reversed and decided in the state's favor. Polyvend had had the contract for the 3 prior years. The conviction for bribery occurred in 1974. The state statute concerning bribery became effective in 1977. The court found that Polyvend did not have a legitimate claim of entitlement to a future state contract. The case review was centered on a "property right" in the future state contract and no such property right was found.[199]

Another issue is the length of time prior to the post-determination hearing. The time given to rebut a proposed action is set at 30 days by the Governmentwide Debarment and Suspension (Nonprocurement) process.[200] This procedure gives the contractor 30 days after receipt of notice to submit "in person, in writing, or through a representative, information and argument in opposition to the proposed debarment." The debarring official then has 45 days after submission of the relevant information to render a determination.[201]

The Governmentwide Debarment and Suspension (Nonprocurement) process recognizes that suspension is

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[191] 103 Cal. Rptr. 689, 500 P.2d 601 (1972).

[192] 488 N.Y.S.2d 532, 128 Misc. 2d 39 (1984), *aff'd*, 489 N.Y.S.2d 1017, 110 A.D. 2d 965 (1985).

[193] Schiavone Constr. v. Larocca, 503 N.Y.S.2d 196, 197, 117 A.D. 2d 440 (1986).

[194] *Id*.

[195] *Id.* 503 N.Y.S.2d at 197.

[196] *Id*. at 197–98.

[197] *Id*. at 198 (citations omitted).

[198] 77 Ill. 2d 287, 32 Ill. Dec. 872, 395 N.E.2d 1376 (1979), *appeal dismissed*, 444 U.S. 1062 (1980).

[199] *Id.* 395 N.E.2d at 1379.

[200] 49 C.F.R. § 29.313(a) (Oct. 1, 2001).

[201] 49 C.F.R. § 29.314(a) (2001).

a serious action to be imposed only when there exists adequate evidence of one or more of the causes set out in the regulations, and immediate action is necessary to protect the public interest.[202] The regulations provide that a contractor may be suspended upon adequate evidence to suspect the commission of an offense listed in 49 C.F.R. § 29.305(a) or a cause for debarment under 49 C.F.R. § 29.305 may exist. The regulations further provide that, "Indictment shall constitute adequate evidence for purposes of suspension actions."[203]

3. Established Time Periods Versus Flexible Time Periods for Suspensions, Debarments, or Disqualifications

When a statute directs suspension, debarment, or disqualification for a prescribed period of time upon a finding of violation of a governmental program, there is little discretion that has to be exercised by the governmental administrator relative to the length of time suspension, debarment, or disqualification is to be effective. The administrator's real function in those circumstances is to see that the determination of the violation is consistent with due process requirements. The courts, therefore, will examine such a statutorily mandated period to determine whether or not it is "penal or punitive" in nature versus being a period of ineligibility that is necessary and appropriate to protect a legitimate government interest.

In the flexible time situation, those statutes that provide that the suspension, debarment, or disqualification may be determined to be up to a certain maximum period of time leave considerable discretion in the administrator's hands to pattern the length of any suspension, debarment, or disqualification to the particular circumstances that exist relative to the violation, the contractor's or subcontractor's particular situation, and any governmental needs or objectives relative to the program. The most serious aspects that the courts will look at in flexible time matters are whether the period of ineligibility is established on an ad hoc basis, whether there is similar treatment of contractors under similar circumstances, as well as whether the length of the suspension, debarment, or disqualification is justified by the facts that are established by the administrative record.

Consistency of the administrator's handling of similar situations will be very important relative to any court challenge. Further, the court will apply a standard of "abuse of discretion" or "arbitrary and capricious" to its review of the period of the suspension, debarment, or disqualification. An administrator who blindly applies the maximum ineligibility period in each and every case may be found to have abused his or her discretion, because the legislative direction is to "determine" an appropriate length of time for the ineligibility, not to exceed the statutory maximum limit. The administrator is required to use discretion in fixing the period.

4. License Revocation

Because a contracting license represents a valuable business interest, it cannot lightly be withdrawn once it has been issued.[204] One protection against arbitrary action by a licensing agency in most states is the inclusion in the licensing laws of the acts or circumstances that may be cause for suspension or revocation.[205] A second protection against arbitrary or unfair suspension or revocation is the existence of mandatory statutory procedures that apply whenever such actions are taken. In general, these require notice of the charges involved, a hearing with opportunity to explain and clear the charges, and a right of judicial review in the event the licensee disputes the licensing agency's ruling.

Suspension or revocation of a contractor's license for cause is a form of disciplinary action administered by the licensing agency. As such, imposition of this penalty has no effect on the contractor's civil liability, even where its failure to adhere to a statutory duty or to follow specifications provides the cause for revocation. The conditions upon which a license is granted are imposed for protection of the public, and are enforced solely through the administrative action of suspending or revoking the license. No civil cause of action by one who suffers injury arises from the licensing agency's action. Similarly, revocation of a contractor's license because of bankruptcy does not have any effect on the collection of claims.[206] Nor does revocation because of a contractor's violation of a labor law give rise to any claim by the employees involved.[207]

Because severe sanctions and penalties may be involved in the disciplinary provisions of contractor licensing laws, courts have been reluctant to construe these laws more broadly than necessary to achieve the statutory purpose.[208] This policy is regularly tested in determinations of whether a contractor's actions or omissions bring its conduct within any of the statutory grounds for suspension or revocation of its contractor's license. Judicial interpretations of contractor licensing laws have refined the list of the leading causes of disciplinary action.

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[202] 49 C.F.R. pt. 29.

[203] 49 C.F.R. § 29.405(b) (2001).

[204] Portions of this section are derived from *License and Qualification of Bidders* by Dr. Ross D. Netherton, and from *Suspension, Debarment, and Disqualification of Highway Construction Contractors* by Darrell W. Harp, published by the Transportation Research Board in 1976 and included in the first edition of SELECTED STUDIES IN HIGHWAY LAW.

[205] A summary of state statutes regarding grounds for contractor license revocation is found in App. C.

[206] Tracy v. Contractor's State License Board, 63 Cal. 2d 598, 407 P.2d 865, 47 Cal. Rptr. 561 (1965).

[207] Lee Moor Contracting Co. v. Hardwicke, 56 Ariz. 149, 106 P.2d 332 (1940).

[208] Peck v. Ives, 84 N.M. 62, 499 P.2d 684 (1972).

Whether specifically required by statute or not, fairness requires that disciplinary action by a licensing agency be based on a hearing, with opportunity for the licensee to explain or contradict the evidence being considered. Normally, such a hearing is held prior to issuing any suspension order so that premature or unwarranted penalties may be avoided. Statutory procedures may, however, provide that where public health or safety justifies it, a temporary suspension order may be issued prior to holding a hearing on the matter.[209]

Where statutory lists of grounds for disciplinary action specify that misconduct must be willful, this intent is an essential element of proof. However, intent may be inferred from the nature of the act.[210]

Closely related to these cases are others involving the adequacy of performance regarding project plans, specifications, and estimates, or other conditions of work.[211] A case-by-case approach to disciplinary action on these grounds is necessary because of the wide variety of conditions involved, including the use of performance specifications and the use of change orders during the progress of work. In practice, construction rarely can be performed without some deviation from the original plans and specifications, and determination of whether deviations reach a point of violating the licensing standard requires consideration of all the circumstances.

In this process, the courts have developed and applied the doctrine of substantial performance by the contractor. As described by the court that adopted this doctrine in California, the guiding principle is that

> [T]here is substantial performance where the variance from the specifications of the contract does not impair the building or structure as a whole, and where after it is erected the building is actually used for the intended purpose, or where the defects can be remedied without great expenditure and without material damage to other parts of the structure, but that the defects must not run through the whole work so that the object of the owner to have the work done in a particular way is not accomplished, or be sure that a new contract is not substituted for the original one, nor be so substantial as not to be capable of a remedy, and the allowance out of the contract price will not give the owner essentially what he contracted for.[212]

A certain amount of leeway has been allowed in holding contractors to the requirement that a valid license must be maintained at all times when their work is in progress. Thus, where a contractor's license expired after 90 percent of a project had been completed, and the remaining work was actually completed under the supervision of licensed professional personnel, the court held that the contractor was in substantial compliance with the licensing law.[213] In contrast, where a contractor's license expired while work was in progress, but the licensee failed to act promptly to renew it or have a licensed manager supervise the remaining work, the court held that was not in substantial compliance with the licensing law.[214] In another case, the contractor was entitled to maintain a claim against the state even though it had not complied with the requirements of a nonresident contractors' registration statute, where the contractor had obtained the required performance bonds that covered payment of state and local taxes and the contractor had substantially completed the registration process prior to completing the project.[215] A low bidder with a class A license but no class B license satisfied the license requirement for the project where the agency had delayed its opinion calling for a class B license for the project.[216]

Courts have been less inclined to apply doctrines of forgiveness where violation of licensing standards appeared to be deliberate or willful. Deliberate action has been found in cases of alleged diversion of funds given to contractors for specific construction work, or misrepresentation of information in license applications or business dealings, or failure to pay bills for labor or materials.[217]

Diversion of funds advanced to assist commencement of construction or other purposes is treated seriously by all licensing agencies. New Mexico's contractor licensing law, which makes diversion of funds a cause for revocation, has been described as "imposing a fiduciary duty upon contractors who have been advanced money pursuant to construction contracts.[218]

Among the causes for disciplinary action listed in typical contractor licensing laws, one of the most difficult to apply is the rule that contractors must perform construction in a workmanlike manner, in accordance with the plans and specifications and reasonably within the agreed or estimated costs. Standards for workmanship may be provided specifically either in the contract plans and specifications, or in a trade or industry code

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[209] State ex rel. Perry v. Miller, 300 S.E.2d 622 (W. Va. 1983).

[210] Bailey-Sperber, Inc. v. Yosemite Inc. Co. 64 Cal. App. 3d 725, 134 Cal. Rptr. 740 (1976) (court rejected the argument that the willfulness of the action must be proved under the California statute).

[211] J.W. Hancock Enterprises v. Ariz. State Registrar of Contractors, 142 Ariz. 400, 690 P.2d 119 (1984); Mickelson Concrete Co. v. Contractors State License Board, 95 Cal. App. 3d 631, 157 Cal. Rptr. 96 (1979).

[212] Tolstoy Constr. Co. v. Minter, 78 Cal. App. 3d 665, 143 Cal. Rptr. 570, 573–74 (1978) (citing Thomas Haverty Co. v. Jones, 185 Cal. 285, 197 P. 105 (1921)); *see also* First Charter Land Corp. v. Middle Atlantic Dredging Co., 218 Va. 304, 237 S.E.2d 145 (1977).

[213] Barrett, Robert & Wood, Inc. v. Armi, 296 S.E.2d 10 (N.C. App. 1982).

[214] Brown v. Solano County Business Dev., Inc., 92 Cal. App. 3d 192, 154 Cal. Rptr. 700 (1979).

[215] Dep't of Transp., State of Ga. v. Moseman Constr. Co., 260 Ga. 369, 393 S.E.2d 258 (1990).

[216] City of Phoenix v. Superior Court, 909 P.2d 502 (Ariz. App. 1995).

[217] Fillmore Products, Inc. v. Western States Paving, Inc., 561 P.2d 687 (Utah 1977).

[218] In re Romero, 535 F.2d 618, 621 (10th Cir. 1976).

applicable to the work in question. Where these sources do not furnish suitable guidance for disciplinary action, licensing agencies and courts have defined "workmanlike manner" as doing the work in an ordinarily skilled manner, as a skilled worker should do it by reference to established usage and accepted industry practices prevailing where the work is performed.[219]

Where the licensing statutes require that failure to follow plans and specifications must be willful or deliberate, evidence of intent may be inferred from the conduct of the parties. Thus, where willful departure from workmanlike standards was charged, the decision of the licensing agency to discipline the contractor was upheld when it was shown that the contractor failed to install an acceptable slab of concrete, and then represented that he could correct the defect by a "pour-over" technique, which only made matters worse. [220] The court found that this "indicates a purposeful departure from accepted trade standards which may be properly characterized as 'willful.'"

The contractor's failure to perform work within the contract price or cost estimate is often associated with failing to follow plans and specifications. Cost overruns are sometimes listed among statutory reasons for license revocation. They may also be associated with incompetent or negligent performance, which are also well-recognized grounds for revocation or suspension. In addition, courts regularly apply an indirect penalty in some instances of cost overrun, by limiting contractor recovery to the dollar ceiling of its license.[221]

Although contractors are not often disciplined because of assisting in the evasion of licensing laws, this possibility is illustrated where a contractor permits its license to be used by unlicensed contractors on a project in which it does not actively participate.[222]

5. Disqualification or Rejection of a Bid Proposal

Loss of eligibility to bid on transportation construction projects may result from various causes set forth in state laws or regulations relating to licensing, prequalification, and conflict of interest.[223] Suspensions or other forms of withdrawal of eligibility are based entirely on statutory or administrative authority and procedures. They are construed strictly, as they are considered regulatory in nature.

Also, disqualification of one or more major contractors may have the practical result of significantly reducing the number of contractors capable of performing certain types of construction, and thus may reduce competition.

Procedures for judicial review of administrative actions denying prequalification or disqualifying certified bidders are essential features of the states' licensing and prequalification systems. Courts have been divided on whether the interest acquired by a low bidder is a constitutionally protected property interest or a liberty interest.[224] However, courts finding either basis for a constitutional right have held that the contractor is entitled to the protections of procedural due process before the bidder can be disqualified on the grounds that it is not responsible.

There are three types of adverse actions: (1) denial of an application for prequalification, or for a change in classification or rating; (2) disqualification of a bidder or rejection of its bid on a particular project; and (3) suspension or revocation of a prequalification certificate for cause.

The statutes and regulations governing prequalification procedures do not make clear distinctions between the bases for these three types of actions. Thus, a finding of "inadequate" financial resources or equipment, or "unsuitable" experience, may be specified as grounds for denial of an initial application, and may also sustain the refusal to consider a contractor's bid in the event that the decisive information on these matters comes to the contracting agency's attention prior to the actual award of a contract. For example, a firm's filing for Chapter Eleven reorganization in bankruptcy was a rational basis for making a determination of lack of responsibility, since financial stability is a factor in contractor responsibility.[225]

Similarly, lack of satisfactory progress or performance on a previous construction job may be cited as grounds for disqualifying a bidder from consideration

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[219] J.W. Hancock Enterprises v. Ariz. State Registrar of Contractors, 142 Ariz. 400, 690 P.2d 119 (1984).

[220] Mickelson Concrete Co. v. Contractors State License Board, 95 Cal. App. 3d 631, 157 Cal. Rptr. 96 (1979).

[221] *Compare* Alan S. Mead & Assoc. v. McGarry, 315 S.E.2d 69 (N.C. App. 1984) (recovery allowed up to license limit) *with* Martin v. Mitchell Cement Contracting Co., 74 Cal. App. 3d 15, 140 Cal. Rptr. 424 (1977) (recovery allowed beyond license limit).

[222] Moore v. Fla. Constr. Industry Licensing Bd., 356 So. 2d 19 (Fla. App. 1978).

[223] A summary of state statutes indicating grounds for disqualification, suspension, and debarment is found in App. F.

[224] *See* Pataula Elec. Membership Corp. v. Whitworth, 951 F.2d 1238 (11th Cir. 1992) (holding that under Georgia law a bidder may have a property interest in the award of a public contract); LaCorte Electrical Const. and Maintenance, Inc. v. County of Rensselaer, 574 N.Y.S.2d 647 (1991) (low bidder does not have a property right in the award of the contract, but has a liberty interest that requires procedural due process if the low bidder's bid is to be rejected); Triad Resources and Systems Holdings, Inc. v. Parish of Lafourche, 577 So. 2d 86 (La. App. 1990) (lowest responsive bidder has protected interest in award of contract requiring procedural due process before the bidder may be disqualified as not responsible).

[225] Adelaide Envtl. Health Assocs. v. New York State Office of General Services, 669 N.Y.S.2d 975, 248 A.D. 2d 861 (1998). Note that New York uses a post qualification system; however, this rule should apply regardless of when the responsibility determination is made. *See also* Lewis v. State Dep't of Business and Professional Regulation, 711 So. 2d 573 (Fla. App. 1998) (failure to satisfy civil judgment was grounds for license revocation even though contractor had filed for bankruptcy; however, evidence that the debt had been discharged in bankruptcy would allow contractor license to be reinstated).

for another contract.[226] This mixture is illustrated by the standard specification for issuance of a proposal by the Connecticut Department of Transportation:

The Commissioner reserves the right to disqualify or refuse to issue a proposal form to any individual, partnership, firm or corporation for reasons including, but not limited to any of the following:

1. For having defaulted on a previous contract.
2. For having failed, without acceptable justification, to complete a contract within the contract period.
3. For having failed to prosecute work in accordance with contract requirements.
4. For having performed contract work in an unsatisfactory manner.
5. For having failed to prosecute work continuously diligently and cooperatively in an orderly sequence.
6. For having failed to file with the Department a recent sworn statement on the form furnished by the Department fully outlining the capital, equipment, work on hand and experience of the bidder; such statement to be valid, must be on file with the Department at least 20 calendar days before application for a proposal form is made.
7. For filing a sworn statement with the Department which, in the Commissioner's judgment, indicates that the bidder does not have the required experience in the class of work to be bid on, does not have the proper labor and equipment to prosecute the work within the time allowed, or does not have sufficient capital and liquid assets to finance the work.[227]

A number of states specifically provide for suspensions or revocations of prequalification classifications or ratings, and have set forth the grounds required in their regulations. Pennsylvania's regulations illustrate this type of provision in requiring the preparation of a "past performance report" to be used in prequalification and responsibility determinations:

> The past performance report shall include evaluation of a contractor's attitude and cooperation, equipment, organization and management, scheduling and work performance. Poor or unsatisfactory ratings for specific work classifications shall constitute justification for revoking classifications previously granted. A contractor who has an overall unsatisfactory rating on performance reports will not be prequalified.[228]

Less specific, but apparently sufficient, is Kentucky's regulation.

> Upon receipt of information or evidence that a holder of a certificate of eligibility has failed to perform satisfactorily or adhere to the laws, regulations administrative or specifications applicable to a contract or a subcontract, the department [of highways] may take action to suspend or revoke the certificate of eligibility or reduce the maximum eligibility amount.[229]

Contractors who are dissatisfied with rulings of certifying officials can, by timely request, have the ruling reconsidered by those officials or by the higher administrative authority that has ultimate responsibility for the prequalification process. In some states contractors enjoy a right to judicial review on the merits.[230] Some courts, however, have refused to examine the issue of disqualification in the context of a bid protest challenging the award of the contract.[231]

Administrative reviews of contractor classifications and ratings for possible reconsideration or revision are usually informal. They are directed entirely to reexamination of the grounds for the disputed action cited in the prequalifying agency's letter of notification to the contractor. These proceedings, however, give the applicant an opportunity to submit further evidence in support of its qualifications. Where prequalification boards or committees make the initial determination of classifications and ratings, requests for review may go to the director of the transportation department or to the state transportation commission.[232] A New York court held that before a bidder may be designated as not responsible, it must be notified of the agency's reasons for its finding of nonresponsibility and must be given an opportunity to appear before the agency and present information or evidence to rebut the agency's finding.[233]

The actions of boards of review and other reviewing authorities are generally declared to be final by the laws or regulations creating them. However, some states confer on the aggrieved applicant an additional right of judicial review. Massachusetts' statute allows for both administrative review within the agency, and for judicial review of the administrative board's determination.

> Any prospective bidder who is aggrieved by any decision or determination of the prequalification committee or the commissioner which affects his right to bid may file a new application for qualification at any time, or within fifteen days after receiving notice of such decision the applicant may request in writing a hearing before an appeal board to reconsider his application or qualifications.

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[226] State, Dep't of Transp. v. Clark Constr. Co., 621 So. 2d 511 (Fla. App. 1993); F.S.A. §§ 339.16, 339.16(1)(b). Such a finding may also sustain the certifying agency's suspension of that contractor's classification and rating for a specified period of time.

[227] *Connecticut Department of Transportation, Standard Specifications for Roads, Bridges, and Incidental Construction*, Form 815, § 1.02.02 (1995).

[228] PA. CODE § 457.10(b) (1999).

[229] 603 KY. ADMIN. RULES 2:015 § 8(1) (Aug. 15, 2000).

[230] *See, e.g.* WASH. REV. STAT. 47.28.070 (denial of prequalification may be appealed within 5 days of determination).

[231] D.A.B. Constructors v. State Dep't of Transp., 656 So. 2d 940, *rehearing denied* (Fla. App. 1995); Sabre Constr. Corp. v. County of Fairfax, 501 S.E.2d 144 (Va. 1998).

[232] *See* HAW. REV. STAT. § 103D-702(a), which allows a bidder an opportunity to be heard before prequalification is denied.

[233] N.Y. State Asphalt Pavement Ass'n v. White, 532 N.Y.S.2d 690, 141 Misc. 2d 28 (1988).

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> Such hearing shall be deemed to be an adjudicatory proceeding, and any bidder or prospective bidder who is aggrieved by the decision of the appeal board shall have a right to judicial review under the applicable provisions of said chapter thirty A.[234]

Ohio's code states that

> Any applicant, other than one who has been debarred, aggrieved by the decision of the director may file a new application at any time for qualification or, within ten days after receiving notification of such decision, the applicant may request, in writing, a reconsideration of the application by a prequalification review board, which the director shall create within the department of transportation with the request for reconsideration, the applicant shall submit additional evidence bearing on the applicant's qualifications. The review board shall consider the matter and either may adhere to or modify the director's previous decision.[235]

Whatever the limits of judicial review prescribed by statute, one court has held that the appellant contractor may not enlarge the scope of that review beyond that created by the statute by alleging facts outside the prequalification process.[236]

6. Criminal Offenses

Most statutes that provide for prequalification of bidders use standards that measure a contractor's ability and capacity to perform contracts in various categories of construction. Typically, financial condition, equipment, experience, and organization are the indicators used to establish eligibility. However, other matters that may affect a contractor's responsibility, such as business honesty and integrity, may also become grounds for rejection of the bid of a properly prequalified low bidder, or may be grounds for suspension or debarment. In practice, it may be difficult to maintain the distinction between prequalification and the determination of a low bidder's responsibility. This is illustrated in a series of cases growing out of New Jersey's landmark decision in *Trap Rock Industries v. Kohl*.[237]

The New Jersey Supreme Court's first decision in *Trap Rock Industries v. Kohl* involved suspension of previously qualified contractors.[238] Indictments had been returned charging criminal offenses by the contractors, and the Commissioner of Transportation ordered suspension of their classification pending final disposition of these charges. No proof of the charges was offered to the Commissioner prior to his order, and the contractors declined an opportunity to present evidence to the Commissioner concerning the matter. The trial court ruled that the suspension was unlawful in the absence of this evidence.[239] The New Jersey Supreme Court reversed the lower court and affirmed the suspension.

The appeal provided an opportunity to discuss two basic issues: (1) the relationship of prequalification actions to the Administrative Procedure Act and (2) the constitutional guarantee of due process of law. In addition to charging that the Commissioner acted without affirmative evidence concerning the truth of the indictments, the contractor claimed that the state's prequalification standards did not specify the misdeeds that would disqualify a bidder. Stressing the legislative mandate that the Commissioner retained the right and duty to reject bidders that were not the lowest responsible bidder, the court declared:

> These cases do not involve the right to engage in business. The contractors are free to do business with anyone willing to deal with them. The question is whether the state must do business with them despite the Commissioner's view that the public interest would be disserved by doing so.[240]

The court continued:

> We find nothing in this statute to evidence a legislative departure from the basic principle that bidding statutes are intended for the benefit of the taxpayer rather than the bidder or prospective bidder. The statute simply provides, so far as feasible, for a determination of qualification before bidding rather than after the bids are in. The opportunity for hearing afforded by this statute merely parallels the right to hearing after the bids are in which the more conventional bidding statutes contemplate. We find no purpose to vest in a preclassified bidder any "right" which derogates the primary right of the state…to do business…with "the lowest responsible bidder."[241]

The court affirmed that the legislative concept of a responsible bidder included moral integrity as much as a capacity to supply labor and materials, and that citizens expected their public officials to do business only with people of integrity, whether as individuals or as officers of corporations. However, important as this element might be in certifying contractor qualifications, neither the prequalification statute nor the Administrative Procedure Act required that the state specify in its rules all the factual patterns constituting actionable lack of moral responsibility. The court found that it was not only infeasible to do so, but that it was more desirable to permit administrative definitions to evolve on a case-by-case basis. For this purpose, the concept of moral responsibility as spelled out in judicial decisions is constitutionally sufficient. The court stressed the distinction between this action of suspension and those involving revocation of a contractor's license to do business, and noted cases where the latter actions were

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[234] MASS. GEN. L. ch. 29, § 8B (West 2001).

[235] OHIO REV. CODE § 5525.07 (2000 Replacement Vol.)

[236] Enertol Power Monitoring Corp. v. State, 108 Or. App. 166, 814 P.2d 556 (1991).

[237] 63 N.J. 1, 304 A.2d 193 (1973).

[238] 59 N.J. 471, 284 A.2d 161 (1971).

[239] Trap Rock Indus. v. Kohl, 115 N.J. Super. 278, 279 A.2d 138, *rev'd*, 59 N.J. 471, 284 A.2d 161 (1971).

[240] 284 A.2d at 164.

[241] 284 A.2d at 166.

properly required to comply with the standards of the Administrative Procedure Act.[242]

A year later, the Department ruled that this suspension also made Trap Rock ineligible to serve as a supplier of materials to a prime contractor whose contract with a local government was funded in any part by the department. Trap Rock argued that prequalification of suppliers was not required by statute, and that to try to do so in all cases would entail great difficulty. The court upheld the suspension, declaring that the contracting agency could not on those accounts "ignore what it learns about those who seek to do business directly with the state."[243]

New Jersey's prequalification statute required applicants to answer a questionnaire regarding financial ability, prior experience, adequacy of plant and equipment, organization, "and such other pertinent and material facts as may be deemed desirable."[244] By its ruling on the suspension of Trap Rock Industries, the New Jersey court raised the question of whether information that customarily is used to determine responsibility and fitness to receive a contract award can also properly be relied on to suspend eligibility to bid on future contracts. The court's decisions affirmed that the Commissioner of Transportation could do this, and could later reinstate the contractor as a qualified bidder when satisfied that the reason for disqualification was removed.

These cases were followed by another that reported the issue of whether the same grounds used to stop work on a project could also sustain a decision to suspend the contractor's eligibility to bid on future contracts with the department.[245] In this instance, the department in effect reversed an earlier decision to reinstate the contractor's eligibility to bid, and imposed a new suspension on the ground that one of the individuals responsible for the earlier corporate criminal acts had not disassociated himself sufficiently from the corporation's management to insulate the corporation from his lack of integrity.

The court found no fault with the department's power to reconsider and modify prior determinations of eligibility when it appeared necessary to protect the public interest, or with the grounds cited to justify suspension of bidding eligibility. But on review of the department's action, the court found that the Commissioner relied on the evidence presented at a prior hearing, and decided to reimpose suspension by applying a contrary and speculative interpretation to the conclusion reached by the previous Commissioner on the same evidence. Warning that "the power to reconsider must be exercised reasonably, with sound discretion reflecting due diligence, and for good and sufficient cause," the appellate court held that, under the circumstances, the department's action was not sustained by the evidence.[246]

7. Responsibility Agreements and IPSIGs or Monitors[247]

a. Use of IPSIGs or Monitors to Protect the Public Trust

Public owners in postqualification states sometimes seek to resolve situations in which low bidders have significant responsibility problems, such as criminal convictions, through developing responsibility agreements that incorporate precautionary elements to prevent recurrence of the conduct that gave rise to such responsibility problems. These may involve the use of IPSIGs, a concept first developed in the New York metropolitan area. An IPSIG, as defined by the International Association of IPSIGs, is an independent, private sector firm with legal, auditing, investigative, management, and loss-prevention skills, employed by an organization to ensure compliance with relevant law and regulations, and to deter, prevent, uncover, and report unethical and illegal conduct by, within and against an organization.[248]

History of IPSIGs.—The IPSIG's role is patterned after the federal inspectors general created by the Inspector General Act of 1978 (IG Act), which assigned inspectors general to each of the federal agencies and tasked them with preventing waste, fraud and abuse.[249] In 1990, the New York State Organized Crime Task Force *Final Report on Corruption and Racketeering in the New York City Construction Industry* raised the idea of adapting the Inspector General concept to government contractors in order to prevent fraud on public construction projects.[250] IPSIGs were later adopted by the New York City School Construction Authority (SCA), established in the wake of that report, for billions of dollars of New York City school construction. "Contrac-

[242] *Id*. at 167. In distinguishing the decision in Gonzalez v. Freeman, 334 F.2d 570 (D.C. Cir. 1964), the court suggested that where a specific act in itself is deemed sufficient to justify the adverse action, it should be specified in the administrative standards.

[243] 305 A.2d at 194.

[244] *Id*. (quoting N.J. STAT. ANN. § 27i7-35.3).

[245] Trap Rock Indus. v. Sagner, 133 N.J. Super. 99, 335 A.2d 574 (1975), *aff'd*, 69 N.J. 599, 355 A.2d 636 (1976).

[246] 335 A.2d at 580. However, this could also have been considered to be an abuse of discretion based on the officer's failure to consider new evidence; generally an officer's failure to exercise his or her discretion at all is an abuse of discretion.

[247] This portion of this volume is drawn from a publication prepared by the authors of the 2011 update to this current volume; KERNESS & SHAWHAN, *supra* note 31.

[248] *See* IAIPSIG Code of Ethics, available at http://www.iaipsig.org/ethics.html (last accessed June 16, 2010).

[249] James B. Jacobs & Ronald Goldstock, *Monitors & IPSIGS: Emergence of a New Criminal Justice Role*, 43 CRIMINAL LAW BULLETIN, No. 2, available at http://www.iaipsig.org/Criminal%20Law%20Bulletin%20-%20James%20Jacobs%20%20Ronald%20Goldstock%20Article.pdf.

[250] RONALD GOLDSTOCK, CORRUPTION AND RACKETEERING IN THE NEW YORK CITY CONSTRUCTION INDUSTRY: FINAL REPORT OF THE NEW YORK STATE ORGANIZED CRIME TASK FORCE (NYU Press, 1991).

tors who faced debarment from government contracts on integrity grounds could nonetheless be awarded contracts it they retained an IPSIG that would report to the SCA..."[251] Other public authorities and New York City agencies adopted the use of IPSIGs thereafter.

Imposing an IPSIG as a Condition for Public Contracts: Use of Monitoring Agreements.—In New York City, when contractors or vendors have been found "non-responsible" for bidding public contracts, individual city agencies have given them an opportunity to demonstrate their restored integrity by negotiating and entering into an compliance agreement providing for an IPSIG, which the subject company retains at its own expense.[252] A standard IPSIG agreement of this type requires the contractor to provide the IPSIG with complete access to its books, records, personnel and operations. The IPSIG maintains a 24-hour hotline used by employees or others to report wrongdoing that affects the contractor. All IPSIG findings are reported directly to the NY City Department of Investigation, which supervises the implementation of the monitoring agreement and works with the IPSIG to develop and implement a strict code of business ethics, as well as a corruption prevention program. In addition, the contractor must agree to have its personnel undergo an ethics training program. Should the contractor default under the monitoring agreement, the City may declare the contractor in default of the agreement.[253]

Example 1: World Trade Center Debris Removal Contract

The changing role of IPSIGs was reflected in the IPSIGs employed on the each of the four no-bid $250-million PANYNJ contacts for removal of debris from the site of the former World Trade Center (WTC) following the 9/11 terrorist attack. Prior to the WTC project, IPSIGs were usually imposed as a condition of doing business in which the company's "responsibility" had already been called into question under a "lowest responsible bidder" letting statute.[254] On the WTC cleanup project, the role of the IPSIG was changed from rehabilitating a "non-responsible" contractor to proactively preventing waste, fraud, and abuse. The IPSIGs monitored the operations of contractors, conducted audits and investigations to ensure compliance with the contracts and applicable laws, performed on-site interviews with subcontractors and suppliers, implemented procedures to ensure that all vendors, suppliers, and subcontractors had the necessary integrity and qualifications, and conducted further on-site investigations as necessary.[255] The results drew praise from participants and outside observers. There were no scandals or charges of significant corruption. A staff report by the House Committee on Management, Integrity, and Oversight of the Committee on Homeland Security concluded that:

> [T]heir deployment (IPSIGs) was an overwhelming success. Private Integrity monitors identified a number of contractors with ties to organized crime which were subsequently removed from the site, found trucks cooping (idling) while on the clock, flagged several attempted frauds that were referred for prosecution, recovered $47 million in over-billing by contractors and subcontractors and saved immeasurable more money by deterring fraud.[256]

Example 2: Port Authority of New York and New Jersey Hub Project

The Port Authority of New York and New Jersey is now requiring the use of IPSIGs in connection with the WTC Transportation Hub project to assist in providing the necessary oversight and monitoring. The purpose of the integrity monitor is to prevent waste, abuse, and/or corruption, detect it, and if detected, to coordinate with the Port Authority Inspector General on the action to be taken. The tasks of the IPSIG include conducting reviews of all existing procedures and processes for fraud, corruption, cost, abuses, safety and environmental risks; implementing corruption prevention programs; reviewing the records of the construction manager and general contractor; monitoring and conducting forensic review of project costs; and providing necessary forensic auditing and investigative services as necessary, as directed by the Port Authority's Inspector General.[257]

Conformance with Sentencing Guidelines.–The Federal Sentencing Guidelines, adopted in November 1991, are indicative of the standards to which business organizations and their officers are now held. One of the guidelines for sentencing provides for the review of steps taken by the organization to ensure that it has an effective program to prevent and detect violations of law.[258] Adoption of a monitor conforms to these requirements.

Similar monitoring programs are part of administrative settlement and compliance agreements negotiated between USDOT and contractors to avoid debarment and suspension as authorized by 2. C.F.R. § 1200.635. Typically these agreements may require the contractor to adopt a code of ethics and corporate compliance pro-

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[251] Jacobs & Goldstock, *supra* note 249, at 223.

[252] Stanley N. Lupkin & Edgar J. Lewandowski, *Independent Private Inspector General: Privately Funded Overseers of the Public Integrity* 10 NY LITIGATOR, Summer 2005, No. 1, at 9; available at http://www.iaipsig.org/nylit-newsl-spring05-lewandowki.pdf (last accessed July 6, 2010).

[253] *Id.* at 9–10.

[254] *Id.* at 9–14.

[255] *Id.* at 12.

[256] Subcommittee on Management, Integration and Oversight of the House Comm. on Homeland Security, Staff. Rep., *An Examination of Federal 9/11 Assistance to New York: Lessons Learned in Preventing Waste, Fraud, Abuse and Lax Management*, Committee Print 109-C, USGPO Document No. 29-452, Aug. 2006; available at http://www.access.gpo.gov/congress/house/cp109-c.pdf (last accessed June 16, 2010).

[257] Port Authority of NY & NJ, Request for Proposals, RFP 9392, Feb. 23, 2006. ch. 2 , Scope of Work, at 7 and Exhibit A, at 2–3.

[258] Neil Getnick & Leslie Ann Skillen, *Structural Reform: The Front Line Fight Against Organized Crime*, 1 NY Litigator, No. 2, Nov. 1995.

gram. They may provide for the company to retain an Independent Monitor to oversee implementation of its Corporate Compliance Program. The Monitor would submit periodic reports directly to FHWA for 3 years regarding the contractor's implementation of measures required by the agreement.

The adoption of monitors can be a useful tool to prevent waste, fraud, and abuse. A key component of a monitor and/or IPSIG arrangement is the requirement that they be truly independent and not subject to control by the contractor they are supposed to be monitoring. Attention should also be focused on the monitor's adherence to a code of ethics to ensure independence and impartiality.

C. SURETY BONDS AND INDEMNIFICATION

1. Introduction

Because public projects are not subject to mechanics or materialmens' liens, public agencies require successful bidders on construction projects to furnish security for satisfactory contract performance.[259] Additional requirements assure that laborers, materialmen, and subcontractors are paid for their goods and services.[260] Others require that taxes and other obligations are paid. Public agencies may also require indemnification for losses incurred because of a contractor's negligence or default. These requirements result in the formation of third-party beneficiary contracts, or suretyships. A summary of state requirements for contractor bonds is found in Appendix F.

Congress addressed this need by enactment of the Miller Act in 1935.[261] The Miller Act requires that before a public works contract utilizing federal funds may be awarded, the contractor must furnish both a payment bond for the benefit of laborers, subcontractors, and materialmen, and a performance bond for the benefit of the United States. States have followed by enacting their own "Little Miller Acts" patterned after the federal statute, and also requiring the provision of payment and performance bonds by public works contractors. The bonds required by both federal and state law customarily are referred to as statutory bonds.

2. Basic Concepts of Suretyship

One of the distinguishing characteristics of suretyship is that it is always collateral to another contract. It is a tripartite agreement in which one party (the surety) agrees to assume liability for the debt or duty of another (the principal) to a third party (the obligee) in the event the principal does not perform its duty under the contract.[262] Under this separate agreement, the surety becomes liable notwithstanding the fact that it has no personal interest in the principal's duty to the obligee, and receives no benefit from it.[263]

Except where they arise by operation of law, suretyships must be created by express agreement of the parties. The agreement must be in writing, as suretyships come within the statute of frauds.[264] Once created, a suretyship remains in effect until terminated, or until the surety is discharged, or until changes in the basic contract by the principal and obligee alter it so substantially that it requires a different performance than was previously contemplated by the surety.

3. Public Policy Regarding Contractors' Bonds

a. Rationale of Contractor Bonds

The requirement for contractors' performance and payment bonds provides a way to protect the public against major deviations in public contract performance. The protection that these bonds offer, however, depends to some extent on the surety's choice among several options open to it in the event the agency terminates a contract for cause. First, the surety may elect to do nothing toward arranging for the completion of the contract and let the agency make arrangements for completing the work. In that event, the surety's liability is limited to the costs of completion less the contract funds held by the agency at the time of termination. Second, the surety may try to have the agency's termination rescinded and finance the contractor in the completion of the work. This course of action is rarely selected, because the fact that there was a termination suggests that the surety may not have found good business reasons for extending financial help earlier when termination might have been avoided. Third, the surety may enter into a takeover agreement with the agency and proceed to complete the contract work. Under such an agreement, the government pays the surety the balance of the contract funds that remain unpaid, and the surety hires another contractor, approved by the agency, to complete the work. If the new contractor's expenses exceed the unspent funds from the original award, the surety may solicit new bids to complete the contract and request the agency to enter into a new contract with the lowest responsible bidder. Again, if the costs of this new arrangement exceed the funds remaining unspent, the surety pays the difference.

From the surety's viewpoint, it is advantageous to cooperate with the agency in arranging for completion of a defaulted contract unless there are serious compli-

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[259] Portions of this section are derived from *Indemnification and Suretyship in Highway Construction Contracts* by Dr. Ross D. Netherton, and *Indemnification and Insurance Requirements for Consultants and Contractors on Highway Projects* by Darrell W. Harp, published by the Transportation Research Board and included in the first edition of SELECTED STUDIES IN HIGHWAY LAW.

[260] First National Bank of Paonia v. K.N.J., Inc., 867 P.2d 152, 154 (Colo. App. 1993).

[261] 40 U.S.C. § 3131 *et seq*. (formerly codified at 40 U.S.C. § 270a. et seq.).

[262] 74 AM. JUR. 2D *Suretyship* § 3 (2001).

[263] Miners' & Merchants' Bank v. Gidley, 150 W. Va. 229, 144 S.E.2d 711 (1965).

[264] WIS. STAT. § 241.02(1)(b) (2001).

cating circumstances. Moreover, most sureties will wish to avoid being placed between the government and the "takeover" contractor, and so will prefer to work out a method for creating a new direct contractual relationship between the government and the party who actually performs the completion work.

Statutes and bid specifications that require performance guarantees generally are satisfied by obtaining a surety bond. Whether cash or other assets may be substituted for a surety bond is a matter of state law. Even if allowed under state law, the use of assets other than cash may result in a dispute regarding whether the value of the assets pledged is adequate. The substitution of other security for the customary three-party surety arrangement has been permitted as providing the functional equivalent of a surety and a reliable source of recovery to which the contracting agency had a right of direct recourse in the event of a contractor's default or insolvency. [265]

Requirements for providing payment and performance bonds are creatures of legislation and apply only to the parties and projects covered by the statute. So, where a state university was created in the state constitution and governed by its own board of regents outside the control of the legislature, it was held that its contracting process was not subject to the bonding requirements of statutes regulating other public agencies' contract procedures.[266] Likewise, where a public garage was not built on land owned by the state or a public entity at the time the contract was executed, no bond was required.[267]

Statutes requiring payment and performance bonds will apply only to public projects. Thus, port authority facilities intended to be operated by private enterprise were not "public works" within the meaning of the statute.[268] A similar result was reached in denying the claim of a concrete supplier to the subcontractor of a private telephone company that was replacing sidewalks at the direction of a local government after the company had removed the original sidewalks to install telephone cable.[269]

b. Agency's Duty Regarding Contractor Bonds

An agency's duty with respect to the contractor bond requirement is defined by statute. Generally, prior to contract award, the agency should verify that the agent signing the bond for the surety has authority to do so, and verify that the surety is registered to do business in the state.

Where a statute establishes an explicit duty to see that a bond or equivalent escrow arrangement is furnished for the protection of suppliers of labor or materials who would be entitled to claim a lien except for the public nature of the project, the public agency's failure to require that security may be negligence. Therefore, in *New England Concrete Pipe Corp. v. D/C Systems of New England, Inc.*, a sub-subcontractor was able to recover for materials and labor supplied for a housing project when the state housing finance agency was shown to have breached its duty to see that a payment bond or equivalent escrow was provided.[270] An agency may also be found to have the duty to verify the validity of a bond rather than merely accepting what purports to be a valid bond. Such was the result in a Michigan case in which the agency provided a certified copy of the bond upon the subcontractor's request.[271] The court found that the agency's action had the effect of verifying the bond's validity. The agency would not have had this duty had it not provided a certified copy of the bond; had the subcontractor not requested a copy of the bond, then it would have borne the risk of the bond being invalid.

Another area that an agency should review is whether the surety is registered in the state. If the surety is incorporated under the laws of another state, it must generally obtain official authorization to do business in the state where the contract is let. This authorization generally involves registration with the Secretary of State or other appropriate state official, and

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[265] Cataract Disposal, Inc. v. Town Board of Town of Newfane, 440 N.Y.S.2d 913, 916, 423 N.E.2d 390, 53 N.Y.2d 266 (1981) (cash deposit in lieu of bond); Central Arizona Water & Ditching Co. v. City of Tempe, 680 P.2d 829, 831 (Ariz. App. 1984) (substitute security); *but see* Cataract Disposal, 440 N.Y.S.2d at 917 (dissent arguing that use of a surety relieves the contracting agency of the responsibility for obtaining a substitute if needed to complete performance, and gives the agency the benefit of the surety's independent assessment of the contractor's reliability).

[266] William C. Reichenbach Co. v. State, 94 Mich. App. 323, 288 N.W.2d 622, 628 (1980).

[267] Murnane Assoc. v. Harrison Garage Parking Corp., 659 N.Y.S.2d 665, 239 A.D. 2d 882 (1997).

[268] James J. O'Rourke, Inc. v. Indus. Nat'l Bank of R.I., 478 A.2d 195 (R.I. 1984) (meat processing plant financed with port authority bonds but operated entirely by private industry, construing R. I. GEN. LAWS, § 37-13-14); *see also* Annotating 48 A.L.R. 4th 1163 (1986).

[269] Modern Transit-Mix, Inc. v. Michigan Bell Tel. Co., 130 Mich. App. 300, 343 N.W.2d 14, 15 (1983) (applying MICH. COMP. LAWS ANN., 129.201); *see also* Davidson Pipe Supply Co. v. Wyo. County Indus. Dev. Agency, 624 N.Y.S.2d 92, 94, 85 N.Y.2d 281, 648 N.E.2d 468 (1995) (energy cogeneration plant developed with assistance of industrial development agency not "public improvement" where all risks and benefits were borne by private entity); Consolidated Elec. Supply, Inc. vs. Bishop Contracting Co., 205 Ga. App. 674, 423 S.E.2d 415 (1992) (YWCA building not a public work).

[270] 495 F. Supp. 1334, 1344–45 (D. Mass. 1980); *see also* H-K Contractors, Inc. v. City of Firth, 101 Idaho 224, 611 P.2d 1009, 1010 (1979) (construing IDAHO CODE, § 54-1926, and holding that general time limits for filing claims do not apply to claims based on failure to require payment bond); George Weis Co. v. Dwyer, 867 S.W.2d 520 (Mo. App. 1993); Palm Beach County v. Trinity Indus., 661 So. 2d 942 (Fla. App. 4 Dist. 1995).

[271] Kammer Asphalt Paving Co. v. East Chine Tp. Schools, 443 Mich. 176, 504 N.W.2d 635, 641 (1994).

designation of a resident agent of the corporation with an in-state address for receiving mail and service of process.[272] In some cases, bonds issued by out-of-state sureties must be countersigned by this resident agent, and filed with a copy of the agent's power of attorney.[273] Occasionally state laws require disclosures of other information about the surety or its resident agent.

Explicit provisions that the surety must be approved by the contracting agency before its bond is acceptable are found in several states. However, even where statutes are silent on this matter, state agencies have claimed that such authority is implicit in their legal responsibility for managing public construction contracts with appropriate protection of the public interest. Whether based on explicit or implicit authority, the requirements established by state transportation agencies for federal-aid highway contracts must not be unduly or unfairly restrictive. Federal highway regulations provide that no procedure shall be required by states in connection with federal-aid highway contracts that operate to restrict competitive bidding by discriminating against the purchase of a surety bond or insurance policy from a surety or insurer outside the state and authorized to do business in the state.[274]

Financial responsibility is implicit in the requirement that sureties must be "acceptable" to the contracting agency. Criteria for acceptance by the state may not be fully set forth in statutes or regulations. Such standards are often departmental policy, which may be applied with flexibility and administrative judgment. In some instances, however, minimum standards of financial condition are published by the state's public works agencies. This concern extends beyond the question of a proposed surety's initial financial rating, and prescribes limits on the dollar amount of a surety's bond commitments at a given time.

Other items that should be reviewed include whether the principal contract has been incorporated into the bond by reference; whether the bond sets out the alternatives available to the surety in the event of contractor default; whether it includes a definition of who may claim under the bond and in what time period a claim must be filed; and whether it is signed by individuals authorized to bind the surety.[275]

Under the Miller Act, the agency has a duty to provide a certified copy of the bond and the principal contract to any one who has furnished labor or materials and who submits an affidavit to the agency stating that he or she has not been paid.[276]

c. Development of the Present Suretyship System

In 1894, Congress enacted the Heard Act, which required construction contractors for the federal government to provide a bond "with good and sufficient sureties, [and] with the additional obligation that such contractor or contractors shall promptly make payments to all persons supplying him or them labor and materials in the prosecution of the work provided for in such contract…"[277] However, under the Heard Act it was possible for subcontractors to bring suit before completion of a project and exhaust the resources of a prime contractor and the surety under the bond before the government could move to protect its interest in assuring performance.[278] Congress then amended the law in 1905 to postpone creditors' recourse to the surety bond until the Federal Government had adequate opportunity to enforce its claims.[279] The federal law remained substantially in this form until passage of the Miller Act in 1935.[280] In the Miller Act, Congress directed that the performance and payment features be executed in separate bonds, each with its own rights and rules for recourse to the surety.[281]

During the period before the Miller Act, a number of states passed legislation permitting a mechanic's lien to attach to the funds earned by a public works contractor while recognizing that the public works themselves were immune from levy or attachment under the lien. Generally, however, state legislation for the protection of laborers, materialmen, and subcontractors before 1935 followed the pattern of the Heard Act in requiring contractors to furnish a surety bond conditioned on performance and payment of claims.[282] After passage of the Miller Act, states began to follow the federal model in amending their own bonding statutes.

[272] *See, e.g.*, WASH. REV. CODE § 23B.15.070 (Supp. 2003).

[273] *See* Shrake Elec., Inc. v. Central Sur. & Ins. Corp., 185 Kan. 230, 342 P.2d 159 (1959) (extent of the authority given by power of attorney).

[274] 23 C.F.R. § 635.110 (2002).

[275] 17 AM. JUR. 2D *Contractors' Bonds* § 3 (1990).

[276] 40 U.S.C. § 3133(a).

[277] Act of Aug. 13, 1894, ch. 280, 28 Stat. 278.

[278] United States v. American Sur. Co., 135 F. 78 (1st Cir. 1905); American Sur. Co. v. Lawrenceville Cement Co., 96 F. 25 (C.C.D. Me. 1899); Davidson Bros. Marble Co. v. United States ex rel. Gibson, 213 U.S. 10, 29 S. Ct. 324, 53 L. Ed. 675 (1909) (jurisdictional problems); United States Fidelity & Guar. Co. v. United States for the Benefit of Kenyon, 204 U.S. 349, 27 S. Ct. 381, 51 L. Ed. 516 (1907) (jurisdictional problems).

[279] As amended, the law required creditors to refrain from suit on the bond for 6 months after completion of final settlement, and allowed the United States a priority over other claimants in the distribution of surety funds. Act of Feb. 24, 1905, ch. 778, 33 Stat. 811, 812.

[280] Act of Aug. 24, 1935, ch. 624, 49 Stat. 793 (formerly codified at 40 U.S.C. §§ 270a–270d (1970), now codified at 40 U.S.C. §§ 3131–134 (2003).

[281] NETHERTON, *supra* note 259.

[282] *Id*.

4. Contractor Bonds in State and Federal Construction Contracts

a. Contractor Bond Coverage Under the Miller Act

The Miller Act provides that before the award of any contract exceeding $100,000 and involving construction, repair, or alteration of a public building or public work of the United States, the contractor must furnish (1) a performance bond of sufficient amount to protect the United States Government, and (2) a payment bond "for the protection of all persons supplying labor and material in the prosecution of the work provided for in the contract."[283] This section has been interpreted to limit recovery on a payment bond posted under the act to those materialmen, laborers, and subcontractors who dealt directly with the contractor or a subcontractor. The policy of limiting claimants who can sue under a Miller Act bond is to permit the prime contractor to protect itself by requiring the subcontractors who perform substantial portions of the prime contract to post bonds assuring that their particular materialmen, subcontractors, and laborers will be paid in the event the subcontractor defaults.[284]

The amount of the bond originally varied—one-half the contract price for contracts up to $1 million; 40 percent of the price for contracts from $1 million to $5 million; and a maximum of $2.5 million for contracts in excess of $5 million.[285] The statute was amended in 1999 to require a performance bond in an amount that the contracting officer deems adequate, and a payment bond in the total amount of the contract, unless the contracting officer determines that that amount is impracticable and sets a lesser amount. However, the payment bond may not be less than the performance bond.[286]

In a second section of the Miller Act, Congress specified that suit on the contractor's payment bond may be brought after 90 days following the final performance of labor or supplying of materials.[287] During this 90-day period, any claimant "having direct contractual relationship with a subcontractor but no contractual relationship express or implied with the contractor" who furnished the bond must give written notice of its claim to the contractor.[288] Also, no suit on the payment bond may be commenced by any claimant after the expiration of 1 year after the labor was performed or the materials supplied.[289]

These requirements were intended to strengthen the positions of the protected parties and provide reasonable procedures for exercising their rights. The legislative history of the statute recognized the widening circle of parties necessarily involved in the large, complex, and costly types of construction being undertaken. However, Congress was also sensitive to the inequity of exposing prime contractors and their sureties to "remote and undeterminable liabilities."[290] In turn, the courts approached the questions arising under this act from the standpoint that its remedial character deserved a liberal construction, favoring achievement of Congress's basic objectives. Yet, the rights of claimants under the Act were entirely statutory in their origin, and so could not be expanded beyond the plain meaning of the statute.[291]

b. Little Miller Acts

The Miller Act provided a model for states to enact their own statutes, or "Little Miller Acts," that would cover public works construction that was not covered by federal law.[292] State law establishing requirements for contractors' bonds or other security relating to performance of public construction projects may also be broader in scope than the federal law embodied in the Miller Act. For example, in addition to bonding requirements, state law may require that a certain percentage of the funds owed on the contract be retained by the contracting agency for the benefit of unpaid subcontractors or suppliers.[293] Many of the states' laws on public contractor bonding stem from early efforts to provide laborers and materialmen a form of protection similar to that which mechanic's liens provided in private construction projects.[294] Many states' statutes also include require-

[283] 40 U.S.C. § 3131(b) (2003).

[284] J.W. Bateson Co. v. U.S. ex rel. Trustees of Nat. Automatic Sprinkler Indus. Pension Fund, 434 U.S. 586 (1978); H.H. Robertson Co. v. Lumberman's Mut. Cas. Co., 94 F.R.D. 578 (W.D. Pa. 1982).

[285] Former 40 U.S.C. §§ 270a (1999) (historical notes).

[286] Construction Industry Payment Protection Act of 1999, Pub. L. 106-49 § 2(a), 113 Stat. 231 (Aug. 17, 1999), codified at 40 U.S.C. § 3131(b) (2003).

[287] 40 U.S.C. § 3133(b)(1) (2003).

[288] 40 U.S.C. § 3133(b)(2) (2003).

[289] 40 U.S.C. § 3133(b)(4) (2003).

[290] Clifford E. MacEvoy v. United States for Use and Benefit of Calvin Tompkins Co., 322 U.S. 102, 110, 646 S. Ct. 890, 88 L. Ed. 1163 (1944).

[291] Thus, the approach to construction of the law has been summed up as follows:

> [Sections 270a-270b…are] remedial in nature and [are] to be liberally construed in order to properly effectuate the congressional intent to protect those who furnish labor or materials for public works, and the strict letter of [such sections] must yield to [their] evident spirit and purpose when this is necessary to give effect to the intent of Congress and to avoid unjust and absurd consequences, [citations omitted] such a salutary policy does not justify ignoring plain words of limitation and imposing wholesale liability on payment bonds.

United States for Use and Benefit of J.A. Edwards & Co. v. Bregman Construction Corp., 172 F. Supp. 517, 522 (E.D.N.Y. 1959); *see also* United States ex rel. Ross v. Somers Constr. Co., 184 F. Supp. 563 (D. Del. 1959).

[292] Norquip Rental Corp. v. Sky Steel Erectors, Inc., 854 P.2d 1185, 1188, 175 Ariz. 199, *review denied* (Ariz. App. 1993).

[293] *See, e.g.,* COLO. REV. STAT. § 38-26-107 (2000).

[294] *See* Western Metal Lath, a Division of Triton Group, Ltd. v. Acoustical and Const. Supply, Inc., 851 P.2d 875, 877 (Colo. 1993).

ments designed to protect the interests of public agencies in a wide range of other matters. These include guarantee of bids, satisfactory performance of contracts, payment of taxes, contribution to workmen's compensation or unemployment funds, performance of maintenance, and issuance of supplies.[295]

The Model Procurement Act also contains a section addressing the requirement of payment and performance bonds.[296] These requirements are similar to the Miller Act requirement for separate payment and performance bonds, but require bond amounts to be 100 percent of the contract price.

c. Statutory Terms and Other Definitions

Much of the Miller Act's annotations interpret the language defining the parties protected and the types of contracts covered. They also discuss what constitutes "labor and materials" supplied "in the prosecution of the work provided for" under a contract. The courts have been asked to clarify the critical dates involved in the 1-year limitation on commencing suit, and the 90-day period for notice of claims, and the sufficiency of the content of the notice. These decisions have also helped shape the meaning of state and local contractor bonding laws or Little Miller Acts that have been patterned after the federal statute.

i. Public Buildings and Public Works.—Because the Miller Act applied to contracts "for the construction, alteration, or repair of any public building or public work of the United States," a threshold question concerned the definition of "public works." In *United States to the Use of Noland Co. v. Irwin*,[297] the Supreme Court gave this phrase a broad scope, consistent with legislative history that contemplated application to public works projects under the contemporaneous National Recovery Act. In contrast to the view that had prevailed under the Heard Act, the Court stated that "the question of title to the buildings or improvements to the land on which they are situated is no longer of primary significance."[298] A more important consideration was whether the structures were constructed for public use and paid for by the Federal Government. Neither was it technically necessary that the contract be made directly with the United States, provided that the work performed was done on behalf of the government under proper authority.[299]

Projects that involve public money but are ultimately privately owned and/or operated buildings also present problems for determining bond requirements under state Little Miller Acts. In Milbrand Co. v. Department of Social Services, [300] a private developer purchased city-owned property under a contract to construct a building in accordance with plans received and approved by the city. The contractor defaulted on payments to a subcontractor, who then sued the city. The court held that the project did not involve a "public building" for which a statutory payment bond was required.[301] A Connecticut court held that whether a project is a "public work" must be determined on a case-by-case basis, and where a building is constructed with public money for private use, the determination depends on the degree of governmental involvement with the project.[302] A Georgia court found that mere receipt of public funds by a private organization did not require application of either the Miller Act or Georgia's Little Miller Act.[303] However, in a case involving construction of both public and nonpublic facilities, the surety was liable to the concrete supplier for concrete used in the nonpublic portion of the project, since the work was completed as part of the covered prime contract.[304]

[295] N.M. STAT. § 13-4-18 (A)(1) (2001) (performance bond); OHIO REV. STAT. § 9.31.1 (2001) (bid security); WIS. STAT. § 779.14(1e)(a) (2001) (including state taxes, workers' compensation, and unemployment insurance).

[296] AMERICAN BAR ASSOCIATION, MODEL PROCUREMENT CODE FOR STATE AND LOCAL GOVERNMENTS § 5-302 (2000).

[297] 316 U.S. 23, 62 S. Ct. 899, 86 L. Ed. 1241 (1942).

[298] 316 U.S. at 29.

[299] United States ex rel. Westinghouse Electric Supply Co. v. National Sur. Corp., 179 F. Supp. 598 (E.D. Pa. 1959).

[300] 117 Mich. App. 437, 324 N.W.2d 41 (1982) (construing MICH. COMP. LAWS, 129.201 (1963)).

[301] 324 N.W.2d at 43; *but see* United States ex rel. Hillsdale Rock Co. v. Cortelyou & Cole, Inc., 581 F.2d 239, 242 (9th Cir. 1978) (payment bond furnished jointly by Stanford University and Atomic Energy Commission). With respect to "public works," see Annotation, 48 A.L.R. 4th 1170.

[302] L. Suzio Concrete Co. v. New Haven Tobacco, Inc., 28 Conn. App. 622, 611 A.2d 921 1992).

[303] Consolidated Elec. Supply, Inc. v. Bishop Contracting Co., 205 Ga. App. 674, 423 S.E.2d 415 (1992) (YWCA received federal funds, but provided no essential government services and was not a governmental agency).

[304] Dixie Bldg. Material Co. v. Liberty Somerset, Inc., 656 So. 2d 1041 (La. App. 4th Cir.) *rehearing denied*, 661 So. 2d 1346 (1995).

ii. Labor Done or Performed.—Many questions regarding the labor covered by the Miller Act payment bonds have involved the requirement that the labor be performed "in the prosecution of the work provided for" in the contract. The language implies that certain services that benefit the contractor are so generalized that they cannot be traced to the contract specifications, and thus are not covered by the bond. However, these limits seldom result in denying a claim because of its remoteness.[305] Claims for work done outside the scope of the contract specifications represent the category most vulnerable to denial, because requirement of their inclusion under the bond would alter the obligation of the surety.[306] Claims for extra work may be allowed where the terms of the bond provide for it and the contractor initially authorizes the work.[307]

Where claims have been made for money withheld from laborers' wages to meet taxes, decisions have varied. Some argue for allowing such claims because the money in question was withheld from laborers' compensation and, in the absence of the withholding directive, would have been paid to the wage earner. Another viewpoint is that that the correct way of looking at the role of the contractor in these circumstances is as a collector of the tax at the point where the laborer receives his or her wages. Wages withheld for taxes generally are not covered by the bond.[308] However, wages withheld to make contributions to union health and welfare funds on behalf of employees are within the bond's coverage.[309]

Applying Iowa's statute, the state court agreed that contributions to health, welfare, and pension funds represented payment for labor or services performed in a construction project, and distinguished those funds from workers' compensation, social security taxes, and board and lodging for employees, which were not in the nature of payment for labor or services.[310]

Federal court decisions on Miller Act bonds have adopted a view that the scope of the phrase "labor and materials" includes those costs that are necessary to provide the products and services or add value to the project of which they are components. Thus, they hold that the statutory coverage of Miller Act bonds does not include attorneys fees, financial charges on overdue accounts, lost profits, cancellation charges, delay damages, escalated material costs, or penalties.[311] State courts have reached the same conclusion under state law regarding personnel administration costs and security interests.[312]

Cases defining "labor in prosecution of the work" as used in the Miller Act have construed the term to include physical work and also activities of architects and other professionals who supervise work done at the project job site. Where the language of the bond is broad enough, it may cover work done by architects outside of the job site.[313] Activities of consulting engineers involving inspection of work being performed by others are within the scope of the statutory coverage.[314] Where professional work does not involve services of a supervisory nature, inspections, job site consultations and job reviews, or similar activities, it is regarded as outside the statutory scope of the bond.[315] In addition, work performed by architects or engineers prior to the con-

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[305] *See, e.g.*, Price v. H.L. Coble Constr. Co., 317 F.2d 312, 316 (5th Cir. 1963) (labor furnished for a subcontractor, involving overseeing and expediting construction work, recruiting workmen, making up payrolls, and reporting periodically to the subcontractor held covered by the payment bond).

[306] Sam Macri & Sons, Inc. v. United States for the Use and Benefit of Oaks Constr. Co., 313 F.2d 119, 123–24 (9th Cir. 1963); United States for the Use and Benefit of Warren Painting Co. v. J.C. Boespflug Constr. Co., 325 F.2d 54, 61 (9th Cir. 1963).

[307] Cent. Gulf Elec. Contractor, Inc. v. M. P. Dunesnil Constr. Co., 471 So. 2d 1148 (La. App. 3rd Cir. 1985).

[308] United States v. Seaboard Sur. Co., 201 F. Supp. 630 (N.D. Tex. 1961).

[309] United States for the Benefit of Sherman v. Carter, 353 U.S. 210, 219, 77 S. Ct. 793, 1 L. Ed. 2d 776 (1957).

[310] Dobbs v. Knudson, Inc., 292 N.W.2d 692, 695 (Iowa 1980) (construing IOWA CODE, 573.2 (1976)); *see also* Trustees of Colo. Carpenters & Millwrights Health Bd. Trust Fund v. Pinkard Constr. Co., 199 Colo. 35, 604 P.2d 683, 685 (1979) (construing COLO. REV. STAT. § 38-26-105 (1973)); Trustees, Fla. West Coast Trowel Trades Pension Fund v. Quality Concrete Co., 385 So. 2d 1163 (Fla. App. 1980) (construing Fla. Stat. Ann. § 255.05 (1978)); *see also* Indiana Carpenters Cent. and Western Indiana Pension Fund v. Seaboard Sur. Co., 601 N.E.2d 352, 355–56*, rehearing denied, transfer denied*, 615 N.E.2d 892 (1994); Alibrandi Building Systems, Inc. v. Wm. C. Pahl Constr. Co., 590 N.Y.S.2d 370, 371, 187 A.D. 2d 957 (1992); Puget Sound Elec. Workers Health and Welfare Trust Fund v. Merit Co., 123 Wash. 2d 565, 870 P.2d 960 (1994).

[311] Can-Tex Indus. v. Safeco Ins. Co. of Am., 460 F. Supp. 1022 (W.D. Pa. 1978) (construing PA. STAT., tit. 8, § 193 (1967)); Lite-Air Products, Inc. v. Fidelity & Deposit Co. of Md., 437 F. Supp. 801, 804 (E.D. Pa. 1977); *see also* United States ex rel. Heller Elec. Co. v. William F. Klingsmith, Inc., 670 F.2d 1227 (D.C. Cir. 1982) (Miller Act claim for damages for contractor's delay and loss of anticipated profits); Concrete Structures of the Midwest, Inc. v. Fireman's Ins. Co. of Newark, 790 F.2d 41 (7th Cir. 1986) (claim for lost profits based on common law bond theory denied).

[312] Primo Team, Inc. v. Blake Constr. Co., 4 Cal. Rptr. 2d 701, 3 C.A. 4th 801, *rehearing denied, modified, review denied* (Cal. App. 4th Dist. 1992) (personal administrator not "furnisher of labor"); Union Asphalt, Inc. v. Planet Ins. Co., 27 Cal. Rptr. 2d 371, 21 C.A. 4th 1762 (1994) (holder of security interest not supplier of labor or materials).

[313] Herbert S. Newman and Partners, P.C. v. CFC Constr. Ltd. Partnership, 236 Conn. 750, 674 A.2d 1313 (1996).

[314] *See* United States ex rel. Charles H. Thayer v. Metro Constr. Corp., 330 F. Supp. 386 (E.D. Va. 1971).

[315] United States ex rel. Naberhaus-Burke, Inc. v. Butt & Head, Inc., 535 F. Supp. 1155, 1160 (S.D. Ohio 1982) ("federal case law has adopted an admittedly somewhat narrow definition of the term…covering only skilled professional work which involves actual superintending, supervision or inspection at the jobsite.").

struction contract are not covered by the bond.[316] This narrow interpretation of "labor" in the federal cases contrasts with the argument that the Miller Act should be read to include all professional services under its protection, and that some states have given broader coverage under their analogous mechanics' lien laws.[317]

iii. Material Furnished or Supplied.—Under both federal and state law, the definition of "materials furnished or supplied" includes all types of materials, items, and substances that are incorporated into the public facility, or consumed in its construction.[318] Other things may be included, however, if circumstances show that they were furnished "in the prosecution of the work provided for" in the contract. Materials may be considered to be furnished in the prosecution of the contract work even though they are not deposited at the construction site, or not wholly consumed in the construction work.[319]

State bonding statutes that use the language of the Miller Act (i.e., "furnished labor or materials in the prosecution of the work provided for in such contract") generally are interpreted as imposing on the claimant a burden of showing only that the materials were "furnished" in connection with a particular project, but not that the specific items furnished were actually incorporated into the construction work. While proof of delivery to a job site is an important, and sometimes decisive, factor in proving that goods were "furnished" in connection with a particular project, it is not an absolute requirement or element of proof of the claim.[320] Invoices and sales slips that itemize materials shipped and are adequately dated can meet the claimant's burden of proof.[321]

Where the "materials furnished" are not consumed in the construction process or physically incorporated into the project, their use in the construction process cannot be easily measured.[322] Consequently, recovery for the value of signs and barricades for use during work on drainage structures, wooden forms for concrete pavement, and sheet pilings for lining ditches during excavation operations have been approved only where other rationale for recovery was available.[323]

Contractors, subcontractors, and materialmen in their daily business practices often do not leave clear trails of the movement of labor, materials, and money in their transactions. Proof of problems resulting where contractual transactions are permitted to become casual is illustrated in *Adams v. Magnolia Construction Co.*[324] A general contractor for construction of a municipal sewer system orally arranged with a subcontractor to have the latter furnish "shells" for the structural components needed in the project. The subcontractor obtained the shells from three sources and stockpiled them in the contractor's storage yard, where they were mixed with other shells and used as needed for a series of projects. When a corporate officer of one of the subcontractor's suppliers was unable to testify that any of its company's shells were actually used by the subcontractor in the bonded project, there was no other trail of business records of physical evidence on which to rely, and the supplier's claim was dismissed. In contrast, where purchase orders, invoices, and correspondence between the parties have been available to establish the transfer of materials from supplier to contractor, the claimant can more easily prove their use by the contractor and the payment for them.[325]

Recognizing the reasonable limits to which a supplier can be expected to go in determining what use is made of its materials once they are turned over to another party, courts have accepted proof of delivery to the work site as evidence that the materials were used in the construction.[326] Where a supplier furnished towing services rather than materials, the proof that they were consumed or used in a bonded project was found

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[316] Union Asphalt, Inc. v. Planet Ins. Co., 27 Cal. Rptr. 2d 371, 21 C.A. 4th 1762 (Cal. App. 2 Dist. 1994).

[317] *See* Annotation, 3 A.L.R. 3d 573 (1965), 28 A.L.R. 3d 1014 (1969).

[318] Quality Equipment Co. v. Transamerica Ins. Co., 243 Neb. 786, 502 N.W.2d 488, 492 (1993) (state law); Poly-Flex, Inc. v. Cape May County Mun. Utilities Auth., 832 F. Supp. 889, 892 (D. N.J. 1993) (federal law).

[319] Montgomery v. Unity Elec. Co., 155 F. Supp. 179 (D. P.R. 1957); United States ex rel. Purity Paint Products Corp. v. Aetna Cas. & Sur. Co., 56 F. Supp. 431 (D. Conn. 1944); Commercial Standard Ins. Co. v. United States for Use of Crane Co., 213 F.2d 106 (10th Cir. 1954) (recovery allowed under a payment bond for pipe put in inventory to replace that which had been taken out to complete the contract; but recovery denied for stockpiled materials where there was no evidence to show which material actually had been used in the performance of public construction, and which had been used for other contracts); United States for the Benefit and Use of Westinghouse Elec. Supply Co. v. Robbins, 125 F. Supp. 25 (D. Mass. 1954).

[320] City Elec. v. Indus. Indem. Co., 683 P.2d 1053, 1057–58 (Utah 1984).

[321] *Id*. at 1059.

[322] Houston Gen. Ins. Co. v. Maples, 375 So. 2d 1012 (Miss. 1979) (construing MISS. CODE, 31-5-1 (1972)).

[323] Constr. Materials, Inc. v. Am. Fidelity Fire Ins. Co., 383 So. 2d 1291 (La. 1980) *writ granted*, 385 So. 2d 256 (liability based on language of bond broader than statute); Slagle-Johnson Lumber Co. v. Landis Constr. Co., 379 So. 2d 479 (La. 1979) (forms destroyed following use); R.C. Stanhope, Inc. Roanoke Constr. Co., 539 F.2d 992 (4th Cir. 1976) (lost sheet piling treated as rental equipment rather than as material consumed).

[324] 431 So. 2d 38 (La. App. 1983) (applying LA. REV. STAT., § 38:2241); *see also* School Dist. of Springfield R-12 ex rel. Midland Paving Co. v. Transamerica Ins. Co., 633 S.W.2d 238 (Mo. App. 1982) (invoices, weight tickets, account records).

[325] Carr Oil Co. v. Donald G. Lambert Contractor, Inc., 380 So. 2d 157 (La. App. 1979) (petroleum products and fuel delivered to contractor's fuel storage tanks at work site and used there by contractor's road equipment).

[326] Wal-Board Supply Co. v. Daniels, 629 S.W.2d 686 (Tenn. App. 1981); Carr Oil Co. v. Donald G. Lambert Contractor, 380 So. 2d 157 (La. App. 1979).

through matching invoices with the transporter's log book showing the routes used.[327]

In order to recover from the surety, a supplier must show that it delivered materials to the contractor or subcontractor in good faith, that it understood and intended that the materials were to be used in prosecution of the contract work, that the contractor or subcontractor diverted the materials from use in the intended project, and that the supplier did not have knowledge or authorize the diversion.[328] Where materials fabricated for use in a tunnel construction project were delivered to the project site, but thereafter were converted by the contractor to other projects, it was held that the bond covered the converted materials originally intended for incorporation into the tunnel project.[329] In this instance the state's bonding statute required that contractors' payment bonds cover "any material specially fabricated…as a component…so as to be unsuitable for use elsewhere."[330]

A common practice of contractors and subcontractors who must deal regularly with materialmen is to maintain open running accounts for the convenience of their employees to make purchases, as needed, during construction activities. This arrangement, however, increases the need to generate evidence of how the purchased materials were used.[331]

Where goods are rejected as unsuitable after delivery to the construction jobsite, courts have questioned whether the materialman is covered by the payment bond.[332] Holding that the materialman had stated a proper claim under the Miller Act even though it did not allege that its goods were supplied for use in a particular project, the federal court stated that for a materialman to recover under the Miller Act:

> [I]t is necessary only that he show that the materials were supplied in prosecution of the work provided for in the contract, that he has not been paid therefore, that in good faith he had reason to believe that the materials were intended for the specified work, and that he complied with the jurisdictional requirements. It is immaterial to its right of recovery that the materialman deliver the materials to the jobsite or that such materials actually be used in…the work. [333]

iv. Other Items.—In determining the coverage of payment bonds required under the states' Little Miller Acts, various marginal items have been considered by the courts. Where the question is whether particular items are materials or equipment, the nature of the item is a more important indicator than the form of the agreement involved. Thus, scaffolding used by a painting contractor was held to be part of its permanent "plant," or stock of tools, and equipment held on hand to perform its work.[334] Under a statute requiring payment bonds for the protection of "all persons supplying labor and materials" in the prosecution of the work, items such as bulldozers, graders, tractors, trucks, and the like were held not to be "materials" that could be covered by the bond.[335]

The same issue arose where a claimant argued that pumps obtained by rent or purchase for use in constructing a municipal sewer system were "supplies used or consumed" by the contractor. Holding that the costs of renting and purchasing the pumps were not covered by the contractor's payment bond, the Colorado court noted that there was a split of authority on the treatment of tools, equipment, and "plant," but found that the majority did not allow recovery from the surety.[336]

Whether activities conducted away from the construction site can qualify as "work done" in completion of a project was considered where sand for a highway project was taken by dragline from a river and deposited at a loading yard, from which it was hauled by another subcontractor to the site of the road work. When a dragline operator sued to recover from the surety for its services, the court held that the claim was allowed.[337] All links in the transportation chain from a protected materialman to the construction job site are covered by the bond, and so the cost of moving sand from the barges to the loading yard was covered.

Fuel furnished for operating machinery used in construction work on the jobsite generally meets the test of

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[327] Harvey Canal Towing Co. v. Gulf South Dredging Co., 345 So. 2d 567 (La. App. 1977).

[328] Pennex Aluminum Co., A Div. of Metal Exchange Corp. v. International Fidelity Ins. Co., 818 F. Supp. 772, 782–84 (M.D. Pa. 1993) *see also* Solite Masonry Units Corp. v. Piland Constr. Co., 232 S.E.2d 759 (Va. 1977); AMOCO Oil Co. v. Capitol Indemnity Corp., 291 N.W.2d 883, 889–91 (Wis. App. 1980) (supplier should have been aware of diversion because of amount of material ordered).

[329] CC&T Constr. Co. v. Coleman Bros. Corp., 8 Mass. App. 133, 391 N.E.2d 1256, 1259 (1979).

[330] *Id*. (Construing MASS. GEN. L., ch. 149, § 29).

[331] Villa Platte Concrete Service, Inc. v. Western Casualty & Surety Co., 399 So. 2d 1320 (La. App. 1981) (proof insufficient to show that items for which claimant sought recovery actually had been furnished under oral contract between claimant and general contractor); Cedar Vale Co-Op Exchange v. Allen Utilities, Inc., 10 Kan. App. 2d 129, 694 P.2d 903 (1985) (claimant's evidence was insufficient to show that items charged to contractor's account were used in project).

[332] United States ex. rel. Lanahan Lumber Co. v. Spearin, Preston & Burrows, Inc., 496 F. Supp. 816 (M.D. Fla. 1980).

[333] *Id*. at Supp. at 817–18 (quoting United States ex rel. Carlson v. Continental Casualty Co., 414 F.2d 431, 433 (5th Cir. 1969)).

[334] Arthur J. Roberts & Co. v. Delfour, Inc., 14 Mass. App. 931, 436 N.E.2d 1246, 1248 (1982) (construing MASS. GEN. LAWS ANN. ch. 149, § 29).

[335] Valliant v. State, Dep't of Transp. and Dev., 437 So. 2d 845 (La. 1983) (construing LA. REV. STAT. § 38:2241 (1980)); Rish v. Theo Bros. Constr. Co., 269 S.C. 226, 237 S.E.2d 61 (1977) (construing S. C. CODE § 33-224 (1975)).

[336] CPS Distributors, Inc. v. Fed. Ins. Co., 685 P.2d 783, 785 (Colo. App. 1984) (construing COLO. REV. STAT. § 38-26-105 (1982)).

[337] Javeler Constr. Co. v. Fed. Ins. Co., 472 So. 2d 258 (La. 1985) (construing LA. REV. STAT. § 38:2241 (1980)).

necessity.[338] So does fuel used for heating buildings at the jobsite used in performing the work.[339]

The obvious need for moving supplies and materials to the jobsite, sometimes over great distances, and within the jobsite has led to construing transportation as a form of "labor" furnished to the contractor, and therefore covered by payment bonds under the Miller Act and Little Miller Acts.[340].

v. Equipment Rental.—The regular use of rental equipment in public works construction has lead some states to list rental charges as items that are covered by statutory payment bonds. Other states, interpreting variously worded statutes that do not explicitly cover rental of equipment, have held that rental costs are included in the general language and legislative purpose of their laws.[341] In the rationale for permitting claims to recover for use of rented equipment, it is the rental payments, as opposed to the value of the equipment as a capital item, that are "consumed" in the performance of the project. Rental payments represent the increment of the useful life of the equipment that is used up for the benefit of the bonded project. Accordingly, the contract agreement establishing the rental must be a genuine lease rather than a purchase and sale. Whether the agreement is for a lease or a sale must be determined by the facts of each case, and is not solely dependent upon the characterization of the transaction. In a Missouri case, the evidence indicated that the claimant's equipment rental agreement was in fact a lease intended for the security of the seller while the claimant purchased the equipment through a series of monthly payments.[342] In another case, the transaction was considered a rental rather than a sale even though the form was entitled "purchase/rental order," but the information filled in on the form was only the rental rate and not the purchase cost.[343]

In contrast, the federal court in *United States Fidelity and Guaranty Co. v. Thompson-Green Machinery Co.* held that the agreements for rental of heavy construction machinery to a highway contractor were genuine leases and not conditional sales. [344]

> Perhaps the most revealing test is whether the so-called lessee is obligated to accept and pay for the property or is obligated only to return or account for the property according to the terms of the lease from which he may be excused only if he exercises the privilege of purchasing it. If the latter is the case the transaction is a true lease, but if the contract, whatever its form, imposes an absolute obligation to pay for and accept the property and the transferor may require its return only upon default of the transferee, the transaction is a conditional sale… [T]he intent of the parties is controlling and is to be ascertained from the whole transaction, not merely from the language employed.[345]

Essentially the same approach was used where liability for rental was challenged because the equipment was idle for part of the period it was in the lessee's possession. Recognizing that in most construction projects rental equipment is used intermittently, the rented items are considered to be "substantially consumed" on the project during the amount of time they are immediately available to the subcontractor for its use.[346]

Where claims against a contractor for costs of equipment use are based on a conditional sales contract, the claimant cannot have recourse to a Miller Act payment bond. Regarding "rental-purchase" agreements, courts have stated that they will look to the substance rather than the form of these transactions. Thus, where the total rent on equipment substantially equals its purchase price, and a purchase option is exercisable for a nominal sum, the transaction has been held to be a conditional sale.[347] In contrast, where the total rent agreed upon was substantially less than the purchase price of the equipment, and the cost of exercising a purchase option was substantial, the transaction was held to be a rental, and unpaid rental charges were covered by the contractor's payment bond.[348]

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[338] State for Use and Benefit of J.D. Evans Equip. Co. v. Johnson, 83 S.D. 444, 160 N.W.2d 637, 640 (1968) (includes gas and oil); United States for Use of United States Rubber Co. v. Ambursen Dam Co., 3 F. Supp. 548 (N.D. Cal. 1933).

[339] Leo Spear Constr. Co. v. Fidelity and Casualty Co. of New York, 446 F.2d 439, 444 (2d Cir. 1971); United States for Use of Elias Lyman Coal Co. v. United States Fidelity & Guar. Co., 83 Vt. 278, 75 A. 280 (1910).

[340] Standard Accident Ins. Co. v. United States for the Use and Benefit of Powell, 302 U.S. 442, 585 S. Ct. 314, 82 L. Ed. 350 (1938); Conesco Indus. Ltd. v. St. Paul Fire and Marine Ins. Co., 619 N.Y.S.2d 865, 210 A.D. 2d 596, *leave to appeal denied*, 628 N.Y.S.2d 52, 85 N.Y.2d 809, 651 N.E.2d 920 (1995) (freight costs included).

[341] *See, e.g.,* Norquip Rental Corp. v. Sky Steel Erectors, Inc., 854 P.2d 1185, 1190–91 (Ariz. App. 1993); McElhose v. Universal Sur. Co., 182 Neb. 847, 158 N.W.2d 288 (1968).

[342] Public Water Supply Dist. No. 3 of Ray County ex rel. Victor L. Phillips Co. v. Reliance Ins. Co., 705 S.W.2d 190 (Mo. App. 1986) (construing MO. ANN. STAT. 107.170 (1987); rental of excavating machinery paid in five monthly installments with option "guaranteeing" conversion to purchase after 5 months' rental). Regarding distinguishing lease and sale transactions, *see* MO. REV. STAT. 400.1-201(37) (1978) and U.C.C. § 1-201(37); United States ex rel. Eddies Sales & Leasing, Inc. v. Fed. Ins. Co., 634 F.2d 1050, 1052 (10th Cir. 1980) (Miller Act).

[343] Chadwick-BaRoss, Inc. v. T. Buck Constr., 627 A.2d 532 (Me. 1993).

[344] 568 S.W.2d 821 (Tenn. 1978) (construing TENN. CODE ANN. § 54-519 (1978).

[345] 568 S.W.2d at 825.

[346] McGee Steel Co. v. State ex rel. McDonald Indus. Alaska, 723 P.2d 611, 617 (Alaska 1986); John A. Artukovich Sons, Inc. v. Am. Fidelity Fire Ins. Co., 72 Cal. App. 3d 940, 140 Cal. Rptr. 434 (1977).

[347] Oesterreich v. Comm'r Int. Rev., 226 F.2d 798 (9th Cir. 1955).

[348] Kitchen v. Comm'r Int. Rev., 353 F.2d 13 (4th Cir. 1965).

vi. Repairs and Replacement of Parts.—Where claims are based on repairs or replacement of parts in a contractor's equipment, a distinction is made between work needed to maintain the contractor's capital investment in equipment and work needed to replace items worn out in the performance of work. Capital expenditures by the contractor are not covered by payment bonds. Where failure of the equipment during its use requires that it be repaired, the bond under Alaska's Little Miller Act was held to cover repair for incidental damage to the equipment and ordinary wear and tear, but not for repair due to a subcontractor's negligence.[349]

In determining whether repairs and parts replacement must be treated as capital investments, the question of substantial consumption of the repaired or replaced items in the work performed under the contract has been one of the most important tests.[350] It is readily applied to such equipment as tires, batteries, and other automotive accessories that regularly need replacement with wear.[351] However, where the items in question cannot be shown to have been substantially consumed in the contract work, any claim for their repair or replacement is open to the objection that payment will have the effect of adding to the value of the contractor's equipment beyond the needs of the current contract and will be for the benefit of work on other contracts.[352]

Consumption of materials in the course of construction work or integration into the final facility is not questioned in the case of many classes of materials. However, it has presented problems for the state courts in connection with claims based on supplying tires or other equipment not entirely worn out in the work performed. One approach that has received wide acceptance was described by the Pennsylvania court in *Commonwealth to the Use of Walters Tire Service v. National Union Fire Ins. Co.:*[353]

> [T]he proper test to be applied is whether or not in a particular case and bonded project there is a reasonable and good faith expectation by the supplier at the time of delivery that the materials under all the circumstances would be substantially used up in the project under way.[354]

However, a year later the same court had to pass on a claim for replacement of the undercarriage of an item of multi-use equipment. The actual use of the equipment following replacement became the decisive factor. The claim was disallowed when it appeared that following its repair the machinery was used 75 percent of the time on other jobsites.[355] Thus, in practice, the test of reasonableness and good faith is likely to be tempered by reference to whether expectations are validated by actual experience on the jobsite.[356]

"Substantial consumption" is the surest test for distinguishing materials from enhancement of capital investment. However, difficult questions of interpretation have remained in the form of claims based on frustrated expectations of the parties or services performed after the contractor or subcontractor completes work on a contract site. Thus, some courts have focused on the degree of consumption that was expected in connection with a particular job rather than the consumption that actually occurred.[357] Also, the language of the contract may indicate an intent to cover a certain degree of repair or replacement. Where the contract called for rental of equipment at the "net cost" to the subcontractor, the subcontractor was entitled to the cost of repair from the payment bond.[358]

5. Surety Bonds: Legal and Administrative Considerations for State DOTs

Most transporation agencies require performance bonds to secure the performance and completion of their projects. Performance bond forms should be carefully reviewed, kept updated, and list the available options of the surety in event of a default. Most performance bonds incorporate by reference the underlying contract between the principal and the obligee. Further discussion about performance bond provisions is contained in section 7(A)(9) of this volume.

To conduct business on federal projects, a surety must be listed on the U.S. Treasury List of Acceptable Sureties. This list, commonly referred as the Treasury List, is also used by some state transportation agencies as a prerequisite for acceptability. The regulations require sureties to honor their bonds promptly, and their

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[349] McGee Steel Co. v. State ex rel. McDonald Indus. Alaska, 723 P.2d 611, 617–18 (Alaska 1986) (applying ALASKA STAT. § 36.25.010 (1986)); *see also* Sim's Crane Serv. Inc. v. Reliance Ins. Co., 667 F.2d 30, 32 (11th Cir. 1982) (holding surety not liable for crane damage that exceeded "expected consumption" of equipment and "unduly enlarged" the bond's intended coverage); John A. Artukovich Sons, Inc. v. Am. Fidelity Fire Ins. Co., 72 Cal. App. 3d 940, 140 Cal. Rptr. 434 (1977) (modification of trencher to meet project specifications); Conesco Indus., Ltd. v. St. Paul Fire and Marine Ins. Co., 619 N.Y.S.2d 865, 867, 210 A.D. 2d 596, *leave to appeal denied*, 628 N.Y.S.2d 52, 85 N.Y.2d 809, 651 N.E.2d 920 (1994) (repair costs allowed).

[350] United States for Use and Benefit of J.P. Byrne & Co. v. Fire Ass'n, 260 F.2d 541 (2d Cir. 1958).

[351] United States for Use of United States Rubber Co. v. Ambursen Dam Co., 3 F. Supp. 548 (N.D. Cal. 1933).

[352] United States for Use and Benefit of Wyatt & Kipper Eng'rs, Inc. v. Ramstad Constr. Co., 194 F. Supp. 379 (D. Alaska 1961); Continental Cas. Co. v. Clarence L. Boyd Co., 140 F.2d 115 (10th Cir. 1944).

[353] 434 Pa. 235, 252 A.2d 593 (1969).

[354] 252 A.2d at 595.

[355] County Comm'rs of Tioga County to the Use of L.B. Smith, Inc. v. C. Davis, Inc., 439 Pa. 285, 266 A.2d 749 (1970).

[356] Mountaineer Euclid, Inc. v. Western Cas. & Sur. Co., 19 Ohio App. 2d 185, 250 N.E.2d 768 (1969) (definition of "repair," discussion of whether it includes parts and labor or labor only).

[357] United States for Use and Benefit of Chemetron Corp. v. George A. Fuller Co., 250 F. Supp. 649 (D. Mont. 1965); United States for Use and Benefit of J.P. Byrne & Co. v. Fire Ass'n, 260 F.2d 541 (2d Cir. 1958).

[358] R.J. Russo Trucking and Excavating, Inc. v. Pa. Resource Systems, Inc., 573 N.Y.S.2d 95, 169 A.D. 2d 239 (1991).

failure to do so may result in removal from the Treasury List.[359] Under the regulations, if a federal agency takes the position that the surety's refusal to pay is not based on adequate grounds, it may report the surety to the Treasury Department. This may, after notice and a hearing, result in removal from the Treasury List. In addition, sureties may also be suspended or debarred from government contracting based on "adequate evidence of misconduct." Such misconduct could involve fraud or unsatisfactory performance.[360]

Other states require that sureties have AM Best ratings of A- or better, be authorized to do business in the state, or be approved by the state agency.

6. Enforcement of Payment Bonds

Before a party can recover for payment under the Miller Act, it must prove several elements: that it supplied materials or labor for the work in the contract at issue; that it has not been paid; and that the jurisdictional requirements for timely and adequate notice have been met.[361] However, a threshold question in the enforcement of the remedies provided in the Miller Act concerns the definition of parties eligible to reach the contractor's payment bond. The Miller Act stated that this class consisted of persons who dealt directly with the prime contractor, or who lacked a direct contractual relationship, express or implied, with the prime contractor, but had a direct relationship with one of its subcontractors. There was, however, no statutory definition of a subcontractor.

State statutes vary in the scope of persons who may recover under the payment bond. For example, Kansas's bond statute limits recovery to the same persons eligible under the Miller Act.[362] However, California's statute provides coverage to subcontractors at any tier.[363]

a. Parties Entitled to Claim

The Miller Act allows claims by subcontractors and by those in a contractual relationship with a subcontractor, including materialmen and suppliers of labor. Questions have thus arisen as to who is a subcontractor. The first guidance provided by the Supreme Court on the definition of subcontractor in the Miller Act came in *Clifford E. MacEvoy Co. v. United States for Use and Benefit of Calvin Tompkins Co.*[364] The court held that the term "subcontractor," as used in the Miller Act, was "one who performs for and takes from the prime contractor a specific part of the labor or material requirements of the original contract."[365] The claimant had sold building materials to one who resold them to the prime contractor for use in a federal construction project. The court held that the claimant was merely a supplier to a materialman, and thus too remote from the prime contractor to be eligible to reach the payment bond. The decision appeared to be consistent with the legislative history Congress had provided on this point and reflected the Court's acceptance of Congressional efforts to strike a balance that accommodated the needs of all the interests involved.[366] The Court in particular cited the inability of the prime contractor to protect itself from claims that are too remote.[367]

The contractual basis of the parties' relationship appears to have been given more weight than the function being performed in the construction process. There is an argument that functional analysis may reduce the chance for use of sham subcontractors in order to limit liability on a payment bond. However, the United States Supreme Court has held that Congress imposed a structurally defined limitation on the right to sue on a payment bond, which was not to be overstepped by a functional examination of the relationships of the contracting parties.[368] The necessary contractual basis of a

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[359] 31 C.F.R. 223.18(a).

[360] BOND DEFAULT MANUAL 236 (Duncan L. Clore ed., American Bar Association, 2d ed. 1995).

[361] *See, e.g.,* S.T. Bunn Constr. Co. v. Cataphote, Inc., 621 So. 2d 1325 (Ala. Civ. App. 1993).

[362] *See* Vanguard Products Corp. v. American States Ins. Co., 19 Kan. App. 2d 63, 863 P.2d 991 (1993) (applying KAN. STAT. § 60-1111; supplier to subsubcontractor not with scope of coverage of bond).

[363] Union Asphalt, Inc. v. Planet Ins. Co., 27 Cal. Rptr. 2d 371, 21 C.A. 4th 1762 (1994) (applying CAL. CIV. CODE §§ 3110, 3181, 3248(c)).

[364] 322 U.S. 102, 64 S. Ct. 890, 88 L. Ed. 1163 (1944).

[365] 322 U.S. at 109. *See also* Aetna Cas. & Sur. Co. v. United States for Use and Benefit of Gibson Steel Co., 382 F.2d 615 (5th Cir. 1967) (fabricator of steel products who gave the contractor no performance bond, received no progress payments, and whose contract amounted to only 2 percent of the total cost of a project was denied status of subcontractor under the Miller Act); United States for the Use of Wellman Eng'r Co. v. MSI Corp., 350 F.2d 285 (2d Cir. 1965) (firm that supplied hydraulic system for opening and closing roof of missile launcher held status of subcontractor even though it performed no installation work on jobsite); Basich Bros. Constr. Co. v. United States for Use of Turner, 159 F.2d 182 (9th Cir. 1946) (firm that supplied sand and gravel to a location leased by the prime contractor where the materials were further processed and delivered to the jobsite was held to be a subcontractor rather than a materialman; the element of privity was strengthened by the prime contractor's payment of the firm's payroll); Brown & Root, Inc. v. Gifford-Hill & Co., 319 F.2d 65 (5th Cir. 1963); United States for the Use and Benefit of F.E. Robinson Co. v. Alpha-Continental, 273 F. Supp. 758 (E.D. N.C. 1967) (suppliers of labor, although not technically in privity with a prime contractor may be accorded the status of subcontractor); Barton Malow Co. v. Metro. Mfg., Inc., 214 Ga. App. 56, 446 S.E.2d 785 (1994).

[366] One congressional committee's report had stated: "A Sub-subcontractor may avail himself of the protection of the bond by giving notice to the contractor, but that is as far as the bill goes. It is not felt that more remote relationships ought to come within the purview of the bond." H.R. REP. NO. 1263, 74th Cong. 1st Sess. 3 (1935).

[367] 322 U.S. at 110.

[368] J.W. Bateson Co. v. United States ex rel. Bd. of Trustees of Nat. Automatic Sprinkler Indus. Pension Fund, 434 U.S. 586 (1978).

claim is most readily shown by written agreements. However, contracts may be implied from the actions of the parties in the absence of a written agreement.[369]

This is illustrated in *United States ex rel. Parker-Hannifin Corp. v. Lane Construction Co.*[370] The claimant was a manufacturer of hydraulic cylinders for operating the gates of an Army Corps of Engineers dam. It supplied these items to a subcontractor, and later sued on the prime contractor's payment bond when the subcontractor went bankrupt without having paid for the gates. Declaring that no general rule could be devised to dispose of cases of this sort, the court identified the following factors that should be considered in determining whether a claimant should be considered to be a subcontractor or material supplier. The first is the nature of the material or service supplied.[371] For example, fungible goods that are part of general inventory (like sand and gravel), the production of which does not require use of a customized manufacturing process in order to meet the prime contractor's specifications, generally are treated as materials handled by a supplier or broker.

The second factor is whether the claimant had to make shop drawings of the items and supervise their fabrication.[372] Items that are custom-made to specifications set out in the prime contract, by one who is responsible for the design, shop drawings, and fabrication of the items, generally are treated as the work of subcontractors. Custom manufacture by itself is not sufficient to establish subcontractor status, but is a major factor in the test.[373] In *Parker-Hannefin*, the court held that the claimant gate manufacturer qualified as a subcontractor whose work was incorporated into the bonded project, and so was eligible to sue on the project's payment bond.[374]

Interpreting definitions in Little Miller Acts, some states have undertaken a functional relationship test to determine whether a party is a subcontractor or a materialman who is too remote to recover under the bond. Under Arizona's statute, the court held that where a supplier was the "functional equivalent" of a subcontractor, it was entitled to the bond's protection.[375] The court found that the correct test involved an examination of the nature of the dealings between the parties.

Some state courts have given their Little Miller Acts broader coverage based on apparent legislative intent.[376] The same result has been reached by treating material suppliers to sub-subcontractors as third-party beneficiaries, commenting that to hold otherwise would permit contractors and subcontractors to insulate themselves from liability by executing a series of subcontracts for that purpose and thwart the intent of the statute.[377]

The Arizona court set out the following test of subcontractor status: (1) Does the custom in the trade consider the supplier a subcontractor or a materialman? (2) Are the items supplied generally available in the open market or are they "customized"? (3) In determining whether the material is "customized," do the plans and specifications call for a unique product, or are they merely descriptive of what is to be furnished? (4) Does the supplier's performance constitute a substantial and definite delegation of a portion of the performance of the prime contract?[378]

Instances in which a surety takes over the completion of a construction project following default by the project's original prime contractor generally are handled by the surety's engaging another construction company to perform the unfinished work. In such a case, the surety is regarded as stepping into the place of the general contractor and the newly engaged contractor becomes a subcontractor for purposes of determining who is covered by the surety's bond.[379]

The type of material or service supplied is not a reliable basis for determining whether a supplier is a subcontractor. Although suppliers of sand, gravel, and aggregate generally are not considered subcontractors, claims for furnishing these materials occasionally have been allowed on this basis.[380] On the other hand, sup-

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[369] United States ex rel. Greenwald Indus. Products Co. v. Barlows Commercial Constr. Co., 567 F. Supp. 464, 466 (D.D.C. 1983) (contractor accepted delivery and used materials supplied by claimant).

[370] 477 F. Supp. 400 (M.D. Pa. 1979).

[371] *Id*. at 411.

[372] *Id*.

[373] *See, e.g.,* LaGrand Steel Products Co. v. A.C.S. Constructors, Inc., 108 Idaho 817, 702 P.2d 855 (Idaho App. 1985) (applying Idaho Code 54-1926) (fabricator was held to be a subcontractor where customized steel plates were a large item in the contract price); Inryco. Inc. v. Eatherley Constr. Co., 793 F.2d 767 (6th Cir. 1986) (fabricator of highway sound barriers manufactured to dealer's specifications, where dealer in turn sold them to a subcontractor, was a supplier to a materialman).

[374] 477 F. Supp. at 412.

[375] Trio Forest Products, Inc. v. FNF Constr., Inc., 182 Ariz. 1, 3, 893 P.2d 1, 3, *reconsideration denied, review denied* (1994).

[376] State ex rel. W.M. Carroll & Co. v. K.L. House Constr. Co., 99 N.M. 186, 656 P.2d 236, 237 (1982) (construing N. M. STAT. ANN., § 13-4-19 (1978)) (statute includes a supplier of any subcontractor, is broader in scope than Miller Act); State ex rel. Certain-Teed Products Corp. v. United Pacific Ins. Co., 389 A.2d 777 (Del. Super. 1978) (construing DEL. CODE, 29-6909 (1978)); Union Asphalt, Inc. v. Planet Ins. Co., 27 Cal. Rptr. 2d 371, 21 C.A. 4th 1762 (1994) (CAL. CIV. CODE §§ 3110, 3181, 3248(c) apply to subcontractors at any tier).

[377] Frost v. Williams Mobile Offices, Inc., 343 S.E.2d 441 (S.C. 1986) (temporary office furnished for staff while military hospital was renovated).

[378] B.J. Cecil Trucking, Inc. v. Tiffany Constr. Co., 123 Ariz. 31, 597 P.2d 184, 187–88 (Ariz. App. 1979) (applying ARIZ. REV. STAT., § 32-1152 (1978)).

[379] H&H Sewer Systems, Inc. v. Ins. Guar. Ass'n, 392 So. 2d 430 (La. 1980).

[380] Standard Accident Ins. Co. v. Basolo, 180 Okla. 261, 68 P.2d 804 (1937) (claimant who supplied sand and gravel for highway construction and delivered it to a location near the jobsite held to be both a subcontractor and materialman); *see also* People for Use and Benefit of Youngs v. United States Fidelity & Guar. Co., 263 Mich. 638, 249 N.W. 20 (1933).

pliers of millwork and hardware items generally have been called contractors, while suppliers of brick, concrete blocks, curbstones, and similar stock items of building supplies have been treated as materialmen. Claims for furnishing fabricated steel items present a range of fact situations that have caused trouble for the courts. Normally the suppliers of these items do not perform any work at the jobsite following delivery, and where they do not, the assignment to them of a materialman's status is understandable. On the other hand, where they perform installation or other services in connection with the construction, their claim to subcontractor status is strengthened.[381]

Viewing the cases as a whole, the results seem to reflect the use of a rather general test that ultimately turns on the degree that the prime contractor shifts or delegates its own responsibility to others. If the responsibility delegated merely entails furnishing or slightly altering standard materials or manufactured items without installing or incorporating them into the construction, the supplier is properly classified as a materialman. But where this responsibility includes installation as well as supply, or involves supplying a custom-built item or a product not generally available, the supplier may be classified as a subcontractor even though its work is performed far from the prime contractor's jobsite.

b. Notification of Claim

i. Time for Providing Notice.—Claimants seeking recourse to a contractor's payment bond under authority of the Miller Act must give written notice of their claim to the contractor within 90 days after the date on which the last labor was performed or the last materials were furnished on which the claim is based. The Miller Act does not address whether notice must be mailed or received within 90 days. However, at least one court has held that notice must be received by the contractor prior to the end of the 90-day period.[382]

State statutes have similar time limitations for filing notice.[383] For example, Florida requires that a claimant have given the contractor notice within 45 days of beginning work on the project that it intends to look to the bond for protection against nonpayment, and must notify the contractor and surety of its claim within 90 days after completing its performance.[384]

Compliance with the requirement for giving timely notice is a jurisdictional requirement for proceeding against the contractor's bond.[385] Where this requirement is in force at the time a contract is awarded and is incorporated by reference into the contract, it applies even though it subsequently is amended or repealed,[386] or a contractor orally undertakes responsibility for a defaulting subcontractor's debts,[387] or fails to object to lack of timely or proper notice of the claim at the commencement of the suit.[388]

A Miller Act claimant may avoid this requirement only by showing that it has entered into a "contractual relationship, express or implied" with the contractor.[389] Such a showing must be unequivocal and must relate to the specific items that comprise the claim. For example, a subcontractor's supplier was excused from giving notice within the statutory period by showing that after the subcontractor's default the contractor executed an agreement to pay the supplier's unpaid balance, and thereafter issued checks made jointly payable to the supplier and subcontractor.[390] In contrast, the claimant was not excused from complying with the notice period where it relied on the contractor's general declaration that it would pay for materials incorporated into the project, despite the fact that the contractor's checks were issued jointly to the supplier and subcontractor.[391] Nor was the necessary contractual relationship present where a claimant relied on its status as a co-prime contractor on the project.[392]

Where a bond provides less stringent notification requirements than what the statute requires, then the terms of the bond will control.[393] However, if the bond

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[381] Jesse F. Heard & Sons v. Southwest Steel Prods., 124 So. 2d 211 (La. Ct. App. 1960).

[382] B & R, Inc. v. Donald Lane Constr., 19 F. Supp. 2d 217 (D. Del. 1998).

[383] Sharpe, Inc. v. Neil Spear, Inc., 611 So. 2d 66, *review denied*, 620 So. 2d 761 (Fla. App. 1 Dist. 1992) (applying FLA. STAT. § 255.05).

[384] FLA. STAT. § 255.05.

[385] U.S. Fidelity & Guar. Co. v. Thompson and Green Machinery Co., 568 S.W.2d 821 (Tenn. 1978) (construing TENN. CODE § 54-519 (1975)); Mid-County Rental Service, Inc. v. Miner-Dederick Constr. Corp., 583 S.W.2d 428 (Tex. Civ. App. 1979) (construing TEX. CIV. STAT. art. 5160 (1987)); U.S. Fidelity & Guar. Co. v. Couch, Inc., 472 So. 2d 614 (Ala. 1985) (construing ALA. CODE § 39-1-1 (1975), delaying suit until 45 days after notice to surety and contractor's failure to pay within 45 days).

[386] United Plate Glass Co., Div. of Chromalloy Am. Corp. v. Metal Trim Indus., 505 A.2d 613 (Pa. Super. 1986) (construing 8 PA. STAT. § 194(b)).

[387] Barboza v. Aetna Cas. & Sur. Co., 18 Mass. App. 323, 465 N.E.2d 290, 293 (1984) (construing MASS. GEN. L. ch. 149, § 29).

[388] Travelers Indem. Co. v. Munro Oil & Paint Co., 364 So. 2d 667 (Miss. 1978) (construing MISS. CODE § 31-5-13 (1972)).

[389] 40 U.S.C. § 3133.

[390] United States ex rel. Billows Elec. Supply Co. v. E.J.T. Constr. Co., 517 F. Supp. 1178, 1182–83 (E.D. Pa. 1981).

[391] Noland Co. v. Armco, Inc., 445 A.2d 1079 (Md. App. 1982) (construing MD. CODE, art. 21, § 3-501 (1980)).

[392] Aetna Cas. & Sur. Co. v. Doleac Elec. Co., 471 So. 2d 325 (Miss. 1985) (construing MISS. CODE, § 31-51-1 (1972)); *see also* Fleisher Eng'r & Constr. Co. v. United States for Use and Benefit of George S. Hallenbeck, 311 U.S. 15, 61 S. Ct. 81, 85 L. Ed. 12 (1940); State Roads Comm'n to the Use of Mobil Oil Corp. v. Contee Sand & Gravel Co., 308 F. Supp. 650 (D. Md. 1970).

[393] Trustees for Michigan Laborers' Health Care Fund v. Warranty Builders, Inc., 921 F. Supp. 471, 475–76 (E.D. Mich. 1996), *aff'd*, 137 F.3d 427 (6th Cir. 1998) (applying Michigan Public Works Act, M.C.L.A. § 129.201).

sets more stringent requirements than allowed by the statute, that provision in the bond may be held to be void and the time limits set by statute will control.[394]

If a state has a requirement for recording the bond, then the notice requirement may apply only if the contractor has recorded the bond in the manner required by statute.[395] If the contractor has not recorded the bond where there is such a requirement, a supplier is not bound by the notice and time limitations.[396]

The difficulties of applying the notice rule arise from the variety of business and accounting arrangements under which materials and services are supplied in construction projects. Where a materialman supplies materials on several occasions, each occasion may be treated by the parties as separate orders, a continuing contract, a running open account, or some other type of purchase arrangement. Contracts calling for supply, installation, testing, and training of others in the use of equipment or components may also make it difficult to determine at what point the notice period begins.[397] In contracts requiring a series of steps, some of the steps may be separated by more than 90 days, and recovery for the earlier shipments may be barred.[398] Cautious suppliers who must make a series of deliveries adopt the practice of filing claims within 90 days following each delivery, rather than relying on the argument that the series is integrated or that it is part of an open account transaction.[399]

Where it was necessary to determine the last date on which material was supplied, arguments have been made to adopt the rule of commercial codes that recognize "constructive delivery" of specially manufactured goods to a subcontractor once those goods are segregated and stored by the manufacturer or supplier pending actual delivery to the work site. The Georgia appellate court rejected the analogy to the Uniform Commercial Code, and held that state law contemplated actual delivery of material to the subcontractor rather than constructive delivery.[400]

Where statutory time limits for giving notice of claims start running from the date of final acceptance of a completed project, that date needs to be identified with certainty, generally by execution of a formal certification of acceptance.[401] Where no benchmarks are provided, determination of whether a notice is given within 90 days after completion and acceptance of a project becomes a factual question of when contract performance was actually finished and the completed facility was accepted by word or conduct of the contracting agency.[402]

As a jurisdictional requirement, a timely notification of a claim must be alleged in the claimant's pleadings.[403] Although circumstances may afford a contractor actual notice of a claim in a timely and sufficient manner, statutes based on the Miller Act are strictly construed to require timely written notice.[404] Actual knowledge of an unpaid account or of the presence of the claimant on the project is not sufficient.[405]

iii. Sufficiency of Notice.—The Miller Act specifies that notice to the prime contractor shall state "with substantial accuracy the amount claimed and the name of the party to whom the material was furnished or supplied, or for whom the labor was done or performed."[406] Inevitably, questions have arisen over the status of correspondence where either the intent or the factual accuracy of the contents were not clear. A rule of reason is applied to these cases, based on the underly-

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[394] Town of Pineville v. Atkinson/Dyer/Watson Architects, P.A., 114 N.C. App. 497, 442 S.E.2d 73 (1994); Dutchess Quarry & Supply Co. v. Firemen's Ins. Co. of Newark, N.J., 596 N.Y.S.2d 898, 190 A.D. 2d 36 (1993).

[395] *See, e.g.*, Martin Paving Co. v. United Pacific Ins. Co., 646 So. 2d 268 (Fla. App. 5 Dist. 1994) (applying FLA. STAT. § 255.05 (1, 2, 4)).

[396] Martin Paving Co. v. United Pacific Ins. Co., 646 So. 2d 268 (Fla. App. 5 Dist. 1994).

[397] *See, e.g.,* Johnson Serv. Co. v. Transamerica Ins. Co., 349 F. Supp. 1220 (S.D. Tex. 1972), *aff'd*, 485 F.2d 164 (5th Cir. 1973).

[398] United States for Use and Benefit of I. Burack, Inc. v. Sovereign Constr. Co., Ltd., 338 F. Supp. 657 (S.D. N.Y. 1972); United States for Use and Benefit of J.A. Edwards & Co. v. Bregman Constr. Corp., 172 F. Supp. 517 (E.D. N.Y. 1959).

[399] *Compare* Noland Co. v. Allied Contr., Inc. 273 F.2d 917 (4th Cir. 1959) *with* United States for Use and Benefit of J.A. Edwards & Co. v. Peter Reiss Constr. Co., 273 F.2d 880 (2d Cir. 1959), *cert. den*., 362 U.S. 951, 80 S. Ct. 864, 4 L. Ed. 2d 869 (1960).

[400] F.L. Saino Manufacturing Co. v. Fireman's Fund Insurance Co., 173 Ga. App. 753, 328 S.E.2d 387 (1985).

[401] Maxson Corp. v. Gary King Constr. Co., 363 N.W.2d 901, 902–03 (Minn. App. 1985) (citing Minn. Dep't of Transp. Standard Specifications for Highway Constr. (1978), as incorporated by reference into the contract).

[402] Alexander Constr. Co. v. C&H Contracting, Inc., 354 N.W.2d 535, 538 (Minn. App. 1984) (construing MINN. STAT. 574.31 (1982), streets and sewers); *but see* Honeywell, Inc. v. Jimmie B. Guinn, Inc., 462 So. 2d 145 (La. 1985) (installation of automatic temperature control system held to be necessary to complete the original project); Worcester Air Conditioning Co. v. Commercial Union Ins. Co., 14 Mass. App. 352, 439 N.E.2d 845, 847 (Mass. App. 1982) (installation of additional ducts, done by subcontractor 4 months after punch list was completed and project was accepted, held to be new work under a new contract).

[403] Continental Contractors, Inc. v. Thorup, 578 S.W.2d 864 (Tex. Civ. App. 1979).

[404] Square D Envtl. Corp. v. Aero Mechanical, Inc., 119 Mich. App. 740, 326 N.W.2d 629, 631 (1982) (notice statute required only a following of "specific step-by-step procedures" and should be strictly construed; legislature did not use the term substantial compliance).

[405] Spetz & Berg, Inc. v. Luckie Constr. Co., 353 N.W.2d 233 (Minn. App. 1984) (construing MINN. STAT., § 574.31 (1979)); Barboza v. Aetna Cas. & Sur. Co., 18 Mass. App. 323, 465 N.E.2d 290, 293 (1984) (construing MASS. GEN. L. ch. 149, § 29 (1972)); Posh Constr., Inc. v. Simmons & Greer, Inc., 436 A.2d 1192 (Pa. Super. 1981).

[406] 40 U.S.C. § 3133 (2003).

ing purpose of the notice requirement that the prime contractor should be made aware of the claims of those with whom it has no direct contractual relationship, or presumably, any regular contact during its supervision of the contract work.[407] The essential character of the notice must be a positive presentation of a claim, stated clearly and comprehensively enough for the prime contractor to know its amount, to whom it is owed, and to whom the labor or material was furnished.[408]

Federal courts construing the Miller Act have not insisted on any particular form of notice, but rather have looked to see if the message given to the contractor informed it of the amount owed, the party to which it was owed, the basis of the debt, and if the message actually got to the contractor.[409] The amount claimed need not be stated with absolute precision, but it must be substantially accurate, or else any discrepancies must be explained so as to make the correct amount ascertainable.[410] Also, courts have recognized the practical limits of requiring copies of billing documents, invoices, and orders identifying parts of claims for multiple items of labor and materials where they are to be paid for on a lump sum basis. [411] State statutes may also specify formalities such as making sworn statements or transmitting notice by registered mail.[412] Where statutory language allows it, courts may construe formalities more liberally, in accordance with the statute's remedial nature.[413] Accordingly, where a contractor was in fact informed of a claim, the notice was not invalid because it was sent in advance of the 45-day notice period,[414] or because the notice was sent by regular mail instead of registered mail,[415] or because the wrong contract number was referenced.[416] Similarly, even where the statute required that an affidavit be submitted by the claimant, a document that contained the required information and included a notarized signature of the claimant was held to be sufficient.[417]

The Miller Act previously required the claimant's pre-claim notice to either be served in the same manner as a summons, or sent by registered mail.[418] Amendments to the Miller Act in 1999 allow a claimant to send its pre-claim notice by "any means which provides written, third-party verification of delivery."[419] This allows use of other delivery options such as certified mail or overnight delivery services.

c. Limitation on Suit

The second major procedural requirement that claimants must meet under the Miller Act is the provision that suit against the payment bond must be filed within 1 year of the "date of final settlement" of the contract. As in the application of the requirement for filing notice of claims, the courts have recognized circumstances in which strict compliance with the limitations on filing suit must be relaxed to achieve the broad objective of the law. The strongest cases for allowance of filing after 1 year have involved major repairs or replacements of components of the facilities supplied, so extensive that the earlier installation does not qualify as performance of the supplier's contract obligation.[420] Administrative work, inspections, testing, and correc-

[407] Fleisher Eng'r & Constr. Co. v. United States for Use and Benefit of Hallenbeck, 311 U.S. 15, 61 S. Ct. 81, 85 L. Ed. 12 (1940).

[408] United States for Use and Benefit of J.A. Edwards & Co. v. Thompson Constr. Corp., 273 F.2d 873 (2d Cir. 1959), *cert. denied*, 362 U.S. 951, 80 S. Ct. 864, 4 L. Ed. 2d 869 (1960); *see also* United States for the Use of Old Dominion Iron & Steel Corp. v. Massachusetts Bonding & Ins. Co., 272 F.2d 73 (3d Cir. 1959) (doubtful language); United States for Use and Benefit of Hopper Bros. Quarries v. Peerless Cas. Co., 255 F.2d 137 (8th Cir. 1959); *cert. denied*, 358 U.S. 831, 79 S. Ct. 51, 3 L. Ed. 2d 69 (1958); United States for Use and Benefit of Franklin Paint Co. v. Kagan, 129 F. Supp. 331 (D. Mass. 1955) (accuracy of claim); Dover Elec. Supply Co. v. Leonard Pevar Co., 178 F. Supp. 834 (D. Del. 1959).

[409] United States ex rel. Joseph T. Richardson, Inc. v. EJT Constr. Co., 453 F. Supp. 435 (D. Del. 1978).

[410] United States ex rel. Honeywell, Inc. v. A&L Mechanical Contractors, Inc., 677 F.2d 383 (4th Cir. 1982).

[411] Sims v. William S. Baker, Inc., 568 S.W.2d 725, 730 (Tex. Civ. App. 1978) (construing TEX. ANN. CIV. STAT. art. 5160, sub. B(a)(2) (1978)); *see also* Featherlite Building Products Corp. v. Constructors Unlimited, Inc., 714 S.W.2d 68 (Tex. App. 1986).

[412] Bastianelli v. National Union Fire Ins. Co., 36 Mass. App. Ct. 367, 631 N.E.2d 566, 568 n.4, (1994); San Joaquin Blocklite, Inc. v. Willden, 228 Cal. Rptr. 842 (1986) (notice by first class, certified, or registered mail to contractor, or personal service); Space Building Corp. v. INA, 389 N.E.2d 1054 (Mass. App. 1979) (sworn statement).

[413] Cinder Products Corp. v. Schena Constr. Co., 22 Mass. App. 927, 492 N.E.2d 744 (1986) (citing M.G.L. c. 149 § 29, requiring service by certified or registered mail; failure to use certified or registered mail was not fatal if actual timely notice is proved).

[414] School Board of Palm Beach County v. Vincent J. Fasano, Inc., 417 So. 2d 1063 (Fla. App. 1982).

[415] Vacuum Systems, Inc. v. Washburn, 651 A.2d 377 (Me. 1994); Bob McGaughey Lumber Sales, Inc. v. Lemoine Co., 590 So. 2d 664 (La. App. 3 Cir. 1991); Consolidated Concrete Co. v. Empire West Constr. Co., 596 P.2d 106, 108–09 (Idaho 1979) (construing Idaho Code, § 54-1929 (1979)); *but see* F.L. Saino Mgf. Co. v. Fireman's Fund Ins. Co., 173 Ga. App. 753, 328 S.E.2d 387 (1985) (construing GA. CODE ANN., § 36-82-104(b) (1987) (notice by regular mail is effective when received, while registered mail notice is effective when mailed).

[416] Dixie Bldg. Material Co. v. Liberty Somerset, Inc., 656 So. 2d 1041 (La. App. 4 Cir. 1995).

[417] Acme Brick, a Div. of Justin Industries v. Temple Assocs., 816 S.W.2d 440, *writ denied* (Tex. App. 1991) (McGregor Act requires only substantial compliance).

[418] Former 40 U.S.C. § 270b(a) (1999).

[419] 40 U.S.C. § 3133(b)(2)(A) (2003).

[420] *Compare* United States for the Use of General Electric Co. v. Gunnar I. Johnson & Son, Inc., 310 F.2d 899 (8th Cir. 1962) *with* United States for Use of McGregor Arch Iron Co. v. Merritt-Chapman & Scott, Corp., 185 F. Supp. 381 (M.D. Pa. 1960).

tive work conducted after delivery do not extend the dates when the limitation period begins to run.[421]

A federal court examined when the statute of limitations begins to run under the Miller Act in *United States v. Fidelity Co. and Deposit of Maryland*.[422] The court compared cases in which the statute was held to begin running at the time of substantial completion, which it found to be the minority view, with those in which the statute began at the time of completion of all of the original requirements of the contract, as opposed to corrections or repairs, which was the majority view.[423] Under the majority view, an uncompleted contract requirement tolls the time for filing, while corrective work does not. Where substantial completion is used as the operative date, the filing period is not extended by insignificant work, even if that work is required under the contract and is not corrective work. The court applied what it called a "middle ground" approach in deciding in favor of allowing a supplier's claim.[424] It did not follow the rule that repair work does not toll the time period, but rather based its decision on the value of the materials involved, the requirements of the original contract, the unexpected nature of the work, and the importance of the materials to the operation of the system.[425]

Once the period of limitation on filing suit begins to run, it is not interrupted or tolled by the occurrence of negotiations between the claimant and the prime contractor over whether the subcontract was duly completed and payment for it was due.[426] Nor is the running of the limitation period changed by amendment of the bond statute to prescribe a different date for its commencement.[427] Where this occurred under Connecticut's Little Miller Act, the court held that the amendment was not retroactive and the provisions of the law in force at the time the claimant's contract was executed were the controlling factor in determining compliance with the filing date. [428]

State bonding statutes with provisions similar to those in the Miller Act prior to 1959 set the time limit for starting suits at 1 year or another specified period after the "final settlement" of the contract.[429] Final acceptance of a project by the public works agency generally is considered as the administrative action constituting final settlement.[430] Exceptions to this rule are recognized, however, where an acceptance is found to be premature because essential work remained to be done after formal acceptance.[431] In order to constitute a final settlement, the public works agency's acceptance must relate to the entire project in order to avoid the risk that the security will be exhausted before the full number of unpaid creditors and their claims are known.[432]

A common practice among agencies contracting for public works construction is to issue a certificate of substantial completion when all work has been performed, inspected, and accepted subject to completion of a "punch list" agreed upon by the parties. In a case under Arizona's Little Miller Act, however, a subcontractor hired to furnish and install an automatic temperature control element of a fire alarm system continued work on punch list items for several months after the certificate of substantial compliance was issued.[433] When a subcontractor later filed suit for unpaid charges, it was held that the period for filing suit started running when the claimant finished work on the punch list. Drawing on federal cases under the Miller Act, the court stated:

> The applicable test asks whether the work was done in furtherance of the original contract, or whether it was for the purpose of correcting defects or making repairs. Work done solely to effect repairs, make corrections or complete final inspection is insufficient to qualify as work pursuant to the original contract and is not considered work per-

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[421] Honeywell, Inc. v. Arnold Constr., 134 Ariz. 153, 654 P.2d 301 (1982); 17 AM. JUR. 2D C*ontractors Bonds* § 207 (1990).

[422] 999 F. Supp. 734 (D. N.J. 1998).

[423] *Id.* at 742.

[424] *Id*. at 745.

[425] *Id*.

[426] Visor Builders, Inc. v. Devon E. Trantor, Inc., 470 F. Supp. 911 (M.D. Pa. 1978).

[427] *See* CONN. GEN. STAT. §§ 49-41, 49-42 (1987).

[428] Am. Masons Supply Co. v. F.W. Brown Co., 164 Conn. 219, 384 A.2d 378 (1978); Manganes Printing Co. v. Joseph Bucheit and Sons Co., 601 F. Supp. 776 (D.C. Pa. 1985).

[429] W.B. Headley v. Housing Auth. of Prattville, 347 So. 2d 532 (Ala. Civ. App. 1977); Medical Clinic Bd. of City of Birmingham-Crestwood v. E.E. Smelley, 408 So. 2d 1203 (Ala. 1981); City of San Antonio v. Argonaut Ins. Co., 644 S.W.2d 90 (Tex. App. 1982) ("final completion of contract").

[430] Transamerica Ins. Co. v. Housing Auth. of City of Victoria, 669 S.W.2d 818 (Tex. App. 1984).

[431] Honeywell, Inc. v. Jimmie B. Guinn, Inc., 462 So. 2d 145 (La. 1985); *see also* Cortland Paving Co. v. Capital District Contractors, Ltd., 490 N.Y.S.2d 51 (1985) (parties agreed to reasonable delay to allow contractor to obtain funds from state); Valley Forge Indus., Inc. v. Armand Constr., Inc., 394 A.2d 677 (Pa. Commw. 1978) (correction of defects required substantial repetition of work).

[432] Maurice E. Keating, Inc. v. Township of Southampton, 149 N.J. Super. 118, 373 A.2d 421 (1977); Safeco Ins. Co. of America v. Honeywell, Inc. 639 P.2d 996, 1001–02 (Alaska 1981) (dispute arose over which one of a series of inspections, certifications, notices, and reports constituted "final acceptance;" court ruled that final settlement required a specific administrative act bearing on the completeness of the contract and approving payment; approval of final pay estimates fit criteria of the law and carried out the purpose of the applicable statute, ALASKA STAT. § 36.25.020); Hall v. U.S. Fidelity & Guar. Co., 436 A.2d 863 (Me. 1981) (where sand and gravel were supplied for highway construction, the necessary administrative act that marked the last date of furnishing labor or materials was the highway agency's final determination of the quantities of materials used in the construction project).

[433] Honeywell, Inc. v. Arnold Constr. Co., 134 Ariz. 153, 654 P.2d 301, 304 (1982) (applying ARIZ. REV. STAT. § 34-223 (1987)).

formed or material supplied within the one year statutory limitation.[434]

Bankruptcy of the prime contractor does not toll or extend the running of the time limit for subcontractors to file suit against the surety bond.[435] Nor does the substitution of a new contractor after default by the original prime contractor affect the running of the time limit.[436] However, the surety may extend its liability for claims arising from an abandoned job by making a specific undertaking to do so when it takes over from the defaulting contractor.[437]

Where the provisions of a surety bond regarding the time for starting suit differ from the terms of the bonding statute, the difference may be treated as converting the surety's statutory liability into a common law liability. The effect of such a conversion was explained in the Florida court in *Motor City Electric Co. v. Ohio Casualty Insurance Co*., where a claim for rental of heavy equipment was sustained even though barred by the statutory limit on filing suit.

> [N]ot every bond furnished incident to a public works project falls within the ambit of the statute…courts recognize a distinction between a statutory bond issued in connection with such a project and a common law bond. A bond…will be construed as a common law bond if it is written on a more extended basis than required by Section 255.05, Florida Statutes (1975)… Morover, ambiguities in the form of such a bond must be construed in favor of granting the broadest possible coverage to those intended to be benefited by its protection.[438]

d. Claimant Has Not Been Paid

In addition to showing that labor or materials are furnished for the project in question, it must be shown that the claimant has not been paid for them. Where a public works agency makes progress payments at predetermined intervals, disputes may occur over allocation of those payments to the creditor's accounts. Generally those disputes arise in the absence of instructions by the debtor at the time of payment, leaving it to the creditor's discretion to say how they shall be applied. This discretion, however, is not unlimited. The rule evolved from Miller Act cases is stated in *St. Paul Fire and Marine Insurance Co. v. United States ex rel. Dakota Electric Supply Co.* as follows:

> If a debtor is under a duty to a third person to devote funds paid by him to the discharge of a particular debt, the payment must be so applied if the creditor knows or has reason to know of that duty. This is so despite the debtor's contrary direction.[439]

Federal courts have not imposed a duty on a claimant to inquire about the source of a payment in litigation under the Miller Act. Nor have state courts read this duty into their state bonding laws for public works construction projects.[440] The reluctance to enforce a duty to demand designation of the source and disposition of payments into an open account, or circumstances where the debtor has several project accounts with the creditor, has not prevented courts from rigorous examinations of the parties' transactions and critical appraisal of whether the creditor knew or had reason to know the source of its payment. If the history and circumstances of an unpaid account make prudent in the course of exercising business judgment to inquire about the debtor's sources and expectations of funds, the court may well find there is sufficient knowledge of the "principal source" of the funds to require the creditor to apply the payment to that project account. Therefore, in *School District of Springfield R-12, ex rel. Midland Paving Co.,* the court held that the creditor's failure to apply a partial payment to the bonded project's account was, while not done in bad faith, done "prematurely and without proper precaution."[441]

e. Waiver of Payment Bond Remedies

Prior to the 1999 amendments, the Miller Act did not address whether a potential claimant could waive its payment bond remedies. The amendment allows such a waiver, so long as it is (1) in writing, (2) signed by the potential claimant, and (3) executed after the potential claimant has first furnished labor or material for use in performance of the contract.[442] Thus a subcontractor or materialman could submit a release form with its invoice, so long as it meets these requirements.

7. Enforcement of Performance Bonds

a. Agencies' Remedies

Actions to enforce the obligations of performance bonds are taken at the initiative of the state.[443] They may be brought at any time within the statutes of limitations for actions on written contracts. As a practical matter, however, the state's action of declaring a contractor in default generally is followed by negotiations between the surety and the contracting agency for the purpose of deciding how the contract can be completed by any of the several options open to the parties. Because both the surety and the contracting agency are better off if they complete the contract, recourse to the courts for enforcement of bonds running in favor of the public is relatively rare. More frequently, suits involv-

[434] 654 P.2d at 304 (citations omitted).

[435] Fountain Sand & Gravel Co. v. Chilton Constr. Co., 578 P.2d 664, 665 (Colo. App. 1978).

[436] Adamo Equip. Rental Co. v. Mack Dev. Co., 122 Mich. App. 233, 333 N.W.2d 40, 42 (1982).

[437] Argonaut Ins. Co. v. M&P Equip. Co., 269 Ark. 302, 601 S.W.2d 824 (1980).

[438] 374 So. 2d 1068, 1069 (Fla. App. 1979).

[439] 309 F.2d 22, 25 (8th Cir. 1962).

[440] Trans-American Steel Corp. v. J. Rich Steers, Inc., 670 F.2d 558 (5th Cir. 1982); Geneva Pipe Co. v. S&H Ins. Co., 714 P.2d 648, 651 (Utah 1986) (citing UTAH CODE ANN. § 58A-1a-12 (1985)).

[441] 633 S.W.2d 238, 253 (Mo. App. 1982).

[442] 40 U.S.C. § 3133(c) (2003).

[443] Town of Melville v. Safeco Ins. Co. of America, 651 So. 2d 404, *writ denied*, 654 So. 2d 333 (La. App. 3 Cir. 1995).

ing performance bond obligations arise through the initiative of the surety, who has become subrogated to a claim on monies held by the contracting agency as retainage or as partial payment earned but not yet paid under a contract. A further discussion of agencies' remedies is contained in section 7(a)(9) of this volume.

The determination that a contractor is in default is a matter of judgment by the contracting agency. An act of default by a contractor does not impose upon the contracting agency any duty to declare it in default of its contract if, despite appearances, the agency believes that it will complete the work satisfactorily.[444] Nor may a surety compel the government to shut down a contractor on the basis of information that satisfied the surety that default may be either imminent or inevitable. Although the surety may sincerely wish to conserve the funds remaining in the government's hands so that those funds may be used to complete the defaulted work, the contracting agency is entitled to a reasonable opportunity to investigate the situation thoroughly.

Once a contractor has been declared in default, and its surety has completed the contract, there may be competition for the agency's remaining funds. Differing results have sometimes occurred in federal decisions relating to the Miller Act, and in decisions under state laws. In Miller Act cases where the Federal Government is a claimant (as, for example, where collection of unpaid taxes is sought), it may claim taxes as a setoff against the surety's share of the retained funds. *United States v. Munsey Trust Co.* established the doctrine for federal law on this question, holding that the government was in the same position as a secured creditor, and so entitled to withhold what it owed the contractor until its own claims were satisfied.[445] The surety, subrogated to the contractor's position, is regarded as never having acquired any superior right to the retained funds.

Such a rule had obvious disadvantages for the surety who elected to complete a defaulted contract, for it could never be sure that it could obtain the full amount of the unpaid funds under the original contract. In the surety's view, it was better off to let the agency complete the contract, and let its suretyship liability be limited to the difference, if any, between the contract price and the actual cost of completion.[446] When this matter was carefully considered, however, the *Munsey* doctrine was not extended beyond the setoff of delinquent taxes. In *Massachusetts Bonding & Insurance Company v. New York*, the New York court discussed the position of subrogated sureties:

> It is settled law that a surety which undertakes to complete a construction contract after its principal has defaulted…becomes entitled to payments due the principal….This right to "first" priority attaches not only to moneys due the principal at the time of default, but to so-called "unearned" moneys which arise from the surety's activities in completing the contract after this principals default.[447]

The same rule for priority of claims on unpaid contract funds has been applied where the surety's lien for payment of defaulted debts is subrogated to the contractor's claim on the retained funds. Tax liens in favor of the government have not been given priority over the surety since the latter's equitable right is viewed as arising at the time the surety posted its bond. Subsequent tax liens against the contractor therefore could not reach funds to which the contractor himself had no claim.[448]

Attempts to enforce liability under performance bonds for failure to meet construction contract specifications may be complicated when they are based on discovery of latent defects in materials or workmanship after a project has been completed and accepted. Some state courts have held that statutory bonds do not cover defects that are known or discoverable by reasonable inspection prior to acceptance. The Florida court initially held that as a matter of law a performance bond surety was not liable for construction defects discovered after the project was certified and accepted as substantially complete and the statute of limitations on the bond had run.[449] Subsequent review of this question, however, has resulted in a holding that acceptance and payment do not necessarily constitute a waiver of rights to claim damages or an estoppel to suit against the surety. Thus, if a contracting agency can prove failure to perform the construction according to the contract, and that it was unaware of this failure at the time the project was accepted, and the defects were not apparent by reasonable inspection, the surety's liability is not as a matter of law ended by the project's acceptance.[450]

Where suits against performance bond sureties because of latent defects are permitted, federal courts have allowed recovery of the costs of redoing the defective workmanship and overpayment of the contractor.[451] Liquidated damages owed by a defaulting contractor were recovered from a performance bond where the

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[444] United States v. Continental Cas. Co., 346 F. Supp. 1239 (N.D. Ill. 1972).

[445] 332 U.S. 234, 67 S. Ct. 1599, 91 L. Ed. 2022 (1947).

[446] Standard Accident Ins. Co. v. United States, 119 Ct. Cl. 749, 97 F. Supp. 829 (1951) (government was permitted to set off damages to a surety's claim under a performance bond); *see also* Gen. Cas. Co. of America v. United States, 131 Ct. Cl. 818, 127 F. Supp. 805 (1955), *cert. denied*, 349 U.S. 938, 75 S. Ct. 783, 99 L. Ed. 1266 (1955).

[447] 259 F.2d 33, 37 (2d Cir. 1958).

[448] United States Fidelity and Guaranty Co. v. Tribourgh Bridge Auth., 297 N.Y. 31, 74 N.E.2d 226 (1947).

[449] Florida Bd. of Regents v. Fidelity & Deposit Co. of Md., 416 So. 2d 30 (Fla. App. 1982); *see also* Sch. Bd. of Volusia County v. Fidelity Co. of Md., 468 So. 2d 431 (Fla. App. 1985) (construing FLA. STAT. § 95.11(2) (1983)).

[450] School Bd. of Pinellas County v. St. Paul Fire & Marine Ins. Co., 449 So. 2d 872 (Fla. App. 1984), *review denied*, 458 So. 2d 274 (Fla. 1984).

[451] City of New Orleans, et al. v. Vicon, Inc., 529 F. Supp. 1234 (E.D. La. 1982) (defective airport runway construction and overpayment due to fixing weight ticket printer to show greater weight than actually received).

language of the contract providing for those damages was specifically incorporated into the bond by reference.[452] Disputes may occur over whether particular types of costs or losses should be regarded as liquidated within the meaning of the contract, and thus may make interpretation of the scope of the bond more difficult. Relying on federal court applications of the Miller Act, recovery from the surety was allowed for damages due to delay in performance, spoilage of stored materials, replacement of inferior fixtures, and losses due to vandalism, but not for "unabsorbed overhead" or disputed supervisory activities by the contractor.[453]

Suits to recover from performance bonds are subject to estoppel by judgment or res judicata. A valid judgment in a previous action between the same parties on the same claim bars another action on the issues raised in that previous suit, and any others that might have been raised at that time. The same result occurs where estoppel by verdict or collateral estoppel prevents the parties from relitigating an issue that was decided in an earlier proceeding between the same parties but on a different cause of action. Such a situation occurred where a claimant supplied materials to a subcontractor on a housing project and sued for a mechanic's lien on the subcontractor's default of payments.[454] This suit was voluntarily dismissed with prejudice, but subsequently, when the local public housing authority took over the unfinished project, the claimant sued to recover from the payment and performance bond. The Illinois court held that on these facts the claimant had a cause of action on the bond. It stated:

> Under the doctrine of estoppel by verdict, a former judgment barred only those questions actually decided in the prior suit—The scope of the bar is narrower than under the doctrine of estoppel by judgment…If there is any uncertainty…that more than one distinct issue of fact is presented to the court, the estoppel will not be applied, for the reason that the court may have decided upon one of the other issues of fact.[455]

Takeover and completion of a construction project by the surety following the contractor's default places the surety in the position of the contractor in relation to the contracting agency, and so entitles it to all the compensation earned by performance of the contract. Thus, where the contracting agency for a highway construction project objected to releasing funds retained to offset damages due to the contractor's default, the Louisiana court held that the agency's takeover agreement with the surety made the latter eligible for the full amount of the contract price once a satisfactory performance was accepted.[456] In this instance, the state and the federal government had provided the construction funds and had claims against the contractor for funds it had diverted, but these were separate matters that could not be set off against the retainage.

Failure of a subcontractor to perform work for which it earlier received partial payment in advance, and replacement of the subcontractor with another, allows the surety on the performance bond to be subrogated to the contractor's rights and remedies. The subrogated surety, however, is also subject to defenses that may arise from the contractor's action. Thus, where a subcontractor performed sporadically and eventually was replaced, the surety sued to recover the advance partial payment and damages for delay of the project. The subcontractor argued that it was excused because the contractor had subsequently been replaced for its default, and the surety had refused to pay further claims against the contractor thereafter. The Michigan court held, however, that the subcontractor's failure to perform was not excused by the contractor's subsequent default or the surety's refusal to pay the costs of modifying the subcontract.[457]

8. Discharge of Surety Obligations

The surety who has furnished a contractor's performance bond or payment bond is discharged upon the successful completion of the contract. However, questions may arise concerning the time and circumstances for termination of the surety's liability. Orderly termination of a suretyship relating to a public construction project typically involves procedures specified in statutes or regulations that must be strictly complied with.

The varying circumstances of construction contracts and contractors' methods may make it difficult to determine precisely when a contractor has completed the "full and faithful performance" and "prompt payment of all claims" that contractors' bonds generally designate as the condition upon which the surety's obligation will be discharged. Accordingly, it is typical for public construction contracts to stipulate that completion will be shown by official acceptance of the work and issuance of a certificate of acceptance by the engineer or other official representative of the contracting agency. Once issued, the overseeing official's acceptance and certificate are conclusive on the parties for all matters within the certificate's scope and the certifying official's authority. In the absence of fraud, arbitrariness, or such gross mistakes as to imply bad faith, the correctness of the

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[452] Pacific Employers Ins. Co. v. City of Berkeley, 158 Cal. App. 3d 145, 204 Cal. Rptr. 387 (1984).

[453] Hartford Accident and Indem. Co. v. Dist. of Columbia, 441 A.2d 969 (D.C. App. 1982).

[454] Decatur Housing Auth. ex rel. Harlan E. Moore Co. v. Christy-Foltz, Inc., 117 Ill. App. 3d 1077, 454 N.E.2d 379 (1983); *but see* Rawick Mfg. Co. v. Talisman, Inc., 706 S.W.2d 194 (Ark. App. 1986) (claim of materialman for turnkey housing project, arising while construction was privately owned and funded, was not divested when project was taken over by public agency).

[455] Decatur Housing Auth., note 454 *supra*, 454 N.E.2d at 383 (emphasis in original; citations omitted).

[456] Reliance Ins. Co. v. Dep't of Transp. and Dev., Office of Highways, 471 So. 2d 248 (La. App. 1985).

[457] Sentry Ins. v. Lardner Elevator Co., 153 Mich. App. 317, 395 N.W.2d 31, 34–35 (1986).

certification may not be disputed and establishes the time of completion of the construction contract.[458]

Aside from the discharge of sureties by this procedure, state laws recognize certain other situations in which the actions of contracting officers may have the effect of releasing a surety from liability on a contractor's bond, even though such a result is not intended. Suretyship doctrine provides that sureties should be protected in their right to rely on the terms of obligations as originally agreed upon. Therefore, any subsequent agreements between the contracting agency (the obligee) and contractor (the principal) that materially alter the surety's obligation without its consent has the effect of releasing the surety from its obligation, if it chooses to exercise this right by giving reasonable notice to the other parties involved in the contract.

Alteration of the surety's obligation occurs when there is a material change in the terms of the underlying contract, or an action by one of the parties that constitutes a material deviation from the contract terms.[459] Most courts determine the materiality of a deviation by considering whether the surety is prejudiced or injured in any way.[460] Some others, however, have linked materiality to the extent that the contract is altered, or that a new agreement is substituted for the old one.[461]

Premature payment of a contractor or subcontractor by the contracting agency provides an illustration of how alteration of surety obligations may occur. Deciding in favor of allowing premature disbursement of progress payments or retainage funds to authorize release of the surety, state courts have held that these actions destroy the security represented by the continued retention of these funds. Thus they have the effect of reducing the contractor's incentive to complete the work to its last detail.[462] Similar results may follow where the surety can show that the time of performance was changed or a different performance was called for, constituting a material change to which the surety did not consent. Thus, where a contractor and subcontractor, without the surety's knowledge or consent, agreed to reduce the time for completing the performance of the subcontract from 80 to 45 days, the surety objected. Noting that the contract contained a provision for liquidated damages of $100 per day for delays, the surety claimed the change in time for performance increased its risk of liability. The court in this case agreed with the surety, and allowed its release.[463]

The same case-by-case scrutiny of the parties' circumstances and the language of the documents concerned typifies the approach to cases where the specifications for the work are changed. For example, a contracting agency may instruct the contractor to use a type of paving material not listed in the contract specifications. If the change does not alter the essential character of the contract, the surety will remain obligated on its bond, even though it has not consented to the change.[464]

Some standard contract forms for public works construction projects provide that the contractor and contracting agency may make changes during the course of the work without releasing the surety. This language raises the question of whether the courts will uphold public agencies in efforts to hold sureties to obligations that are not fully and finally spelled out when the surety executes its bond. Where the agencies have complied with their own procedures for making authorized changes, the courts generally have denied sureties' request for release. In most instances, this result has been based on the surety's consent to changes that must reasonably be expected in the course of construction work.[465] Indeed, the public interest may be served by allowing some latitude for modification of plans that were based on advance estimates of needs and working conditions.

The extent to which contracts may be altered after they have been executed is, however, always subject to scrutiny if the surety feels that the net effect of a change is to substitute a new and different agreement for the one it undertook to guarantee.[466] In such circumstances, the language of the bond becomes the focal point of inquiry.

Release of a surety because of material alteration of its obligation without its consent depends on the surety's own action in asserting and justifying its demand by showing injury. In connection with this latter requirement, disagreement exists over the extent of injury that must be shown, and over the consequences of the occasional case in which it is shown that the alteration actually benefited the surety.[467] From the surety's viewpoint, however, this burden may become a formidable one, as many of the changes that occur in

[458] State Highway Dep't v. MacDougald Constr. Co., 189 Ga. 490, 6 S.E.2d 570, 137 A.L.R. 520 (1939); Sioux City v. Western Asphalt Paving Corp., 223 Ia. 279, 271 N.W. 624, 109 A.L.R. 608 (1937).

[459] Ferguson Contr. Co. v. Charles E. Story Constr. Co., 417 S.W.2d 228 (Ky. Ct. App. 1967); Gruman v. Sam Breedon Constr. Co., 148 So. 2d 759 (Fla. App. 1963).

[460] 74 AM. JUR. 2D *Suretyship* § 208 (2001).

[461] City of Peekskill v. Continental Ins. Co., 999 F. Supp. 584 (S.D. N.Y. 1998) (issuance of new and materially different site plan approval to new developer after expiration of original plan approval, without surety's knowledge and consent, extinguished surety's obligations under bond).

[462] Gibbs v. Hartford Accident & Indem. Co., 62 So. 2d 599 (Fla. 1952).

[463] Bopst v. Columbia Cas. Co., 37 F. Supp. 32 (D. Md. 1940); *but see* Phoenix Assurance Co. of New York v. City of Buckner, 305 F.2d 54 (8th Cir. 1962) (surety was not prejudiced by extension of time, not released).

[464] State for Use of County Court v. R.M. Hudson Paving & Constr. Co., 91 W. Va. 387, 113 S.E. 251 (1922).

[465] Honolulu Roofing Co. v. Felix, 49 Haw. 578, 426 P.2d 298, 314–15 (1967).

[466] Trinity Universal Ins. Co. v. Gould, 258 F.2d 883 (10th Cir. 1958).

[467] Maryland Cas. Co. v. Eagle River Union Free High School Dist., 188 Wis. 520, 205 N.W. 926 (1925); Village of Canton v. Gobe Indem. Co., 201 820, 195 N.Y.S. 445 (1922).

the course of a construction project cannot conveniently be brought to its prior attention or delayed until submitted for its consent.

Although release of the contractor-principal from liability on the construction contract has the effect of also releasing the contractor's surety from further liability on its performance and payment bonds, this result is permitted only where the contractor's release is full and final. If payment of less than the amount demanded is used to satisfy a claim, that payment must be tendered only on condition that it will be accepted in full payment of that claim. Unless the intent of both the tender and acceptance are clearly shown, the payment cannot extinguish the liability of the principal or its surety.[468]

The fact that a contractor-principal has been paid in full by the contracting agency, and has paid its subcontractors in full, is not a defense against liability to the supplier who has not been paid by the subcontractor. This may occur where the subcontractor becomes bankrupt or abandons the project before it pays its creditors in full,[469] or where the subcontractor had several unpaid accounts with the claimant and failed to specify to which account its payment should be applied.[470]

Liability of a contractor may be extinguished where its contract is determined to be illegal, but the illegality must be of a nature as to make the contract void. Thus, where a contract was not submitted to the Attorney General for approval before being awarded, the court held that the contract was not void and the surety was not discharged.[471]

9. Indemnification for Loss or Liability

In some states, statutory bonding requirements specify that contractors must furnish security to save the contracting agency harmless from costs resulting from specified acts or omissions of the contractor or its employees or subcontractors. These contracts are in the nature of indemnification rather than suretyship. Indemnity differs from suretyship in several essential respects. It is likely to be an original undertaking, whereas suretyship is always accessory to another basic agreement between the principal and obligee of the surety bond. Indemnity is a two-party transaction, whereas suretyship is a tripartite agreement. Indemnity contemplates a duty to make good the losses or costs suffered because of the way the contract was performed when default or negligence occurs. An indemnitor becomes liable when efforts to avoid or recoup losses have been unsuccessful. A surety is directly and immediately liable for the performance of the duty it has undertaken.

The distinction between a contract of indemnity and one of surety was made by the California court in *Leatherby Insurance Company v. City of Tustin*.[472] Here the issuer of a performance bond and payment bond for a street widening project paid five claims against the prime contractor and sought to recover from funds withheld by the contracting agency. The agency refused, citing the provisions of the state Department of Public Works' Standard Specifications, incorporated by reference into the city's contract, that the contractor "shall protect and indemnify [the city] against any claims, and that includes the duty to defend…." But the California court concluded that this incorrectly characterized the position of the surety. It said that execution of the performance and payment bonds created two duties, namely: to assure performance of the contract according to specifications, to the point of stepping into the contractor's place to complete the work if necessary, and to see that all laborers and materialmen were paid if the contractor failed to pay them. These were duties to the contracting agency and to the laborers and materialmen, not to the contractor, and were limited in their extent by the amount of the bond. The language of the state's standard specifications was interpreted as the basis for the requirement that the contractor provide a surety bond to see that the laborers and materialmen were paid.

Where defective workmanship or materials are due to negligence and result in loss to a public agency through tort damages, the agency generally has no chance of being indemnified for those damages by the negligent contractor's performance bond. In Texas, liability on statutory performance bonds was held not to extend to indemnification for tort damages, and would be allowed only where the language of the bond or other agreement was sufficient to turn the statutory bond into a common law bond.[473] In the absence of such language, the Texas court ruled that the bond was entirely a statutory creation for the purpose of assuring the contracting agency that the construction would be done according to plans, specifications, and contract documents, and liability under it was limited to the statute's scope and purpose. A similar restrictive interpretation of the surety's liability applies to one who is not a party to the bond. Where the owner of land adjacent to the site of a water system project filed suit because construction operations caused flooding and loss of business when access was blocked, the court denied the claimant's right to sue, explaining that to allow tort

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[468] Envirex, Inc. v. Cecil M. Garrow Constr., Inc., 473 N.Y.S.2d 63, 99 A.D. 2d 307 (1984).

[469] D.W. Clark Road Equip., Inc. v. Murray Walter, Inc., 469 A.2d 1326 (N.H. 1983); *see also* Naylor Pipe Co. v. Murray Walter, Inc., 421 A.2d 1012 (N.H. 1980); City of Chicago ex rel. Charles Equipment Co. v. U.S. Fidelity & Guar. Co., 142 Ill. App. 3d 621, 491 N.E.2d 1269 (1986).

[470] Trans-American Steel Corp. v. J. Rich Steers, Inc., 670 F.2d 558 (5th Cir. 1982); Sumlin v. Hagan Storm Fence Co., 409 So. 2d 818 (Ala. 1982).

[471] State v. Am. Motorists, Inc. Co., 463 N.E.2d 1142, 1148 (Ind. App. 1984) (statute requiring attorney general's signature on contracts was enacted to protect public funds, therefore could not be invoked by surety to avoid paying under performance bond).

[472] 76 Cal. App. 3d 678, 143 Cal. Rptr. 153 (1977).

[473] City of Marshall v. American General Ins. Co., 623 S.W.2d 445 (Tex. App. 1981) (construing TEX. REV. CIV. STAT. ANN. art. 5160, sub'd. A(a)).

claims to share in the bond might reduce to nothing its ability to perform its function.[474]

In most states, sovereign immunity no longer shields public agencies and officials from suit, particularly with regard to negligence claims. Most states have methods by which claimants can obtain adjudication of claims arising out of public construction work. Accordingly, expansion of the contractor's bond obligation to include indemnification of the contracting agency for damages that it may have to pay because of the contractor's negligence is one way to protect the public.

The same objective is achieved by requiring contractors to carry insurance against various types of third party liability. Requirements concerning insurance coverage of the principal parties involved in a public works construction project are customarily set out in the contract specifications. Typically such an insurance package is comprehensive, including workmen's compensation insurance, public liability for personal injury and property damage, and various special coverages suggested by the type of construction involved. A contractor's failure to provide the required insurance may entitle the owner to common law indemnification.[475]

Beyond the threshold question of why provisions for indemnification are desirable in contractor's bonds, others arise concerning the scope of the obligation required by the statutes. In the language of indemnification law, guaranty against "damage" differs significantly from guaranty against "liability." In the case of the former, the obligation to indemnify cannot be enforced until and unless actual damage is shown to have been sustained by the indemnitee. In the latter case the obligation is enforceable as soon as the indemnitee's legal liability is established.

Enforcement of statutory requirements for indemnification of public works agencies may involve questions of whether enforcement is barred because of the presence of negligence on the part of the indemnitee. Courts have tended to deny the enforceability of indemnity bonds where the indemnitee's own negligence is a factor.[476] Some courts have indicated that active negligence is not necessary, but that an indemnitee may be barred from enforcing an indemnity bond where it merely acquiesced in allowing a dangerous condition on a work site to persist for an unreasonably long period of time, during which a third party suffered injury.[477] In Mississippi, the impropriety of enforcing indemnification for the benefit of one whose own negligence was a cause of its loss is recognized in legislation declaring such agreements contrary to public policy.[478]

The nature of transportation facilities and construction create other factual situations regarding the effects of negligence by employees of subcontractors, materialmen, or other third parties. Contractors view these situations as risks over which they generally have little practical control. Clauses for "holding harmless" are viewed as far too general to enable contractors to measure their risks precisely, or to obtain insurance that fully covers their potential liability. Competitive bidding is likely to reflect errors on the side of overinsurance and indemnity bonding as contractors seek to protect themselves against these risks.

Although not as specific in its reference to the contractor's bond, a Wisconsin statute raises the question of whether suit could be brought under a contractor's performance or payment bond for wrongful application of funds. This statute recites that

> All moneys, bonds or warrants paid or become due to any prime contractor or subcontractor for public improvements are a trust fund only in the hands of the prime contractor or subcontractor and shall not be a trust fund in the hands of any other person. The use of the moneys by the prime contractor or subcontractor for any purpose other than the payment of claims on such public improvement, before the claims have been satisfied, constitutes theft…and is punishable under Section 943.20. This section shall not create a civil cause of action against any person other than the prime contractor or subcontractor to whom such moneys are paid or become due. Until all claims are paid in full, have matured by notice and filing or have expired, such money, bonds and warrants shall not be subject to garnishment, execution, levy or attachment. [479]

Although liability on a subcontractor's bond may be, and usually is, limited by the language of the bond to payment of claims that comply with statutory notice requirements, these requirements can be waived. Thus, where a subcontractor by separate agreement undertook to protect, indemnify, and save the general contractor from "all claims, suits and actions of any kind and description," and the contractor paid several of the subcontractor's unpaid creditors, it was held that the more restrictive liability provided for in the language of the bond was waived.[480]

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[474] Long v. City of Midway, 169 Ga. App. 72, 311 S.E.2d 508 (1983) (construing GA. CODE ANN. § 36-82-104).

[475] Isnardi v. Genovese Drug Stores, Inc., 662 N.Y.S.2d 790, 791, 242 A.D. 2d 672 (1997).

[476] This seems particularly true where the language of the indemnity agreement is broad in describing the obligation. *See, e.g.,* Arnold v. Stupp Corp., 205 So. 2d 797 (La. Ct. App. 1967), *petition for cert. not considered*, 251 La. 936, 207 So. 2d 540 (1968); Kansas City Power & Light Co. v. Federal Constr. Corp., 351 S.W.2d 741 (Mo. 1961); Southern Pacific Co. v. Layman, 173 Ore. 275, 145 P.2d 295 (1944); Kroger Co. v. Giem, 215 Tenn. 459, 387 S.W.2d 620 (1964).

[477] Whirlpool Corp. v. Morse, 222 F. Supp. 645 (D. Minn. 1963).

[478] MISS. CODE § 31-5-41 (2003).

[479] WIS. STAT. § 779.16 (2001).

[480] Miner-Dederick Constr. Co. v. Mid-City Rental Services, Inc., 603 S.W.2d 193 (Tex. 1980).

SECTION 3

BIDDER MISTAKES AND REMEDIES

A. BID MISTAKES

1. Bid Irregularities

A public contract cannot be awarded on terms that vary from those contained in the invitation for bids.[1] A bid must conform in all material respects to the invitation for bids; a bidder cannot be allowed after bid opening to supply an essential element that was missing from its bid.[2] However, not every irregularity in a bid requires rejection of the bid. In order for rejection to be required, a variation from the bid specifications or instructions must be of a type that essentially destroys the competitive nature of bidding. The variation must be substantial, and in order to be substantial, it must affect the amount of the bid and give the bidder an advantage or benefit not allowed other bidders.[3] In order to be waived by the contracting agency, a deviation from the specifications or instructions must be inconsequential; in other words, it must not provide that bidder with an advantage over other bidders, and must not otherwise defeat the goals of public contracting in insuring proper use of public funds and avoidance of corruption.[4] Generally, the test applied is to determine whether waiver of the irregularity would deprive the agency of its assurance that the contract will be entered into, performed, and guaranteed according to the specifications, and whether the irregularity is such that it undermines competitive bidding by giving one bidder an advantage over others.[5]

a. Major vs. Minor Irregularities

A material defect in the bid is one that would allow the bidder to avoid the binding nature of its bid without forfeiting its bid bond, and it cannot be waived.[6] The distinction between waivable and nonwaivable bidding requirements sometimes may be spelled out in the language of applicable statutes. For example, Louisiana's Public Bid Law specifically states that the requirements of the statute, requirements in the advertisement for bids, and substantive requirements stated on the bid form may not be considered informalities and may not be waived by the agency.[7] Nonwaivable statutory requirements may be as detailed as inclusion of the bidder's certificate of responsibility number on the outside of its bid envelope.[8] But frequently, the distinction between waivable and nonwaivable deviations must be discerned through a careful evaluation of the actual impact of the irregularity.[9]

b. Incomplete, Non-Responsive, or Irregular Bids

Frequently bids are prepared under circumstances that increase the chance of innocent error. It is common for bidders to wait as long as possible before the filing deadline to complete their bids, for by so doing they may be able to take advantage of late price changes for materials.[10] In other instances, this longer time also may be used beneficially to analyze the project specifications and verify the technical data upon which the contracting agency has based its estimates. Preparation and submission of bids under pressure increases the danger of many types of error. Typical of the irregularities that may have to be evaluated by contracting agencies are the following:

- Bid is not signed or is not dated.[11]
- Bid does not include corporate resolution authorizing representative to sign bid.[12]
- Bid does not disclose bidder's stockholders where

[1] Portions of this section are derived from *Competitive Bidding and Award of Highway Construction Contracts* by Dr. Ross D. Netherton, published by the Transportation Research Board in 1976 and included in the first edition of SELECTED STUDIES IN HIGHWAY LAW.

[2] Sevell's Auto Body Co. v. N.J. Highway Auth., 306 N.J. Super. 357, 703 A.2d 948, 951 (A.D. 1997); L. Pucillo & Sons, Inc. v. Township of Belleville, 249 N.J. Super. 536, 592 A.2d 1218, 1224, *certification denied*, 127 N.J. 551, 606 A.2d 364 (1991) (citing Palomar Constr., Inc. v. Township of Pennsauken, 196 N.J. Super. 241, 482 A.2d 174 (A.D. 1983)).

[3] Wilson Bennett, Inc. v. Greater Cleveland Regional Transit Auth., 925, 67 Ohio App. 3d 812, 588 N.E.2d 920, *jurisdictional motion allowed*, 53 Ohio St. 3d 717, 560 N.E.2d 778, *cause dismissed*, 57 Ohio St. 3d 721, 568 N.E.2d 1231 (1990).

[4] Ghilotti Constr. Co. v. City of Richmond, 53 Cal. Rptr. 2d 389, 390, 45 C.A. 4th 897, *review denied* (1996); *see also* AMERICAN BAR ASSOCIATION, MODEL PROCUREMENT CODE FOR STATE AND LOCAL GOVERNMENTS § 3-202(6) (2000).

[5] United States v. Joint Meeting of Essex & Union Counties, 997 F. Supp. 593, 600 (D. N.J. 1998); Matter of Protest of Award of On-Line Games Production and Operation Services Contract, Bid No. 95-X-20175, 279 N.J. Super. 566, 653 A.2d 1145, 1160 (1995) (both citing Meadowbrook Carting Co. v. Borough of Island Heights, 138 N.J. 307, 650 A.2d 748 (1994)).

[6] Spawglass Constr. Corp. v. City of Houston, 974 S.W.2d 876, 885 (Tex. App. 1998).

[7] Boh Bros. Constr. Co., L.L.C. v. Department of Transp. and Dev., 698 So. 2d 675, 678 (La. App. 1 Cir. 1997); La. R.S. § 38:2212 subd. A(1)(b). However, the agency may still waive deviations that are not substantive in nature. *Id*.

[8] City of Durant v. Laws Constr. Co., 721 So. 2d 598, 602 (Miss. 1998).

[9] A.A.B. Elec., Inc. v. Stevenson Public School Dist., 5 Wash. App. 887, 491 P.2d 684, 686–87 (1971).

[10] *See* City of Atlanta v. J.A. Jones Constr. Co., 370, 260 Ga. 658, 398 S.E.2d 369, 370, *on remand*, 198 Ga. App. 345, 402 S.E.2d 554, *cert. denied*, 111 S. Ct. 2042 (1990).

[11] *See, e.g.,* A.A.B. Elec., Inc. v. Stevenson Public School Dist., 5 Wash. App. 887, 491 P.2d 684, 686 (1971) (bid was rejected because it was unsigned, bidder could have accepted or rejected the award in retrospect, which gave that bidder an advantage over other bidders).

[12] George W. Kennedy Constr. Co. v. City of Chicago, 135 Ill. App. 3d, 306, 481 N.E.2d 913, 916 (1985) (corporation secretary's signature was not sufficient to bind bidder where the bid did not include a certified copy of the corporate by-laws or other authorization for secretary to bind corporation).

required by statute.[13]

• Bid papers do not acknowledge the bidder's receipt of changes in plans, additions to specifications, or other addenda.[14]

• Bidder does not include lists of current equipment, a description of previous experience, or an updated financial statement.[15]

• Bidder fails to list subcontractors as required by statute or the invitation for bids.[16]

• Arithmetical errors occur in estimating materials or extending unit prices to derive total prices.[17]

• Bid papers are not submitted on the right forms or in the required number of copies.[18]

• Prices submitted are for an alternate item in lieu of an item specified.[19]

• Prices are not given for an alternative called for in the invitation for bids.[20]

• Bidder does not include its plan of operation with the bid, including completion date.[21]

• Bidder has failed to attend the pre-bid meeting.[22]

• Cost item is omitted.[23]

• Bidder fails to include affirmative action plan.[24]

In addition, the AASHTO Guide Specifications contract provisions[25] also consider the proposal irregular or non-responsive if:

• The proposal is incomplete, indefinite or ambiguous because it contains unauthorized additional, conditional or alternate bids or other irregularities.

• The proposal fails to furnish a properly executed guaranty (bid bond or equivalent).

• The proposal includes added provisions that reserve the bidder's right to accept or reject a contract award.

• There is evidence of collusion among bidders.

• The proposal is materially unbalanced.

• The bidder firm and an affiliated corporation submit more than one bid or proposal for the same contract.

Consistent with the rule that there must be strict adherence to formal specifications and procedures in the submission, opening, and acceptance of bids, courts have upheld the rejection of bids that are irregular when submitted.[26] On the other hand, where an irregu-

[13] George Harms Constr. v. Borough of Lincoln Park, 161 N.J. Super. 367, 391 A.2d 960, 965–66 (1978).

[14] George & Benjamin General Contractors v. Virgin Island Dep't of Property and Procurement, 921 F. Supp. 304, 309 (D. V.I. 1996) (failure to acknowledge receipt of addendum may be waived as minor informality if the bid clearly indicates that the bidder received the amendment, such as when the addendum adds an item of work and the bidder has included a bid for that item).

[15] J.H. Parker Constr. Co. v. Board of Aldermen, City of Natchez, 721 So. 2d 671, 677 (Miss. App. 1998) (city had discretion to waive prequalification statement where bidder from response); TEC Electric, Inc. v. Franklin Lakes Board of Educ., 284 NJ. Super. 480, 665 A.2d 803, 806 (1995) (omitted prequalification statement was waivable as an immaterial defect and it was an abuse of discretion to deny the waiver; statement that was omitted would have duplicated what had already been submitted with respect to assurances regarding financial responsibility, plant, and equipment, and there was no evidence of advantage to the bidder); Gunderson v. University of Alaska, Fairbanks, 922 P.2d 229, 235 (Alaska 1996) (permitting use of different hauling equipment from that specified in request for proposals was harmless); Peninsula Correctional Health Care v. Department of Corrections, 924 P.2d 425, 428 (Alaska (1996)) (submission of resumes of employees as representative sample of who would be working on project, and not as commitment that those employees would be assigned to project, did not render bid nonresponsive); Arakaki v. State of Haw., 87 Haw. 147, 952 P.2d 1210, 1214 (1998) (it was error for agency to reject all bids and determine that low bidder was nonresponsive on the grounds that the low bidder had requested permission to supplement its bid with its qualification and experience list). *But see* City of Durant v. Laws Constr. Co., 721 So. 2d 598, 602 (Miss. 1998) (bidder's failure to include statutorily required certificate of responsibility number on outside of bid envelope is nonwaivable deviation).

[16] Ray Bell Constr. Co. v. School District of Greenville County, 331 S.C. 19, 501 S.E.2d 725, 729–30 (1998) (bid was nonresponsive as listing alternative subcontractors was contrary to subcontractor listing law requirements; alternatives gave bidder opportunity to choose among listed subcontractors, which was an advantage not enjoyed by other bidders).

[17] *See, e.g.,* Department of Transp. v. Ronlee, Inc., 518 So. 2d 1326, 1328 *review denied*, 528 So. 2d 1183 (Fla. App. 3 Dist. 1987).

[18] George & Benjamin General Contractors v. Virgin Islands Dep't of Property and Procurement, 921 F. Supp. 304, 309 (D. V.I. 1996); *see also* Sedor v. West Mifflin Area School District, 713 A.2d 1222, 1225 (Pa. Commw. 1998) (laches may apply to action to enjoin an award to a bidder who used wrong bid form).

[19] Bodies by Lembo v. Middlesex County, 286, N.J. Super 298, 669 A.2d 254, 256 (A.D. 1996); *see also* Southern Foods Group, L.P. v. State, Dep't of Educ., 974 P.2d 1033, 1042, 89 Haw. 443 (1999) (alternate bids submitted where they were not called for, in violation of bidding regulations, was properly rejected as nonresponsive).

[20] Hall Constr. Co. v. N.J. Sports Auth., 295 N.J. Super. 629, 685 A.2d 983, 988 (A.D. 1996) (failure to submit bid on alternate renders bid nonconforming).

[21] Kokosing Constr. Co. v. Dixon, 72 Ohio App. 3d 320, 594 N.E.2d 675, 680 (1991).

[22] Scharff Bros. Contractors, Inc. v. Jefferson Parish Sch. Bd., 641 So. 2d 642, 644, *reconsideration denied*, 644 So. 2d 398 (La. App. 5 Cir. 1994).

[23] Matter of Protest of Award of On-Line Games Production and Operation Services Contract, Bid No. 95-X-20175, 279 N.J. Super. 566, 653 A.2d 1145, 1163–64 (1995).

[24] Kokosing Constr. Co. v. Dixon, 72 Ohio App. 3d 320, 594 N.E.2d 675, 680 (1991). However, the bidder's failure to include a signature on the affirmative action plan was not a material deviation. *Id.* 594 N.E.2d at 680.

[25] AASHTO Guide Specification, Division 100, Section 102.07, at pp. 12-13; see also Section 1 *supra*.

[26] Ardmare Constr. Co. v. Freedman, 191 Conn. 497, 467 A.2d 674, 676 (1983) (use of rubber stamp rather than hand-

larity is determined to be minor and has no adverse effect on the competition among bidders, contracting agencies have been upheld in their waiver of the defect.[27]

The Ohio Revised Code can provide useful guidance. It provides that a contract will be considered responsive if the proposal responds to the bid specifications in all material respects and contains no irregularities or deviations that would affect the amount of the bid or otherwise give the bidder a competitive advantage.[28]

Materiality of a particular specification is a question of law.[29] Whether irregularities in bidding and acceptance may be waived by the contracting agency generally has been determined by consideration of their practical effect on the basic purpose of the competitive bidding system. Thus, the question of waiving a bidder's failure to file certain forms with the bid is evaluated in terms of the risk that an unfair advantage may be granted by allowing this oversight to be corrected after bid opening.[30] Under an Ohio decision, a letter clarifying the bid that was received after the bid opening was found to be a deviation from the bid specifications, destroying the competitive nature of the bidding process.[31] By contrast, the bidder's omission of a two-page specification sheet was found to be insubstantial and did not affect the bid process or give the bidder a competitive advantage over the other bidders.[32] Similarly, waiver of oversights in the formalities of opening bids requires consideration of whether the action will result in giving any bidder an advantage that the others do not have,[33] or provide the bidder a competitive advantage as set forth in the Ohio Revised Code.

Determination of when a bid is accepted must be made by reference to the contracting agency's rules of procedure. Where bids for a construction contract were the subject of several motions at the same meeting of the agency's governing body, it was held that the last action in the continuous session of the commission's meeting was controlling, and earlier motions to accept a particular bid did not give rise to a bidding contract at that time and by that act.[34] Also, where a contracting agency's rules of procedure require that acceptance is not completed until the bidder is formally notified, the time of notification is controlling, even though the successful bidder was represented at the county commission meeting at which the contract was awarded.[35]

Among the consequences of acceptance of a bid is the general rule that the bidder may not thereafter make changes in the list of subcontractors that it has submitted without the approval of the contracting agency.[36] Some states have specific legislation to discourage bid shopping or bid peddling in connection with construction contract awards.[37] This promotes the dual purposes of maintaining fairness in dealings between prime and subcontractors as well as protecting public works projects from excessive costs.[38] However, where a bid statute does not require listing of subcontractors and the invitation for bids does not have such a requirement,

written signature on bid); Colombo Constr. Co. v. Panama Union Sch. Dist., 136 Cal. App. 3d 868, 186 Cal. Rptr. 463, 466 (1982) (bidder who made a mistake in original bid is prohibited from further bidding on same project); E.M. Watkins & Co. v. Board of Regents, 414 So. 2d 583, 587 (Fla. App. 1982) (failure to list subcontractors in bid); Gibbs Constr. Co. v. Board of Supervisors, La. State Univ., 447 So. 2d 90, 92 (La. App. 1984) (failure of bidder to attend pre-bid conference); Williams v. Board of Supervisors, La. State Univ. and Agricultural and Mechanical College, 388 So. 2d 438, 441 (La. App. 1980) (failure to describe equipment according to instructions); Grace Constr. Co. v. St. Charles Parish, 467 So. 2d 1371 (Fla. App. 1985); George W. Kennedy Constr. Co. v. City of Chicago, 135 Ill. App. 3d 306, 481 N.E.2d 913, 916 (1985) (omission of bidder's president's signature on corporate signature and acceptance pages); Matter of Bayonne Park, Lincoln Park and James J. Braddock-North Hudson Park Bikeway System, Hudson County, 168 N.J. Super. 33, 401 A.2d 705, 709 (1979) (successful low bidder delayed return of executed contract beyond period permitted in bid instructions).

[27] *See, e.g.*, Lovisa Constr. Co. v. N.Y. State Dep't of Transp., 435 N.Y.S.2d 123 (1980) (low bidder did not list mobilization costs separately for particular facilities, but inserted one gross figure for all mobilization costs).

[28] OHIO REV. CODE 9.212.

[29] George Harms Constr. v. Borough of Lincoln Park, 161 N.J. Super. 367, 391 A.2d 960, 965 (1978).

[30] Excavation Constr., Inc. v. Ritchie, 230 S.E.2d 822, 825 (W. Va. 1976) (refusal to waive failure to file a "free competition affidavit" with original bid papers was not abuse of discretion).

[31] Rein Constr. Co. v. Trumbull County Bd. of Commr's, 138 Ohio App. 3d 622, 741 N.E.2d 979 (2000).

[32] Lewis & Michael, Inc. v. Ohio Dep't of Admin. Servs., 103 Ohio Misc. 2d 29, 724 N.E.2d 885 (1999).

[33] Butler v. Federal Way School Dist. No. 210, 17 Wash. App. 288, 562 P.2d 271, 276 (1977) (contracting agency mislaid bid and did not open it until 15 minutes after others were opened in the presence of other bidders, irregularity could be waived); Farmer Constr., Ltd. v. State Dep't of Gen. Admin., 98 Wash. 2d 600, 656 P.2d 1086 (1983) (omission of signature on bid form was not material where bid bond was signed and bid bond and proposal referred to each other and were connected by internal reference; bidder would be bound by bid and lack of signature on cover page was not an advantage).

[34] Berry v. Okaloosa County, 334 So. 2d 349, 350 (Fla. App. 1976).

[35] *Id*. at 351.

[36] *But see* McCandlish Elec., Inc. v. Will Constr. Co., 107 Wash. App. 85, 25 P.3d 1057 (2001) (subcontractor listing statute did not provide listed subcontractor with cause of action when prime contractor substituted another subcontractor; subcontractor's remedy was to try to enjoin award and execution of contract).

[37] CAL. PUB. CONT. CODE § 4101 *et seq*. (1999).

[38] *See* Bay Cities Paving & Grading, Inc. v. Hensel Phelps Constr. Co., 128 Cal. Rptr. 632, 634, 56 C.A. 3d 361 (1976) ("Bid shopping is the use of the lowest bid already received by the general or prime contractor to pressure other subcontractors into submitting even lower bids; bid shopping is prohibited by the statute after the award of the prime contract.").

then a bidder's failure to do so may be waived.[39] This is particularly so where the court has determined that the subcontractor listing would not have prevented bidders from bid shopping.[40] However, where a statute requires listing of subcontractors, the bidder's failure to do so is a nonwaivable deviation, even if the invitation for bids is silent on that requirement.[41]

An agency may require subcontractor listing in its invitation for bids where it is not necessarily required by statute, or may set out more detailed requirements than are required by statute. In such a case, the bidder's failure to comply with the more stringent requirements may be grounds for determining that the bid is nonresponsive. A California court in *MCM Construction v. City and County of San Francisco* held that the City acted within its discretion when it rejected the low bid as nonresponsive for not complying with its requirement that it provide the subcontract price of all of its listed subcontractors, even though this requirement went beyond the requirements of California's subcontractor listing statute.[42]

In addition to not being able to change the individual subcontractors or prices listed, a bidder also cannot change the subcontractor percentages in its bid after bid opening. Where the specifications permitted only 50 percent of the work to be subcontracted and the bidder proposed to subcontract over 80 percent, the higher amount could not be waived, nor could the bidder alter the percentages.[43] Many of these irregularities cannot adversely affect the competitive bidding process. Others, such as failure to submit a plan of operation or an updated financial statement, might affect a contract award.

In practice, the character and consequences of a bid's variance influence the disposition of the bid. Where the variances are minor, and the bid conforms substantially to the specifications, courts have held that acceptance of the bid as originally submitted does not destroy the competitive character of the bidding. Rejection appears to be required only where the bid variance would create a substantial difference between the terms of the bid and the announced specifications of the project, and would give that bidder an advantage not enjoyed by other bidders.

Difficulties arise in practical application of the rule to individual cases, since variances may result from a wide range of fact situations. The reported cases have concerned all major types of specifications—quantity, quality, and condition of materials; schedules for work and deliveries; geometric and structural design; organization of work; and numerous special provisions.[44] They have also disclosed a wide variety of language used in both bids and specifications. The courts have approached these cases with a pragmatic objective of preventing situations in which any bidder is allowed to bid in a way that gives its proposal an advantage that is not also enjoyed by the other bidders. The impact on bid prices is, therefore, the pivotal point in distinguishing allowable and prohibited variances. Those that have a minimal effect or no effect on price may be permitted to remain in the competition for the contract award. It is not important to the rule that the variant bid might provide an additional benefit to the contracting agency. If it contemplates a material change, and thus departs from the basis on which the other bids are evaluated, the variance must be rejected.

c. Unsigned Bids

Normally, the lack of a signature is a material defect that cannot be waived. In the absence of a signature of a person that can bind the bidder to its bid, the bidder is free to refuse to execute the contract without forfeiting its bid bond should it decide that it is in its interest to do so.[45] This is an advantage not enjoyed by other bidders, and so constitutes a material and substantial deviation. However, where the cover page was not signed but the addendum was signed, the court held that the lack of a signature on the cover page was not a material and substantial deviation, as the signature on the addendum was sufficient to bind the bidder.[46]

Likewise, where there was a signature in three other places in the bid, including the bid bond, the lack of a signature on the cover page was waivable; the bid and bid bond could be treated as one signed instrument.[47] However, whether a signature on the bid bond is enough to bind the bidder to its bid must be determined with reference to the documents. Where the bid bond and the bid are internally connected and make references to one another, they may be held to be one document. In such a case, the signature on the bid bond will

[39] Williams Bros. Constr. v. Public Bldg Comm'n of Kane County, 243 Ill. App. 3d 949, 612 N.E.2d 890, 895, *appeal denied*, 152 Ill. 2d 582, 622 N.E.2d 1229 (1993).

[40] *Id*. at 897.

[41] Gaglioti Contracting, Inc. v. City of Hoboken, 307, N.J. Super. 421, 704 A.2d 1301 (1997).

[42] 78 Cal. Rptr. 2d 44, 51, 66 Cal. App. 4th 359 (Cal. App. 1998).

[43] Valley Crest Landscape, Inc. v. City Council of City of Davis, 49 Cal. Rptr. 2d 184, 190, 41 C.A. 4th 1432 (1996) (the agency cannot permit changes in subcontractor percentages after bid opening; specifications permitted only 50 percent of the work to be subcontracted, and a higher percentage could not be waived).

[44] Annotation, 65 A.L.R. 835 (1930); Annotation, 69 A.L.R. 697 (1930); Annotation, 114 A.L.R. 1437 (1938).

[45] A.A.B. Elec., Inc. v. Stevenson Pub. Sch. Dist., 5 Wash. App. 887, 491 P.2d 684, 686 (1971) (bid was rejected because it was unsigned, bidder could have accepted or rejected the award in retrospect, which gave that bidder an advantage over other bidders).

[46] Leaseway Distribution Centers, Inc. v. Department of Admin. Services, 49 Ohio App. 3d 99, 550 N.E.2d 955, 960–61 (1988) (addendum is part of bid package to which bidder is bound).

[47] Spawglass Constr. Corp. v. City of Houston, 974 S.W.2d 876, 885 (Tex. App. 1998) (bid was signed in three other places including bid bond; bid and bond were connected by internal references and could be treated as one signed instrument).

bind the bidder, even if the signature on the cover page of the bid is lacking.[48] However, if they are not so connected as to make the bid bond part of the bid and thus part of the offer itself, then the signature on the bid bond alone may be insufficient.[49]

Another material defect occurs when the bid does not include a corporate resolution authorizing a representative to sign the bid.[50] As in the case of a missing signature, the bidder would have the opportunity to refuse to execute the contract by claiming that the signer did not have authority to bind the corporation. This is considered a material and substantial deviation that cannot be waived by the contracting agency.

d. Late Bids

Whether an agency must reject a late bid or may waive the lateness as an informality depends on the degree of discretion given the agency in its bidding statutes.[51] Most states require that a late-submitted bid must be rejected.

The Virginia Supreme Court in *Holly's, Inc. v. County of Greensville* held that the second lowest bidder was entitled to reversal of the award of the contract to a lower bidder whose bid had not been timely submitted.[52] The court stated that the requirement in the invitation for bids fixing the time for submission of bids was one that had to be strictly complied with, and noncompliance was not a minor defect or informality that may be waived. Rather, it was a material and formal requirement to be complied with. The court in *City of Atlanta v. J.A. Jones* discussed the reason for adhering strictly to the time set for submission of bids, noting that a contractor may adjust its prices up until the last minute that the bid is submitted. Therefore, even a 3-minute delay in submission of a bid was considered to be an unfair advantage not enjoyed by other bidders.[53]

However, not all states take such a strict position regarding timeliness of bids. For example, the Wisconsin Court of Appeals held that a city had discretion to accept a late bid, where the statute under which it advertised for bids did not preclude the opening of a late-submitted bid.[54]

A bid officer's declaration of the time at bid opening is presumed to be correct unless the protester shows clearly that the time was inaccurate.[55] In *Washington Mechanical Contractors v. Department of the Navy*, a federal district court found that where the agency itself had shown that its bid clock was fast, it was not error to accept a late bid as timely when it was timely when the adjustment was made for the fast clock. The protester who would have been the low bidder otherwise could not show that the Navy was wrong in determining that its clock was fast.[56]

A more unusual situation is the one in which the bidder delivers the bid to the right place at the right time, but through some oversight of the agency staff it is not "received" on time. Two courts reached different results in this situation. In *Statewide Roofing v. Eastern Suffolk Board of Cooperative Educational Services,* [57] the parcel delivery service had delivered the bidder's bid prior to the deadline for submission, but had placed it on the administrator's desk rather than delivering it to the room in which bid opening would occur, and the package was not discovered until after all other bids had been opened and announced. The agency subsequently opened the bid in the presence of others; the agency had confirmed that it had arrived prior to the deadline, which precluded any inference of dishonesty, favoritism, or fraud. The New York court held that it was not error for the agency to award the contract to that bidder, who was the lowest responsible bidder.[58] There had been no benefit to the bidder, and it remained on the same footing as the other bidders. However, in another case in which the bid was delivered to the correct place but was not "received" by the contracting officer in time for bid opening, the court held that the bid was properly rejected as untimely.[59]

e. Balanced and Unbalanced Bids

Where project advertisements specify that bids must be expressed in unit prices, contracting agencies must be prepared to deal with unbalanced bids. The distinction between balanced and unbalanced bids lies in the extent to which the unit price assigned to each bid item realistically reflects the item's share of the total cost or work. A balanced bid for a particular cost item carries its full and correct share of the total price. An unbalanced bid does not, so that some items are overpriced and others are low or only nominally priced.[60] Thus,

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[48] Farmer Constr., Ltd. v. State Dep't of Gen. Admin., 98 Wash. 2d 600, 656 P.2d 1086 (1983) (omission of signature on bid form was not material where bid bond was signed and bid bond and proposal referred to each other and were connected by internal reference; bidder would be bound by bid and lack of signature on cover page was not an advantage).

[49] A.A.B. Elec., Inc. v. Stevenson Public School Dist., 5 Wash. App. 887, 491 P.2d 684, 686–87 (1971) (bid bond was not part of bid, but rather was condition precedent to acceptance of offer).

[50] George W. Kennedy Constr. Co. v. City of Chicago, 135 Ill. App. 3d 306, 481 N.E.2d 913, 916 (1985).

[51] *See* B. Waagner and E. Evans, *Agency Discretion in Bid Timeliness Protests: The Case for Consistency*, 29 PUB. CONT. L.J. 713, 724–37 (2000).

[52] 250 Va. 12, 458 S.E.2d 454, 458 (1995).

[53] *See, e.g.,* City of Atlanta v. J.A. Jones Constr. Co., 260 Ga. 658, 398 S.E.2d 369, 370 *on remand*, 198 Ga. App. 345, 402 S.E.2d 554, *cert. denied*, 111 S. Ct. 2042, 500 U.S. 928 (1990).

[54] Power Systems Analysis v. City of Bloomer, 197 Wis. 2d 817, 541 N.W.2d 214, 216 (Wis. App. 1995).

[55] Washington Mechanical Contractors, Inc. v. United States Dep't of the Navy, 612 F. Supp. 1243 (S.D. Cal. 1984).

[56] *Id*.

[57] 661 N.Y.S.2d 922, 173 Misc. 2d 511 (N.Y. Supp. 1997).

[58] *See also* Butler, *supra* note33.

[59] Holly's, Inc. v. County of Greensville, 250 Va. 12, 458 S.E.2d 454, 457 (1995).

[60] Turner Constr. Co. v. N.J. Transit Corp., 296 N.J. Super. 530, 687 A.2d 323, 327 (1997).

without changing the total price, a contractor may arrange the unit prices for the specifications of a project so as to achieve unusually favorable, and sometimes unintended, results.

The attractiveness of unbalanced bidding in certain situations is easy to understand. A contractor who needs to build up or recoup working capital as soon as possible may unbalance a bid by setting high prices on items of work performed early in the project. In this way the contractor can ease the financial strain incurred in mobilizing the construction plant and equipment, purchasing materials, and the general costs of starting up the project. These are all expenses that the contractor otherwise could not expect to liquidate until the work progressed over a substantial period of time. There is, however, a risk to the public if this practice is abused. An unscrupulous or unqualified bidder may unbalance a bid in a way that results in excessively high payments early in the work, only to default and leave the surety or the contracting agency to finish the project and pay for those items that were underestimated in the bid.

Federal regulations and ASSHTO Guide specifications divide unbalanced bidding into two categories: materially unbalanced and mathematically unbalanced. They define a materially unbalanced bid as a bid which generates reasonable doubt that the award will result in the lowest ultimate cost to the government. They further define a mathematically unbalanced bid as one containing lump sum or unit bid items which do not reflect the reasonable actual costs plus a reasonable share of the bidder's anticipated profit, overhead and other indirect costs.[61]

Federal regulations also require an examination of all unit prices to determine conformance with the engineers' estimate.[62] Part of this bid analysis may include a review of unbalanced bid items. In order to detect a mathematically unbalanced bid, an analysis of the item and the engineers' estimate and other bid prices should be conducted. Although the bid is mathematically unbalanced, it still may be acceptable depending on the degree of and reasons for the unbalancing. The determination of a materially unbalanced bid is generally done on a case-by-case basis, and the procedures for making such determinations vary amongst the states.

Many state DOTs use the BAMS.DSS "Tms*port" software program, which helps to identify unbalanced bid items as well as to analyze bids for any indicia of potential bid-rigging. Careful attention should be paid to the bid for mobilization, which can mask unbalancing, and token bid items that show large variations from the engineers' estimate. In addition, the reason for the unbalancing should be examined, because it may be caused by inaccurate bid quantity estimates, plan errors, or changes in design, which require further evaluation to determine whether the initial apparent low bidder is in fact the actual low bidder. If the agency examination determines that there is reasonable doubt that the award would result in the lowest ultimate cost, then the bid is materially unbalanced and should be rejected.[63]

As one example of a state DOT provision addressing unbalanced bidding, Ohio Standard Contract Provision 102.08 is patterned after the federal definitions. It provides for the rejection of a materially unbalanced bid when the Department determines that it will not result in the lowest ultimate cost to the Department.

A mathematically unbalanced bid is not necessarily nonresponsive. A reasonably unbalanced bid may be perfectly proper.[64] However, a bid may be considered nonresponsive when it is mathematically and materially unbalanced.[65] When the bid is so grossly unbalanced that it results in an advance payment, it is materially unbalanced and must be rejected. In *McKnight Const. Co. v. Department of Defense*, [66] the agency concluded that items with exceptionally high prices would be done early in the project, while the later work was priced "ridiculously low." Thus it was not an abuse of discretion to reject the bid.

Unbalanced bidding may also be used where a bidder believes that the contracting agency's estimates for quantities of certain items are low, and that these quantities will have to be increased as the work progresses. In those circumstances the contractor can increase profits by unbalancing the bid in favor of these items without increasing the total price of the proposal. In other instances, inaccurate estimates may work to the disadvantage of a contractor, because any substantial increase or reduction in the quantity of materials or work after construction operations have commenced may distort the factors that determine a contractor's actual cost, so that the unit price submitted in the bid is thrown out of balance, with resulting loss of profits.

Because of these possibilities for unanticipated profits or losses, and the susceptibility to fraud and collusion, unbalanced bids are not favored. Bidding specifications sometimes provide for permissive rejection of unbalanced bids.[67] In this way, unbalanced bidding may be scrutinized case-by-case, and its effect on the cost to the contracting agency can be analyzed. This approach is to be preferred to outright prohibition of unbalanced bidding. Unbalanced bids are not per se fraudulent, nor

[61] 23 C.F. R. 635.102.

[62] 23 C.F.R. 635.114(c).

[63] FHWA, CONTRACT ADMINISTRATION CORE CURRICULUM PARTICIPANT MANUAL AND REFERENCE GUIDE, § III, State Procedures, at 26–27 (2006); http://www.fhwa.dot.gov/programadmin/contracts/cacc.pdf.

[64] 687 A.2d at 327.

[65] SMS Data Products Group, Inc. v. United States, 900 F.2d 1553, 1557 (Fed. Cir. 1990).

[66] 85 F.3d 565, 570–71 (11th Cir. 1996).

[67] *See, e.g.*, Washington State Department of Transportation, 2000 Standard Specifications for Road, Bridge, and Municipal Construction § 1-02.13(2)(b) (bid may be considered irregular and may be rejected if "[a]ny of the unit prices are excessively unbalanced (either above or below the amount of a reasonable bid) to the potential detriment of the Contracting Agency.").

are they always evidence of substantial error. The rule appears to still be:

An unbalanced bid that does not materially enhance the aggregate cost of the work cannot be complained of. If there is no deception or mistake as to the quantities, and if the ordinances have fairly been complied with, and the quantity and quality of the work has been estimated as nearly as practical, there is no ground for alleging substantial error merely because of an unbalanced bid under which the contract was let, and if the cost of the work has not thereby been enhanced, there is no ground for alleging fraud.[68]

Cooperation between the contractor and the contracting agency should eliminate the risk of unfair practice and minimize the area in which inaccuracies exist. Such a policy is sometimes set forth in the transportation agency's own standard specifications.

The distinction between genuine and apparently unbalanced bids was made in *Department of Labor and Industries v. Boston Water and Sewer Commission*, [69] in which the complainant protested a bid for construction of underground sewer lines. The Commission's specification for the work called for the contractor to install temporary sheeting, for which the apparent low bidder listed a unit price of a penny per square foot. Although it determined that this bid was not unbalanced, "front-end loaded," or otherwise inflated; was made in good faith; and did not violate any of the State's public contract laws; the Department of Labor and Industries instructed the defendant Commission to reject the bid as unresponsive and contrary to the Department's policy.[70] The trial court explained that the Department of Labor and Industries had taken the position that penny bidding of certain items of the contract is unlawful even where the bid is not facially unbalanced. This position was taken as a result of the department's interpretation of the law and a longstanding and publicly known policy against any form of penny bidding. The basis of this policy was a conclusion that "because of the potential bid manipulation and the possible resulting harm to the awarding authority and the general public…unrealistic bids must be rejected as unresponsive to the bid requirements."[71] On appeal, however, the Massachusetts Appellate Court reversed this ruling. It held that the Department lacked authority to promulgate rules or regulations that controlled the bidding process, and its announced policy could not be permitted to have the practical effect of law.[72] The court also distinguished the practice of "penny bidding" from the case where the "equal footing" of bidders was destroyed by artificially low bids that conferred special advantages on one of the bidders.[73]

In another case, *Turner Construction Company v. New Jersey Transit Corporation*, [74] the bidder had submitted a bid of zero for one item. Rather than construe this as a failure to submit a unit price on an individual bid item, which would be a material defect, the court construed it as an unbalanced bid, which is not defective merely because it is unbalanced. In this case, a bid of zero was comparable to a nominal or penny bid. The court stated: "Every contractor may apply his own business judgment in the preparation of a public bid, and his willingness to perform one of the items for a nominal amount is but his judgmental decision in an effort to underbid his competitors."[75]

The court thus found that the zero bid for one bid item was a waivable defect.

f. Qualified Bids

Serious difficulties may arise when bids do not conform fully or precisely to the plans, terms, or specifications in the project announcement. When bids are at variance with these aspects of the project announcement, it is unlikely that the contracting agency will receive the end product it desires. It is also not possible to fairly compare all bidders on a common set of work standards. Bids may be inconsistent with advertised plans, terms, and specifications, but still offer an acceptable end product. However, such bids should be treated as counterproposals, which are not responsive. This was the result in *Bodies by Lembo v. Middlesex County*, [76] a New Jersey case in which the second low bidder's alternative for an "equivalent" product that was less than the price of the low bidder was declared invalid. The court ordered that the low bidder be awarded the contract as it was advertised and did not allow the county to readvertise.[77]

A bidder's conditional response to a request for proposals also will generally be considered nonresponsive. A responsive bid is considered an offer to contract with the agency; a bid that proposes something other than that requested in the invitation for bids or that conditions its response will be considered a counter-offer, and a nonresponsive bid. For example, a bidder's conditional response to one item of a request for proposals for the supply of reflective sheeting materials and supporting services for reflective license plates was considered a nonwaivable material deviation from the request for

[68] In re Anderson, 109 N.Y. 554, 17 N.E. 209 (1888).

[69] 18 Mass. App. 621, 469 N.E.2d 64 (1984).

[70] *Id*. at 66.

[71] *Id.*

[72] *Id*. at 67.

[73] *Id*. at 68. The court noted that in the instant case, at least five other contractors had listed bids of one penny per square foot for temporary sheeting. 469 N.E.2d at 66.

[74] 296 N.J. Super. 530, 687 A.2d 323, 327 (1997).

[75] 687 A.2d at 327 (quoting Riverland Constr. Co. v. Lombardo Contracting Co., 380 A.2d 1161, *aff'd*, 388 A.2d 626 (1978)).

[76] 286 N.J. Super. 298, 669 A.2d 254, 256 (A.D. 1996). In addition to including an alternative product, the bid also contained deficiencies that the bidder had been permitted to correct after bids were opened.

[77] *Id.* 669 A.2d at 260.

proposals.[78] This was found to create a situation in which the agency could not be assured that the contract would be performed, and gave the bidder a competitive advantage.

g. Improper Bid Bonds

An example of a material deviation that could not be waived is found in a case in which the bid was submitted with a letter from the surety stating that it did not anticipate any difficulty in providing bonds, rather than guaranteeing that the bonds would be provided.[79] The court found this defect to be a substantial deviation from a material condition because there was no guaranty that the surety would issue the bonds on the date that bids were due.[80]

h. Failure to Acknowledge Addenda

In *George & Benjamin General Contractors v. Virgin Island Department of Property and Procurement*, the court noted that the applicable regulations allowed that failure to acknowledge receipt of addendum may be waived as a minor informality if the bid clearly indicated that the bidder received the amendment, such as when the addendum added an item of work and the bidder included a bid for that item.[81] Adherence to this requirement insures that bidders are all submitting bids on the basis of the same information.

i. Other Material Deviations.–Where the invitation for bids specifically required the prospective bidders to attend a pre-bid meeting at the construction site, the court held that the bidder's failure to attend was adequate grounds for the agency's rejection of its bid.[82] The agency's reason for requiring attendance was to ensure that all bidders had adequate notice of the site conditions and could take those conditions into account in their bids. Although the bidder who had not attended the pre-bid meeting submitted a lower bid than the bidders who did attend the meeting, the agency was justified in concluding that the second low bid was the more realistic one, more likely taking into account the actual site conditions. The court did not, however, determine whether the agency was required to reject the bid because of the bidder's failure to attend the meeting, only that it was not arbitrary to have done so. If the bidder's failure to attend gave it more of an opportunity to claim that it was entitled to additional compensation due to changed conditions, then it could be considered a deviation that gave it an advantage over other bidders, requiring rejection. However, under most changed condition clauses, the bidder would probably be held to knowledge of the information provided in the pre-bid conference whether it had a representative at the meeting or not. In addition, requiring that the bidder inspect the site does not protect the agency from changed condition claims.[83] Failure to attend the pre-bid conference is most likely a nonmaterial deviation that the agency could choose to waive in an appropriate case, as it is not a factor that likely affects the price of the bid or that gives the non-attending bidder an advantage over other bidders.[84] However, where the agency was concerned about the bidders being informed about the specific site conditions, for the purpose of avoiding claims of changed conditions, it was not arbitrary for the agency to enforce that requirement in the invitation for bids and reject the nonconforming bidder. The agency has discretion to determine whether a deviation is material or nonmaterial, and its decision generally will be upheld if supported by a rational basis.[85]

Another case in which the bidder was rejected for failure to attend the pre-bid conference went even further in supporting the agency's rejection, holding that the contractor did not even qualify as a "bidder" due to its failure to attend.[86] The advertisement and contract documents had set the time, date, and place for the pre-bid meeting, and had provided that "no bid shall be accepted from any contractor who does not have a responsible representative attend this meeting." Only one contractor attended, and it was awarded the contract. The court again did not determine whether the agency had the power to waive this requirement, only that it was proper to have rejected the bid on that basis.

ii. Nonmaterial Deviations.–Where the agency finds that the bidder's deviation from the instructions or specifications will not affect its price and will not give that bidder an advantage over other bidders, the deviation may be waived. A common example is an mathematical error, such as in extending unit prices to derive total prices. A patent error in the statement of a unit price as $400 rather than $4 was found to be a waivable, nonmaterial error where the bidder's intent was obvious from the computed total for the quantity of that item.[87]

In *Colonnelli Bros., Inc. v. Village of Ridgefield,*[88]

[78] Matter of Request for Proposals No. 98-X-29314 Reflective Sheeting License Plates, 315 N.J. Super. 266, 717 A.2d 998, 1001 (A.D. 1998).

[79] DeSapio Constr., Inc. v. Township of Clinton, 276 N.J. Super. 216, 647 A.2d 878 (1994).

[80] *Id*. at 880–81.

[81] 921 F. Supp. 304, 309 (D. V.I. 1996)

[82] Scharff Bros. Contractors v. Jefferson Parish Sch. Bd., 641 So. 2d 642, 644, *reconsideration denied*, 644 So. 2d 398 (La. App. 5 Cir. 1994).

[83] R.J. Wildner Contracting v. Ohio Turnpike Comm'n, 913 F. Supp. 1031 (N.D. Ohio 1996).

[84] *See* Terminal Constr. Corp. v. Atlantic County Sewerage Auth., 67 N.J. 403, 341 A.2d 327, 332 (1975) (failure to attend federally-required pre-award conference was for bidder's benefit, and was waivable).

[85] Varsity Transit, Inc. v. Board of Educ. of City of N.Y., 515 N.Y.S.2d 520, 521, 130 A.D. 2d 581, *appeal denied*, 519 N.Y.S.2d 1029, 70 N.Y.2d 605, 513 N.E.2d 1309 (1987).

[86] Gibbs Constr. Co. v. Board of Supervisors, La. State Univ., 447 So. 2d 90, 92 (La. App. 1984).

[87] Spina Asphalt Paving Excavating Contractors v. Borough of Fairview, 304 N.J. Super. 425, 701 A.2d 441, 443 (A.D. 1997).

[88] 665 A.2d 1136, 284 N.J. Super. 538 (1995).

however, the bid specifications stated that unit prices would prevail over extended totals. The bidder had written the numerical amount of $10,000 for "maintenance of traffic during construction," but had written out "one hundred dollars no cents." The bidder then added $10,000 into the total price. The agency engineer had estimated that item at $5,000, and the bids had ranged from $2,000 to $15,000. When the bid was recalculated using the unit prices, it was found that that bid was in fact the lowest bid. However, the agency rejected the bid as nonresponsive. The trial court held that the fact that the totals were in error was a waivable defect. The appellate court reversed, holding that the trial court had improperly interfered with the agency's discretion, and upheld the rejection.[89] The court distinguished this case from cases in which the error is obvious and the bidder's intent is easily discerned from the bid document. In this case, the error was not obvious, and allowed the bidder to choose which number to use after bid opening.[90]

A similar situation arises when figures are transposed. This was considered a minor error that could be corrected by the agency, because the error was so obvious it was easily determined what the bidder's intent was.[91] Also, an error in the estimation of the amount of waste material to be generated was considered waivable where the quantity was intended to be an estimate and the possibility of error was contemplated by the parties.[92]

Another error deemed waivable was a bidder's deviation in submitting the name of one subcontractor in the wrong envelope.[93] Also, the bidder's failure to file a biennial corporate report or pay nominal corporate taxes was not a material defect requiring rejection, as it did not give that bidder an advantage over others.[94]

A number of cases address whether a bidder's failure to include prequalification information with its bid is a material defect requiring rejection. In most of these cases, the bidder already has filed its prequalification materials and has been prequalified in order to submit a bid in the first place. Therefore, courts have found these defects to be waivable in that they do not give that bidder an advantage over others and do not affect the bidder's price.[95] However, the requirement of prequalification itself is not considered a mere formality. Where a bidder had no prequalification statement on file, the fact that it did not include the prequalification information with its bid could not be waived.[96] In some states, a bidder is not even entitled to receive the bid package and submit a bid unless it has first been prequalified, so this would not be an issue.[97]

2. Bidder Remedies

When errors occur in cost calculations, or the terms of the project advertisement or bid are not correctly construed, the resulting confusion may seriously delay or jeopardize the contract award. In the case of contracts for large and complex highway construction projects, this risk is increased by the sheer size of the task of checking the plans, specifications, and estimates to detect mistakes. It may also be complicated by the fact that state codes and administrative regulations rarely provide comprehensive procedures for correcting mistakes. Thus, where controversies cannot be settled administratively by the contracting agency, the parties must adjudicate their claims in court.

a. Bid Protests

i. Letting Agency Review vs. External Control Agency Review.–The U.S. Government and a number of states have adopted either regulations establishing bid protest procedures or administrative procedures relating to the exercise of statutory discretion for review and approval of contract awards. One significant distinction to be drawn in assessing such procedures is whether they are administered by the letting agency or by an external control agency. A letting agency is the agency that advertises for and opens competitive bids, awards contracts, and administers contracts. An external control agency is a federal or state agency with independent statutory authority to review and approve or disapprove the award of contracts, including the authority to override contract award decisions by letting agencies.

In the former situation, the letting agency, while considering any bid protests, retains control over the award of its own contracts. In the latter situation, while the letting agency may still have authority to let its own contracts and nominal authority to make contract award decisions, the review of bid protests and ultimate control over the authority to award contracts rests with the external control agency, rather than the letting agency.

Examples of bid protest processes administered by letting agencies are provided by the States of Maryland and Virginia.

In Maryland, bid protests are governed by state procurement regulations, which provide for protests to be filed with "the appropriate procurement officer."[98]

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[89] 665 A.2d at 1138–39.

[90] *Id*.

[91] George & Benjamin General Contractors v. Virgin Island Dep't of Property and Procurement, 921 F. Supp. 304, 309 (D. V.I. 1996).

[92] R.J. Wildner Contracting v. Ohio Turnpike Comm'n, 913 F. Supp. 1031, 1041–42 (N.D. Ohio 1996).

[93] MCM Constr., Inc. v. City & County of S.F., 78 Cal. Rptr. 2d 44, 54–55, 66 C.A. 4th 359, *review denied* (1998).

[94] Lower Kuskokwim School Dist. v. Foundation Services, 909 P.2d 1383, 1387–88 (Alaska 1996). Note that the filing requirement here was one that is considered to be a revenue mechanism as opposed to a licensing requirement specific to contractors, or a prequalification requirement.

[95] *See supra* note 15.

[96] Modern Continental Constr. Co. v. City of Lowell, 391 Mass. 829, 465 N.E.2d 1173, 1180 (1984).

[97] *See* WASH. REV. CODE § 47.28.070 (2001).

[98] Consolidated Maryland Regulations (COMAR) § 21.10.02.02.

While the procurement officer is required to notify and consult with the Office of the Attorney General, the procurement officer makes the determination on the bid protest.[99] The decision by the procurement officer is subject to review by a reviewing authority and also subject to an appeals procedure, but reviews and appeals occur only after the procurement officer has made a determination.[100]

In Virginia, bid protests are governed by the Virginia Public Procurement Act. Under the provisions of this Act, bid protests are submitted in writing to "the public body, or an official designated by the public body," which let the contract and the public body or designated official make the determination on the bid protest.[101] Public bodies may establish an administrative procedure for a disinterested person or panel to hear appeals from protests of decisions to award contracts, or awards of contracts, and the decisions of such disinterested persons or panels shall be final and conclusive and shall not be set aside, absent a judicial determination that such a decision was fraudulent, arbitrary, capricious, or grossly erroneous.[102]

The U.S. Government and New York State provide typical examples of bid protest processes administered by external control agencies.

The bid protest process for U.S. Government contracts is governed by the regulations of the U.S. Government Accountability Office (GAO), formerly known as the General Accounting Office. The GAO bid protest regulations, 4 C.F.R. Part 21, have been in effect for a number of years. GAO's regulations include provisions governing filing,[103] time for filing,[104] notice of protest, submission of agency report, and time for filing comments in report,[105] protective orders,[106] exclusion of certain specified issues from protests,[107] withholding of award and suspension of contract performance,[108] hearings,[109] remedies,[110] time for decision by GAO,[111] express options and flexible alternative procedures,[112] the effect of judicial proceedings,[113] distribution of decisions,[114] non-statutory protests,[115] and requests for reconsideration.[116] These provisions are sufficiently lengthy and detailed to appear more the province of specialized practitioners than accessible to the uninitiated.

The GAO regulations afford sufficient opportunities for long procedural delays to the point that Congress included a requirement in the National Defense Authorization Act for federal fiscal year (FFY) 1996 that GAO issue bid protest decisions within 100 days after the protest were filed, and GAO had to amend its regulations accordingly.[117]

In New York State, statutory authority for the letting and award of contracts nominally rests with contracting agencies.[118] All state contract awards are, however, subject to the review and approval of the Office of the State Comptroller (OSC), and a state contract is not considered to be final and legally in effect unless and until it has been approved by OSC.[119] New York State has not enacted any statute making express provision for bid protests, but OSC decided to implement bid protest procedures through the issuance of an administrative bulletin to state agencies in 2008.[120]

While nominally guidelines, the OSC bid protest procedures rival GAO's regulations for complexity. Although acknowledging that a letting agency might establish its own bid protest procedures and requiring protesters to resort to such procedures first if the letting agency has provided notice of such procedures in its solicitation documents, the OSC guidelines offer protesters the opportunity to file protests directly with OSC where agencies have failed to establish or provide notice of such procedures, or where facts giving rise to a protest are not known until the expiration of any filing deadlines established by agency procedures. The OSC guidelines also offer protesters the opportunity to appeal to OSC from agency determinations on bid protests.

Whether in the case of an initial protest filed with OSC or an appeal to OSC from an agency determination, the OSC guidelines grant broad discretion to OSC's Bureau of Contracts to determine whether a hearing is necessary and what level of formality a hearing may require, to waive any deadline or other requirements in the guidelines, to require the contracting agency or any other interested party to address any additional issues raised by OSC, and to obtain information relevant to the procurement from

[99] COMAR §§ 21.10.02.05 and 21.10.02.09(A).

[100] COMAR §§ 21.10.02.09(B), 21.10.02.10, 21.10.03.02, and 21.10.07.02.

[101] Virginia Public Procurement Act § 2.2-4360(A).

[102] Virginia Public Procurement Act § 2.2-4365(A).

[103] 4 C.F.R. § 21.1.

[104] 4 C.F.R. § 21.2.

[105] 4 C.F.R. § 21.3.

[106] 4 C.F.R. § 21.4.

[107] 4 C.F.R. § 21.5.

[108] 4 C.F.R. § 21.6.

[109] 4 C.F.R. § 21.7.

[110] 4 C.F.R. § 21.8.

[111] 4 C.F.R. § 21.9

[112] 4 C.F.R. § 21.10.

[113] 4 C.F.R. § 21.11.

[114] 4 C.F.R. § 21.12.

[115] 4 C.F.R. § 21.13.

[116] 4 C.F.R. § 21.14.

[117] *See* GAO's Notice of Final Rule, 61 Fed. Reg. 39039, July 26, 1996.

[118] *See, e.g.*, N.Y. HIGH. LAW § 38.

[119] N.Y. FINANCE LAW § 112.

[120] New York State Office of the State Comptroller, Procurement and Disbursement Guidelines Bulletin No. G-232, issued July 10, 2008, and updated Aug. 6, 2008; available online at http://www.osc.state.ny.us/agencies/gbull/g_232.htm, last accessed on Nov. 21, 2011.

outside sources.[121]

Although presented as guidelines, in the case of an initial protest, they authorize OSC's Bureau of Contracts to issue written determinations that "shall make findings of fact and conclusions of law on any issues in dispute." In the case of an appeal, the OSC guidelines authorize OSC's Bureau of Contracts to "evaluate the merits of the protest, the contracting agency's determination and any response submitted by an interested party," and to issue a written determination "addressing the issues raised by the appeal." [122]

The OSC guidelines are still sufficiently new, and at the time of the 2012 update to this volume, it is not yet clear whether any benefits they may convey—by providing checks and balances on unfettered letting agency discretion in making contract awards, and by providing initially unsuccessful bidders a second chance to win contracts by challenging an award to the lowest bidder—will outweigh the costs they impose by increasing the uncertainties of the contract award process, and by reducing the timeliness of final determinations on contract awards.

ii. Protests Prior to Bid Opening.—A bid protest filed prior to bid opening is the appropriate means for a bidder to challenge the legality of the bid instructions or specifications included in the invitation for bids. Such a challenge allows the agency to save expense to bidders, assure fair competition among them, and correct or clarify plans and specifications prior to bid opening.[123] The challenge must be directed at specifications that are so vague that bidders cannot formulate an accurate bid based on them, or that are unreasonable in that they are impossible to comply with or too expensive to comply with and remain competitive in the bidding process.[124]

A challenge to the bid specifications must be brought in a timely manner or may be deemed waived. A bidder cannot wait until after bid opening and then challenge a specification if the bidder is unsuccessful. A timely challenge will give the agency the opportunity to correct a flawed specification, either by addendum or by rejecting all bids and readvertising. It will also allow other bidders to modify their bids if necessary to conform to the corrected or clarified specification.[125]

Although this type of protest is generally used to challenge special provisions in the contract specifications, a bidder in an Alabama case attempted to prevent the Department of Transportation from applying its standard specifications in a contract. In *Alabama Department of Transportation v. Blue Ridge Sand and Gravel*, the court balanced the potential public harm of premature road failures against the bidder's potential loss of profits, and upheld the use of the department's standard specification requiring that gravel for use in hot mix asphalt have a specific bulk gravity.[126]

iii. Standing to Protest Award.—States vary in whether they allow a disappointed bidder to challenge an award where that bidder is not also a state taxpayer.[127] For example, Pennsylvania, Colorado, and Washington courts have required that one must be a taxpayer in order to enforce the requirements of public bidding laws, such as that public contracts be awarded to the lowest responsible bidder.[128] In Washington, the court has held that in order to prove taxpayer status, the bidder must show that it pays the type of taxes that are funding the project, and that it asked for the Attorney General's Office to take action before filing suit.[129]

However, many states do allow the bidder to protest the award where it contends that the contract was awarded to a higher bidder because the bidding procedure did not permit the bidders to compete on equal terms.[130] For example, Florida's courts have held that a person who has at least some potential stake in the contract to be awarded will have standing to challenge the bidding process.[131] In New York, an Ohio contractor was found to have standing to challenge the contract award on the basis that it alleged noncompliance by the agency with its procedures, and the contractor had suffered injury in fact that was different from that suffered by the public at large.[132]

One federal court has held that a disappointed bidder may challenge the contract award only if it is "within the zone of active consideration" for the award of the contract.[133] Because the federal Administrative

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[121] *Id*.

[122] *Id*.

[123] Capeletti Bros. v. Department of Transp., 499 So. 2d 855, 857 (Fla. App. 1 Dist. 1986).

[124] Advocacy Center for Persons with Disabilities, Inc. v. State, Dep't of Children and Family Services, 721 So. 2d 753, 756 (Fla. App. 1998) (challenge must be to specifications themselves, and not to policy decisions to privatize services).

[125] *See* Optiplan, Inc. v. School Board of Broward County, 710 So. 2d 569, 572 (Fla. App. 4th Dist. 1998) (unsuccessful bidder waived its right to challenge race-based selection criteria by submitting bid based on specifications that it later sought to challenge).

[126] 718 So. 2d 27, 32 (Ala. 1998).

[127] For a discussion of whether aggrieved bidders should have standing to protest awards regardless of taxpayer status, *see* David Sullivan, *Disappointed Bidder Standing To Challenge A Government Procurement Contract Award: A Proposal For Change In Kentucky*, 88 KY. L. J. 161–82 (1999).

[128] Ray Angelini, Inc. v. City of Phila., 984 F. Supp. 873, 884 (E.D. Pa. 1997).

[129] Dick Enterprises, Inc. v. Metro/King County, 83 Wa. App. 566, 922 P.2d 184, 187 (1996).

[130] Metropolitan Express Services, Inc. v. City of Kansas City, Mo., 23 F.3d 1367, 1370–71 (8th Cir. 1994), *rehearing denied, appeal after remand*, 71 F.3d 273 (1995).

[131] Advocacy Center of Persons With Disabilities, Inc. v. State, Dep't of Children and Family Services, 721 So. 2d 753, 755, *rehearing denied* (Fla. App. 1 Dist. 1998).

[132] AEP Resources Service Co. v. Long Island Power Auth., 686 N.Y.S.2d 664, 669, 179 Misc. 639 (1999).

[133] Ellsworth Assocs. v. United States, 926 F. Supp. 207, 211 (D.D.C. 1996); Ralvin Pacific Properties, Inc. v. United States, 871 F. Supp. 468, 472 (D.D.C. 1994); *see also* Transactive Corp.

Procedure Act (APA) is written in somewhat broader terms than many state APAs, federal courts are more likely to allow a bidder who is not also a taxpayer to challenge an award.[134] The United States Supreme Court's general test for standing is generally relied upon to determine whether a bidder has standing: "The essence of the standing question, in its constitutional dimension, is 'whether the plaintiff has "alleged such a personal stake in the outcome of the controversy" as to warrant *his* invocation of federal-court jurisdiction and to justify exercise of the court's remedial powers on his behalf.'"[135]

Whether other bidders who responded to the invitation for bids are entitled to notice of the protest, and may participate in the proceeding, is another question. Generally, the bidder who has been awarded the contract should be considered to have standing, and to have an interest sufficient to support intervention in a court proceeding or recognition of its interests by the agency in an administrative proceeding. However, a proposed rule in Florida that would have required the agency to forward copies of a bid protest and notice of hearing to all other bidders was held to be arbitrary and an invalid exercise of its rule-making authority.[136]

A Georgia court has held that taxpayers lacked standing to challenge the award of a contract and to enjoin payment to a contractor who had been awarded an on-call contract for paving. In *Faulk v. Twiggs County*,[137] the contractor had obtained a competitively bid unit price contract, but the contract was indefinite as to quantity; the county intended to designate areas for paving as funds became available. In a similar case, the court ruled that unsuccessful bidders did not have standing to challenge an award as taxpayers because the injury that they suffered was private and not shared by the public at large.[138]

Generally, a bidder must at a minimum be one who is within the zone of active consideration for the award in order to have standing. However, in *L. Pucillo & Sons v. Belleville Township*, [139] a New Jersey case, a potential bidder was found to have standing to protest where it alleged that it was deterred from submitting a bid by the size of the performance bond required, and the amount of the bond specified was subsequently waived for another bidder.

iv. Standard and Scope of Review.—Generally, contracting agencies have broad discretion in evaluating bids and awarding contracts. Therefore, a disappointed bidder must show that the contract award had no rational basis, or that it involved a clear and prejudicial violation of an applicable statute or regulation.[140] A disappointed bidder bears a heavy burden to show that the award decision had no rational basis.[141] One court has described the review for abuse of discretion in these terms: "The awarding agency has the right to be wrong in the exercise of its discretion, but not the right to be 'unfairly, arbitrarily wrong.'"[142]

Other courts have stated the standard of review as being whether the agency's decision on who is the lowest responsible bidder was arbitrary, unreasonable, or capricious.[143] The agency's compliance with its own bidding regulations will be reviewed for whether the agency's decision is correct as a matter of law.[144] The agency and its officials and employees are presumed to have acted in good faith, and any party challenging the agency's action must present strong evidence of bad faith in order to overcome this presumption.[145] The agency's findings of fact will generally not be reversed unless a reviewing court concludes that a finding is clearly erroneous in view of the entire record.[146]

The court's standard of review will have to take the statutory language into account. For example, where the statute allows the agency to select the lowest *and best* responsive bid, the agency may be held to have a higher degree of discretion than one that is obligated by its statute to select the lowest responsive bid. One court has held that where the statute allowed the agency to award the contract to the bidder submitting the lowest and best bid, the bid selection is solely within the sound discretion of the agency, and its decision will be re-

v. N.Y. State Dep't of Social Services, 665 N.Y.S.2d 701, 704, 236 A.D. 2d 48 (N.Y. App. 1997) (contractor who merely filed intention to bid lacked standing to challenge award, without a showing that it met the qualifications set out in the request for proposals) and Brem-Air Disposal v. Cohen, 156 F.3d 1002, 1003 (9th Cir. 1998) (contractor lacked standing to challenge award after end of bid proposal period as it could no longer qualify as a prospective bidder).

[134] *See* 5 U.S.C. § 702 ("person suffering legal wrong because of agency action, or adversely affected or aggrieved by agency action").

[135] Village of Arlington Heights v. Metropolitan Housing Dev. Corp., 429 U.S. 252, 260–61 (1977) (quoting Warth v. Seldin, 422 U.S. 490, 498–99 (1975) (emphasis in original)).

[136] Division of Admin. Hearings v. Department of Transp., 534 So. 2d 1219, 1220 (Fla. App. 1 Dist. 1988).

[137] 504 S.E.2d 668, 670 (Ga. 1998).

[138] Mid-Missouri Limestone v. County of Callaway, 962 S.W.2d 438, 441 (Mo. App. 1998).

[139] 592 A.2d 1218, 1222 (N.J. Super. A.D. 1991).

[140] Latecoere Intern. Inc. v. United States Dep't of the Navy, 19 F.3d 1342, 1356 (11th Cir. 1995); Robert E. Derektor of Rhode Island, Inc. v. United States, 762 F. Supp. 1019, 1022 (D.R.I. 1991).

[141] Saratoga Dev. Corp. v. United States, 21 F.3d 445, 456, 204 U.S. App. D.C. 351 (D.C. Cir. 1994).

[142] Williams v. Board of Supervisors, La. State Univ. and Agricultural and Mechanical College, 388 So. 2d 438, 441 (La. App. 1980).

[143] Matter of Protest of Award of On-Line Games Prod. and Operation Services Contract, Bid No. 95-X-20175, 279 N.J. Super. 566, 653 A.2d 1145, 1158 (1995).

[144] State Contracting and Eng'g Corp. v. Department of Transp., 709 So. 2d 607, 610 (Fla. App. 1 Dist. 1998).

[145] China Trade Center, L.L.C. v. Washington Metro. Area Transit Auth., 34 F. Supp. 2d 67, 70–71 (D.D.C. 1999).

[146] Southern Foods Group, L.P. v. State, Dept. of Educ., 89 Haw. 443, 974 P.2d 1033, 1042 (1999).

viewed only for fraud or abuse of discretion.[147]

Although no formal contract exists prior to the acceptance of a bid by the agency, the agency may be considered to have an implied-in-fact contract with bidders to consider all bids fairly. Its failure to do so may result in the awarded being voided. In considering whether an agency has breached this duty, a court will look at (1) whether there is evidence of subjective bad faith on the part of the agency, (2) whether there is a reasonable basis for the agency's decision, (3) the amount of discretion afforded by the statutes and regulations, and (4) whether there is proof that the statutes or regulations have been violated.[148]

Ordinarily, the scope of a court's review will be limited to the record in existence before the agency.[149]

v. Procedures and Evidence.—When a disappointed bidder invokes a statutory review process, the agency must follow the statute's procedural steps.[150] In addition to protecting the due process rights of the disappointed bidder, these statutory requirements may be held to be necessary to further public policy goals such as ensuring public confidence in the public bidding system, and ensuring that all who participate in the public procurement process are treated fairly and equitably.[151] This is also consistent with the requirements that the agency follow its own procedures prior to the submission of bids and in the consideration of bids.

Likewise, the aggrieved bidder is held to compliance with any statutory filing requirements for challenging the award of a contract. In a Virginia case, these requirements were held to be a limitation imposed on a substantive right rather than mere procedural requirements, and the unsuccessful bidder's failure to comply with the filing requirements warranted dismissal of its case with prejudice.[152] Requirements may include filing an administrative claim prior to filing in court. Failure to do so may be considered a failure to exhaust administrative remedies, and will bar pursuit of the protest in court.[153]

Where the rules pertaining to protests require that it be filed within a certain time period, the bidder's failure to comply with the timeliness requirement will bar its challenge.[154] The disappointed bidder must plead that it has timely complied with the filing requirements; its failure to include in its protest the facts needed to determine the timeliness of its filing required dismissal of its protest.[155] A Mississippi court has held that where award is subject to approval by FHWA, the time for appeal runs from the time that the contract is executed, and not from the time of award.[156]

Even where another bidder had filed a timely protest, the California court held that a bidder's failure to comply with mandatory procedures regarding the timing and manner of its own protest that were set forth in the bid instructions required dismissal of its protest.[157] In other words, the fact that the agency was not prejudiced by the late filing, due to the fact that there was already a protest pending, did not relieve the bidder from compliance with the filing requirements.

In a bid protest proceeding, an unsuccessful bidder could not bring in evidence of issues that were not included in its notice of protest, even if the other parties stipulated to admission of the evidence.[158]

vi. Injunctive Relief.—Injunctive relief may be available to the protesting bidder, providing that it can meet the standard requirements for such relief, namely that it will suffer irreparable harm and that it has a likelihood of success on the merits.[159] However, in order to pursue injunctive relief, a contractor must act in a timely manner. A bidder that does not pursue injunctive relief in a timely manner, even though it has readily ascertainable facts sufficient for such a request for relief, may be barred by laches. Further, a bidder may waive its rights to pursue any relief if it does not first ask the court to enjoin the award and execution of the contract to the higher bidder.[160] The rationale for this is that the agency should be allowed to correct any errors, or if necessary, rebid the project.[161] A Louisiana court held that an aggrieved bidder may seek to have the contract declared null and void without first obtaining an

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[147] Wilson Bennett, Inc. v. Greater Cleveland Regional Transit Auth., 67 Ohio App. 3d 812, 588 N.E.2d 920, 925, *jurisdictional motion allowed*, 42 Ohio St. 3d 717, 560 N.E.2d 778, *cause dismissed*, 57 Ohio St. 2d 721, 568 N.E.2d 1231 (1990).

[148] Southfork Systems, Inc. v. United States, 141 F.3d 1124, 1132 (Fed. Cir. 1998).

[149] China Trade Center, L.L.C., *supra* note 145, at 70.

[150] Alexander & Alexander, Inc. v. State, 596 So. 2d 822, 828 (La. App. 1 Cir. 1991), *rehearing denied* (1992).

[151] *Id*. at 828.

[152] Sabre Constr. Corp. v. County of Fairfax, 501 S.E.2d 144, 146–47 (Va. 1998).

[153] *See* Mosseri v. FDIC, 924 F. Supp. 605, 608 (S.D. N.Y. 1996).

[154] Sabre Constr. Corp., *supra* note 152, at 146–47.

[155] Widnall v. B3H Corp., 75 F.3d 1577, 1585 (Fed. Cir. 1996).

[156] J.H. Parker Constr. Co. v. Board of Aldermen, City of Natchez, 721 So. 2d 671, 674 (Miss. App. 1998).

[157] MCM Constr., Inc. v. City and County of S.F., 78 Cal. Rptr. 2d 44, 55-57, 66 C.A. 4th 359 (Cal. App. 1998), *review denied*.

[158] Pacificorp Capital, Inc. v. State Through Division of Admin., Office of State Purchasing, 612 So. 2d 138, 139 (La. App. 1 Cir. 1992).

[159] San Diego Beverage & Kup v. United States, 997 F. Supp. 1343, 1345 (S.D. Cal. 1998); Tri-State Asphalt Corp. v. Com. Dep't of Transp., 135 Pa. Commw. 410, 582 A.2d 55, 60, appeal denied, 527 Pa. 659, 593 A.2d 4429 (1990).

[160] South Lafourche Metal Bldgs., Inc. v. Grand Isle Fire Dep't Through Jefferson Parish Fire Dist. No. 10, 582 So. 2d 970 (La. App. 5 Cir. 1991); Hartman Enters. v. Ascension--St. James Airport and Transp. Auth., 582 So. 2d 198, 200-01, *writ denied*, 582 So. 2d 195, *reconsideration denied*, 584 So. 2d 669 (La. App. 1 Cir. 1991); Webb Constr., Inc. v. City of Shreveport, 665 So. 2d 653, 656 (La. App. 2 Cir. 1995).

[161] Hard Rock Constr., Inc. v. Parish of Jefferson, 688 So. 2d 134, 137 (La. App. 5 Cir. 1997).

injunction, but may not seek damages unless it has either timely filed for an injunction or shown that timely suit for an injunction was impossible.[162]

Washington's courts have held that unless an injunction is issued prior to execution, a disappointed bidder does not have standing to enjoin performance of the executed contract.[163] Once the contract is signed, the bidder lacks standing to enjoin performance.

Another question is whether the bidder is entitled to a mandatory injunction, ordering the agency to award it the contract. In *Clark Construction Company v. Pena*, [164] the federal district court held that the contractor was entitled to such a mandatory injunction, compelling the Alabama Department of Transportation to award the contract to the protesting bidder. In that case, the FHWA had refused to concur in the award to the lowest responsible bidder, on the grounds that a traffic control note had been omitted from the approved plans and specifications. The court found that this was an immaterial omission, and was not grounds for rejecting all bids and readvertising.[165]

Because the granting of a mandatory injunction ordering the award of the contract is an extraordinary measure, the contractor must prove its entitlement to such relief, and such a remedy will ordinarily be granted only if the disappointed bidder can show that it is clear that it would have been awarded the contract "absent the flawed nature of the bidding process." [166] One federal court refused to order that remedy, choosing instead to defer to the agency's expertise and discretion and noting somewhat curtly, "This Court does not desire to become a GSA contracting officer."[167] In such a case, the proper remedy was rejection of all bids and readvertisement of the project.[168] In a California case, the court held that because the state has a statutory right to reject all bids, the lowest bidder does not have a right to compel award by writ of mandate.[169] However, the Louisiana Supreme Court has held that while a wronged bidder does not have a cause of action for damages due to the fact that there is no contract between it and the awarding agency, it may be entitled to injunctive relief, including an action to compel award of the contract to that bidder.[170]

Courts are more likely to order award of a contract in a case where the court has found that there have been violations of statute or bidding rules by the agency. The District of Columbia Circuit has held that the court may order the contract awarded to a particular bidder when it is clear that but for the illegal behavior of the agency, the contract would have been awarded to that bidder.[171] In another case, the First Circuit ordered that the agency award the contract to the next low bidder rather than readvertise the project.[172] The court held that the agency's violations of federal regulations required invalidation of the award. But for those violations, one of the other bidders would have obtained the award.[173] The court explained why it was ordering award to the next low bidder rather than re-solicitation: "To have a set of bids discarded after they are opened and each bidder has learned his competitor's price is a serious matter, and it should not be permitted except for cogent reasons."[174]

Where a statute authorizes injunctive relief, it may not necessarily entitle the unsuccessful bidder to any further relief beyond enjoining the execution of the contract. For example, an Alabama statute that allows an aggrieved bidder to bring an action to enjoin execution does not also entitle the bidder to damages.[175]

In addition to seeking injunctive relief, the bidder may also ask for declaratory relief or may bring a mandamus action against the agency. In a declaratory judgment action, the court would be asked to rule that the award to a bidder other than the low bidder was invalid, with essentially the same result—and the same standards applicable—as in an action for injunctive relief. However, in a mandamus action, the bidder may seek only an order directing the agency to carry out a ministerial function. Because the selection of the lowest responsible bidder involves the exercise of discretion, a mandamus action will ordinarily not lie.

Some courts have held that a low bidder has a property interest in the award of the contract, and is entitled to due process. This may be established by showing that it was actually awarded the contract and then subsequently deprived of the contract, or that the agency had limited discretion and that the bidder should have been awarded the contract.[176] Establishment of such an entitlement may further entitle the wronged bidder to a mandatory injunction.

vii. Requests to Invalidate Executed Contracts.—

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[162] B.F. Carvin Constr. Co. v. Jefferson Parish Council, 707 So. 2d 1326, 1327–28 (La. App. 5 Cir. 1998).

[163] Dick Enters. v. Metro/King County, 83 Wash. App. 566, 922 P.2d 184, 185–87 (1996).

[164] 930 F. Supp. 1470 (M.D. Ala. 1996).

[165] *Id*. at 1492.

[166] Ralvin Pacific Properties, Inc. v. United States, 871 F. Supp. 468, 475 (D.D.C. 1994).

[167] *Id*.

[168] *Id*.

[169] Rubino v. Lolli, 89 Cal. Rptr. 320, 321, 10 Cal. App. 3d 1059 (1970) (citing CAL. GOV'T. CODE § 14335, which provides that if acceptance of lowest responsible bid is not in best interest of state, agency may reject all bids and re-advertise).

[170] Webb Constr., Inc. v. City of Shreveport, 714 So. 2d 119, 122 (La. App. 2 Cir. 1998).

[171] Delta Data Systems Corp. v. Webster, 744 F.2d 197, 204 (D.C. Cir. 1984).

[172] Ulstein Maritime, Ltd. v. United States, 833 F.2d 1052 (1st Cir. 1987).

[173] *Id*. at 1058.

[174] *Id*. at 1058–59 (quoting International Graphics v. United States, 4. Cl. Ct. 515, 518 (1984)).

[175] Jenkins, Weber and Assocs. v. Hewitt, 565 So. 2d 616, 618 (Ala. 1990) (citing ALA. CODE §§ 41-16-1, 41-16-31, state procurement statutes).

[176] Cleveland Constr., Inc. v. Ohio Dep't of Admin. Services, 121 Ohio App. 3d 372, 700 N.E.2d 54, 69 (Ohio App. 1997).

Most courts have held that unless contract execution is enjoined, the disappointed bidder has no remedy; it must act to enjoin execution in order to preserve its opportunity to challenge the award to another bidder. However, some courts have held that the executed contract may be challenged by an unsuccessful bidder so long as that bidder does not delay its action. Otherwise, its action may be barred by laches. In *Western Sun Contractors Co. v. Superior Court*, the Arizona Court of Appeals held that a bidder's challenge was not barred by laches where it was not filed until the day after the contract was executed, but the bidder had sought reconsideration 2 days earlier.[177]

b. Withdrawal of Bids Before Bid Opening

Mistakes discovered prior to the opening of bids are easily handled. Standard specifications published by state highway and transportation agencies typically provide for withdrawal and revision of proposals, or filing of new ones, prior to the time and date scheduled for opening the bids. In some instances the right to correct the mistake and file a revised bid or new proposal is denied in order to avoid any appearance of collusion. In others, the contracting agency requires that if a bidder is granted the privilege of withdrawing its bid because of an alleged mistake, it may not file a revised bid or substitute a new bid in any subsequent round of bidding on that same contract.

Essentially, all procedures established for handling bid mistakes discovered before bid opening are designed to facilitate the withdrawal of erroneous bids, and thereafter, depending on the contracting agency's policy, to facilitate correction of the mistake or substitution of a new bid. In this process the main concern of the law is to maintain the integrity of the competitive bidding process and avoid the appearance of collusion or unfair advantage in any form.

c. Withdrawal of Bid After Bid Opening

While bidders in a competitive bidding process would appear to have a strong economic incentive to ensure that their bids are prepared carefully and submitted accurately, most state and municipal DOTs have experienced a bid mistake, that is, a request by a low bidder, subsequent to the opening of competitive bids but prior to the award of a contract, to be allowed to withdraw the bid without penalty because the bidder made a significant but purportedly unintentional error in preparing and submitting the bid and would incur significant financial hardship if compelled to enter into a contract based on the bid as submitted.

To err is human, and genuine errors do occur from time to time. Contractors' estimators may have multiple responsibilities with the firm, materials prices may be changing as the deadline for bid submissions approaches, and so forth. Forcing a contractor with a long track record of good perfomance to incur a major financial penalty due to a human error, a penalty which might affect the firm's viability in a highly competitive and difficult economy, is not necessarily in the public interest.

While public owners need to take such matters into consideration and grant relief where it can be shown to be genuinely jusitified, public owners need to exercise caution. In particular, when multiple bid error requests are received from the same firm or firms within a few months of each other, and when a review of agency bidding records reveals that the bidders involved compete against each other in the same geographic market, closer inquiry is warranted.

This is particularly the case when a certain pattern emerges. Such firms may accept contracts at very low prices whenever any firms from outside the area attempt to compete in the local market. When such firms are only bidding against each other, however, without any outside bidders participating, they may engage in a rotating pattern of bid errors in which members of the group repeatedly withdraw unusually low bids in favor of much higher second bids from other members of the group. The withdrawing firms may then turn up as subcontractors or material suppliers on each other's contracts. Under such circumstances, public owners have reasonable grounds for suspecting that the supposed bid errors may in fact be intentional and being made as part of a bid-rigging arrangement.

Public owners may have particular grounds for suspicion when some of the other bids submitted for a contract on which a request for bid withdrawal based upon a bid mistake is submitted appear to be unusually high, contain more rounded numbers than usual, or appear to have been prepared or signed in the same handwriting. Such indicators give public owners reasonable grounds for closer scrutiny into the possibility that losing firms have agreed to submit accommodation bids as part of a bid-rigging scheme. Submission of a very low bid with an intentional error allows the members of the group to be assured of having a sufficiently low price to claim the contract if outside competitors attempt to break into the local market, but otherwise to claim bid error, withdraw the lowest bid in favor of a higher bid by a member of the local group, and reward the withdrawing bidder by giving that firm a subcontract or material supply arrangement on the contract.

State or municipal DOTs or other public owners encountering such circumstances may wish to consult with the USDOT OIG or other appropriate investigative authorities about how to determine whether an apparent pattern is merely coincidental or an indicator of bid-rigging.

Assuming that no pattern of recurrent bid error claims has been identified and that circumstances instead indicate the likelihood that the claim of bidding error is genuine and advanced in good faith, the public owner must then examine the situation from a different perspective.

When a mistake is not discovered until bids have been opened, or where for other reasons a bid contain-

[177] 159 Ariz. 223, 766 P.2d 96, 100 (1988).

ing an error is not withdrawn prior to opening, the consequences are more serious. When bids are opened they are considered to be formally tendered offers, and each bidder is obligated to accept and perform a contract if it should be selected as the lowest responsible bidder. Moreover, the bid forms used by most public highway agencies contain specific statements by the bidder that it will accept a contract and execute it within a specified time if one is offered. Both by law and by contract, therefore, the bidder is obligated to stand by the offer it has made in its bid. Where relief is available to prevent excessive hardship from forcing a bidder to perform a contract based on a mistake, it comes through the courts' application of equitable principles and remedies to the claims of the parties involved.

In a few instances, special legislative procedures facilitate this recourse to equity. One illustration is provided by Wisconsin legislation relating to municipal public works contracting. Under this legislation, if a mistake is discovered and the contracting officer is notified prior to the bid opening, the erroneous bid is returned unopened to the bidder, with the restriction that it is not entitled to bid again on that contract unless it is readvertised. If, on the other hand, the mistake is discovered after bids are opened, the bidder who desires to withdraw must give notice of this fact without delay, and must produce evidence that its mistake was not caused by carelessness or lack of care in examining the project plans and specifications. In the event its bid bond or security deposit is forfeited, the statute provides that it may be recovered by proving to a court of competent jurisdiction that the mistake was not due to "carelessness, negligence, or inexcusable neglect."[178]

An Ohio Revised Code provision indicates that the agency may permit a bidder to withdraw a bid if it provides a written request together with a sworn statement of the grounds within 48 hours after bid opening. The bid must have been submitted in good faith, and the reason that the bid was substantially lower was a clerical mistake evident in the face of the bid, as opposed to a judgment mistake, and was actually due to arithmetic error or unintentional omission of a substantial quantity of work labor or material or material made in the compilation of the bid.[179] If the agency determines that the conditions for bid withdrawal have not been met, its director may award to the bidder, and if such bidder fails to enter into the contract and furnish a bond, he may declare the deposit check bid bond forfeit as liquidated damages and award the contract to the next lowest bidder.

California legislation for the relief of bid mistakes is similar to Wisconsin's law in its essential features and design. It denies the bidder any direct relief for an erroneous bid, and prohibits the bidder from any further bidding on the project on which the erroneous bid was made. But it authorizes court action for the recovery of forfeited security deposits upon proof that (1) a mistake was in fact made; (2) the contracting agency was notified in writing within 5 days after the opening of bids, with a detailed description of how the mistake occurred; (3) the mistake makes the bid materially different than was intended by the bidder; and (4) the mistake was made in preparing the bid form, and was not due to poor judgment, or carelessness in inspecting the work site or in reading the plans and specifications.[180]

d. Equitable Relief for Bid Mistakes

In litigation involving bid mistakes, the bidder's remedy generally is rescission of the bid, or the contract, if it has been awarded, or recovery of a forfeited bid security. Where action is brought by the contracting authority, it generally is for recovery on a surety bond posted as bid security. In these cases, the rights of the public agencies and private contractors are determined by the same principles of equity that apply to analogous situations involving private parties.

i. Reformation.—It is a general rule that the remedy of reformation of a bid or contract, frequently given to relieve against the consequences of a mutual mistake, will not be given to relieve against a unilateral mistake. The distinction between the two situations is said to be in the danger that in the latter case one of the parties would be forced into an agreement that was foreign to its intention. Rather, reformation is appropriate where the contract fails to express the intent of the parties as the result of a mutual mistake, or in the event of a unilateral mistake coupled with the inequitable conduct of the other party.[181]

In *Iversen Const. Corp. v. Palmyra-Macedon Central School District*, the court relied on Federal Court of Claims cases where the remedy of reformation had been extended beyond cases of mutual mistake to cases in which the agency knew or should have known of the error.[182] In that case, the bidder had made a clerical error of nearly $800,000 on a $5.5 million bid. Architects who were present at the bid opening had expressed surprise at the low bid, and had discussed the possibility of error. Later that day, the bidder discovered the error—one sheet of subbids had not been included in the total bid. The bidder immediately notified the architects and the school district of the error, submitted documentation of how the error occurred, and sought to withdraw its bid.[183]

The district did not respond, but rather several days later awarded the bid to Iversen, who again tried to withdraw its bid. The bidder then sought rescission. The court concluded that it was unconscionable to require the bidder to perform at the mistaken bid price.[184] The district responded asking for reformation of the contract. The court found that all prerequisites for equi-

[178] WIS. STAT. § 66.29(5) (1999).

[179] OHIO REV. CODE C 5525.01.

[180] CAL. PUB. CONT. CODE § 5103 (1999).

[181] Department of Transp. v. Ronlee, Inc., 518 So. 2d 1326, 1328 *review denied*, 528 So. 2d 1183 (Fla. App. 3 Dist. 1987).

[182] 539 N.Y.S.2d 858, 861, 143 Misc. 2d 36 (1989).

[183] 539 N.Y.S.2d at 859.

[184] *Id*. at 860.

table relief were met: (1) the mistake was of such consequence that enforcement of the contract would be unconscionable, (2) the mistake was material, (3) the mistake occurred despite the use of ordinary care, and (4) the other parties could be placed in the status quo.[185] In deciding between ordering rescission or reformation, the court found that reformation would place all parties in the status quo, because even the reformed bid was still the lowest bid. In addition to relying on federal cases, the court noted the rule that an agency cannot take advantage of an inaccurate bid if the agency is notified promptly of the mistake. Also the court noted that reformation gave the greatest benefit to the taxpayers, as it would allow the work to be done at the lowest cost.[186]

The prohibition against negotiating with bidders generally precludes reformation of the bid after bid opening, which would run contrary to the federal prohibition against negotiation on federal-aid contracts. Thus, it leaves the agency with the choice to permit the contractor to withdraw its bid and then proceed to the next bidder. In making the decision on whether to allow withdrawal of the bid without penalty, the agency will need to consider the magnitude of the error, its materiality to the construction project, and whether it was made in good faith. In unusual circumstances, a bidder may be allowed to correct its mistake after bid opening, or to reform its bid. However, a high standard of proof may be required by the agency in order for it to allow reformation, provided that it has the statutory ability to do so.[187] For example, if a bidder has made a mistake and the agency's conduct is determined to be inequitable, then the bidder may be entitled to reform the contract. However, in *Department of Transportation v. Ronlee, Inc.* the court described the standard that the bidder must meet in order to show that the agency's conduct was inequitable.[188] In that case, which involved bids for an interchange construction project, the second low bid exceeded the low bid by about 5 percent. Five days after bid opening, the low bidder advised the Department that it had made an error of about $300,000, or around 2 percent of its total bid price, due to an erroneous transcription of a unit price. The Department responded to the bidder that it was aware of the unbalanced price, but that it was unable to make a price adjustment. The bidder made no effort to withdraw its bid on the grounds of having made an error in its bid, but rather executed the contract and performed for 21 months.

In seeking additional compensation, the contractor then asserted that it was entitled to reform the contract to correct the erroneous unit price in its bid, on the grounds that the Department's conduct had been inequitable in that it had failed to inform the contractor of the error. However, the court held that the contractor waived any right that it had to either reformation or rescission when it had knowledge of its error 10 days prior to the start of construction, but chose to perform the contract rather than attempt to withdraw its bid.[189] Further, the court held that the Department's conduct was not inequitable when it failed to call the bidder's attention to its error, because the bidder discovered its own error at about the same time that the Department discovered it.[190]

ii. Rescission.—Rescission may be the appropriate remedy in the event of a bid mistake that is "so material and fundamental that it precluded a meeting of the minds necessary for the creation of a contract."[191] A significant number of cases in which relief has been granted for a unilateral mistake in bidding have evolved a general rule regarding the criteria for successful recourse to equity in such cases. The Maryland court in *City of Baltimore v. De Luca-Davis Construction Company* discussed this matter as follows:

The general rule as to the conditions precedent to rescission for unilateral mistakes may be summarized thus: 1, the mistake must be of such grave consequences that to enforce the contract as made or offered would be unconscionable; 2, the mistake must relate to a material feature of the contract; 3, the mistake must not have come about because of the violation of a positive legal duty or from culpable negligence; 4, the other party must be put in status quo to the extent that he suffers no serious prejudice except the loss of his bargain.[192]

In *De Luca-Davis*, the erroneous cost estimate resulted from copying unit prices incorrectly on the bidder's worksheets, and the contracting agency was notified of the mistake as soon as it was discovered at the bid opening. In addition, 5 days after the bid opening, a complete written explanation of the mistake was presented to the proper agencies of the city in support of a request for rescission of the bid and return of the bid deposit. Such prompt action by the bidder strengthened its claim for relief by forestalling action on the part of the contracting agency that would have been irreparable, and similar instances of early notification have been noted in other cases where rescission has been allowed.

In a leading California case, a majority of the court took the position that clerical errors in bid preparation did not come within the scope of the equitable rule denying relief. [193] The court said:

> There is a difference between mere mechanical or clerical errors made in tabulating or transcribing figures and er-

[185] *Id.*

[186] *Id.* at 861.

[187] McKnight Constr., Inc. v. Department of Defense, 85 F.3d, 565, 570 (11th Cir. 1996).

[188] 518 So. 2d at 1328.

[189] *Id.*

[190] *Id.*

[191] Naugatuck Valley Dev. Corp. v. Acmat Corp., 10 Conn. App. 414, 523 A.2d 924, 927 (1987) (citing Geremia v. Boyarski, 107 Conn. 387, 140 A. 749 (1928)).

[192] 210 Md. 518, 527, 124 A.2d 557, 562 (1956).

[193] M. F. Kemper Constr. Co. v. City of L.A., 37 Cal. 2d 696, 235 P.2d 7 (1951).

> rors of judgment, as, for example, understanding the cost of labor or materials. The distinction between the two types of error is recognized in the cases allowing rescission and in the procedures provided by the state and federal governments for relieving contractors from mistakes in bids on public work…Generally relief is refused for error in judgment and allowed only for clerical or mathematical mistakes…Where a person is denied relief because of an error in judgment, the agreement which is enforced is the one he intended to make, whereas if he is denied relief from a clerical error, he is forced to perform an agreement he had no intention of making.194

A dissenting opinion in this case presented the opposing view of the effects of mistakes in this way:

> When it is necessary for a person to make calculations or estimates, in order to determine the sum which he will bid for an offered contract, or to determine the cost to him of a proposed contract, or whether or not it will be advantageous to him to enter into it, he must assume the risk of any error or oversight in his computations, and cannot have relief in equity on the ground of mistake, if he reaches a wrong conclusion through inadvertence, misunderstanding of that which is plain on its face, or mathematical error.195

Among the other criteria for granting equitable relief from the penalties of a unilateral bid mistake, the courts have frequently stressed the requirement that the error must relate to a material feature of the contract, and must be of such magnitude or character as to make enforcement of the offer or contract unconscionable.[196] This requirement generally is found in conjunction with the corollary rule that equity will not allow withdrawal of an erroneous bid or return of a forfeited security deposit unless it appears that reasonable diligence and care were used in preparing the bid, and that the contracting agency will suffer no serious injury, except the loss of its original contract.

These propositions reflect the concern of equity for the essential qualities of fairness and realism in judging the bidder's claim for relief. Diligence and care in preparing bids are essential to success in claiming equitable relief, but they are requirements that must be applied in the light of each bidder's circumstances. For example, errors in calculating the expenses of excavation were considered in the light of evidence that when the bidder's representatives visited the construction site, they were misled by old right-of-way stakes and flags, which suggested the highway was to be built through loose dirt rather than through a rocky area that was the correct route.[197] Clerical errors, such as omitting digits or decimal points, are recognized as likely to occur in spite of diligent efforts to prevent such errors, and so are not automatically equated with negligence. If the circumstances include factors that reasonable persons would expect to make the bidding process more difficult or increase the chance of error, the standard of care to which bidders must conform reflects this fact.[198]

"Negligence" or its equivalent lack of care in bid preparation, as this concept is applied to claims for equitable relief for bid mistakes, means carelessness that exceeds the tolerance that the business and governmental community typically allow themselves in carrying on their own affairs. Reasonably understandable failure to calculate or present bid information correctly and completely will not bar equitable relief unless obvious carelessness or lack of good faith are present. When claims of mistake suggest that either carelessness or lack of good faith are present, the bidder is considered as having violated its duty to compete in good faith, and its claim to equitable relief generally is fatally weakened.

In *Puget Sound Painters v. State*, [199] the bidder underestimated the area of bridge towers to be painted by about half. The court held that it would be entitled to equitable relief if it acted in good faith and without gross negligence; was reasonably prompt in giving notice to the agency of the error in its bid; would suffer substantial detriment by forfeiture of its bid bond; and if the agency's status was not greatly changed.[200]

In a much more recent Colorado case, *Powder Horn Constructors v. City of Florence*, the court also imposed a good faith standard in limiting the requirement that the bidder prove that its error was not negligent.[201] In that case, Powder Horn Constructors was the low bidder on a water treatment facility. The day after bid opening, the City's project engineer noticed that one bid item was substantially lower than the same item in the other bids, and notified Powder Horn, suggesting that it review that item. The following day, Powder Horn informed the project engineer that it had mistakenly omitted the cost of one major item in that bid item, at a cost of $66,000, or about 10 percent of its bid. Powder Horn also submitted a letter to the engineer, stating that a subtotal from one worksheet had been inadvertently omitted from the final bid amount, and advised the engineer that the bid and bid security were being withdrawn.[202]

However, the city council voted to award the contract to Powder Horn anyway, which then refused to accept the award. The City then awarded to the second low bidder. The City sued Powder Horn and its surety, asserting that they were entitled to the amount of the bid bond as liquidated damages, to partially compensate the City for the difference between Powder Horn's bid and the second low bid.[203]

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[194] *Id.* 235 P.2d at 11–12.

[195] *Id.* at 14, citing BLACK, ON RESCISSION & CANCELLATION, § 142.

[196] *See* Department of Transp. v. American Ins. Co., 491 S.E.2d 328, 331 *reconsideration denied* (Ga. 1997).

[197] State By and Through its Road Comm'n v. Union Constr. Co., 9 Utah 2d 107, 339 P.2d 421 (1959).

[198] M. F. Kemper Constr. Co. v. City of L.A., 37 Cal. 2d 696, 235 P.2d 7, 11 (1951).

[199] 45 Wash. 2d 819, 278 P.2d 302, 304 (1954).

[200] *Id*.

[201] 754 P.2d 356 (Colo. 1988).

[202] *Id*. at 358.

[203] *Id*.

The trial court had found that Powder Horn did not exercise reasonable care in preparing its bid, and that it was liable to the City in the amount of its bid bond. However, the court also found that there had been a unilateral material mistake, that requiring Powder Horn to perform the contract would be unconscionable, and that the City was not prejudiced by the withdrawal of the bid. However, the court found that Powder Horn's negligence prevented rescission of its bid. The Court of Appeals affirmed.[204]

The Colorado Supreme Court reversed, disagreeing with the lower courts that the right of rescission could be conditioned on the exercise of reasonable care by the bidder in these circumstances.[205] The court noted the distinction between mathematical or clerical errors and errors of judgment, pointing out that it was undisputed that the error in this case was clerical and not an error of judgment. The court noted the policies underlying the requirement to prove an absence of negligence, including protection of the integrity of the bidding process, fostering consistency in bid preparation, and discouraging fraud and collusion. But the court distinguished the case in which the mistake is discovered prior to award:

> However, requiring a bidder to demonstrate freedom from negligent conduct when the bid has not been accepted and the bid contains a mechanical error, as distinguished from an error of judgment, will significantly restrict the availability of this equitable remedy in circumstances wherein recognition of the remedy would not undermine those policies.[206]

The court pointed out that the term "mistake" necessarily implies some degree of negligence, and that it would be extremely difficult to prove that the mistake was both material and that it was non-negligent. Rather, the court chose to impose a standard of whether the bidder made an honest or good faith mistake, and to consider "gross or extreme negligence" as evidence of the bidder's lack of good faith.[207] Therefore, the court allowed rescission, without forfeiture of the bid bond, where the bidder's mistake was made in good faith and the public agency did not rely to its detriment on the mistaken bid.[208]

In considering a choice between a standard of simple negligence or gross negligence, the Connecticut court chose to adopt neither. Rather, the court held only that the degree of negligence involved was an equitable factor to be considered by the agency, and ultimately by the court, in determining whether the bidder could withdraw without forfeiting its bond. In that case, *Naugatuck Valley Devel. Corp. v. Acmat Corp.*,[209] the agency had been awarded liquidated damages in the amount of the bid bond because of the bidder's failure to execute the contract. The bidder had become aware of a mistake in its bid 14 days after bid opening, but had notified the agency at that time. The bidder wanted to negotiate with the agency, but the agency was precluded from doing so. In trying the issue of liquidated damages, the trial court required the bidder to prove that its mistake was free from negligence in order to avoid the damages. The appellate court reversed, holding that whether the bidder was entitled to relief for its mistake was based on equitable principles, and that the bidder's degree of negligence was one equitable factor to be considered.[210]

The duty to deal in good faith is, of course, as binding on the contracting agency as on the bidder. Where a bid clearly discloses that in all probability it contains a mistake, the contracting agency is charged with that knowledge. Later, if it is shown that a mistake in fact has occurred, the agency may not take advantage of the bidder by acting in reliance on a bid when there is evidence or suspicion of error.[211] "An offeree 'will not be permitted to snap up an offer that is too good to be true; no agreement based on such an offer can…be enforced by the acceptor.'"[212]

Warning that a mistake has been made may be given by any evidence that under the circumstances is recognizable by the bidder or contracting agency as an error. In particular, it may be shown by an unusually great disparity of one bid in comparison with others.[213] For example, in a Minnesota case, the contracting officer noted a discrepancy in bids for a moving contract in that the other bids were three to four times the amount of the low bid. The officer contracted the bidder to inquire whether it intended the bid that it submitted, and the bidder confirmed its confidence in its bid.[214] The court refused to allow equitable relief for the bid mistake, stating that where the bidder is a professional in its field, it is reasonable for the agency to rely on the bid, particularly after the agency has called the bidder's attention to a possible error and has been reassured that that was the bid intended.[215]

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[204] City of Florence v. Powder Horn Constructors, Inc., 716 P.2d 143 (Colo. App. 1985).

[205] Powder Horn Constructors, Inc. v. City of Florence, 754 P.2d 356 (Colo. 1988).

[206] *Id*. at 361.

[207] *Id*. at 362.

[208] Although the agency had awarded the contract to Powder Horn, it did so with full knowledge of the mistaken bid and could not be said to have relied to its detriment on the mistake. *Id*. at 361.

[209] 10 Conn. App. 414, 523 A.2d 924 (1987).

[210] *Id.* 523 A.2d at 927.

[211] *But see* Department of Transp. v. Ronlee, Inc., 518 So. 2d 1326, 1329, *review denied*, 528 So. 2d 1183 (Fla. App. 3 Dist. 1987) (agency's failure to call to bidder's attention a 2 percent error in calculations, where bidder learned of error shortly after agency did, was not fraud or inequitable conduct that would entitle bidder to reformation).

[212] A.A. Metcalf Moving & Storage Co. v. North St. Paul Sch. Dist., 587 N.W.2d 311, 318 (Minn. App. 1998) (quoting Speckel by Speckel v. Perkins, 364 N.W.2d 890, 893 (Minn. App. (1985)).

[213] *See* Powder Horn Constructors, 754 P.2d at 358.

[214] A.A. Metcalf, 387 N.W.2d at 314.

[215] *Id*. at 318.

e. Bid Security Forfeiture and Exoneration

Bidding instructions that purport to prohibit or restrict withdrawal of bids have been construed as inapplicable to situations involving an honest unilateral mistake. In the same manner, courts have given similar construction to statements providing for forfeiture of deposits or surety bonds serving as security to assure execution of contracts. Because state laws and regulations require bid security in terms of a percentage of the total amount of the bid, the security deposit may represent a substantial amount of money, which a bidder cannot afford to lose. Much of the litigation over bid mistakes, therefore, is concerned with imposition of forfeiture of defaulted deposits, or attempted return of a security deposit following bid withdrawal.

Where a bid mistake is remediable by withdrawal of the bid, and the contracting agency is promptly notified of the error, equity will order return of the security deposit or cancellation of the bid bond. These results are based partly on the policy that once the contracting agency is aware of a bid error, it is unjust to take advantage of this situation and impose a forfeiture, and partly because after the bid is withdrawn the reason for the security ceases to exist.

Where there is a mistake in a bid such that the bidder will be permitted to withdraw its bid, it must be a mistake that either directly affects the price or that makes the bid materially different from that which was intended by the bidder. In a typical case where the reasoning supports equitable recovery or cancellation of bid security, notice of the mistake is received by the contracting agency before it accepts the erroneous bid. Frequently the discovery is made and notice given before the bid opening. Failure to give notice to the contracting agency before acceptance of an erroneous bid weakens the case for return of bid security, but forfeiture of security is not always the result in these situations. If a bidder notifies the agency after the agency's acceptance of its offer, but before a contract has been signed, and before there is any change in position in reliance on the erroneous bid, it may be successful in obtaining return of its deposit or cancellation of its bid bond.

In a unique case from New York, NYSDOT rejected the contractor's claim for "honest error," and when the contractor refused to execute the contract, NYSDOT contemplated an action to recover the amount of the bid bond. The contractor's error was not deemed to be of such a magnitude to cause irreparable financial harm. NYSDOT's decision was later reversed for failing to file its procedures pursuant to the State Administrative Procedures Act.[216]

State statute, however, may prohibit the court from granting equitable relief in the case of a bid mistake. Oklahoma's statute provides that the bid bond "shall" be forfeited if the apparent low bidder does not execute the contract. Even where the contractor brought the mistake to the agency's attention prior to contract award, the court held that the trial court lacked the equitable power to prevent forfeiture of the bid bond in light of the mandatory statutory language.[217]

Often a decisive factor in determining recovery of bid security is whether the contracting party has acted in reliance on the bidder's mistake. In the great majority of cases where equitable relief was requested, bid security was not recovered if the mistake was not discovered or reported until after the agency had made a contract award. Yet, occasionally there are circumstances in which bid mistakes are not discovered and reported until after contract award, and because no culpable negligence is chargeable to it, the bidder is permitted to recover its bid security. An older Kentucky case, *Board of Regents of Murray State Normal School v. Cole*, illustrates the required combination of circumstances.[218] In that case, the agency had inquired about a possible mistake at the time of bid opening, and the bidder verified its bid as correct. Relying on this assurance, the agency awarded that bidder the contract, only to have the bidder discover its mistake shortly thereafter. The court granted relief to the bidder. However, it did not apply the doctrine that an executory contract can be canceled when it is entered into with a unilateral mistake on a material point and without culpable negligence. Rather, the court chose to treat the matter as a rescission of the contract. The parties were restored to their original positions as nearly as possible by the return of the bidder's deposit, and payment by the bidder of the contracting agency's actual expenses of readvertising the project for new bids.

If the bidder chooses not to exercise its option to rescind its bid and re-attain its bid bond, it will not be entitled to reform the contract once it is executed.[219] Absent mutual mistake, the court will not reform the contract.[220]

f. Damages for Erroneous Rejection of Bid

Some states' courts have held that a disappointed bidder has no cause of action for damages against the awarding agency, even if the contract was wrongly awarded.[221] These courts have based their conclusions on the fact that the fundamental policy underlying pub-

[216] Matter of J.D. Posillico, Inc. v. Dep't of Transp. of the State of New York, 160 A.D. 2d 1113; 553 N.Y.S.2d 903 (1990).

[217] J.D. Graham Constr., Inc. v. Pryor Public Sch. Indep. Sch. Dist. No. 1, Mayes County, 854 P.2d 917, 920, *cert. denied* (Ok. App. 1993) (statute stated that bid bond "shall" be forfeited if bidder does not execute contract); 61 OKLA. STAT. ANN. § 107(B).

[218] 209 Ky. 761, 273 S.W. 508 (1925).

[219] Midway Excavators, Inc. v. Chandler, 128 N.H. 654, 522 A.2d 982, 984 (1986).

[220] *Id*.

[221] C.N. Robinson Lighting Supply Co. v. Board of Educ. of Howard County, 90 Md. App. 515, 602 A.2d 195, 200, *cert. denied*, 326 Md. 662, 607 A.2d 7 (1992); BBG Group, L.L.C. v. City of Monroe, 96 Wash. App. 517, 521, 982 P.2d 1176 (1999); Debcon, Inc. v. City of Glasgo, 28 P.3d 478, 485 (Mont. 2001) (citing cases from numerous jurisdictions that hold that aggrieved bidder cannot recover lost profits or other expectancy damages under negligence theory).

lic bidding laws is protection of the public interest, and not protection of contractors. At the same time, other courts have recognized that a bidder may be entitled to its bid preparation costs in the event that it is unfairly denied award of the contract. A smaller number have allowed additional damages for the aggrieved low bidder.

Generally, whether the court will consider the award of either bid preparation costs or lost profits depends on the bidder's diligence in seeking to enjoin the contract award or execution. A Maryland court held that it was not inequitable to find that the bidder has no cause of action for damages where it did not seek an injunction.

A timely challenge is compatible with the public interest since it serves to force compliance with the purpose of the bidding procedure. After the project is completed, however, it is difficult to perceive how the public interest is served by investing the low bidder with a cause of action for damages. The public has already paid for the difference between the lowest bid and the bid which was accepted. The taxpayer should not be further penalized.[222]

i. Bid preparation costs.—Recovery of bid preparation costs may be an appropriate remedy when a frustrated bidder proves that it should have been awarded the contract.[223] The Georgia Supreme Court has held that where a governmental entity has frustrated the bid process and awarded the contract to an unqualified bidder, the bidder whose bid was unfairly rejected is entitled to its reasonable bid preparation costs.[224] The court found that lost profits would unduly penalize the taxpayers, while compensating the bidder for effort that it did not make and risks that it did not take.[225] Awarding bid preparations costs was also found to be the appropriate remedy in *Bolander & Sons Co. v City of Minneapolis*, in which the work under the contract had already begun by the time the unsuccessful bidder prevailed in its challenge to the award of the contract to another bidder.[226] The bidder in that case was also awarded its attorney fees incurred in bringing the bid protest.[227] However, the bidder must show that the rejection of its bid was improper and that the agency's conduct was arbitrary and capricious or in bad faith.[228] Federal courts have held that in order to be awarded bid preparation costs, the bidder must show that the agency violated its "implied contract to have the involved bids fairly and honestly considered."[229] The court further quoted:

Proposal preparation expenses are a cost of doing business that normally are "lost" when the effort to obtain the contract does not bear fruit. In an appropriate case, however, a losing competitor may recover the costs of preparing its unsuccessful proposal if it can establish that the Government's consideration of the proposals submitted was arbitrary or capricious. The standards that permit a disappointed competitor to recover proposal preparation expenses are high and the burden of proof is heavy.[230]

The court went on to further explain what criteria might be used to determine if the government has acted arbitrarily or capriciously in evaluating bids:

One is that subjective bad faith on the part of the procuring officials, depriving a bidder of the fair and honest consideration of his proposal, normally warrants recovery of bid preparation costs. A second is that proof that there was "no reasonable basis" for the administration decision will also suffice, at least in many situations. The third is that the degree of proof of error necessary for recovery is ordinarily related to the amount of discretion entrusted to the procurement officials by applicable statutes and regulations. The fourth is that proven violation of pertinent statutes or regulations can, but need not necessarily be a ground for recovery.[231]

Alabama's public works statutes specifically authorize the award of bid preparation costs when an aggrieved bidder successfully challenges the award of a contract as being contrary to public bidding laws and obtains an injunction, so long as the action is brought within 45 days of award.[232]

ii. Lost Profits.—Ordinarily, even if a disappointed bidder's challenge to the agency's award is successful, it may not recover money damages.[233] The Washington Supreme Court has held that awarding damages to a disappointed low bidder inherently conflicts with the primary purpose of competitive bidding, which is pro-

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[222] Robinson, *supra* note 221, at 200 (quoting Gulf Oil Corp. v. Clark Co., 94 Nev. 116, 575 P.2d 1332, 1334 (1978).

[223] Credle v. East Bay Holding Co., 263 Ga. 907, 440 S.E.2d 20, 21 (1994).

[224] City of Atlanta v. J.A. Jones Constr. Co., 260 Ga. 658, 398 S.E.2d 369, 371, *on remand*, 198 Ga. App. 345, 402 S.E.2d 554 (1990), *cert. denied*, 111 S. Ct. 2042 (of two possible remedies, lost profits or bid preparation costs, the award of bid preparation costs is the better alternative).

[225] *Id*.

[226] 438 N.W.2d 735, 738, *review granted, affirmed*, 451 N.W.2d 204 (1989).

[227] *Id.* 438 N.W.2d at 738. The Federal Equal Access to Justice Act (EAJA), 28 U.S.C. § 2412, may also provide a basis for attorney fees. Taylor Group, Inc. v. Johnson, 915 F. Supp. 295, 297–98 (M.D. Ala. 1995) (contractor was "prevailing party" for purposes of EAJA where it obtained relief on the merits of its claims both in the issuance of a temporary restraining order that prohibited award to the bidder's rival and in obtaining a subsequent settlement with the agency).

[228] E.W. Bliss Co. v. United States, 77 F.3d 445 (Fed. Cir. 1996).

[229] *Id*. at 447 (citation omitted).

[230] *Id*. (Quoting Lincoln Servs., Ltd. v. United States, 678 F.2d 157, 158, 230 Ct. Cl. 416 (1982)).

[231] *Id*. (Quoting Keco Industries v. United States, 492 F.2d 1200, 1204 (1974) (citations omitted)).

[232] ALA. CODE 39-5-4 (2002).

[233] Delta Chemical Corp. v. Ocean County Utilities Auth., 250 N.J. Super. 395, 594 A.2d 1343, 1346 (1991); Ralph L. Wadsworth Constr. Co. v. Salt Lake County, 818 P.2d 600, 602, *cert. denied*, 832 P.2d 476 (1991).

tecting public funds.[234] The court also held that the rejected low bidder's opportunity to obtain an injunction allows the bidder some recourse while still being within the bounds of protecting both the bidder's and the public's mutual interests in the competitive bidding process.[235] In addition, in the Peerless Food Case the Washington court held that because there is no contract between the aggrieved bidder and the agency, the bidder is not entitled to damages.[236] Similarly, Arkansas's courts have held that a bidder's remedy is limited to enjoining award of the contract or termination of a wrongfully awarded contract.[237]

However, the New Hampshire Supreme Court has held that where a disappointed low bidder has complied with all of the requirements of the invitation for bids, but was denied award of the contract through conduct of the awarding agency that amounts to bad faith, then it may be entitled to recover its lost profits.[238] Similarly, Mississippi's Supreme Court has held that compensatory damages under the law of contracts are the proper measure of damages for an aggrieved bidder that was entitled to the contract award.[239] Montana has also recognized that in the event of bad faith or negligence on the part of the agency, a wronged bidder may be entitled to relief beyond invalidation of the contract.[240] However, in a later case, the Montana court held that an aggrieved bidder may not recover lost profits or other expectancy damages under a negligence theory.[241]

Where courts have awarded lost profits as the measure of damages for wrongful bid rejection, they have done so after a finding of bad faith on the part of the contracting agency. In *Peabody Construction Company v. City of Boston*, the court found that the bidder had complied with all of the requirements in the invitation for bids, and that its bid was rejected through agency conduct that amounted to bad faith.[242] The appropriate measure of damages was held to be the profit that the bidder would have earned on that job.

iii. Section 1983 Damages.—Failing to recover anticipated profits when their bids are wrongfully rejected, some contractors have attempted to recover damages under the Civil Rights Act, 42 U.S.C. § 1983. Where a state statute requires that a bid be awarded to the lowest responsible bidder, some courts have found that the lowest responsible bidder has a constitutionally protected interest in obtaining an award of the contract.[243] Based on this, the aggrieved bidder may seek damages against the contracting agency for the violation of its constitutional right to obtain the award. However, federal courts have set a similar standard for obtaining damages in the public contract setting as for other types of violations. In order to be eligible to pursue damages under Section 1983, a contractor must show not only a deprivation of rights, but also an inability to obtain a remedy in state court. Where state law provides for some review of the state agency's action, a bidder is unlikely to be successful in pursuing damages under § 1983.[244]

In order to establish a claim under § 1983, the bidder must show that the agency acted under color of state law to deprive the bidder of a right protected by the United States Constitution.[245] In public contracting, the bidder must establish that it had a legitimate claim of entitlement to the award of the contract by showing that it was actually awarded the contract at any procedural stage, or that the applicable rules limit the discretion of the agency officials as to whom the contract should be awarded.[246] The right to reject any and all bids usually confers enough discretion on the agency that this standard is difficult to meet. However, even the power to reject all bids does not allow the agency to act arbitrarily.[247]

In a Sixth Circuit case that illustrates the effect of agency discretion, the bidder was notified that it was the lowest responsible bidder, but that it would be expected to sign the project labor agreement required for the project that it had not yet signed.[248] The bidder re-

[234] Peerless Food Products, Inc. v. State, 119 Wash. 2d 584, 835 P.2d 1012 (1992) (bid is offer rather than acceptance of contract; therefore there is no cause of action for damages); Dick Enterprises v. Metro/King County, 83 Wa. App. 566, 922 P.2d 184 (1996).

[235] Dick Enterprises, *supra* note 234, at 185.

[236] Peerless, *supra* note 234, 835 P.2d at 1016.

[237] Milligan v. Burrow, 52 Ark. App. 20, 914 S.W.2d 763, 765 (1996) (based on state's sovereign immunity).

[238] Marbucco Corp. v. City of Manchester, 137 N.H. 629, 632 A.2d 522, 525 (1993).

[239] City of Durant v. Laws Constr. Co., 721 So. 2d 598, 606 (Miss. 1998).

[240] ICS Distributors, Inc. v. Trevor, 903 P.2d 170 (Mont. 1995).

[241] Debcon, Inc. v. City of Glasgow, 28 P.3d 478, 485 (Mont. 2001).

[242] 28 Mass. App. Ct. 100, 546 N.E.2d 898, 902 (1989).

[243] *See* Cleveland Constr., Inc. v. Ohio Dep't of Admin. Services, 121 Ohio App. 3d 372, 700 N.E.2d 54, 69 (1997). Pataula Elec. Membership Corp. v. Whitworth, 951 F.2d 1238, 1241 (11th Cir. 1992), *rehearing denied*, Georgia Power Co. v. Pataula Elec. Membership Corp., 506 U.S. 907, *appeal after remand*, Flint Elec. Membership Corp. v. Whitworth, 68 F.3d 1309, *opinion modified*, 77 F.3d 1321 (11th Cir. 1996) (Georgia law requires award to lowest responsible bidder).

[244] State ex rel. Educ. Assessments Systems, Inc. v. Cooperative Educ. Services of N.M., Inc., 115 N.M 196, 848 P.2d 1123, 1130 (1993) (although procurement code does not provide for damages it does provide adequate legal remedy by providing for protest and for appealable determination of protest); Church & Tower, Inc. v. Miami-Dade County, Florida, 11 F. Supp. 2d 1376, 1379 (S.D. Fla. 1998) (neither debarment nor city's refusal to consider bidder's bid pending investigation violated due process where there was an adequate procedure for disappointed bidders to challenge debarment procedure and each bid refusal by appeal to state court).

[245] Enertech Elec., Inc. v. Mahoning County Comm'rs, 85 F.3d 257, 259, 260 (6th Cir. 1996).

[246] Cleveland Constr., Inc., *supra* note 243, at 69.

[247] Pataula, *supra* note 243, at 1243.

[248] Enertech Elec., Inc., *supra* note 245, at 259.

fused to sign the project labor agreement, and its bid was then rejected. The court held that where the county had the ability to award to the "lowest and best bidder," and the county required a project labor agreement that the bidder refused to sign, the county had acted within its discretion and had not violated the bidder's constitutional rights.

In addition to alleging a property interest in the award of the contract, a bidder may allege a property interest in its prequalification to bid. In *Systems Contractors Corp. v. Orleans Parish School Board*, the bidder sought Section 1983 damages for its disqualification from bidding on a particular project and its debarment from bidding on future projects.[249] The bidder had been given written notice of its disqualification and debarment, but not prior to bid opening. The bidder was then given an opportunity to present its case directly to the agency. It then had the option of appealing the agency decision to an arbitrator. The court held that the bidder was not entitled to written notice of the disqualification and debarment prior to bid opening, and that the opportunity to appeal to the agency and to an arbitrator provided an adequate post-deprivation remedy sufficient to defeat a claim for § 1983 damages.[250]

In other cases, the contractor's claim under § 1983 has involved the contractor's contention that its right to free speech was violated by the contracting agency. In *Progressive Transportation Services v. County of Essex*, the court held that there was no First Amendment violation where the speech at issue was based on the contractor's own personal interest and did not involve issues of public concern.[251] Thus the contractor was not entitled to damages under § 1983 for its retaliation claim. However, the United States Supreme Court has held that the free speech rights held by individuals under the First Amendment also apply to government contractors. In *O'Hare Truck Service v. Northlake*, the contractor alleged that it was removed from the City's rotating list of towing contractors for political reasons because it had refused to contribute to the mayor's reelection campaign, and that it was being denied the opportunity to bid on city contracts.[252] The Court held that the contractor's allegations stated a cause of action under § 1983.[253]

Please note also the further discussion of §1983 issues in section 3(A)(8), below.

iv. Other Remedies.—In Louisiana, a frustrated bidder sued the successful bidder, alleging that the successful bidder had assisted in or encouraged a wrongful act in violation of a state statute that created liability for such actions.[254] The court upheld the validity of the award, and held that the same statute would apply to the consulting engineer retained by the agency, who allegedly conspired with the agency and the successful bidder who wrongfully obtained the contract.[255] The Federal False Claim Act may provide a similar remedy where the unsuccessful bidder alleges that the successful bidder has obtained the contract through false statements in its bid.[256]

The Eighth Circuit ruled that a contractor could be entitled to damages from its subcontractor for the subcontractor's bid errors that were used by the prime contractor in preparing its bid, based on a state law theory of implied warranty.[257]

Even where the bidder was awarded a contract under specifications later determined in a bid protest to have been illegal, it was not entitled to damages in a New Jersey case.[258] The court ordered that because of the illegal specifications, the contract had to be readvertised. The bidder submitted another bid, but was not the low bidder in the second round of bids. However, this was not a basis for damages. Similarly, in *Percy J. Matherne Contractor v. Grinnell Fire Protection Systems Company*, the prime contractor was allowed to recover from the subcontractor for the increased cost of substituting another subcontractor, where it relied to its detriment on the subcontractor's bid in submitting its bid.[259]

g. Innovations in Bid Challenges and Protests: Section 1983 Litigation

Several state transportation agencies have been subject to new legal challenges involving contractors who have initiated civil rights litigation under 42 U.S.C. § 1983.

There are reasons why contractors' attorneys might elect to file civil rights litigation under § 1983 rather than raising bid challenge or protest issues through other forms of litigation, such as state-court proceedings to challenge state agency decisions as arbitrary, capricious, an abuse of discretion, or in excess of statutory authority. The statute of limitations on § 1983 actions may be longer that the statutes of limitation for such state proceedings. Attorneys' fees and costs may also be available to counsel for winning plaintiffs in § 1983 actions, but not in such state court proceedings.

[249] 148 F.3d 571 (5th Cir. 1998).

[250] *Id*. at 575. Although state law provided for additional procedural steps such as written notification prior to award and retention of records of the disqualification hearing, these were not required by the United States Constitution. *Id*.

[251] 999 F. Supp. 701 (N.D. N.Y. 1998).

[252] 518 U.S. 712, 116 S. Ct. 2353, 135 L. Ed. 2d 874 (1996).

[253] *Id.* 518 U.S. at 720. The Court also pointed out that had the mayor solicited contributions as a *quid pro quo* for not terminating the contractor or for keeping the contractor on the City's list, the mayor may have violated state bribery statutes. *Id*. at 721.

[254] Enerland Recovery Services, Inc. v. Parish of Lafourche, 619 So. 2d 129, 134 (La. App. 1 Cir. 1993).

[255] *Id*. at 134.

[256] United States ex rel. Alexander v. Dyncorp, Inc., 924 F. Supp. 292, 298 (D.D.C. 1996).

[257] C.L. Maddox, Inc. v. Benham Group, Inc., 88 F.3d 592, 600 (8th Cir. 1996).

[258] Morie Energy Management, Inc. v. Badame, 575 A.2d 885, 888, 241 N.J. Super. 572 (N.J. Super. A.D. 1990).

[259] 915 F. Supp. 818, 825–26 (E.D. La. 1995).

Noteworthy is the case of *Glover v. Mabrey*[260] involving Glover Construction Co. Inc. and six officials of ODOT. The complaint alleged violations of the contractor's First and Fourteenth Amendment rights. Glover had been in a dispute concerning the construction of Oklahoma Highway 64 where he encountered major problems. ODOT blamed Glover's poor workmanship and use of improper materials, while Glover blamed ODOT's design. ODOT allegedly revoked Glover's prequalification status while an injunction was in place. Glover asserted retaliation for the exercise of his First Amendment right to free speech and Fourteenth Amendment right to due process and equal protection.

The U.S. Court of Appeals of the Tenth Circuit affirmed a lower court decision that denied defendants' motion to dismiss and their claim of qualified immunity, on the grounds that Glover's complaint sufficiently alleged that ODOT employees wrote or adopted a recommendation that Glover be denied its prequalified bidder status in retaliation for its public criticism of the Highway 61 design, in violation of the First Amendment. The court dismissed the remaining allegations because the complaint failed to state claims for which relief might be granted. [261] Subsequently, Glover filed a third amended complaint under 42 U.S.C.§ 1983, alleging further retaliation against Glover for his efforts to adjudicate his claims and numerous other issues. Subsequently, the contractor elected not to pursue the action.

Similarly, NYSDOT has also been subjected to 42 U.S.C. § 1983 litigation in *Marinaccio, Sr., Accadia Contracting, Inc v. Joseph Boardman, et al. as employees of New York State DOT*.[262] In this case, the contractor commenced litigation under 42 U.S.C. § 1983 claiming violations of a contractor's First Amendment rights to free speech and association and for tortious interference with business relationships. The contractor, Mr. Marinaccio, asserted that the defendant state employees violated his rights to free speech and association under the First Amendment when they conditioned the award of a contract on barring Mr. Marinaccio from communication with DOT employees and consultants. The jury found for plaintiff that the state employee violated his First Amendment rights, but also found that the state employees were entitled to qualified immunity. In addition, the jury returned a verdict in favor of defendants on the tortious interference claim. The contractor appealed from the jury verdict, and the court denied plaintiff's motion for judgment as a matter of law and motions for a new trial.

These cases provide illustrative examples of how lengthy and time-consuming § 1983 litigation can be.

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[260] Glover v. Mabrey, 384 Fed. Appx. 763 (10th Cir. 2010).

[261] *Id.*

[262] Paul Marinaccio, Sr., et al. v. Joseph H. Boardman et Joseph H. Boardman et al., 2007 U.S. Dist. LEXIS 16088 (N.D.N.Y. 2007).

SECTION 4

DISADVANTAGED BUSINESS AND LABOR REQUIREMENTS

A. MINORITY AND DISADVANTAGED BUSINESS ENTERPRISE REQUIREMENTS

1. Federal-Aid Transportation Projects: EEO and DBE Requirements Under Statutes and Regulations [1]

a. Requirements of USDOT DBE Regulations, 49 C.F.R. Part 26

In reviewing the following summaries of the requirements of the USDOT DBE regulations, it should be borne in mind that these are brief summaries of lengthy and often complex provisions, intended to provide an accessible introduction for a general readership. Any practitioners engaged in handling matters governed by these regulations would be well advised to go beyond these introductory summaries and review the regulations carefully.

i. 49 C.F.R. Part 18, Relevant Requirements.—While the bulk of USDOT DBE requirements are set forth in 49 C.F.R. Part 26, significant requirements are also set forth in 49 C.F.R. Part 18, particularly in 49 C.F.R. § 18.36, which governs procurement on federal-aid transportation projects. This requires state DOT contracts for federal-aid projects to include all clauses required by federal statutes and executive orders and their implementing regulations.[2] It also requires state DOTs to maintain a contract administration system which ensures that contractors perform in accordance with contract terms and conditions.[3] This regulation requires state DOTs to "take all necessary affirmative steps" to assure that minority and women's business enterprises and labor surplus area firms are used as contractors and subcontractors on federal-aid projects, including maintaining solicitation lists of such firms, assuring that they are solicited as subcontractors whenever they are potential sources, dividing subcontract work into smaller tasks to permit maximum participation by such firms, and using the service of the Small Business Administration (SBA) and the Department of Commerce.[4] Further, this regulation incorporates into USDOT's procurement requirements for federal-aid projects the DBE requirements of § 105(f) of the Surface Transportation Assistance Act (STAA) of 1982, Section 106(c) of the Surface Transportation and Uniform Relocation Assistance Act (STURAA) of 1987, and 49 C.F.R. Part 23.[5] Finally, this regulation incorporates into USDOT's procurement requirements for federal-aid projects the requirement of 23 USC § 140(b) that Indians be given preferential employment on all Indian Reservation road projects and contracts.[6]

ii. Part 26, Overview.—Most of USDOT's detailed requirements for participation of DBEs in projects funded by USDOT federal-aid programs are set forth in 49 C.F.R. Part 26. These regulations, significantly amended in 2011 as discussed later in this section,[7] are divided into Subparts covering general provisions; administrative requirements; goals, good-faith efforts, and counting; certification standards; certification procedures; and compliance and enforcement. While each of the subparts covers specific aspects of the DBE program, state DOTs must consider Part 26 in its entirety and must construe its different provisions together to understand fully and clearly how USDOT intends and requires its federal-aid DBE requirements to be administered.

iii. Part 26 Subpart A, General.—The general provisions of USDOT's DBE requirements are set forth in 49 C.F.R. Part 26 Subpart A. Subpart A indicates that its objectives include ensuring nondiscrimination in the award of federal-aid highway projects, to create a level playing field for DBEs to compete on, to ensure that DBE requirements are narrowly tailored, to ensure that only eligible firms participate, to remove barriers to the participation of DBEs in federal-aid projects, and to give state DOTs some flexibility in providing opportunities for DBEs.[8] Subpart A indicates that USDOT DBE requirements apply to state DOTs receiving federal-aid highway funds under ISTEA or TEA-21, but do not apply to any projects performed entirely with state funding and without any federal-aid funding.[9] It provides specific definitions for the terms used throughout Part 26.[10]

Subpart A prohibits state DOTs from discriminating against anyone on the basis of race, color, sex, or national origin in making contract awards. It also prohibits state DOTs from using any administrative methods that have the effect of impairing or defeating the objectives of the program with respect to individuals of any race, color, sex, or national origin.[11]

Subpart A authorizes the U.S. Secretary of Transportation, FHWA, and certain other USDOT units to issue official written interpretations of or written guidance concerning Part 26, so long as certain requirements are met. Only such interpretations and guidance express the official views of USDOT, FHWA, or any of USDOT's other operating administrations.[12]

Subpart A specifies what records state DOTs are required to maintain and submit to USDOT and FHWA as part of the administration of DBE requirements for federal-aid projects.[13]

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[1] Interview with Ann Maestri of NYSDOT.

[2] 49 C.F.R. § 18.36(a).

[3] 49 C.F.R. § 18.36(b)(2).

[4] 49 C.F.R. § 18.36(e).

[5] 49 C.F.R. § 18.36(n).

[6] 49 C.F.R. § 18.36(s).

[7] See USDOT Docket No. OST-2010-0118, Final Rule eff. Feb. 28, 2011, 76 Fed. Reg. 5083 (Jan. 28, 2011).

[8] 49 C.F.R. § 26.1.

[9] 49 C.F.R. § 26.3(a) and (d).

[10] 49 C.F.R. § 26.5.

[11] 49 C.F.R. § 26.7.

[12] 49 C.F.R. § 26.9.

[13] 49 C.F.R. § 26.11.

Subpart A also sets forth, in detail, what specific assurances state DOTs must make to FHWA in each federal-aid financial assistance agreement regarding DBE participation in projects; and what specific assurances state DOTs must obtain from their contractors and contractors must obtain from their subcontractors, regarding use of DBE subcontractors on federal-aid projects.[14]

Subpart A includes provisions establishing procedures for state DOTs to use in applying to the Secretary of Transportation, FHWA, or other USDOT operating administrations for exemptions or waivers from DBE requirements, and criteria governing USDOT and FHWA review and approval or disapproval of such applications.[15]

iv. Part 26 Subpart B, Administrative Requirements.—The administrative requirements which state DOTs must comply with under USDOT's DBE regulations are set forth in 49 C.F.R. Part 26 Subpart B.

Subpart B provides expressly that state DOTs receiving federal-aid funding under statutes to which Part 26 applies are not eligible to receive federal-aid funding from USDOT unless USDOT has approved their DBE programs and they are in compliance with such programs and Part 26. While agencies are not required to submit periodic updates on their DBE programs, they are required to submit any significant changes in their DBE programs to USDOT for approval.[16]

State DOTs receiving federal-aid funding are required by Subpart B to issue, circulate throughout their organizations, and distribute to contractors and DBEs, a signed and dated policy statement expressing their commitment to the DBE program, stating its objectives, and outlining responsibilities for its implementation.[17]

Subpart B also includes an express requirement that state DOTs receiving federal-aid funding have a DBE liaison officer who has direct and independent access to the state DOT's chief executive officer and is responsible for implementing all aspects of the state DOT's DBE program, and requires state DOTs to have adequate staff to administer the program in compliance with Part 26.[18]

Where disadvantaged individuals own and control financial institutions, Subpart B requires state DOTs to investigate the services offered by such institutions, to make reasonable efforts to use such institutions, and to encourage prime contractors to do so as well.[19]

Subpart B also addresses prompt payment issues, including detailed requirements for state DOTs to take certain prompt payment measures in connection with their DBE programs. Such measures include contract clauses requiring contractors to pay subcontractors for satisfactory performance within 30 days from the state DOT's payments to the prime contractors for such work, and payment by prime contractors to subcontractors of retainages within 30 days after satisfactory completion of the subcontractors' work. They also require state DOT DBE programs to include appropriate means of enforcing such prompt payment requirements, with several possible approaches outlined in the regulations.[20]

Under Subpart B, state DOTs must maintain and update DBE directories, including specified types of contact information and NAICS codes for all types of work which each DBE is eligible to be certified.[21] Under USDOT's 2011 amendments to the regulations, the state DBE directories must use the most specific applicable North American Industry Classification System (NAICS) codes to describe the types of work performed by the DBEs, and may not limit the number of NAICS codes listed for each firm.[22]

State DOTs that determine that DBE subcontracting firms are so over-concentrated in certain types of work as to unduly burden the opportunities for non-DBE subcontractors to perform such types of work are required to devise appropriate measures to address this, and to obtain FHWA and/or other USDOT operating administration approval for such measures.[23]

State DOTs are delegated authority by Subpart B to establish a DBE business development program to assist DBEs to gain the ability to compete effectively for work outside the DBE program; and to establish "mentor-protege" programs under which other DBE or non-DBE firms may be the principal source of business development assistance to DBE firms.[24]

Subpart B requires state DOT DBE programs to include monitoring and enforcement mechanisms to ensure that subcontract work is actually performed by the DBEs to which it is committed; to report to USDOT on actual DBE attainments; and to ensure compliance with Part 26 by all "program participants," a term which appears to include not only contractors but also municipalities receiving federal-aid funding for municipal projects through state DOTs.[25]

State DOT DBE programs must also, in accordance with Subpart B, include elements structuring contracting requirements to facilitate competition by small business concerns. Subpart B expressly requires state DOTs to submit such elements to FHWA and/or other USDOT operating administrations for approval by February 28, 2012, and outlines strategies which state DOTs may include in such elements.[26]

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[14] 49 C.F.R. § 26.13.

[15] 49 C.F.R. § 26.15.

[16] 49 C.F.R. § 26.21.

[17] 49 C.F.R. § 26.23.

[18] 49 C.F.R. § 26.25.

[19] 49 C.F.R. § 26.27.

[20] 49 C.F.R. § 26.29.

[21] 49 C.F.R. § 26.31.

[22] Jo Anne Robinson, The New DBE Rules, presentation to Transportation Research Board conference in New Orleans, Louisiana, July 2012.

[23] 49 C.F.R. § 26.33.

[24] 49 C.F.R. § 26.35.

[25] 49 C.F.R. § 26.37.

[26] 49 C.F.R. § 26.39.

v. Part 26 Subpart C, Goals, Good-Faith Efforts, and Counting.—The provisions of USDOT's DBE requirements concerning contract DBE goals, good-faith efforts by contractors to comply with such goals, and what criteria govern the counting of DBE participation toward such goals, are set forth in 49 C.F.R. Part 26 Subpart C.

In accordance with federal statutes authorizing USDOT's DBE program, USDOT has established as a national-level aspirational goal that not less than 10 percent of federal-aid funding is to be expended with DBEs, except to the extent that the Secretary of Transportation determines otherwise.[27]

Under Subpart C, state DOTs are not permitted to use quotas for DBEs on federal-aid projects, and may not use set-aside contracts for DBEs unless no other method could reasonably be expected to redress egregious instances of discrimination.[28]

Subpart C sets forth multistep procedures for state DOTs to follow in setting overall DBE participation goals for their federal-aid construction programs. These are sufficiently lengthy and complex that they will not be described in detail here. Suffice it to say that state DOT officials responsible for administration of DBE programs must become thoroughly familiar with their specific requirements.[29]

USDOT may penalize state DOTs that fail to have an approved DBE program or to establish an overall DBE goal; but may not penalize state DOTs that have such programs and goals but fail to meet such goals, unless the state DOTs have failed to administer their DBE programs in good faith. The regulations include specific requirements that state DOTs must follow to demonstrate to USDOT and FHWA that they are administering their DBE programs in good faith, in the event that they fail to meet their DBE goals. These include, among other things, a requirement for the recipient to submit to the appropriate USDOT operating division, such as FHWA, an end of fiscal year report by December 30 if the recipient has failed to meet its overall DBE goal. The report must analyze the reasons for the shortfall, and set forth specific steps to address the problems identified in the analysis and enable the goal to be met the following year. The regulations also authorize FHWA to impose conditions and corrective actions upon any state DOTs failing to meet their DBE goals.[30]

Subpart C sets forth in considerable detail what means state DOTs must use to demonstrate that they meet DBE goals, including maximum feasible use of race-neutral means of facilitating DBE participation.[31] Subpart C also spells out in great detail what procedures state DOTs must use to award federal-aid contracts only to bidders who make good-faith efforts to meet DBE goals.[32] Interestingly, these procedures now include some specific provisions to be followed for handling DBE goals and compliance on DB projects.[33] They also prohibit prime contractors on federal-aid projects from terminating DBE subcontractors without state DOT approval, and specify the circumstances under which this may be permissible.[34] Further, Subpart C includes highly detailed provisions governing who state DOTs are to count as DBE participation in federal-aid projects as counting toward fulfillment of DBE goals, with a focus on ensuring that the work is actually performed by the DBE for whose participation credit is sought.[35]

vi. Part 26 Subpart D, Certification Standards.—The standards for state certification of DBEs for USDOT's federal-aid programs are set forth in 49 C.F.R. Part 26 Subpart D.

The regulations allocate burden of proof in certification proceedings. Women, Black Americans, Hispanic Americans, Native Americans, Asian-Pacific Americans, Subcontinent Asian Americans, or other minorities determined by the SBA, who certify that they are members of such a group, are entitled to a rebuttable presumption that they are socially and economically disadvantaged. While entitled to such a rebuttable presumption, firms seeking certification still bear the burden of demonstrating, by a preponderance of the evidence, that they meet the regulations' requirements concerning business size, ownership, and control. State DOTs are to make determinations concerning whether the requirements for certification are satisfied by considering all the facts in the record, viewed as a whole.[36] The regulations provide procedures for state DOTs to follow in order to verify the genuineness of an applicant's membership in a presumptively disadvantaged group if the DOTs have a well-founded reason to question the individual's claim of membership in that group.[37] The regulations also provide that an applicant's presumption of entitlement can be rebutted by evidence demonstrating that the individual has a personal net worth in excess of $1.32 million.[38]

Individuals not belonging to a presumptively disadvantaged group may still apply for DBE status. State DOTs are required to make case-by-case determinations on such applications. Such applicants bear the burden of proving that they are socially and economically disadvantaged, as well as meeting the other requirements for certification.[39]

Participation by DBEs in federal-aid projects is based not only upon membership in a presumptively

[27] 49 C.F.R. § 26.41.

[28] 49 C.F.R. § 26.43.

[29] 49 C.F.R. § 26.45.

[30] 49 C.F.R. § 26.47. *See also* Robinson, *supra* note 22.

[31] 49 C.F.R. § 26.51.

[32] 49 C.F.R. § 26.53.

[33] 49 C.F.R. § 26.53(e).

[34] 49 C.F.R. § 26.53(f).

[35] 49 C.F.R. § 26.55.

[36] 49 C.F.R. §§ 26.61 and 26.67.

[37] 49 C.F.R. § 26.63.

[38] 49 C.F.R. § 29.67(b)(1).

[39] 49 C.F.R. § 26.67(d).

disadvantaged group, but also upon business size. USDOT's regulations require DBEs to be small businesses, and incorporate the definition of such firms established by the SBA. USDOT also requires that, to be certified as DBEs, firms cannot have had average annual gross receipts over the firm's past 3 fiscal years in excess of $22.41 million.[40]

To be eligible for certification as a DBE, firms must be able to demonstrate that they are at least 51 percent owned by socially and economically disadvantaged individuals. Such ownership must be real, substantial, and continuing, going beyond pro forma ownership; the disadvantaged owners must also enjoy the customary incidents of ownership and share in the risks and profits commensurate with their ownership, as shown by the substance and not just the form of the firm's arrangements.[41] USDOT has adopted requirements that establish a number of specific additional tests to determine whether ownership of an applicant firm by disadvantaged persons is genuine.[42]

To be eligible for certification as a DBE, firms must also be independent, and their viability cannot depend upon their relationship with another firm such as a prime contractor. The disadvantaged owners must control the board of directors of the firm; have the power to direct or cause the direction of the firm's management, policy, and operations on a day-to-day as well as long-term basis; and have an overall understanding of, and managerial and technical competence and experience directly related to, the type of business in which the firm is engaged, and the firm's operations.[43] As with ownership, USDOT has adopted requirements that establish a number of specific additional tests to determine whether control of an applicant firm by disadvantaged persons is genuine.[44]

In making certification decisions, state DOTs may consider whether a firm has exhibited a pattern of conduct indicating its involvement in attempts to evade or subvert the intent or requirements of the DBE program. This includes evidence of failure to perform a commercially useful function on past projects, although such evidence may not be considered for any other purpose in certification decisions.[45] USDOT has also adopted various other rules governing DBE certification, the basic purpose of which is to prevent the DBE program from being undercut by sham firms controlled by nondisadvantaged contractors.[46]

vii. Part 26 Subpart E, Certification Procedures.—The certification procedure provisions of USDOT's DBE requirements are set forth in 49 C.F.R. Part 26 Subpart E.

The USDOT regulations require each state to establish a single Unified Certification Program (UCP) for the state, covering all DOTs (i.e., municipal as well as state) receiving federal-aid funding from USDOT, and providing "one-stop shopping" for firms seeking certification as DBEs for performing highway subcontracting work within the state.[47] Each UCP is required to maintain a unified directory of DBEs, updated at least once yearly and posted on the Internet as well as available in print.[48] While the UCP may take any form acceptable to the recipients in that state, it is subject to approval or disapproval by the U.S. Secretary of Transportation, and is required to comply with all USDOT directives and guidance concerning certification matters and cooperate fully with USDOT oversight, review, and monitoring.[49]

In making certification decisions, UCPs must follow procedures set forth in the regulations. To summarize briefly, these include such things as collecting the application forms provided by the regulations; interviewing the principals of each firm applying for DBE certification, reviewing their resumes, and performing on-site visits to the firm's offices and any active work sites; analyzing the firm's stock ownership, bonding and financial capacity, work history, and list of equipment owned and licenses held; and requiring that the applicant attest to the truthfulness of the information submitted on the applications form.[50] UCPs are required to safeguard the confidentiality of any proprietary business information obtained during certification reviews, but are also required to making information concerning DBEs available upon written request to other UCPs, DOTs, or recipients considering the eligibility of a DBE firm.[51] Once certified, a DBE firm remains certified unless and until the UCP revokes its certification, although UCPs are authorized to conduct certification reviews 3 years from the date of the firm's most recent certification, or sooner if appropriate in light of changed circumstances.[52]

Two or more states may form a regional UCP, or enter into written reciprocity agreements between UCPs.[53] Even where states do not do so, when a firm certified in one state applies to another state for DBE certification, the new state's UCP may, in its discretion, choose to accept the home state's certification after confirming with the home state that the certification remains valid. If the UCP in another state does not choose to accept the home state certification, the regulations set forth detailed procedures for that UCP to follow in accepting and reviewing the firm's application for DBE certification.[54]

[40] 49 C.F.R. § 26.65; and 13 C.F.R. § 121.402.

[41] 49 C.F.R. § 26.69.

[42] 49 C.F.R. § 26.69(d) through (j).

[43] 49 C.F.R. § 26.71.

[44] 49 C.F.R. § 26.71(c) through (q).

[45] 49 C.F.R. § 26.73(a).

[46] 49 C.F.R. § 26.73(b) through (h).

[47] 49 C.F.R. § 26.81.

[48] 49 C.F.R. § 26.81(g).

[49] 49 C.F.R. § 26.81(a).

[50] 49 C.F.R. § 26.83(a) through (c).

[51] 49 C.F.R. § 26.83(d) and (g).

[52] 49 C.F.R. § 26.83(h); and *see also* 49 C.F.R. § 26.87.

[53] 49 C.F.R. § 26.81(e) and (f).

[54] 49 C.F.R. § 26.85.

When a UCP denies an application for DBE certification, the UCP must provide the firm with a written explanation of the reasons for denial, referencing evidence in the record supporting the decision, and make all documents and information upon which the denial is based available to the firm.[55] When a UCP denies certification to a firm certified by the SBA, the UCP must notify the SBA in writing, including the reason for denial.[56] When a UCP denies an application for certification, it must establish a time perio of no more than 12 months before the firm may reapply.[57] Following an administratively final denial of certification, the firm may appeal the denial to USDOT.[58]

When a UCP or DOT receives a complaint that a currently certified DBE firm is ineligible for such certification, the UCP must treat such a complaint as confidential. It must also review its records concerning the firm, request additional information as needed, and investigate the complaint as necessary. If the UCP finds the complaint unfounded, the UCP must notify both the complainant and the DBE firm. If the UCP finds reasonable cause to believe that the DBE firm is ineligible, however, it must provide written notice to the firm, setting forth the reasons involved, and provide the firm with an opportunity for an informal hearing during which the firm may respond. In any such hearing, the UCP or DOT bears the burden of proving by a preponderance of the evidence that the DBE firm is not eligible for certification, based upon information previously unavailable, concealed, or misrepresented at the time of certification; a change in USDOT certification standards, or a UCP error in granting the original certification.[59]

Firms whose application for DBE status is denied, or whose DBE certification is revoked, may submit administrative appeals to USDOT within 90 days after the UCP or state DOT's final decision. USDOT will then request the UCP to provide a complete copy of the administrative record involved, review such record, and make its decision based upon the record, without making a *de novo* review of the matter or conducting a hearing. USDOT has a policy of determining such appeals within 180 days after receiving the complete administrative record from the UCP. The pendency of such an appeal to USDOT does not stay or suspend the effect of the UCP's denial or revocation, which shall remain in effect unless and until overturned by USDOT.[60] The USDOT regulations specify what actions UCPs, state DOTs, or other recipients are required to take following a USDOT determination on a DBE certification appeal, depending upon the outcome of such appeal.[61]

USDOT's 2011 amendments to its regulations include new procedures involving interstate certification of DBEs. These are discussed separately in connection with the 2011 amendments in Section 4(1)(b), below.

viii. Part 26 Subpart F, Compliance and Enforcement.—The compliance and enforcement provisions of USDOT's DBE requirements are set forth in 49 C.F.R. Part 26 Subpart F.

These regulations begin by indicating that recipients, a category that includes state and municipal DOTs, may be subject to formal enforcement actions by USDOT if they fail to comply with the requirements of Part 26, including the suspension or termination of federal-aid funding or refusal to approve projects, grants, or contracts until deficiencies or remedied. The regulations note, however, that recipients will not be subject to compliance actions if a federal court has ruled the Part 26 requirement involved to be unconstitutional.[62]

Any person who believes that a state or municipal DOT has failed to comply with its obligations under Part 26 may file a written complaint with the FHWA Office of Civil Rights or the equivalent office for any other USDOT operating administration, but must do so within 180 days after the date of the alleged violation or learning of a continuing course of violations. The Office of Civil Rights may protect the complainant's identity. FHWA and other USDOT operating administrations may also review compliance by state or municipal DOTs on their own initiatives at any time. If investigation of a complaint, or such a review, finds reasonable cause to find a state or municipal DOT in noncompliance, FHWA or another appropriate USDOT office will send the state or municipal DOT written notice, including an opportunity to request conciliation proceedings within 30 days. If such a request is made, FHWA or another appropriate USDOT office will pursue conciliation for at least 20, but not more than 120, days from such request. If this results in a written conciliation agreement between FHWA or USDOT and the state or DOT involved, specifying measures the state or municipal DOT has taken or will take to ensure compliance, then the matter is considered closed, subject to ongoing monitoring of implementation of the conciliation agreement. If a state or municipal DOT does not request conciliation, or a conciliation agreement is not signed within 120 days after a request for conciliation, then FHWA or USDOT will undertake enforcement proceedings.[63]

Contractors or DBE subcontractors who attempt to meet DBE goals or other DBE program requirements through false, fraudulent, or deceitful statements or representations or under circumstances indicating a serious lack of business integrity or honesty, may be subject to USDOT suspension or debarment proceedings, and/or proceedings for civil remedies under 49

[55] 49 C.F.R. § 26.86(a).

[56] 49 C.F.R. § 26.86(b).

[57] 49 C.F.R. § 26.86(c).

[58] 49 C.F.R. § 26.86(d); and *see also* 49 C.F.R. § 26.89.

[59] 49 C.F.R. § 26.87.

[60] 49 C.F.R. § 26.89.

[61] 49 C.F.R. § 26.91.

[62] 49 C.F.R. § 26.101.

[63] 49 C.F.R. § 26.103. Enforcement actions for FAA programs are governed by 49 C.F.R. § 26.105.

C.F.R. Part 31.[64] USDOT may also refer to the DOJ, for criminal prosecution under 18 U.S.C. § 1001 or other applicable provisions of law, any person who makes a false or fraudulent statement in connection with participation in the DBE program or otherwise violates applicable federal statutes.[65]

USDOT's regulations on DBE compliance and enforcement also include provisions protecting the confidentiality of proprietary business information involved in such matters, protecting the confidentiality of information on complainants, and requiring the full and prompt cooperation of all state and municipal DOTs, and of all contractors and subcontractors involved, with USDOT compliance and certification reviews, requests for information, and investigations.[66] The regulations also prohibit state and municipal DOTs, contractors, and any other DBE program participants from intimidating, threatening, coercing, or discriminating against any complainant, witness, or other person participating in any manner in any compliance or enforcement investigation or proceeding.[67]

ix. Part 26, Appendices.—USDOT's Part 26 DBE regulations are accompanied by several appendices. Appendix A provides USDOT administrative guidance concerning what constitutes "good faith efforts" within the meaning of the Part 26 regulations. Appendix B sets forth the Uniform Report of DBE Awards or Commitments and Payments Form that state and municipal DOTs are required to use when reporting to FHWA and USDOT on such matters. Appendix C provides DBE Business Development Program Guidelines. Appendix D furnishes Mentor•Protege Program Guidelines. Appendix E offers USDOT administrative guidance to UCPs and state or municipal DOTs in making individual determinations of social and economic disadvantage in the cases of those who apply for DBE status but are not members of a presumptively disadvantaged group, and seek to demonstrate social and economic disadvantage on an individual basis. Appendix F provides the Uniform Certification Application Form. [68]

b. The 2011 Amendments to 49 C.F.R. Part 26

USDOT conducted a significant rulemaking from 2009 to early 2011, amending 49 C.F.R. Part 26 to address a number of perceived issues concerning the DBE program. According to FHWA's Office of Chief Counsel, this rulemaking followed a series of meetings with various stakeholders in 2008 and 2009, and publication of an Advanced Notice of Proposed Rulemaking in 2009, with Phase I of the new rules going into effect on February 28, 2011.[69] USDOT characterized the completion of this rulemaking as improving the accountability of the DBE program by "increasing accountability for recipients with respect to meeting overall goals, modifying and updating certification requirements, adjusting the personal net worth (PNW) threshold for inflation, providing for expedited interstate certification, adding provisions to foster small business participation, improving post-award oversight, and addressing other issues."[70] Among the issues addressed by the rulemaking were the following.

i. Counting Purchases from Prime Contractors.—USDOT considered, but rejected, construction industry requests for prime contractors and DBEs to be allowed to claim DBE participation credit for construction materials that a DBE had purchased from the prime contractor performing the contract. USDOT indicated that it indicated such a pass-through arrangement as inconsistent with the most important principle of counting DBE participation, namely that credit should only be counted for value added to the transaction by the DBE itself. USDOT also noted that the existing approach, which it decided to leave unchanged, had been part of the DBE regulations since 1999.[71]

ii. Terminations of DBE Firms.—USDOT addressed concerns stated by state and municipal DOTs, prime contractors, contractors' trade associations, and DBE subcontractors alike in revising somewhat the approach taken by the regulations to prime contractors' terminations of DBE firms. Noting that all parties considered this issue to be problematic for different and conflicting reasons, USDOT adopted a somewhat revised approach under which prime contractors can terminate DBE subcontractors for good cause shown, and with the written consent of the recipient, i.e., the state or municipal DOT administering the project.

To terminate a DBE firm, prime contractors must provide written notification to the DBE, with a copy to the recipient, of its intent to request to terminate/substitute the DBE, and the reason therefore. Prime contractors must give DBEs 5 days to respond, unless an emergency situation is involved. Prime contractors must demonstrate good cause for the termination. The new regulation provides nine examples of situations that would show good cause, plus a general provision for "other good cause you determine compels termination." Prime contractors must, prior to termination, also obtain the consent of the state DOT or other recipient to do so. These requirements apply not only to terminations during the course of performing the work, but also to pre-award substitution of previously proposed DBE subcontractors.[72]

USDOT explained that its revised approach would allow prime contractors to terminate and replace DBEs that were genuinely failing to perform subcontract work satisfactorily in accordance with normal industry standards, but would prevent prime contractors from dis-

[64] 49 C.F.R. § 26.107(a) through (d); and *see* 49 C.F.R. pt. 31.

[65] 49 C.F.R. § 26.107(e).

[66] 49 C.F.R. § 26.109.

[67] 49 C.F.R. § 26.109(d).

[68] See 49 C.F.R. pt. 26, Apps. A through F.

[69] Robinson, *supra* note 22.

[70] Summary of USDOT Docket No. OST-2010-0118, Final Rule eff. Feb. 28, 2011, 76 Fed. Reg. 5083 (Jan. 28, 2011).

[71] 76 Fed. Reg. 5083 at 5084, Jan. 28, 2011.

[72] Robinson, *supra* note 22.

missing DBEs arbitrarily merely to profit from performing the work themselves or in situations where the DBE's failure to perform resulted from bad faith or discriminatory actions on the part of the prime contractor.[73]

iii. Personal Net Worth.—USDOT noted that a large majority of those commenting on its rulemaking supported the proposal to raise the PNW cap for DBEs from the prior $750,000 to $1.32 million. USDOT explained that this was appropriate in order to make an inflationary adjustment to adjust the current figure to match the real dollar value of the prior figure, which dated back to 1999, based on consumer price index figures for the intervening years. While USDOT received some objections that raising the cap would benefit firms that were not genuinely disadvantaged or benefit larger DBEs at the expense of smaller ones, and that Individual Retirement Accounts and other retirement assets should be excluded from PNW calculations, it decided to make the inflation adjustment as proposed. Acknowledging comments that a revised USDOT form for making PNW calculations, with additional guidance and instructions, would be helpful, USDOT indicated that it would take this issue under advisement for a future rulemaking on DBE issues, which it hoped to pursue later in 2011.[74]

iv. Interstate Certification.—USDOT's proposal to facilitate interstate certification of DBEs, with a short 30-day review period and the burden of proof resting on any agencies opposing recognition of certifications from other states, drew a large number of comments. In general terms, DBE firms and contractors' trade associations supported USDOT's proposal to make it easier for DBEs certified in their home states to obtain certification in other states. State DOTs, in contrast, expressed concerns that this would tend to undercut the integrity of the DBE program because some states had weak certification programs that allowed ineligible firms to obtain certification. Facilitating interstate certification, they argued, would allow such ineligible firms to work even in states administering strong and thorough certification programs.

While deciding to proceed with measures to make interstate certification easier, USDOT responded to the concerns of state DOTs by revising its proposed approach. In the final rule as adopted, with an effective date of January 1, 2012, a DBE certified in its home state could seek certification in another state, State B, by presenting its home state certification to State B, which would then have 60 days to review it. State B would have the option of accepting the home state's certification as acceptable, thus granting the DBE firm certification in State B as well. If State B concluded, however, that the home state certification was not acceptable and the firm was ineligible for certification, State B would have to provide the applicant with a written statement of the specific and detailed reasons why State B had reached that conclusion, and allow the firm an opportunity to respond. Grounds for State B's denial of certification might include such things as fraud, new information, factual errors, misapplication of certification requirements, State B legal requirements, or failure to supply required information. State B would be required to provide the DBE with an opportunity to be heard regarding its objections. The firm would then bear the burden of proof of demonstrating by a preponderance of the evidence that the firm met the applicable certification requirements. State B would be required to issue its decision within 30 days after the DBE's opportunity to be heard, and would have to enter any certification denials or decertifications in USDOT's Department Office of Civil Rights database.[75]

v. Other Certification-Related Issues.—USDOT's rulemaking solicited comments on whether there should be a requirement for periodic certification reviews or updates of on-site reviews, and on whether firms that withdrew certification applications should be subject to a waiting period before resubmitting such applications. Those submitting responses also commented about arbitrary state limitations on the number of NAICS codes a firm could be certified for; whether state DOTs should be compelled to accept SBA certifications, since SBA had gone to a self-certification process; whether state DOTs should be allowed to consider investments by prime contractors in subcontractors as calling DBE status into question; and whether state DOTs should be allowed to count former personal assets that owners had transferred to DBE firms as counting toward PNW calculations.

In adopting the final rule, USDOT decided not to require updated on-site reviews of certified firms on any specified mandatory interval, leaving that to the discretion of UCPs and state DOTs; but noted that USDOT strongly encouraged UCPs and state DOTs to conduct updated on-site reviews of certified DBEs on a regular and reasonably frequent basis, particularly when they became aware of any changes in circumstances or allegations of misconduct, stating that "regularly updated on-site reviews are an extremely important tool in helping avoid fraudulent firms or firms that no longer meet eligibility requirements from participating in the DBE program." USDOT indicated that it was inappropriate for UCPs and state DOTs to apply the waiting period provision of 49 C.F.R. § 26.86(c) to firms which withdrew and then refiled applications, noting that putting the refiled applications at the end of the line of pending applications was sufficient to protect UCPs from excessive workload associated with refilings. Responding to comments, USDOT adopted a new provision prohibiting UCPs and state DOTs from arbitrarily limiting the number of NAICS codes a DBE firm could be certified for. It also deleted former §§ 26.84 and 26.85 concerning SBA certifications, since SBA had gone to a self-certification process differing from USDOT's DBE proc-

[73] 76 Fed. Reg. 5083, 5084–5085, (Jan. 28, 2011).

[74] 76 Fed. Reg. 5083, 5085–5087 (Jan. 28, 2011).

[75] 76 Fed. Reg. 5083, 5087–5089 (Jan. 28, 2011); and *see* 49 C.F.R. § 26.85(d)(2). *See also* Robinson, *supra* note 22.

ess in important respects. While not adopting a new rule on prime contractor investments in DBEs, USDOT indicated that state DOTs reviewing prime contractor requests to use such DBEs on projects should scrutinize such relationships very closely, with particular attention to the independence, affiliation, and commercially useful function of the DBE. While not prohibiting owner transfers of personal assets to DBEs, USDOT indicated that UCPs and state DOTs could examine such transfers and continue to count the assets toward PNW if they concluded that the transfers had been ruses to circumvent PNW requirements rather than genuine investments in the business.[76]

vi. Accountability and Goal Submissions.—USDOT proposed that if a state or municipal DOT or other recipient failed to meet its overall DBE goal, it would have to analyze the shortfall within 60 days, explain the reasons for it, devise corrective actions, and submit such information to FHWA or other USDOT operating administrations. While there would be no requirement to meet a goal, failing to take these follow-up steps if goals were missed could be considered as a lack of good faith, which could lead to a finding of noncompliance with the program. USDOT also solicited comments on a recent prior rulemaking concerning the submission of goals on 3-year rather than 1-year cycles, with a focus on annual projections within 3-year goals. Both of these proposals drew extensive comments, some of which characterized the accountability measures as establishing quotas rather than goals.

USDOT adopted the accountability provision as proposed, responding to comments by indicating that the program involved goals rather than quotas, and that no recipients would be penalized for failing to meet goals. USDOT pointed out that any effective good-faith effort by recipients to administer the DBE program would necessarily involve measures to evaluate performance, analyze the reasons for any shortfalls, and look for ways to avoid future shortfalls, and that measures requiring efforts to do so would simply promote accountability and transparency, rather than establishing rigid quotas. With regard to 3-year goals and annual projections, USDOT indicated that it had no objections to recipients' preparing and submitting annual projections for administrative purposes, but that the 3-year goal figure would still be applied on an annual basis in terms of determining whether there was any shortfall which would trigger accountability requirements.[77]

vii. Program Oversight.—USDOT's rulemaking proposed to require that recipients (state and municipal DOTs) certify that they had monitored the paperwork and on-site performance of DBE contracts to make sure that DBEs actually performed them. Comments by DBEs supported the proposal, indicating that this would reduce the likelihood that contractors would abuse DBEs after contract award. Comments by some recipients, however, opposed the proposal on the basis that it would be too burdensome administratively, particularly for agencies with small staffs.

USDOT's response to the comments was revealing. USDOT pointed out that, for the DBE program to be meaningful, DBEs actually had to perform the work that was supposedly subcontracted to them, and that its regulations already required recipients to have a monitoring and enforcement mechanism to ensure that DBEs were actually performing the work claimed. USDOT went on to say:

The FHWA review team that has been examining state implementation of the DBE program found that many states did not have an effective compliance monitoring program in place. DBE fraud cases investigated by the Department's Office of Inspector General and criminal prosecutions in the Federal courts have highlighted numerous cases in which recipients were unaware, often for many years, of situations in which non-DBE companies were claiming DBE credit for work that DBEs did not perform.[78]

While refraining for workload reasons from requiring more pervasive monitoring, USDOT decided to require that recipients memorialize the monitoring they were already required to perform and do so on every contract on which DBE participation was claimed, and not just on a sample or percentage of such contracts.[79]

viii. Small Business Provisions, Including Race-Neutral Provisions.—USDOT's Notice of Proposed Rulemaking (NPRM) proposed requiring recipients to add an element to their DBE programs to foster small business participation in contracts, with a focus on race-neutral measures. The majority of commenters supported the proposal, and USDOT decided to adopt it. This included adoption of a new 49 C.F.R. § 26.39, "Fostering Small Business Participation," with state or municipal DOTs or other recipients required to submit to the appropriate USDOT operating divisions by February 28, 2012, the program elements they had developed "to structure contracting requirements to facilitate competition by small business concerns." Recipients were, among other things, allowed to include a race-neutral small business set-aside for prime contracts under a stated amount, such as $1 million. For multi-year DB projects or other large projects, recipients were allowed to require bidders for prime contracts to identify elements of the project or subcontracts of a size that small businesses, including DBEs, could reasonably perform. For prime contracts not involving DBE goals, recipients were allowed to require the prime contractor, rather than performing all of the work itself, to provide subcontracting opportunities of a size that small businesses, including DBEs, could reasonably perform. Recipients were also allowed to structure procurements to facilitate the ability of small businesses, including DBEs, to form joint ventures or consortia that could compete for and perform prime contracts. For recipients to meet a projected portion of their goals through race-

[76] 76 Fed Reg. 5083, 5089–5091 (Jan. 28, 2011).

[77] 76 Fed Reg. 5083, 5091–5093 (Jan. 28, 2011).

[78] 76 Fed. Reg. 5083, 5093 (Jan. 28, 2011).

[79] 76 Fed. Reg. 5083, 5093–5094 (Jan. 28, 2011).

neutral measures, USDOT authorized recipients to ensure that a reasonable number of prime contracts were of a size that small businesses, including DBEs, could reasonably perform. Finally, USDOT expressly required that recipients actively implement such program elements, as part of good-faith implementation of their DBE programs.[80]

USDOT did not, however, take any immediate action on the issue of duplicative bonding requirements for DBEs, deferring action on that to a follow-up rulemaking that USDOT is planning to pursue.[81]

Examples of possible state DOT or other recipient strategies for incorporating small business elements into their DBE programs might include such things as unbundling contracts, small business set-asides, small business goals, structuring procurements to be feasible for joint ventures of small businesses, and reducing the size of prime contracts to be feasible for small businesses to serve as prime contractors.[82] USDOT has also offered administrative guidance to state DOTs and other recipients on related matters such as how to define "small business", whether there should be a PNW requirement, micro-small business programs, supportive services, and implementation.[83]

With regard to efforts by state and municipal DOTs and other recipients to develop and implement such small-business elements of their DBE programs, including race-neutral elements, note that the TRB issued a timely publication in April 2011, just 2 months after USDOT's adoption of these new requirements, analyzing experience to date with the implementation of race-neutral measures in state DBE programs.[84] The research involved in the preparation of this publication, NCHRP Synthesis 416, included a survey of state DOTs. The publication addressed topics including a summary of the state responses to the survey, state strategies for implementing race-neutral measures, state DBE program challenges and solutions, and case examples drawn from the experiences of the Florida, Rhode Island, and Colorado state DOTs.

The authors' conclusions indicated that supportive services and training measures were widely used by the states responding to the survey and were ranked among the most effective measures. They found that some of the strategies considered to be the most effective, including reserving small contracts for small businesses and using targeted loan mobilization programs, could have high payoffs but posed challenges to implement. They indicated that state DOTs considered improving communications between DBEs and prime contractors to be important both for maintaining existing relationships and establishing new relationships between such firms. State DOTs indicated that the most frequent and difficult challenges to the success of state DBE programs included the weak economy, DBE firms' lack of access to capital, high fuel costs, and DBEs' lack of experience and equipment in connection with certain types of work. Those states that employed targeted measures indicated that selecting the right firms to receive such benefits was an important part of being successful.[85]

ix. USDOT on Continuing Compelling Need for DBE Program.—In concluding its evaluation of comments on the NPRM, USDOT noted the existence of a continuing compelling need for the DBE program, citing among other things testimony presented by the DOJ before the House Transportation and Infrastructure Committee in March 2009.[86]

x. Further USDOT Action Anticipated.—USDOT personnel have indicated that the agency is giving active consideration to taking further action in this area, although it is not entirely clear whether such action would come in the form or further rulemaking or would be limited to administrative guidance to recipients. While no major new policy initiatives are apparently contemplated, USDOT is seeking to develop additional program modifications to address various administrative issues raised by people involved in the administration of the DBE program. Among other things, USDOT is apparently seeking to improve its DBE certification application forms and the uniform reports that it requires state DOTs and other recipients to submit.[87]

2. Historical Background: Executive Order 11246 and Its Progeny

While the primary focus of state and municipal DOT officials involved in the ongoing daily administration of DBE requirements now rests upon the USDOT 49 C.F.R. Part 26 regulations discussed above, the DBE program, and related EEO requirements, cannot be fully understood without understanding their historical roots and their development over time, including significant constitutional litigation at the U.S. Supreme Court level in recent decades.

Requirements for "nondiscrimination" in public contracts present few constitutional issues.[88] Instead, they reinforce the requirements of the Fifth and Fourteenth

[80] 49 C.F.R. § 26.39(a) and (b), as adopted by USDOT Docket No. OST-2010-0118, Final Rule eff. Feb. 28, 2011, 76 Fed. Reg. 5083, 5087 (Jan. 28, 2011).

[81] 76 Fed. Reg. 5083, 5094 (Jan. 28, 2011).

[82] Robinson, *supra* note 22.

[83] *Id.*

[84] PATRICK CASEY, ANDREA THOMAS & JAMES THEIL, IMPLEMENTING RACE-NEUTRAL MEASURES IN STATE DISADVANTAGED BUSINESS ENTERPRISE PROGRAMS (NCHRP Synthesis 416, Transportation Research Board, 2011). This publication is available at http://onlinepubs.trb.org/onlinepubs/nchrp/nchrp_syn_416.pdf, last accessed on July 18, 2012.

[85] *Id*. at 30.

[86] 76 Fed. Reg. 5083, 5095 (Jan. 28, 2011).

[87] Robinson, *supra* note 22.

[88] Portions of this section are derived from Orrin F. Finch, *Minority and Disadvantaged Business Enterprise Requirements in Public Contracting* Vol. 3, at 1582-N1, Transportation Research Board, The National Academies, Washington, D.C. (1985).

Amendments as well as the statutes designed to implement those constitutional provisions.[89] Eventually, however, nondiscrimination requirements gave way to affirmative action requirements. Affirmative action plans were designed to redress the lingering effects of past discrimination and gave rise to significant constitutional questions.[90]

a. The Equal Employment Opportunity Program

EEO, affirmative action, and the Minority Business Enterprise (MBE) and DBE programs all have a common origin in Executive Order (EO) 11246. As early as 1941, President Roosevelt under the War Manpower Act ordered that provisions of nondiscrimination be included in all federal defense contracts. The rationale was that nondiscrimination would ensure a large work force in the wartime effort. This order was continued by all succeeding presidents and led to the issuance of EO 11246 on September 24, 1965, by President Johnson. This order expanded the 1941 order to apply to all federally assisted construction contracts, and mandated that contractors and subcontractors take affirmative action to ensure that no applicant for employment was discriminated against by reason of race, color, religion, sex, or national origin. The Department of Labor was made responsible for the administration of the EEO program and was authorized by the President to adopt regulations to implement the order. This new obligation of affirmative action was more than a prohibition against discrimination. It called for establishment of goals and monitoring of achievement.

Each bidder on a federally assisted contract was required to submit an affirmative action plan (AAP) with a schedule of goals to be achieved in employing minority workers for several trades involved in the construction. Each AAP had to receive Department of Labor approval before the low bidder could be awarded the contract. However, an alternative developed whereby the bidder or the specifications could incorporate any of the several "hometown plans" approved by the Department of Labor for the community involved.[91] Hometown plans were tripartite plans involving the contractors, the unions, and the minority community. The success of the plans therefore depended on the ability of the community leaders to work with unions and local contractors' associations to obtain mutual concurrence in a plan acceptable to the Department of Labor.

One of the first legal challenges to the program involved a hometown plan known as the "Philadelphia Plan" in *Contractors Association of Eastern Pennsylvania v. Secretary of Labor*.[92] The challenge was that the Philadelphia Plan was social legislation of local application enacted by the federal executive without congressional or constitutional authority. The court's decision rested on the power of the President, rather than Congress, to impose fair employment conditions incident to the power to contract.

The opinion relied upon Justice Jackson's opinion in *Youngstown Sheet & Tube Company v. Sawyer,* in which the Court held that an EO seizing steel mills was not within the constitutional power of the President.[93] In that opinion, Justice Jackson divided presidential authority into three categories: (1) presidential acts responding to an express or implied authorization of Congress; (2) measures inconsistent or incompatible with the expressed or implied will of Congress; and (3) actions taken in the absence of either congressional grant or denial of authority, express or implied. The third category took into account three interrelated features: the possibility of concurrent authority, congressional acquiescence in conferring executive authority, and the fact that the test of authority may depend more on events than on theories of law.

The Third Circuit then traced the development EO 11246 from the original 1941 EO requiring nondiscrimination covenants in all defense contracts. Based on a historical analysis of EO 11246, the court concluded that the executive action was a valid exercise of contract authority within Justice Jackson's third category. This conclusion was fortified by acquiescence of Congress, since it had for many years continued to appropriate funds for both federal and federal-aid projects with knowledge of the preexisting EOs.

EO 11246 and its implementing regulations at 41 C.F.R. Part 60 are enforced by the U.S. Department of Labor, Office of Federal Contract Compliance, rather than by FHWA, USDOT, or state transportation departments.[94]

b. The Minority and Women Business Enterprise Program

The EEO program was designed to promote affirmative action in the employment of construction workers. Affirmative action for M/WBE in construction developed more slowly than EEO, but had more impact on the industry and on state and local governments.[95]

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[89] *See*, 49 C.F.R. pt. 21 (2001).

[90] *See* Note, *Executive Order No. 11246: Anti-Discrimination Obligations in Government Contracts*, 44 N.Y.U. L. REV. 590 (1969).

[91] For a history of the development of the home town plan theories *see* Comment, *The Philadelphia Plan: A Study in the Dynamics of Executive Power*, 39 U. CHI. L. REV. 723 (1972); Leiken, *Preferential Treatment in the Skilled Building Trades: An Analysis of the Philadelphia Plan*, 56 CORNELL L. REV. 84 (1970); and Jones, *The Bugaboo of Employment Quotas*, 1970 WIS. L. REV. 341 (1970).

[92] 442 F.2d 159 (3d Cir. 1971), *cert. denied*, 404 U.S. 854, 92 S. Ct. 98.

[93] 343 U.S. 579, 72 S. Ct. 863 (1952).

[94] FHWA Order 4710.8, "Clarification Of Federal Highway Administration (FHWA) And State Responsibilities Under Executive Order 11246 And Department Of Labor (DOL) Regulations in 41 C.F.R. Chapter 60," Feb. 1, 1999.

[95] *See* Levinson, *A Study of Preferential Treatment: The Evolution of Minority Business Enterprise Assistance Programs*, 49 GEO. WASH. L. REV. 61 (1980).

Section 8(a) of the Small Business Act of 1953 authorized the Federal SBA to contract directly with small businesses on behalf of various federal procurement agencies.[96] Through its regulatory authority, the SBA developed a set-aside program for socially and economically disadvantaged small businesses. The absence of congressional authority for this preferential program was challenged in a number of equal protection cases, but these challenges were largely unsuccessful for lack of standing based on the plaintiffs' inability to show that they would otherwise qualify for certification and participation under the Small Business Act.[97]

However, Congress supplied legislative authority in 1978, requiring eligibility for 8(a) status to include both social *and* economic disadvantage. Socially disadvantaged persons were defined as those "…who have been subjected to racial or ethnic prejudice or cultural bias because of their identity as a member of a group without regard to their individual qualities."[98] Economic disadvantage also had to be proved. It was defined as: "those socially disadvantaged individuals whose ability to compete in the free enterprise system has been impaired due to diminished capital and credit opportunities as compared to others in the same business area who are not socially disadvantaged…."[99]

This involved an examination of the individual's total net worth. While the individual had to qualify socially and economically, it was the business entity, whether sole proprietorship, partnership, or corporation, that received the certification. But to qualify for certification, the business entity had to also be at least 51 percent owned and controlled by socially and economically disadvantaged individuals and qualify as a "small" business.

In 1980, USDOT instituted the M/WBE program for all recipients of federal transportation funds. The program was not initiated in response to specific congressional direction, but was based on Title VI of the Civil Rights Act and on several transportation statutes containing general provisions directing federal agencies to prevent discrimination.[100]

The M/WBE program was unique in several respects. First, each transportation agency or "recipient" was directed to prepare overall annual goals for federal approval and to establish specific goals for minorities and women businesses for each construction contract. Second, traditional award to the lowest responsible bidder was modified to require a two-step bidding process in which (1) bids were opened to determine prices, and then (2) those bidders desiring to remain in competition were to submit their M/WBE participation documentation by a stated date and time. Award was then to be made to the lowest responsible bidder with a "reasonable price" meeting the specific M/WBE goals. If none met the goal, award was to be made to the bidder with the highest M/WBE participation and a "reasonable price." A "reasonable price" was the highest price at which the agency would award the contract if there were a single bidder.[101]

The regulation also permitted set-asides where authorized by state law and found necessary for the state to meet its annual goal. A further condition for use of set-asides provided that there must be at least three capable MBEs identified as available to bid on the contract to provide adequate competition for the contract.[102]

Numerous lawsuits were filed challenging the regulations, including *Central Alabama Paving v. James*.[103] In that case, the court concluded that USDOT was acting beyond the bounds of congressional authority in promulgating the M/WBE regulations and had not determined prior to issuing the regulations whether prior discrimination had occurred against the minority groups and women favored by the program.

c. Good-Faith Efforts and the DBE Program

In the early 1980s, USDOT issued new interim regulations eliminating the two-step bidding process and replacing it with a good-faith effort standard for contract award. This permitted the states to award to the low bidder even if the MBE or WBE goal was not met, provided that the bidder could demonstrate that it made good-faith efforts to secure minority or women subcontractors but was unable to achieve the goal. The new regulations also eliminated the conclusive presumption of social and economic disadvantage being applied to the listed minorities and replaced it with a rebuttable presumption.[104] Congress then passed STAA, of 1982, which included a one-sentence provision in Section 105(f):

> Except to extent the Secretary [of Transportation] determines otherwise, not less than ten percent of the amounts authorized to be appropriated under this Act shall be expended with small business concerns owned and controlled by socially and economically disadvantaged individuals as defined by section 8(d) of the Small Business Act (15 U.S.C. 637(d)) and relevant subcontracting regulations promulgated pursuant thereto[105]

USDOT's next regulations were issued on July 21, 1983.[106] Those regulations followed the lead of the Small Busines Act regulations and provided a rebuttable presumption that the members of designated mi-

[96] 15 U.S.C. § 637(a)(1)(B).

[97] *See, e.g.,* Fortec Constructors v. Kleppe, 350 F. Supp. 171, 173 (D.D.C. 1972) (SBA had authority to designate projects for SBA subcontract awards and plaintiff could not challenge the award without alleging denial of a right and opportunity to compete under the 8(a) certification program, i.e., that it was entitled to and was denied 8(a) status).

[98] 15 U.S.C. § 637(a)(5) (2002).

[99] 15 U.S.C. § 637(a)(6)(A) (2002).

[100] 64 Fed. Reg. 5096 (Feb. 2, 1999).

[101] 45 Fed. Reg. 21184 (Mar. 31, 1980).

[102] *Id*.

[103] 499 F. Supp. 629 (M.D. Ala. 1980).

[104] *See* FINCH, *supra* note 88.

[105] Pub. L. No. 97-424.

[106] 48 Fed. Reg. 33432 (July 21, 1983).

nority groups are socially and economically disadvantaged. For example, a wealthy minority or woman business owner would be ineligible because he or she was not economically disadvantaged. The DBE program was restricted to those identified with a minority group and those with Small Busines Act Section 8(a) certifications, and the regulations mandated that the state recipients honor all Small Busines Act Section 8(a) certifications.[107]

In 1987, Section 105(f) of STAA was replaced by Section 106(c) of the STURAA:

> Except to the extent that the Secretary [of Transportation] determines otherwise, not less than 10 percent of the amounts authorized to be appropriated under titles I, II, and III of this Act or obligated under titles I, II, and III (other than section 203) of the Surface Transportation Assistance Act of 1982 after the date of the enactment of this Act shall be expended with small business concerns owned and controlled by socially and economically disadvantaged individuals. [108]

One major change was that women were presumptively included within the class of socially and economically disadvantaged individuals:

> The term "socially and economically disadvantaged individuals" has the meaning such term has under section 8(d) of the Small Business Act (15 U.S.C. 637(d)) and relevant subcontracting regulations promulgated pursuant thereto; *except that women shall be presumed to be socially and economically disadvantaged individuals for purposes of this subsection*.[109]

Congress then passed ISTEA, in 1991, which continued the requirement that not less than 10 percent of the federal highway funds be spent on contracts or subcontracts with DBEs.[110] Section 1003 of ISTEA defined a "small business" as one with average annual gross receipts of less than $15,370,000 for the preceding 3 years, with the amount to be adjusted upward for inflation in subsequent years.[111] Section 1003 also incorporated the Section 8(d) definition of disadvantaged businesses. TEA-21, passed in 1998, also continued the Federal DBE program.[112]

3. Historical Background: Constitutional Review of Affirmative Action Programs

The U. S. Supreme Court has reviewed a number of affirmative action cases that have ultimately required significant changes in the DBE program. These decisions show the development of the strict scrutiny standard of review that now applies to these programs.

In one case, the Court struck down an AAP in an admissions policy for university medical students.[113] The Court also addressed whether programs served a compelling state interest and whether "societal discrimination" was an adequate basis for AAP requirements.[114] *Fullilove* upheld the constitutionality of an MBE program established by Congress for public construction for economically depressed communities.[115] *Croson* applied a strict scrutiny standard for local public works projects, and *Adarand* applied the same standard to federal projects.[116] *Adarand* required major changes to the DBE program, resulting in issuance of a new rule by USDOT on February 2, 1999.[117]

a. Fullilove v. Klutznick

The *Fullilove* case involved an AAP created by Congress rather than by EO or administrative action.[118] This case later served as the basis for adding Section 105(f) of the STAA of 1982, establishing the DBE program for federal-aid highway appropriations.

In May 1977, Congress enacted the Public Works Employment Act (PWEA), appropriating $4 billion for federal grants to state and local governments for local public works projects.[119] The main objective was to alleviate widespread unemployment. It included an MBE provision requiring that "…no grant shall be made under this Chapter for any local public works project unless the applicant gives satisfactory assurance…that at least 10 per centum of the amount of each grant shall be expended for minority business enterprises" with provision for administrative waiver by the Secretary of Commerce.[120] Regulations issued by the Secretary required competitive bidding and award by local entities to prime contractors responsive to the MBE requirements. The 10 percent MBE goal could be waived if the bidder could demonstrate that MBE subcontractors

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[107] 48 Fed. Reg. 33432 (July 21, 1983); *see* 13 C.F.R § 124.104(c)(2).

[108] Pub. L. No. 100-17 (Apr. 2, 1987), § 106(c)(1).

[109] Pub. L. No. 100-17 (Apr. 2, 1987), § 106(c)(2)(B) (emphasis added).

[110] Pub. L. No. 102-240, 105 Stat. 1914.

[111] *Id.* § 1003(b)(2)(A).

[112] Pub. L. No. 105-178 (June 9, 1998).

[113] Regents of the Univ. of Cal. v. Bakke, 438 U.S. 265, 98 S. Ct. 2733 57 L. Ed. 2d 750 (1978) ("strict scrutiny" test applied to protect minorities against discrimination would apply equally to protect any and all members of society, including nonminorities from discrimination).

[114] Wygant v. Jackson Board of Educ., 476 U.S. 267, 106 S. Ct. 1842 90 L. Ed. 2d 260 (1986) (more tenured white teachers were laid off in preference to retaining probationary minority teachers in order to maintain affirmative actions gains in minority hirings; providing minority role models was not a compelling state interest and reliance on societal discrimination failed to provide the needed evidence of prior acts of discrimination; means chosen were not narrowly tailored to accomplish purpose).

[115] *See infra* note 118 and accompanying text.

[116] *See infra* note 129 and note 57, and accompanying text.

[117] *Id.*; 49 C.F.R. pt. 26 (2000).

[118] Fullilove v. Klutznick, 448 U.S. 448, 100 S. Ct. 2758 65 L. Ed. 2d 902 (1980).

[119] 91 Stat. 116.

[120] 91 Stat. 116; 42 U.S.C. § 6705(f)(2).

were not available at a reasonable price. Otherwise, the contract would be awarded to another bidder.[121]

The Supreme Court held that the objectives of the MBE provisions of the Act were within the proper exercise of the powers of Congress and passed constitutional muster. The MBE provision fell within Congress's broad constitutional authority, and the means selected, using racial and ethnic criteria as described in the legislation and implemented by the regulations, did not violate constitutional guarantees of nonminorities.

The most significant basis of the holding was that the AAP was enacted by Congress:

> A program that employs racial or ethnic criteria, even in a remedial context, calls for close examination; yet we are bound to approach our task with appropriate deference to the Congress, a co-equal branch charged by the Constitution with the power to "provide for the…general Welfare…" and "to enforce, by appropriate legislation" the equal protection guarantees of the Fourteenth Amendment.…[122]

Also, Congress was not required to make findings or create a record. The Court found that the legislative history of the PWEA was sufficient to support a congressional conclusion that minorities had been denied effective participation in public contracts.[123]

The Court favored the "nonmandatory" nature of the AAP, referencing the waiver provisions implemented by the regulations.[124] The AAP thus was able to avoid the "quota" stigma and possible disqualification. The Court also noted the competitive bidding requirement, which created incentives to prime contractors to meet their MBE obligations to qualify as responsive bidders and to seek out the most competitive, qualified, and bona fide minority subcontractors.[125] Finally, the Court noted the Act's narrow focus, short duration, and minimal impact on nonminorities innocent of past discriminatory practices.[126]

b. Croson v. City of Richmond

In *J.A. Croson v. City of Richmond,*[127] the City of Richmond advertised for competitive bids to refurbish the plumbing fixtures in its city jail. By ordinance, the City had established a minority preference program that required nonminority-owned prime contractors to subcontract at least 30 percent of the total contract to MBEs. J.A. Croson submitted the only bid and provided no minority participation, although it had contacted several minority suppliers without success. Croson requested a waiver of the MBE requirement, which the City denied. A major portion of the contract involved the purchase of plumbing fixtures, so Croson next arranged for a minority supplier, but at a price higher than the original supplier relied upon in the bid. The City also rejected the higher contract price to accommodate the MBE supplier.

The federal district court upheld the City's minority plan. The Fourth Circuit Court of Appeals initially affirmed, but on remand following a Supreme Court order directing reconsideration in light of an intervening decision, the Fourth Circuit reversed the judgment on the basis that the ordinance violated the Federal Equal Protection Clause.[128] The Supreme Court affirmed the Fourth Circuit ruling.[129]

For the first time, a majority agreed that racially based preference programs would be subject to the constitutional strict scrutiny test. This case also reinforced the Court's earlier plurality ruling in *Wygant v. Jackson Board of Education* that reliance on "societal discrimination" will not suffice.[130] The effect of these two principles of strict scrutiny and inability to rely on societal discrimination meant that classifications based on race would be presumed invalid. Justice O'Connor's opinion, which was divided into six distinct parts, represented the majority views of the Court on all but Part II, which dealt with whether *Fullilove* provided authority for local legislative bodies to adopt an AAP without independent findings of past discrimination.[131]

Part I affirmed the court of appeals based on the earlier *Wygant* ruling against reliance on "societal discrimination:" "As the court read this requirement, '[f]indings of *societal* discrimination will not suffice; the findings must concern "prior discrimination *by the government unit involved*."'"[132]

The Court found that the city council had not made findings of prior discrimination.[133] The Court affirmed the Fourth Circuit's ruling that the 30 percent set-aside was chosen arbitrarily and was not narrowly tailored.[134]

The City relied heavily on *Fullilove v. Klutznick*, arguing that *Fullilove* was controlling and provided the City with "sweeping legislative power to define and attack the effects of prior discrimination in its local construction industry."[135] In distinguishing *Fullilove*, Justice O'Connor viewed Sections 1 and 5 of the Fourteenth Amendment as limitations on the powers of the states and an enlargement of the power of Congress

[121] *Id*.

[122] 448 U.S. at 472, 100 S. Ct. 2772.

[123] 448 U.S. at 478.

[124] *Id*. at 488–90.

[125] *Id*. at 481.

[126] *Id*. at 484.

[127] J.A. Croson v. City of Richmond, 779 F.2d 181 (4th Cir. 1985).

[128] 822 F.2d 1355 (4th Cir. 1987).

[129] Richmond v. J.A. Croson Co., 488 U.S. 469, 109 S. Ct. 706, 102 L. Ed. 2d 854 (1989).

[130] 488 U.S. at 486 (citing Wygant v. Jackson Board of Educ., 476 U.S. 267 106 S. Ct. 1842, 90 L. Ed. 2d 260 (1986)).

[131] *See* Contractors Ass'n of Eastern Pa. v. City of Phila., 735 F. Supp. 1274, 1288–92 (E.D. Pa. 1990) for an extensive discussion of Justice O'Connor's opinion by Chief Judge Bechtle.

[132] 488 U.S. at 485 (emphasis in original).

[133] *Id*.

[134] *Id*. at 486.

[135] *Id*.

to identify and redress the effects of societal discrimination.[136]

In Part III-A, for the first time in a majority holding, the Supreme Court ruled that all classifications based on race will be subject to strict scrutiny, whether they benefit or burden minorities or nonminorities. Thus, all such classifications by states and local governments would be presumed invalid: "We thus reaffirm the view expressed by the plurality in *Wygant* that the standard of review under the Equal Protection Clause is not dependent on the race of those burdened or benefited by a particular classification…."[137]

In Part III-B of the majority opinion, the Court set out the requirement that the "factual predicate" underlying the AAP be supported by adequate findings of past discrimination without reliance on generalized assertions of past discrimination:

> We think it clear that the factual predicate offered in support of the Richmond Plan suffers from the same two defects identified as fatal in Wygant…. Like the "role model" theory employed in Wygant, a generalized assertion that there has been past discrimination in an entire industry provides no guidance for a legislative body to determine the precise scope of the injury it seeks to remedy….[138]

The Richmond City Council had attempted to establish a factual predicate by relying on the exclusion of blacks from skilled construction trade unions and training programs, and on statements made by proponents of the plan that there had been past discrimination in the industry and that minority business had received less than 1 percent of the prime contracts from the City, while minorities represented 50 percent of the city's population. But the majority disagreed that this was adequate: "None of these 'findings,' singly or together, provide the city of Richmond with a 'strong basis in evidence for its conclusion that remedial action was necessary.' There is nothing approaching a prima facie case of a constitutional or statutory violation by *anyone* in the Richmond construction industry."[139]

The Court concluded that the City was applying its preferential program as a strict quota rather than attempting to use its provisions as a goal. For example, Croson was a sole bidder who demonstrated what could be described as good-faith efforts to secure a minority supplier both before and after the bidding, yet the City rejected its bid.

> While there is no doubt that the sorry history of both private and public discrimination in this country has contributed to a lack of opportunities for black entrepreneurs, this observation, standing alone, cannot justify a rigid racial quota in the awarding of public contracts in Richmond, Virginia. Like the claim that discrimination in primary and secondary schooling justifies a rigid racial preference in medical school admission, an amorphous claim that there has been past discrimination in a particular industry cannot justify the use of an unyielding racial quota.[140]

The Court concluded that, "none of the evidence presented by the City points to any identified discrimination in the Richmond construction industry," and ruled that as a consequence, "the city has failed to demonstrate a compelling interest in apportioning public contracting opportunities on the basis of race."[141]

In Part IV, the Court observed that without the specificity needed to identify the past discrimination, it could not assess whether the Richmond Plan was narrowly tailored. But the majority did not view the 30 percent quota as being narrowly tailored to any legitimate goal. Justice O'Connor noted the City's failure to consider any alternatives to the race-based quota system, its rigid adherence to the 30 percent quota, and its refusal to grant a waiver. "Under Richmond's scheme, a successful black, Hispanic, or Oriental entrepreneur from anywhere in the country enjoys an absolute preference over other citizens based solely on their race. We think it obvious that such a program is not narrowly tailored to remedy the effects of prior discrimination."[142]

Part V concerns the failure of the City to explore possible "race-neutral devices" to increase contracting opportunities for small contractors of all races:

> Simplification of bidding procedures, relaxation of bonding requirements, and training and financial aid for disadvantaged entrepreneurs of all races would open the public contracting market to all those who have suffered the effects of past societal discrimination or neglect. Many of the formal barriers to new entrants may be the product of bureaucratic inertia more than actual necessity, and may have a disproportionate effect on the opportunities open to new minority firms….[143]

The majority emphasized that "[n]othing we say today precludes a state or local entity from taking action to rectify the effects of identified discrimination within its jurisdiction."[144] At the same time the Court noted the importance of adequate findings:

> Proper findings in this regard are necessary to define both the scope of the injury and the extent of the remedy necessary to cure its effects. Such findings also serve to assure all citizens that the deviation from the norm of equal treatment of all racial and ethnic groups is a temporary matter, a measure taken in the service of the goal of equality itself. Absent such findings, there is a danger that a racial classification is merely the product of unthinking stereotypes or a form of racial politics….[145]

c. Adarand Constructors v. Pena

Adarand Constructors, Inc. v. Pena answered the question as to whether strict scrutiny would apply to

[136] *Id*. at 491.

[137] *Id*. at 494.

[138] *Id*. at 498 (citations omitted; emphasis in original).

[139] *Id*. at 500.

[140] *Id*. at 499.

[141] *Id.* at 505.

[142] *Id.* at 508.

[143] *Id.* at 509–10.

[144] *Id.* at 509.

[145] *Id*. at 510.

federal contracting.[146] Adarand Constructors was a Colorado construction company that specialized in guardrail work. As such, it regularly competed for subcontracts on highway construction projects. In 1989, the Central Federal Lands Highway Division of FHWA awarded a prime contract to Mountain Gravel & Construction Company. The terms of the direct federal construction contract provided that Mountain Gravel would receive additional compensation if it gave subcontracts to "socially and economically disadvantaged individuals."[147] Adarand was not certified as a DBE. The subcontract that Adarand competed for was awarded to a DBE, despite the fact that Adarand was the low bidder. The prime admitted that but for the additional payment the prime would receive for hiring the DBE, it would have hired Adarand.[148]

Federal law required that the construction contract state that "'the contractor shall presume that socially and economically disadvantaged individuals include Black Americans, Hispanic Americans, Native Americans, Asian Pacific Americans, and other minorities or any other individual found to be disadvantaged by the [Small Business] Administration pursuant to section 8(a) of the Small Business Act.'"[149] Adarand claimed that the provision discriminated on the basis of race in violation of the Fifth Amendment obligation not to deny anyone equal protection of the law. The district court had granted the government's summary judgment motion.[150] The Tenth Circuit affirmed, based on its understanding that *Fullilove* set out an intermediate scrutiny standard for race-based federal action.[151] The Supreme Court vacated the court of appeals ruling and remanded the case to the trial court.[152]

The Court reviewed the development of its views regarding rights protected by the Fifth Amendment, beginning with the 1940s cases that upheld the internment of Japanese Americans.[153] Those cases resulted in the Court's holding that there is a difference between the rights protected by the Fourteenth Amendment and those protected by the Fifth Amendment, and that the Fifth Amendment "provides no guaranty against discriminatory legislation by Congress."[154] However, the Court noted that even in so holding, the earlier Court had stated in the *Hirabayashi v. United States* decision that "'distinctions between citizens solely because of their ancestry are by their very nature odious.'"[155]

The Court noted that despite the uncertainty in their details, the cases through *Croson* established three general propositions with respect to governmental race classifications: (1) skepticism, or a requirement that a racial preference receive "a most searching examination"; (2) consistency, or a requirement that the same standard apply whether a particular class is burdened or benefited; and (3) congruence, or the application of the same standard under either the Fifth Amendment or the Fourteenth Amendment.[156] Applying these principles, Justice O'Connor concluded as follows:

> Taken together, these three propositions lead to the conclusion that any person, of whatever race, has the right to demand that any governmental actor subject to the Constitution justify any racial classification subjecting that person to unequal treatment under the strictest judicial scrutiny….
>
> ….
>
> Accordingly, we hold today that all racial classifications, imposed by whatever federal, state, or local governmental actor, must be analyzed by a reviewing court under strict scrutiny. In other words, such classifications are constitutional only if they are narrowly tailored measures that further compelling governmental interests.[157]

Finally, Justice O'Connor set out the requirement that remedies be narrowly tailored:

> The unhappy persistence of both the practice and the lingering effects of racial discrimination against minority groups in this country is an unfortunate reality, and government is not disqualified from acting in response to it…When race-based action is necessary to further a compelling interest, such action is within constitutional constraints if it satisfies the "narrow tailoring" test this Court has set out in previous cases.[158]

The Court remanded *Adarand* to the district court for a determination of whether any of the ways that the government was using the subcontractor compensation clauses could survive strict scrutiny.[159]

The result of the *Adarand* decision was the adoption of new regulations by the USDOT that were intended to be consistent with the requirements of strict scrutiny, and that provide a remedy for demonstrated discrimination, but that do not rely on the "societal discrimination" that had been a basis for racial preference programs in the past.

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[146] 515 U.S. 200, 115 S. Ct. 2097, 132 L. Ed. 2d 158 (1995).

[147] 515 U.S. at 205, 209. The subcontracting compensation clause at issue provided:

> Monetary compensation is offered for awarding subcontracts to small business concerns owned and controlled by socially and economically disadvantaged individuals…
>
> The Contractor will be paid an amount computed as follows:
>
> 1. If a subcontract is awarded to one DBE, 10 percent of the final amount of the approved DBE subcontract, not to exceed 1.5 percent of the original contract amount….

[148] *Id*. at 205.

[149] *Id*. (citations omitted).

[150] Adarand Constructors, Inc. v. Skinner, 790 F. Supp. 240 (D. Colo. 1992).

[151] Adarand Constructors, Inc. v. Pena, 16 F.3d 1537 (10th Cir. 1994).

[152] Adarand Constructors, Inc. v. Pena, 515 U.S. 200, 204–05, 115 S. Ct. 2097, 132 L. Ed. 2d 158 (1995).

[153] *Id*. at 213–14 (citing Hirabayashi v. United States, 320 U.S. 81, 63 S. Ct. 137, 87 L. Ed. 1774 (1943)).

[154] *Id*. at 213 (citations omitted).

[155] *Id*. at 215 (quoting *Hirabayash*i, 320 U.S. at 100).

[156] *Id*. at 223–24.

[157] *Id*. at 224, 227.

[158] *Id*. at 237 (citation omitted).

[159] *Id*. at 238–39.

d. Adarand on Remand: Review of Revised USDOT Regulations

The U.S. Supreme Court remanded the *Adarand* case to the district court for a determination of whether the USDOT regulations met the new standard of review that it set out in that case. The federal district court subsequently held that the Subcontractor Compensation Clause (SCC) was unconstitutional as not being narrowly tailored.[160] The Tenth Circuit found on review that because the Colorado DOT had certified Adarand as a DBE, its case was moot.[161] The U.S. Supreme Court vacated that decision and remanded the case to the Tenth Circuit for consideration on the merits.[162]

The Tenth Circuit held that while the SCC failed to pass strict scrutiny, the new USDOT regulations were narrowly tailored and were constitutional.[163] The court noted the standard set out by the Supreme Court, which required that the government prove a compelling interest with evidence of past and present discrimination in federally funded highway construction.[164] The court found adequate evidence in the many studies considered by Congress in its enactment of amendments to the Federal Highway Act.[165] The government's evidence demonstrated two particular barriers to minority participation in subcontracting: those that created a barrier to the formation of minority- and women-owned firms, and those that acted as a barrier to participation by DBEs.[166] The most significant obstacles identified were lack of access to capital and inability to get surety bonds.[167] The government also presented evidence that "when minority firms are permitted to bid on subcontracts, prime contractors often resist working with them."[168] The court concluded that the government's evidence established "the kinds of obstacles minority subcontracting businesses face," and that these obstacles are different from those faced by other new businesses.[169] The court also found evidence of discrimination in disparity studies, and studies of minority business participation after affirmative action programs were discontinued.[170] The court therefore concluded that there was evidence to support the contention that there was a compelling interest to be served by the DBE requirements.

The court further found that the new USDOT regulations were narrowly tailored to address the compelling interest. The court based this conclusion on the fact that (1) the program relies in large part on race-neutral means of achieving its goals;[171] (2) there are time limits on the duration of the DBE certification program;[172] (3) the program is flexible, and includes waiver provisions;[173] (4) the program is numerically proportional to the numbers of available firms, and allows good-faith efforts to meet requirements;[174] (5) there is an acceptable burden on third parties;[175] and (6) the DBE program is neither over- nor under-inclusive in that minority firms above a certain gross income level are ineligible for it.[176]

4. Challenges to AAPs After Croson and Adarand

a. State and Local Programs

Croson and *Adarand* led to challenges being filed against state and local M/WBE programs as well as DBE programs administered by recipients, based on contentions that those programs would not survive strict scrutiny.[177]

Phillips & Jordan, Inc. v. Watts involved a challenge to an FDOT DBE program.[178] FDOT was authorized under state law to implement a program to remedy disparities based on race, national origin, and gender, based on a showing of past and/or continuing discrimination in the award of state-funded highway contracts.[179] The program required annual goals for minority participation, and allowed FDOT to set aside contracts for DBEs. The goals and set-asides were supposed to be based on a finding of "significant disparity" in a disparity study.

FDOT set aside certain maintenance contracts for black- or Hispanic-owned businesses, despite the fact that there was no evidence that the agency had ever discriminated against these groups in the award of maintenance contracts. Rather, FDOT claimed it was a "passive participant" in discrimination practiced in the

[160] Adarand Constructors, Inc. v. Pena, 965 F. Supp. 1556 (D. Colo. 1997).

[161] Adarand Constructors, Inc. v. Slater, 169 F.3d 1292 (10th Cir. 1999).

[162] Adarand Constructors, Inc. v. Slater, 528 U.S. 216, 120 S. Ct. 722, 145 L. Ed. 2d 650 (2000).

[163] Adarand Constructors, Inc. v. Slater, 228 F.3d 1147 (10th Cir. 2000). The court noted that by the time of this decision, the SCCs were no longer used by FHWA in its direct federal contracts. *Id*. at 1159 n.4.

[164] *Id*. at 1164.

[165] *Id*. at 1167 (citing "The Compelling Interest for Affirmative Action in Federal Procurement," 61 Fed. Reg. 26,050, 26,051–52 & nn.12–21 (1996)).

[166] *Id*. at 1167–68.

[167] *Id*. at 1169

[168] *Id*. at 1170 (citing 61 Fed. Reg. at 26, 058–59).

[169] *Id*. at 1172.

[170] *Id*. at 1172–75.

[171] *Id*. at 1178–79.

[172] *Id*. at 1179.

[173] *Id*. at 1180–81.

[174] *Id*. at 1181–83.

[175] *Id*. at 1183.

[176] *Id*. at 1183–86.

[177] For a summary of court decisions on state and local DBE/M/WBE programs following Croson, *see* D. Rudley and D. Hubbard, *What a Difference A Decade Makes: Judicial Response To State And Local Minority Business Set-Asides Ten Years After*, City of Richmond v. J.A. Croson, 25 S. ILL. U. L.J. 39–93 (2000).

[178] 13 F. Supp. 2d 1308 (N.D. Fla. 1998).

[179] FLA. STAT. § 339.0805(1)(b).

private sector.[180] In reviewing the program, the court applied the strict scrutiny analysis mandated by *Croson*.[181] The "strong basis in evidence" that *Croson* required as proof of past discrimination could not be based on "societal discrimination" or on an unsupported assumption regarding past discrimination in a particular industry. Rather, it must be based on a showing of the agency's own active or passive participation in past or present discrimination, possibly by prime contractors, bonding companies, or financial institutions.[182]

Defending its program, FDOT argued that it must have been a passive participant in discrimination based on its disparity study, which compared the number of contracts awarded by FDOT with the number of available DBEs. The court rejected this argument, noting that any such discrimination must be demonstrated with particularity.[183] While statistical evidence may serve this purpose, it does not do so where the "identity of the wrongdoers is unknown."[184] The court found that FDOT officials had merely speculated that FDOT had been a possible participant in discrimination by primes, bonding companies, and financial institutions, with no evidence to establish who may have engaged in any discriminatory practices.[185] The court held that an AAP must be focused on "those who discriminate."[186] A disparity study that relied on "ill-defined wrongs" committed by "unidentified wrongdoers" was insufficient under *Croson*.[187]

In *Louisiana Associated General Contractors v. State*, the Louisiana Supreme Court held that its own state constitution precludes any AAP, even one that passes strict scrutiny under *Croson*. The court held that the Louisiana Bid Preference Act violated the equal protection requirements of the state constitution.[188] The Louisiana Health Care Authority had set aside a clinic renovation project as a DBE-only project in its advertisement for bids.[189] The program created a bid preference for minority contractors, in that all contractors could bid, but a certified MBE would receive the bid if its bid was within 5 percent of the lowest responsive and responsible bid, provided that the MBE agreed to contract for the amount of the lowest bid.[190] AGC challenged the specification on the grounds that it violated equal protection. The court enjoined the receipt and acceptance of bids, and also enjoined the agency from continuing to advertise the project as a set-aside. The agency readvertised the project without the set-aside provision; however, the court did not consider the issue moot as the agency intended to bid future contracts as set-asides.[191]

The court relied on *Croson* and *Adarand* for the principle that the same standard applies regardless of what race is burdened or benefited.[192] The court found even less tolerance for the program in the state constitution than in the U.S. Constitution, however, holding that the state constitution allows *no* scrutiny to be applied to the program. Rather, the court held that when a law discriminates against a person by classifying him or her on the basis of race, "it shall be repudiated completely, regardless of the justification behind the racial discrimination."[193]

The state agency utilized the program in part to qualify for federal funds. The court refused to allow this as a basis for what it considered a prohibited discriminatory program, and found that the "absolute and mandatory language used in the prohibition against laws which discriminate on the basis of race found in the constitution does not change simply because the state may stand to lose federal funds…."[194]

California's M/WBE program was declared to be unconstitutional as violating the equal protection clause in *Monterey Mechanical Co. v. Wilson*.[195] Despite the fact that the program allowed contractors to either comply with the contract goals or show good-faith efforts to do so, the court found that the program was not supported by evidence of past or present discrimination against the protected groups. The state did not present any evidence of past or present discrimination, relying only on general findings stated in the legislation. Finding that the program also was not narrowly tailored, the court noted that the program included a number of minority groups who were highly unlikely to be found in California.

A city ordinance allowing set-aside contracts was challenged by a contractor association in *Contractor's Association of Eastern Pennsylvania v. City of Philadelphia*.[196] The ordinance allowed the use of set-asides for black contractors; if there were insufficient black contractors available for competitive bidding, then the goal could be met through subcontracting.[197] The City utilized the subcontracting portion of the ordinance exclusively, and did not create set-asides. Meeting the subcontracting goal was considered an element of responsiveness. Good-faith efforts were to be considered, however, if at least one bidder met the goal; then all others were presumed not to have used good-faith efforts. If no bidder met the goals, the one who had the

[180] 13 F. Supp. 2d at 1312, 1314.

[181] *Id*.

[182] *Id*. at 1313.

[183] *Id*.

[184] *Id*.

[185] *Id*. at 1314.

[186] *Id*.

[187] *Id*.

[188] 669 So. 2d 1185 (La. 1996).

[189] LA. REV. STAT. 39:1951 et seq.

[190] 669 So. 2d at 1201.

[191] 669 So. 2d at 1189.

[192] *Id*. at 1198.

[193] *Id*.

[194] *Id*. at 1200.

[195] 125 F.3d 702 (9th Cir. 1998), *rehearing denied*, 138 F.3d 1270.

[196] 91 F.3d 586 (3d Cir. 1996).

[197] *Id*. at 592–93.

highest minority participation was granted a waiver and awarded the contract.[198]

The district court found that the ordinance created a protected segment of city construction work for which non-DBEs could not compete.[199] Relying on *Croson*, the court applied strict scrutiny, noting that a program can withstand strict scrutiny only if it is "narrowly tailored to serve a compelling state interest." The court then set out the test as follows:

> The party challenging the race-based preferences can succeed by showing either (1) that the subjective intent of the legislative body was not to remedy race discrimination in which the municipality played a role or (2) that there is no "strong basis in evidence" for the conclusions that race-based discrimination existed and that the remedy chosen was necessary. (citation omitted).[200]

The court ultimately rejected the program on the basis that it was not narrowly tailored.[201] Where the only identified discrimination was by the City in its award of prime contracts, a program that focused exclusively on subcontracting did not provide a narrowly tailored remedy. The court thus declared the subcontracting portion of the ordinance unconstitutional under *Croson*.[202] Regarding the set-aside provision, the City did not have evidence to show that a 15 percent set-aside was necessary to remedy the discrimination, where that figure was much higher than the percentage of minority firms qualified to do City construction work.[203]

The court also addressed the ordinance's failure to include race-neutral measures, such as relaxed bonding or prequalification requirements for newer businesses. In addition, the City could have used training and financial assistance programs to assist disadvantaged contractors of all races. Because these measures were available to the City, the court found that to the extent the program did not utilize race-neutral measures, it was not narrowly tailored and was thus unconstitutional.[204]

An example of a program that was upheld after *Croson* is found in *Domar Electric v. City of Los Angeles*.[205] A bidder challenged a contractor "outreach" program that was required by a city ordinance as being inconsistent with the city charter and with competitive bidding rules. The program required only that contractors make a good-faith effort to include DBEs as subcontractors; it did not require bid preferences or quotas, nor did it allow the City to set aside contracts for DBEs. The ordinance stated that a contractor's good-faith efforts would be evaluated by considering its efforts in (1) identifying and selecting specific work items for subcontracting to DBEs, (2) advertising that work to DBEs, (3) providing information to the DBE contractor community, and (4) negotiating in good faith with DBE subcontractors that were interested in subcontracting. The program set goals, but a bidder's failure to meet the goal in its bid did not disqualify the bidder or render its bid nonresponsive. There was no advantage gained from meeting the goal, nor was there a disadvantage from not meeting the goal.[206]

Domar was the low bidder, but failed to provide documentation of its good-faith efforts by the deadline. The contract was then awarded to the next low bidder, and Domar appealed. The superior court denied its appeal, but the court of appeals reversed, finding the outreach program unconstitutional under *Croson*.[207] The California Supreme Court reversed, holding that the outreach program was constitutional. The program did not conflict with the city charter, even though it was not specifically authorized by the charter. It was also consistent with the goals of competitive bidding, such as excluding favoritism and corruption. The court reasoned that competitive bidding requirements necessarily imply that there be equal opportunities provided to all who may be interested in bidding. The outreach program only required that minority and women businesses be contacted and equal opportunities provided to them to bid on subcontracts.[208]

b. Federal Programs

A federal court examined the constitutionality of USDOT's DBE program in light of the *Adarand* decision in *In re Sherbrooke Sodding Company*.[209] This case was both a facial and an as-applied challenge to the DBE program authorized by ISTEA in 1991 as well as the Minnesota Department of Transportation's (MnDOT) DBE program.[210] The court also considered a 1996 memorandum in which FHWA directed the states to "count the participation of DBE primes as 100 percent both towards meeting overall recipient goals and…toward meeting contract-specific goals."[211] The result of this change in policy was that DBE prime contractors were exempt from DBE subcontract requirements, which would continue to apply to non-DBE primes.

The court noted that under *Adarand*, the government bears the burden of showing that the DBE program is constitutional by proving that its race and gender classifications are narrowly tailored to serve a compelling governmental interest.[212] MnDOT claimed

[198] *Id*. at 593.

[199] Contractors Ass'n of Easton Pa. v. City of Pa., 893 F. Supp. 419, 426 (E.D. Pa. 1995).

[200] *Id*. 91 F.3d at 597.

[201] *Id*. at 605.

[202] *Id*. at 606.

[203] *Id*. at 607.

[204] *Id*. at 609.

[205] 9 Cal. 4th 161, 885 P.2d 934, 36 Cal. Rptr. 521 (1994).

[206] 9 Cal. 4th at 167.

[207] *Id*. at 168–69.

[208] *Id*. at 172–73.

[209] 17 F. Supp. 2d 1026 (D. Minn. 1998).

[210] Pub. L. No. 102-240, 105 Stat. 1914 (1991); 49 C.F.R. (1996).

[211] 17 F. Supp. 2d. at 1029.

[212] *Id*. at 1033. Although the Supreme Court has not indicated that it would apply strict scrutiny to gender-based classifications, this court was invited by the parties to do so, and for

that it was simply implementing a federal government program, and was therefore relieved from any duty to show that the program was narrowly tailored to serve a compelling state interest.[213] The court assumed that MnDOT was properly implementing the program, and turned to USDOT for proof that the program should survive strict scrutiny.

USDOT claimed (1) that Congress had made an adequate finding of past discrimination to support a compelling governmental interest, and (2) that Congress was not required to make such findings on a state or local basis, but rather could do so nationally. The court agreed with this argument, relying in part on the decision on remand in *Adarand* in which the district court in Colorado found that Congress had a "strong basis in evidence" to support a race-conscious program.[214]

The court then focused its analysis on whether the DBE program was narrowly tailored. The court found no evidence that Congress considered race-neutral alternatives to the DBE program. Noting that the Supreme Court had suggested several potential race-neutral measures in *Croson*, none of which were evident in the USDOT program, the court found a lack of such alternatives to "strongly suggest the DBE program is Constitutionally flawed."[215]

The court further found that the DBE program was not limited in duration, where *Adarand* required that such a program "'will not last longer than the discriminatory effects it is designed to eliminate.'"[216] However, due to ISTEA's sunset provision, the court did not consider this factor significant. More significant were the problems that the program placed an undue burden on innocent parties, was not sufficiently flexible, and tended to haphazardly include as DBE's virtually all nonwhite people.[217] The court held regarding the lack of flexibility: "Whatever the terminology or palliative applied, whether the program be called an 'aspirational goal' or ameliorated by a 'flexible waiver,' the bottom line is that there is still a quota that is imposed by the government. This quota penalizes some and advantages other, each without Constitutional justification."[218]

The court thus held that the USDOT DBE program failed to pass strict scrutiny as required by *Adarand*.

5. Narrowly Tailoring the DBE Requirements

During 1999, in response to the *Adarand* and *Sherbrooke Sodding* decisions, USDOT undertook a substantial revision of the DBE program in order to develop a program that would withstand strict scrutiny. First, the agency concluded that the Congressional debate surrounding the adoption of TEA-21 provided sufficient findings of a compelling governmental interest in remedying any discrimination in federally assisted transportation contracting.[219] The remainder of the rule adoption process was directed at creating a program that was narrowly tailored to address that discrimination. USDOT addressed each element of the narrow-tailoring test set out in *Adarand*: 1) determining the necessity of relief; 2) considering the efficacy of alternative (race-neutral) remedies; 3) providing for flexibility of relief, through use of waivers and good-faith efforts standards; 4) limiting duration of relief to the time needed to effect the remedy; 5) setting goals in relation to the relevant market; 6) considering the impact on the rights of third parties; and 7) inclusion of appropriate beneficiaries.[220]

The language in TEA-21 largely retained the 10 percent goal contained in previous legislation, which had always been applied by USDOT as requiring that each contract have a 10 percent DBE goal. However, USDOT's new rules recharacterized the meaning of the statutory goal language, interpreting it as a national overall goal:

> Section 26.41 makes clear that the 10 percent statutory goal contained in ISTEA and TEA-21 is an aspirational goal at the national level. It does not set any funds aside for any person or group. It does not require any recipient or contractor to have 10 percent (or any other percentage) DBE goals or participation. Unlike former part 23, it does not require recipients to take any special administrative steps (e.g. providing a special justification to DOT) if their annual overall goal is less than 10 percent. Recipients must set goals consistent with their own circumstances. (§ 26.45) There is no direct link between the national 10 percent aspirational goal and the way a recipient operates its program….[221]

a. Race-Neutral Alternatives

One of the reasons that the court found the USDOT program to not be narrowly tailored was its lack of race-neutral alternatives. As part of its revision, USDOT required recipients to first rely on race-neutral measures to meet the "maximum feasible portion" of their overall DBE goals.[222] Race-neutral alternatives include measures such as outreach, technical assistance, procurement process modifications, and other means of increasing opportunities for all small businesses, not just DBEs.[223] It may also include relaxing bonding requirements and prequalification standards for new or small businesses. Prompt payment requirements for all subcontractors are also race-neutral and have the effect of assisting DBEs that cannot tolerate delay in payment.[224] Also, when a DBE firm is awarded a prime

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the purposes of the motions before it, the court did apply strict scrutiny to the gender classifications. *Id*.

[213] *Id*. at 1033–34.

[214] *Id*. at 1034–35 (citing Adarand Constructors, Inc. v. Pena, 965 F. Supp. 1556, 1576–77 (D. Colo. 1997).

[215] *Id*. at 1035.

[216] *Id*. (quoting *Adarand*, 515 U.S. at 238).

[217] *Id*. at 1036–37.

[218] *Id*. at 1037.

[219] 64 Fed. Reg. at 5100-01 (1999).

[220] 64 Fed. Reg. at 5102-03.

[221] 64 Fed. Reg. at 5097.

[222] 64 Fed. Reg. at 5102.

[223] 64 Fed. Reg. at 5112.

[224] 49 C.F.R. § 26.29 (2000).

contract on the sole basis that it is the lowest responsible bidder, then that is considered to be a race-neutral alternative.[225] Recipients are expected to estimate how much of the overall goal they can meet through the use of race-neutral alternatives. Only then are they to set contract DBE goals.

b. Flexibility Through Contract Goals and Good-Faith Efforts Standards

Under the 1999 regulations, the contract is to be awarded to the lowest responsible bidder meeting the specified DBE goals or demonstrating good-faith efforts in its attempt to meet the goals.[226] One of the significant points made by the 1999 regulations is that in setting contract goals, they do not intend that a recipient be required to accept a higher bid from a DBE prime contractor when a non-DBE has submitted a lower bid. Thus the rule does not interfere with state and local requirements to award to the lowest responsible bidder. The comment to the rule notes that selection of subcontractors by bidders is not subject to any low-bid rule; a bidder may select any subcontractor that it wants, and generally does so based on its familiarity and experience with a subcontractor, the quality of the subcontractor's work, and the subcontractor's reputation in the community.[227] These factors can be as significant as price.[228] This was the basis for the requirement of good-faith efforts. "Contractors cannot simply refuse to consider qualified, competitive DBE subcontractors."[229]

The 1999 rules made major changes to the use of contract goals, in the interest of addressing the "flexibility" issue identified in *Adarand*. As noted earlier, the 10 percent goal in TEA-21 was interpreted by USDOT to be an overall national "aspirational" goal, and not a goal for any given contract.

Recipients have broad discretion to choose whether or not to use a goal on any given contract, and if they do choose to use a contract goal, they are free to set it at any level they believe is appropriate for the type and location of the specific work involved….[230]

In addition to providing flexibility to recipients in implementing DBE programs, flexibility is provided for each individual contract in that if a bidder fails to meet any goals established for that contract, it may satisfy the regulatory requirement by showing that it made good-faith efforts to do so. Examples of what might constitute good-faith efforts are listed in Appendix A to the 1999 rule. These include (1) soliciting the interest of DBEs through all "reasonable and available means," such as attendance at pre-bid conferences and advertising; (2) selecting portions of the work that may be subcontracted to DBEs, breaking out contract items into "economically feasible units"; (3) providing interested DBEs with adequate information; (4) negotiating in good faith with interested DBEs; (5) not rejecting DBEs as unqualified without a thorough investigation of their capabilities; (6) making efforts to assist DBEs in obtaining bonds, lines of credit, or insurance; (7) assisting DBEs in obtaining necessary equipment and supplies; and (8) utilizing minority and women's organizations for recruitment of DBEs.[231]

Any analysis of good-faith efforts must be made against this standard, although other factors, positive or negative, can legitimately be considered when included in the bidding specifications. For example, a bidder is not obligated to accept a minority whose price is "unreasonable."[232] This means that it is not sufficient that all the lowest subcontract prices were accepted and none were minorities. It must be demonstrated by the bidder that good faith negotiations were conducted with minorities and that their prices were unreasonable.

However, a system that required bidders to subcontract with DBEs regardless of price would likely violate the standards of *Croson* and *Adarand*. In *Monterey Mechanical Co. v. Sacramento Regional Sanitary District*, the California court of appeals found that a local requirement that M/WBE subcontracts could be rejected only for "significant price difference" violated the state statutory standard for evaluating good-faith efforts.[233] By requiring the bidder to accept a much higher priced M/WBE, the local agency effectively required that a bidder preference be accorded M/WBE subcontractors. In addition, the court found that the "negotiation in good faith" requirement only applies where there are interested M/WBEs with whom to negotiate on price. It did not require the bidder to "encourage" or "persuade" M/WBEs to submit subcontractor bids.[234]

Objective standards for judging good-faith efforts are difficult to discern from case law. The task imposed on state highway agencies is to analyze all the relevant facts and apply their best judgment. The natural course of action for an agency is to attempt to save a low bid where possible. The agency's exercise of its discretion will generally be upheld unless a clear abuse of discretion can be proved. The best course of action is to set out all of the standards in the bid specifications and then apply them as uniformly as possible. The *Monterey Mechanical* court did, however, find that it was reasonable to use a comparative approach in evaluating good-faith efforts. Although "comparative compliance" is not the standard, it is more reasonable for an agency to more closely scrutinize the efforts of a bidder who comes nowhere near the goal, as opposed to one who closely approaches it.[235]

[225] 64 Fed. Reg. at 5112.

[226] 49 C.F.R. § 26.53(b) (2000).

[227] 64 Fed. Reg. at 5099–5100.

[228] *Id*.

[229] *Id*. at 5100.

[230] 64 Fed. Reg. at 5102.

[231] 64 Fed. Reg. at 5145–56; 49 C.F.R. pt. 26, app. A (2001).

[232] 48 Fed. Reg. 33441-2, July 21, 1983, preamble commentary.

[233] 44 Cal. App. 4th 1391, 52 Cal. Rptr. 2d 395 (1996).

[234] *Id.* 52 Cal. Rptr. 2d at 406–07.

[235] 52 Cal. Rptr. 2d at 407.

c. Setting Overall Goals

The comments to the final 1999 rule include extensive discussion of how overall goals should be set. USDOT set out a two-step process that includes determining a base figure for the overall goal, and then making adjustments to that figure to account for conditions affecting the availability of DBEs in a given area.[236]

6. Justifying State Participation in USDOT DBE Program: Conducting Disparity and Availability Studies

Given the *Croson* decision's requirement that race-based standards be narrowly tailored to pass the strict scrutiny test, there have been a series of subsequent cases testing the constitutionality of the DBE program as administered in specific states.[237] In *Northern Contracting, Inc. v. Illinois Department of Transportation*,[238] the U.S. Court of Appeals for the 7th Circuit upheld the Illinois DOT's FFY 2005 DBE plan as narrowly tailored. In *Sherbrooke Turf, Inc. v. Minnesota Department of Transportation*, [239] the U.S. Court of Appeals for the 8th Circuit upheld the validity of Minnesota DOT's participation in the DBE program. In *Western States Paving Co. v. Washington State Department of Transportation*,[240] however, the U.S. Court of Appeals for the 9th Circuit struck down the Washington State DOT's participation in the DBE program, finding that while the statute and regulations underlying the program facially met the strict scrutiny test, the Washington State DOT's implementation of the program was not sufficiently narrowly tailored.

One of the main factors accounting for the difference between the 7th and 8th Circuit decisions and the 9th Circuit decision was that the Illinois and Minnesota DOTs had undertaken statistical studies of DBE disparity and availability, while the State of Washington DOT had not done so prior to the litigation.[241]

Reflecting federal case law, USDOT's DBE program regulations, 49 C.F.R. Part 26, require that state DOTs narrowly tailor their DBE efforts to actual evidence of discrimination within their state construction markets. In particular, the regulations require that state DOTs and other federal-aid recipients must establish DBE goals based on "demonstrable evidence" of the relative availability of DBE firms compared to all firms ready, willing, and able to participate in federal-aid projects, and that the goal must reflect the state DOT's or other recipient's "determination of the level of DBE participation you would expect absent the effects of discrimination."[242]

While USDOT's regulations do not expressly require state DOTs or other recipients to conduct DBE disparity and availability studies, the 9th Circuit's decision in the *Western States Paving* case discussed above indicates that, as a practical matter, such studies may be, at minimum, highly advisable for a state DOT's participation in the Federal DBE program to withstand judicial review.

Considering this a high priority, the TRB's NCHRP undertook a research project resulting in the publication of a report in 2010 that provides state DOTs with guidelines for conducting such studies.[243] That report is essential reading for state DOTs participating in USDOT's DBE program, especially for those that have not undertaken such a study.

In addition to the state DOTs in Illinois and Minnesota, DOTS in a number of other states have also undertaken availability and disparity studies. Even without a systematic survey, a brief electronic search turns up reports documenting availability and disparity reports issued by, among others, the Arizona DOT,[244] California DOT (CalTrans),[245] Idaho DOT,[246] North Carolina DOT,[247] and Oregon DOT.[248]

What should a state DOT undertaking such a DBE disparity and availability study focus on? The NCHRP

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[236] 64 Fed. Reg. at 5109–5111.

[237] See JOHN WAINRIGHT & COLETTE HOLT, GUIDELINES FOR CONDUCTING A DISPARITY AND AVAILABILITY STUDY FOR THE FEDERAL DBE PROGRAM 3-5 (NCHRP Report 644, Transportation Research Board, 2010); available at http://onlinepubs.trb.org/onlinepubs/nchrp/nchrp_rpt_644.pdf, last accessed on Nov. 17, 2011; hereinafter cited as "NCHRP Report 644." The discussion of case law here summarizes briefly the longer analysis in that publication.

[238] 2007 U.S. App. LEXIS 4162 (7th Cir. Feb. 7, 2007).

[239] 345 F.3rd 964 (8th Cir. 2003).

[240] 407 F.3rd 983 (9th Cir. 2005).

[241] *Id.* at 997, as cited in NCHRP Report 644, at 5 n.22.

[242] 49 C.F.R. § 26.45.

[243] NCHRP Report 644, This subsection of the 2011 update to this volume is based to a significant extent upon that much longer and more detailed report, which the authors of the 2011 update acknowledge and recommend.

[244] ARIZONA DEPARTMENT OF TRANSPORTATION CIVIL RIGHTS OFFICE/MGT OF AMERICA, INC., AVAILABILITY ANALYSIS AND DISPARITY STUDY FOR THE ARIZONA DEPARTMENT OF TRANSPORTATION—FINAL REPORT (2009).

[245] CALIFORNIA DEPARTMENT OF TRANSPORTATION, AVAILABILITY AND DISPARITY STUDY—FINAL REPORT (2007); available at http://www.dot.ca.gov/hq/bep/study/Avail_Disparity_Study_Final_Rpt.pdf, last accessed on Nov. 17, 2011.

[246] IDAHO DEPARTMENT OF TRANSPORTATION/BBC RESEARCH & CONSULTING, A STUDY TO DETERMINE DBE AVAILABILITY AND ANALYZE DISPARITY IN THE TRANSPORTATION CONTRACTING INDUSTRY IN IDAHO—FINAL REPORT (2007); available at http://itd.idaho.gov/civil/pdf/Disparity/Study.pdf, last accessed on Nov. 17, 2011.

[247] NORTH CAROLINA DOT/EUQUANT, 1 MEASURING BUSINESS OPPORTUNITY: A DISPARITY STUDY OF NCDOT'S STATE AND FEDERAL PROGRAMS: ECONOMIC AND STATISTICAL ANALYSIS–FINAL REPORT (2009).

[248] OREGON DEPARTMENT OF TRANSPORTATION/MGT OF AMERICA INC., DISPARITY STUDY UPDATE FOR THE STATE OF OREGON DEPARTMENT OF TRANSPORTATION—FINAL REPORT (2011); available at http://www.oregon.gov/ODOT/CS/CIVILRIGHTS/sbe/dbe/docs/DisparityUpdate2011_FinalReport.pdf?ga=t,n, last accessed on Nov. 17, 2011.

report, published in 2010, devotes chapters to detailed treatments of the legal standards for DBE programs,[249] designing defensible DBE programs,[250] a model disparity study,[251] and study resource issues,[252] and includes an appendix on the importance of comprehensive subcontract data collection to the performance of effective studies.[253] Rather than trying to summarize or paraphrase that report here, the authors of the 2011 update to this volume simply refer readers to it as the best currently available information on such matters, especially since it is readily available online at the time this update is being prepared.[254]

7. Compliance with and Enforcement of DBE Requirements

a. Compliance and Enforcement: Civil Compliance Under USDOT Regulations

Compliance and enforcement of DBE requirements are governed by 49 C.F.R. Part 26 Subpart F. The provisions of Subpart F are summarized in Section 4(A)(1)(a)(viii) of this current volume, above.

The USDOT regulations contemplate, in general, that state and municipal DOTs will be cooperative and diligent participants in administration of the DBE program, will take effective administrative action to identify and address problems, and will work cooperatively with USDOT and its OIG in dealing with serious problems. Civil compliance begins with administrative efforts by state UCPs to perform thorough and effective reviews of firms during the DBE certification process, and periodic reviews of certification as appropriate. It continues with efforts by state and municipal DOTs to exercise due diligence in the review and approval or disapproval of proposed DBE subcontractors prior to award of federal-aid construction contracts; and to perform appropriate monitoring in the field, by DOT or consultant construction field personnel, of whether DBE subcontractors are actually performing, with their own forces, the work which has been subcontracted to them.

While the regulations contemplate voluntary cooperation by state and municipal DOTs and other recipients, USDOT has the power, either on its own initiative or in response to complaints, to undertake reviews of state or municipal DOT and other recipient compliance with the requirements of the Federal DBE program and its regulations, to undertake efforts at conciliation with nonconforming DOTs and other recipients upon request, and to undertake enforcement actions against noncompliant state or municipal DOTs and other recipients that do not request conciliation or enter into a conciliation agreement resolving the issues to USDOT's satisfaction. Such enforcement actions may potentially include suspension or revocation of federal-aid funding for the DOT's and other recipient's federal-aid construction programs.[255]

USDOT also has authority to investigate prime contractors or DBE subcontractors suspected of seeking to conceal noncompliance with DBE program regulations and requirements through false and fraudulent means and to commence federal suspension or debarment proceedings against them if warranted by the evidence.[256] As discussed in Section 4(A)(1)(b)(vii), above, USDOT actively examined the area of DBE enforcement during 2011, and is pursuing internal administrative initiatives to strengthen its enforcement efforts in this area.

Unintentional, unwitting, minor, technical violations of the DBE regulations, particularly first-time violations, are likely to draw administrative compliance or enforcement efforts by state or municipal DOT personnel. As discussed below, more serious cases may move compliance actions beyond civil enforcement.

b. Federal Criminal Prosecutions for DBE Fraud

When USDOT becomes aware through investigation, either on its own initiative or in response to complaints, of intentional, willful, premeditated efforts to circumvent compliance with the DBE program and conceal such circumvention through false, fraudulent, or deceitful statements or representations, or under circumstances indicating a serious lack of business integrity or honesty, USDOT has authority to refer such cases to the DOJ, for criminal prosecution under 18 U.S.C. § 1001 or other applicable provisions of law.[257]

The DOJ has expressed increasing interest in, and has been devoting increasing efforts and resources to, active investigation of such cases. This is due not only to an interest in supporting the federal policies underlying USDOT's DBE program, but also to a growing recognition that DBE fraud is often related to, or leads to discovery and investigation of, more widespread criminal activity. In some parts of the United States, this has included not merely tax evasion or construction fraud by corrupt construction contractors, but also efforts by organized crime to extort ongoing payoffs from construction contractors, to bribe public officials, or to use DBE subcontracts as a cover for laundering the proceeds of drug smuggling, prostitution, gambling, and other criminal enterprises through purportedly legitimate business activities.

In areas where evidence has revealed DBE fraud to be associated with criminal activities of this type, the DOJ has increasingly turned to assembling multi-agency task forces combining resources and expertise not just from the USDOT OIG, but also from the Federal Bureau of Investigation (FBI), the U.S. Depart-

[249] NCHRP Report 644, at 1 et seq.

[250] *Id.* at 9 et seq.

[251] *Id.* at 29 et seq.

[252] *Id.* at 54 et seq.

[253] *Id.* at 60 et seq.

[254] *Id.*

[255] 49 C.F.R. §§ 26.101 and 26.103.

[256] 49 C.F.R. § 26.107(a) through (d); and *see* 49 C.F.R. pt. 31.

[257] 49 C.F.R. § 26.107(e).

ment of Labor Office of Labor Racketeering, the Internal Revenue Service Criminal Investigation Division, the U.S. Postal Inspection Service, and the Criminal Divisions of U.S. Attorneys' Offices, to conduct sophisticated, multifaceted criminal investigations. Rather than simply reviewing paper or electronic administrative records, such investigations are increasingly relying upon the use of confidential informants, undercover investigators, electronic surveillance, and other investigative tools originally developed for handling organized crime, narcotics and public corruption cases. In prosecuting such cases, the DOJ is making effective use not just of 18 U.S.C. § 1001, but also of other federal statutes with broader reach and stronger penalties, including the federal mail fraud, wire fraud, and Racketeer Influenced and Corrupt Organizations Act (RICO) statutes.[258] Such statutes can include penalties involving terms of federal imprisonment and fines of a size going well beyond traditional assumptions about penalties for white-collar crime. These efforts have resulted in some major convictions, plea bargains and civil settlements.

From 2009 to 2011, the U.S. Attorney, Eastern District of New York (EDNY), pursued federal criminal charges in a DBE fraud case involving Perini Corporation's Civil Division which had been investigated by a multi-agency Federal Construction Fraud Task Force. The case involved NYSDOT and New York City DOT highway and bridge projects totaling approximately $284 million. Prosecutors charged that Perini and its executives submitted DBE subcontractors to obtain award of the contracts, and then used a variety of non-DBE firms to do the actual work, paying the DBE firms three to five percent of the subcontract amounts for processing payroll and other required paperwork. The Perini Corporation paid $9.75 million under a civil settlement to resolve its potential corporate criminal and civil liabilities in the matter. This did not end prosecution of some of the individuals involved, however. After obtaining guilty pleas from owners of some of the DBE firms involved, the U.S. Attorney pursued criminal charges against two Perini executives. On October 29, 2010, John Athanasiou, a former Vice President of Perini Corporation's Civil Division, pled guilty to money laundering and conspiracy charges for his role in the case. Despite those guilty pleas, Zohrab B. Marashlian, the former President of Perini Corporation's Civil Division, who had been paid $14 million in salary and bonuses by Perini during the period involved, chose to take his case to trial. On March 9, 2011, following a 4-week trial, a federal jury found Mr. Marashlian guilty of mail fraud, conspiracy to launder money, and conspiracy to commit mail and wire fraud. Two days after being found guilty, while free on bond but facing a maximum possible sentence of 20 years' imprisonment, a fine of up to $23 million and criminal forfeiture of over $11 million, he committed suicide.[259]

In another DBE case pursued by the U.S. Attorney (EDNY), the Schiavone Construction Company, LLC, entered into a civil nonprosecution agreement with the U.S. Attorney's Office on November 29, 2010, in which it agreed to forfeit $20 million, admitted committing wire fraud and evading DBE requirements on $691 million in federal-aid contracts between 2002 and 2007, including two mass transit projects and a water treatment plant project, and agreed to undertake remedial measures to ensure compliance with the DBE program.[260]

In a DBE fraud case in New York pursued by the U.S. Attorney Southern District New York (SDNY), Skanska USA Civil Northeast Inc. entered into a nonprosecution agreement on March 31, 2011, under which it admitted no wrongdoing but agreed to pay $19.6 million to resolve allegations that it had been involved in DBE fraud. The nonprosecution agreement was announced on the same day that mail fraud and conspiracy indictments were unsealed against a DBE subcontractor, Environmental Energy Associates and two of its owners for helping Skanska evade DBE requirements; Skanska allegedly listed that firm as a DBE subcontractor to obtain the award of multiple federal-aid mass transit projects, even though the firm had no employees or equipment and performed no work.[261]

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[258] *See, e.g.*, 18 U.S.C. §§ 1341, 1343, 1349, 1962, and 1963.

[259] USDOT OIG, Former New York Construction Company Vice President Pleads Guilty in Connection with $19 million DBE Fraud, Oct. 29, 2010, available at http://www.oig.dot.gov/library-item/5431, last accessed on Nov. 18, 2011; U.S. Attorney (E.D.N.Y.), Press Release, Former President of Perini Corp. Civil Division Convicted in $19 Million Disadvantaged Business Entities Fraud, available at http://www.justice.gov/usao/nye/pr/2011/2011mar10b.html, last accessed on Oct. 18, 2011; John Marzulli & Brian Kates, *Construction Exec Commits Suicide Two Days Before Sentencing for $19M Federal Highway Fraud*, N.Y. DAILY NEWS, Mar. 14, 2011, available at http://articles.nydailynews.com/2011-03-14/news/29147042_1_perini-construction-exec-federal-highway, last accessed on Nov. 18, 2011.

[260] William Rashbaum, *Construction Giant Admits Fraud Over Minority Firms*, N.Y. TIMES, Nov. 29, 2010, available at http://www.nytimes.com/2010/11/30/nyregion/30fraud.html, last accessed on Nov. 18, 2010; U.S. Attorney (E.D.N.Y.), Press Release, Schiavone Construction to Pay $20 Million and Costs of Investigations to Resolve Public Works Hiring Fraud, Nov. 29, 2010, available at http://www.justice.gov/usao/nye/pr/2010/2010nov29.html, last accessed on Nov. 18, 2011.

[261] William K. Rashbaum, *Contractor Agrees to Pay $19.6 Million in Fraud Case*, N.Y. TIMES, Mar. 31, 2011, available at http://www.nytimes.com/2011/04/01/nyregion/01fraud.html, last accessed on Nov. 18, 2011; Debra K. Rubin, *Skanska Agrees to $19.6M Payment to Avoid Possible DBE Fraud Charges*, ENRNewYork, Apr. 4, 2011, available at http://newyork.construction.com/new_york_construction_news/2011/0404_SkanskaAgreesPayment.asp, last accessed on Nov. 18, 2011.

In a DBE fraud case in Pennsylvania investigated by a multi-agency federal task force and prosecuted by the U.S. Attorney, Middle District of Pennsylvania, Ernest G. Fink, a former part owner and chief operating officer of Schuylkill Products Inc. and its subsidiary CDS Engineers Inc., manufacturers of prefabricated concrete bridge beams used in federal-aid highway projects in Pennsylvania and surrounding states, pled guilty on August 16, 2010, to conspiracy to defraud USDOT and commit mail and wire fraud. In pleading guilty, Mr. Fink admitted that he used Marikina Construction Corp., a small DBE from Connecticut, to obtain more than 300Pennsylvania Department of Transportation (PennDOT) federal-aid highway contracts and Southeastern Pennsylvania Transit Authority (SEPTA) mass transit projects totaling $136 million over a period of 15 years that his own firms actually performed. Three other construction executives, Marikina owner Romeo P. Cruz, former Schuylkill Products Vice President Dennis F. Campbell, and former CDS Vice President Timothy G. Hubler, had already pled guilty in the case. The U.S. Attorney also indicted Mr. Fink's former co-owner and nephew, Joseph W. Nagle, in the case. His attorneys obtained a trial court ruling to allow Mr. Fink, who had not yet been sentenced following his guilty plea, to testify as a defense witness under a grant of immunity for anything he testified to, which the U.S. Attorney appealed to the U.S. Court of Appeals for the Third Circuit. On August 19, 2011, the Third Circuit refused to grant the appeal, effectively giving Mr. Fink immunity from anything he might testify to during Mr. Nagle's trial from being used against him in connection with his own sentencing on his prior guilty plea.[262] The case against Mr. Nagle went to trial, and the trial took 4 weeks. On April 5, 2012, the jury in the U.S. District Court for the Middle District of Pennsylvania found Mr. Nagle guilty on 26 of the 30 charges in the indictment, including conspiracy to defraud USDOT and commit wire and mail fraud, 11 counts of wire fraud, six counts of mail fraud, conspiracy to commit money laundering, and 11 counts of money laundering.[263]

In a DBE fraud case in Minnesota investigated by the USDOT OIG, the U.S. Attorney's Office (Minnesota), and the Civil Division of the DOJ, Minnesota Transit Constructors agreed on August 24, 2011, to pay the United States $4.6 million to resolve potential exposure to False Claims Act liability based on allegations that the firm committed to using DBE subcontractors to obtain a federal-aid light rail project contract, but then had the work performed by non-DBE subcontractors, with the DBE firms merely used to make it appear that they were doing the work. This case was interesting, in that it may be one of the first times that the False Claims Act has been used effectively for DBE enforcement purposes.[264]

c. Bidder Responsibility: Substitutions

Under USDOT's DBE regulations in effect as of the 2011 update to this volume, including the 2011 amendments to those regulations, state or municipal DOT awards of federal-aid contracts are, among other things, subject to 49 C.F.R. § 26.53. Pursuant to that regulation, when a state or municipal DOT or other recipient has established a DBE goal for a federal-aid project, it may only award the contract for the project to a bidder or offeror who either documents that it has obtained enough DBE participation to meet the goal, or documents that it made adequate good-faith efforts to meet the goal, even though it did not succeed in obtaining enough DBE participation to do so.[265]

The USDOT DBE regulations allow state or municipal DOTs or other recipients to choose between requiring submission of the necessary DBE documentation as part of the bidder's bid or offeror's offer, or in the alternative, prior to contract award. To document sufficient DBE participation, the bidder or offeror must submit at the required time a list identifying all DBE firms which will participate in the contract, including names and addresses, a description of the work that each DBE firm will perform, the dollar amount of each DBE's participation, written documentation of the contractor's commitment to use each DBE to perform such work, and written confirmation from each DBE that it will be participating as described.[266]

Because submission of an acceptable DBE participation plan identifying each DBE involved and the work it will perform is a legal condition precedent for state or

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[262] *$136 Million Fraud—Orwigsburg Man Pleads Guilty in 15-Year Conspiracy to Defraud USDOT*, TIMES NEWS, Aug. 17, 2010, available at http://www.tnonline.com/2010/aug/17/136-million-fraud, last accessed on Nov. 18, 2011; U.S. Attorney (MDPa) Press Release, Former Owner of Schuylkill Products Pleads Guilty to Largest Disadvantaged Business Enterprise Fraud in USDOT History, Aug. 16, 2010, available at http://www.justice.gov/usao/pam/news/2010/Fink_08_16_10.htm, last accessed on Nov. 18, 2011; John Shiffman, *Rare Legal Gambit Succeeds in Fraud Case*, PHILADELPHIA INQUIRER, Aug. 19, 2011, available at http://articles.philly.com/2011-08-19/news/29905574_1_fraud-case-immunity-appeals, last accessed Nov. 18, 2011.

[263] Stephen J. Pytak, *Former Owner of Schuylkill Products Found Guilty in Historic Fraud Case*, REPUBLICAN HERALD, Apr. 7, 2012; available at http://republicanherald.com/news/former-owner-of-schuylkill-products-found-guilty-in-historic-fraud-case-1.1296623, last accessed July 26, 2012; *see also* Former President and Owner of Schuylkill Products Convicted in Largest Disadvantaged Business Enterprise Fraud in Nation's History, FBI press release, Apr. 6, 2012, available at http://www.fbi.gov/philadelphia/press-releases/2012/former-president-and-owner-of-schuylkill-products-convicted-in-largest-disadvantaged-business-enterprise-fraud-in-nations-history, last accessed July 26, 2012.

[264] U.S. Department of Justice Press Release, Minnesota Transit Constructors to Pay U.S. $4.6 Million to Resolve False Claims Act Liability, Aug. 24, 2011, available at http://www.justice.gov/opa/pr/2011/August/11-civ-1080.html, last accessed on Nov. 18, 2011.

[265] 49 C.F.R. § 26.53(a).

[266] 49 C.F.R. § 26.53(b).

municipal DOTs to obtain FHWA concurrence to award a federal-aid contract, contractors are not free simply to substitute other firms, even other certified DBEs, for approved DBE subcontractors listed in the project plan once the plan has been approved by the state DOT and FHWA and the contract has been awarded. USDOT's regulations expressly prohibit contractors from terminating any approved DBE and substituting another firm, without obtaining the state DOT's prior written approval, being able to demonstrate good cause for terminating the previously submitted DBE, and providing the previously submitted DBE with written notice and 5 days to respond.[267] USDOT does not leave the issue of "good cause" up to the unfettered discretion of either the contractor or the state DOT; to constitute "good cause" justifying the termination of a previously submitted DBE, the reason for termination must fit within one of nine specific reasons set forth in the regulations, or constitute "other good cause" in USDOT's view.[268]

Whether a contractor has met DBE goals is usually treated as a bid responsiveness issue rather than as a lack of bidder responsibility. A failure to include a DBE plan with the bid is a material deviation and renders the bid nonresponsive.[269] The Minnesota court held that this was not an omission that could be corrected by the bidder after bid opening. "Whether or not other bidders would be prejudiced by subsequential insertion, the government's broad policy objective [of minority participation] may be prejudiced by the omission."[270]

The 1999 revision to the FHWA DBE rules allows recipients to consider compliance with DBE requirements as a matter of either responsibility or responsiveness. Although there were arguments to be made for one or the other, USDOT took the position that recipients should be allowed to exercise their discretion in how to treat this issue.[271]

Where the state chooses to treat compliance as a matter of responsiveness, bidders occasionally have problems if they include a subcontractor DBE who turns out not to have been certified in time for bid submission. Several cases have considered whether such bidders may substitute a certified DBE after bid opening but prior to award. Although these cases address AAPs decided prior to *Adarand* and the 1999 USDOT rules, the analysis regarding responsiveness is still valid.

In *Regional Scaffolding & Hoisting Co. v. City of Philadelphia*, the low bidder was not permitted to substitute for an uncertifiable MBE.[272] The specifications required that the listed MBE be certified before the time of award to be counted toward the goal. It also provided that failure to submit a completed schedule of M/WBE participation or request for waiver with the proposal would result in rejection of the bid as nonresponsive. In addition, the listing of a minority or female constituted a representation that the listed subcontractor was available and capable of completing the work with its own forces.

Two of the low bidder's subcontractors, listed as an MBE and as a WBE, were not certified at the time of bidding and failed to obtain certification in time for the award. The regulations applicable to the program permitted substitutions after award where the subcontractor withdrew from the project. The low bidder here requested the right to substitute before award. This request was denied by the City. The court concluded that the City's consistent "no substitution" policy was not arbitrary or capricious.[273]

However, where compliance was treated as a matter of responsibility, the court allowed substitution even after award. In *Holman Erection Co. v. Orville E. Madsen & Sons, Inc*., the Supreme Court of Minnesota held that the prime contractor's listing of a nonminority subcontractor in its winning bid did not result in a binding subcontract, and that the contractor was free to use a different subcontractor to fulfill its MBE obligations.[274]

d. Bidder Responsibility: Submission of Supplemental AAP Information After Bid Opening

As noted above, USDOT's DBE regulations give state or municipal DOTs or other recipients a choice between requiring bidders to submit the requisite DBE information as part of their sealed bids, or offerors in their offers; or, in the alternative, requiring them to submit such information prior to contract award.[275] Aside from the timing of submission, USDOT's regulatory requirements concerning the contents of such submissions are the same.[276]

Where the state DOT requires the information to be submitted as part of the sealed bid or offer, and considers compliance to be an element of responsiveness, failure to submit the required MBE information as specified will result in a nonresponsive bid, provided that the requirement in the bid specifications is unambiguous and valid. In *James Luterbach Const. Co. v. Adamkus*, the specifications directed bidders to supply certain information regarding their efforts to comply with a 10 percent MBE goal, and warned that failure to submit that information "may" cause rejection of the bid as nonresponsive.[277] The low bid was rejected as being

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[267] 49 C.F.R. § 26.53(f).

[268] 49 C.F.R. § 26.53(f)(3).

[269] Bolander & Sons Co. v. City of Minneapolis, 438 N.W.2d 735, 738 (Minn. App. 1989) *review granted, aff'd*, 451 N.W.2d 204 (1990).

[270] *Id*. at 738 (quoting Northeast Constr. Co. v. Romney, 485 F.2d 752, 759 (D.C. Cir. 1973)).

[271] 64 Fed. Reg. at 5115, 5134 (1999); 49 C.F.R. § 26.53(b)(3) (2000).

[272] 593 F. Supp. 529 (E.D. Pa. 1984).

[273] *Id*. at 536. It was probably significant that the city rejected all bids rather than award to the next bidder, whose price was considered unreasonable.

[274] 330 N.W.2d 693 (Minn. 1983).

[275] 49 C.F.R. § 26.53(b)(3).

[276] 49 C.F.R. § 26.53(b)(2).

[277] 577 F. Supp. 869 (E.D. Wis. 1984).

nonresponsive because it had set out "0" minority participation, even though the bidder had offered supplemental information saying that the "0" was inadvertent and that the 10 percent goal would be met. The bidder appealed the Village's determination to the EPA regional administrator, who concluded that the Village had acted improperly in rejecting the low bid. The court upheld EPA's ruling, finding that the use of "may" in the specifications failed to make MBE compliance an element of responsiveness.[278]

In *Noel J. Brunell & Son, Inc. v. Town of Champlain*, the low bidder failed to complete its bid documents by filling in its MBE participation to achieve the 10 percent goal.[279] The Town refused to award on the basis that it was an incomplete, nonresponsive bid. The contractor contended the information was not required because the specifications stated that within 5 days the low bidder would be notified to supply detailed information regarding each MBE to be employed on the project. The court held in favor of the bidder, as the specifications were considered to treat MBE participation as an element of responsibility rather than responsiveness.

USDOT's regulations do, as indicated above, allow state or municipal DOTs or other recipients the option of requiring bidders or offerors to submit their DBE plans subsequent to bid or offer opening, but prior to contract award. A variety of concerns have been expressed, however, about considering efforts made after bid opening to secure the award, as opposed to good-faith efforts expended before bid opening in preparation of the bid. One of these is that if a bidder is not required to secure minority commitments in advance of bid preparation, the low bidder is provided with the option of "bid shopping" for DBE subcontractors to meet the goal or be disqualified for the award as it chooses. Another is that this practice tends to lead to negotiations between the low bidder and the agency over what further efforts and participation will be accepted as a condition for award.

Another concern of public agencies is that subsequent submittals of information can provide the low bidder with an option for the award. By withholding the documentation the bid becomes nonresponsive, or the bidder not responsible, providing an escape from the proposal should the bidder so choose, and giving that bidder an advantage over other bidders. WSDOT has made such an action subject to a bond forfeiture:

Failure to return the insurance certification and bond with the signed contract as required in Section 1-03.3, or failure to provide Disadvantaged, Minority or Women's Business Enterprise information if required in the contract, or failure or refusal to sign the contract shall result in forfeiture of the proposal bond or deposit of this bidder. If this should occur, the Contracting Agency may then award the contract to the second lowest responsible bidder or reject all remaining bids. If the second lowest responsible bidder fails to return the required documents as stated above within the time provided after award, the contract may then be awarded successively in a like manner to the remaining lowest responsible bidders until the above requirements are met or the remaining proposals are rejected.[280]

In a Washington State case, *Land Const. Co. v. Snohomish County*, the court held that the bidder could not substitute a certified WBE after bid opening where it would provide the bidder with a substantial advantage over other bidders.[281] The specifications required each bidder to list only certified MBE and WBE subcontractors. The low bid was rejected because the WBE listed was not on the WSDOT list of certified WBEs and no substitution was permitted.

The court recognized that the awarding authority could waive an irregularity if it was not material. "The test of whether a variance is material is whether it gives a bidder a substantial advantage or benefit not enjoyed by other bidders."[282] The conclusion was that allowing substitution would be a material variation in bidding and that the bid was not responsive:

Land Construction would enjoy a "substantial advantage" over other bidders if permitted to submit the low bid with a non-certified WBE and then substitute a certified WBE after the bids are opened in that it could refuse to make such a substitution if it discovered that its bid was too low. Because it is the acceptance, not the tender, of a bid for public work which constitutes a contract Land Construction would have no obligation to perform under a bid containing a non-certified WBE. Before its bid is accepted, Land Construction could not be compelled to substitute a certified WBE. Snohomish County could not accept this low bid until it contained a certified WBE. If Land was permitted to make this substitution after the bids are opened, control over the award of public work contracts would pass from the municipality involved to the low bidder.[283]

Although commenters on the proposed rule advocated that the rule should state whether compliance was a responsibility or responsiveness matter, USDOT concluded that agencies should retain this discretion. This was also in keeping with the fact that agencies deal with responsibility differently—some have extensive prequalification requirements, under which only prequalified bidders are allowed to bid. Others, particularly smaller agencies, deal with responsibility through postqualification measures, in which only the low bidder must submit evidence of responsibility.[284] For these

[278] *Id*. at 871.

[279] 95 Misc. 2d 320, 407 N.Y.S.2d 396 (App. 1979), *aff'd*, 64 A.D. 2d 757, 408 N.Y.S.2d 447 (1978).

[280] Washington State Department of Transportation, Standard Specifications for Road, Highway, and Bridge Construction, § 1-03.5 (2002) (available on WSDOT's Web site, www.wsdot.wa.gov).

[281] 40 Wash. App. 480, 698 P.2d 1120 (1985).

[282] 698 P.2d at 1122 (quoting Duffy v. Village of Princeton, 240 Minn. 9, 60 N.W.2d 27, 29 (1953).

[283] *Id*. (citation omitted).

[284] *See* Section 2 for a discussion of prequalification and postqualification.

agencies, addressing DBE compliance as part of a responsibility determination is more cost effective. Commenters pointed out that requiring that DBE compliance be an element of responsiveness serves to deter bid-shopping.[285] However, agencies retain the ability to require that even though documentation might be submitted only after the low bidder has been identified, it must have been prepared and commitments obtained prior to bid opening.

The importance of the distinction goes mainly to questions of due process and necessity for a hearing before rejecting a bid or bidder. Generally, if a low-responsive bidder is determined not to be responsible, it is entitled to a hearing before the agency. However, a bid may be rejected as nonresponsive without providing a hearing to the bidder. This too is addressed in the 1999 regulations. If a bidder's good-faith efforts are questioned, an opportunity for administrative reconsideration must be provided, regardless of whether the agency has treated the issue as an element of responsibility or of responsiveness.[286] The bidder must be afforded the opportunity to provide written documentation and meet with an agency representative on whether it either met the DBE goal or made good-faith efforts. The agency must assign a different individual to evaluate the bidder's request than whoever made the initial determination.[287] The agency's subsequent determination is final and not appealable to USDOT.[288]

8. Certifications and Appeals

As discussed in Section 4(A)(1)(a)(6) and (7), above, state certification of DBEs is governed by USDOT regulations 49 C.F.R. Part 26 Subpart D.[289] Readers are referred to that section for a discussion of current (as of the 2011 update to this volume) USDOT requirements governing state certification organizations, practices, and procedures, which have been revamped in recent years. The following discussion of certification is retained from prior editions of this volume, but should be considered primarily for historical purposes, including case law that may have influenced the development of the USDOT regulations over time, rather than for practical application at this point.

In 1987, Congress required the Secretary of Transportation to establish minimum uniform criteria for DBE certifications:

> The Secretary shall establish minimum uniform criteria for State governments to use in certifying whether a concern qualifies for purposes of this subsection. Such minimum uniform criteria shall include but not be limited to on-site visits, personal interviews, licenses, analysis of stock ownership, listing of equipment, analysis of bonding capacity, listing of work completed, resumes of principal owners, financial capacity, and type of work preferred.[290]

Amendments to the DOT regulations were filed to implement the changes.[291] USDOT determined that it was already administering uniform standards for certification and added only a requirement that recipients compile and update their DBE directories annually.[292]

a. The Certification Process

Certification of DBEs is a state function subject to review by USDOT on appeals taken by applicants who are denied certification or by third parties challenging a certification. The state must certify that the applicant is (1) a small business entity, (2) owned, and (3) controlled by, (4) an economically, and (5) socially disadvantaged person.[293]

Each word in this definition is critical. First, the applicant is a "concern" or "entity," which may be a corporation, partnership, or sole proprietorship. This entity, as opposed to the qualifying individual or individuals, must be a "small business concern" as defined in Section 3 of the Small Business Act and as implemented in the Small Business Act regulations.[294] As of 2000, this meant that the business concern or entity seeking certification had gross receipts of not more than $16.6 million as an average for the prior 3 years, but the Secretary has authority to adjust this amount for inflation, and has done so since that time.[295] Different figures and formulas apply as to certain specialty firms and manufacturers.[296]

Next, the entity must be owned and controlled by a qualifying disadvantaged individual or individuals.[297] Ownership means that 51 percent or more of the business must be owned by eligible individuals, and control means that the eligible business owners themselves control and direct the firm's management and daily business operations.[298] These appear as straightforward propositions, but in closely held or family-owned business arrangements it may be difficult to distinguish between actual conditions and appearances.

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[285] 64 Fed. Reg. at 5115.

[286] 49 C.F.R. § 26.53(d) (2000).

[287] 49 C.F.R. § 26.53(d)(2) (2000).

[288] 49 C.F.R. § 26.53(d)(5) (2000).

[289] 49 C.F.R. § 26.61 et seq.

[290] Pub. L. No. 100-17 § 106(c)(4). This same language was included in TEA-21. Pub. L. No. 105-178, tit. I, subtit. A. §1101(b)(4).

[291] 52 Fed. Reg. 39225-39231 (Oct. 21, 1987).

[292] 49 C.F.R. pt. 26, subpt. C, § 26.45 (f)(1) (Oct. 21, 1987).

[293] 49 C.F.R. pt. 26, subpt. D (2000); 49 C.F.R. § 26.67(a)(2)(i)(iii) (personal net worth criteria for qualification of individual).

[294] *See* 5 U.S.C. § 632(a)(2001).

[295] 49 C.F.R. § 26.65(b) (2000).

[296] *See* 13 C.F.R. pt. 121 regarding determinations of business size.

[297] *See* Lane Constr. Corp. v. Hennessy, 98 Misc. 2d 500, 414 N.Y.S.2d 268 (App. 1979) (firm with a majority of its stock owned by women sought to compel the state transportation commission to place its name on the MBE/WBE registry; in denying the application the court held that majority ownership alone was not sufficient).

[298] 49 C.F.R. §§ 26.69, 26.71 (2000).

i. Ownership.—To meet the requirement for ownership, the minority's or woman's interest must encompass the risks and benefits that normally accompany ownership of a business. If the interest does not include those risks and benefits, then it may be inadequate to establish minority or woman ownership.

In *American Combustion, Inc. v. Minority Business Opportunity Commission*, ACI had been certified as an MBE under the District of Columbia's Minority Contracting Act.[299] ACI submitted the lowest bid on a mechanical construction contract, bidding in joint venture with a nonminority firm. However, ACI's certification had expired and it was given an opportunity to reapply. Another bidder protested ACI's minority status. Following a hearing by the Commission, the reapplication was denied. Stock in ACI was supposedly owned by two minorities and three whites, with controlling ownership held by the minorities. The hearing revealed that the stock ownership of the black owners was actually in the form of "options," because the stock was purchased with little or nothing down and the balance was to be paid from bonuses and profits with no risk of financial loss to the minorities. Thus, it was concluded that no bona fide transfer of ownership had taken place, and the court refused to enjoin award of the contract to the second bidder or to reinstate ACI's certification.[300]

In another case, *Agricultural Land Services v. State*, the female co-owner's personal loans to the company, which constituted 60 percent of its assets, were not considered capital investments under the 1987 rule.[301] The disadvantaged owner's contribution must be an actual investment of capital and not a loan.

USDOT rules address this issue in stating that capital contributions of the minority owner must be "real and substantial."[302] Examples of insufficient contributions include "a promise to contribute capital, [or] an unsecured note payable to the firm or an owner who is not a disadvantaged individual…."[303]

ii. Control of Business.—State law will determine the legality of particular business arrangements. For example, if a qualifying minority owns controlling interest in a close corporation, but control is in a four-person board of directors, a majority of three is required for corporate action. Therefore, the minority is not in control. However, if state law permits a by-law amendment delegating total control to the minority owner with controlling interest, the requirement would be satisfied if that individual actually is in control.

Agricultural Land Services also addressed the issue of when a business is family-owned and is owned and operated by both disadvantaged and non-disadvantaged individuals. Such a business cannot be presumed to be controlled or owned by the disadvantaged individual, even if the members jointly handle business responsibilities and decision-making.[304] The firm must describe how the disadvantaged owner exercises majority control.

The USDOT rules specifically address situations when a woman business owner has acquired the business due to the death of her husband or in a divorce settlement. In these cases, the assets are considered to be "unquestionably hers."[305] However, if a woman owner acquires the business as a gift, then the business is presumed not to be held by a socially and economically disadvantaged individual.[306] To overcome this presumption, the owner must prove by clear and convincing evidence that the transfer was not made for the purpose of obtaining DBE certification and that the disadvantaged individual actually controls the "management, policy, and operations of the firm."[307]

A District of Columbia case, *Jack Wood Constr. Co. v. United States Dept. of Transp.*, prompted USDOT to more clearly explain what is meant by "control" of the firm.[308] In that case, the court had overturned a USDOT decision denying DBE certification based on the woman owner's lack of control of the business. Mr. and Mrs. Wood were joint owners of the company. The business had been certified as a DBE after the owner transferred some of his shares to his daughter, making it more than 51 percent female-owned. Mrs. Wood had always been involved in the company's bidding and decision-making, but Mr. Wood provided the technical expertise. After Mr. Wood's death, Mrs. Wood inherited his shares in the company, with the remaining shares still being owned by their daughter. Mrs. Wood then relied on another male employee for technical expertise in bid preparation, but retained the decision-making authority on what jobs to bid and the amount of the company's bid.

After certifying the company as a DBE for 14 years, the Arkansas Highway and Transportation Department determined that the company did not qualify as a DBE because Mrs. Wood, even though she was president of the company, did not meet the federal standard for control of the firm.[309] Rather, the agency found that a male employee "controlled" the company as he had the technical expertise and that Mrs. Wood lacked the background and ability "to independently control the operations of [the] business" under the federal regulation.[310]

The district court held this to be an abuse of discretion.[311] The agency had relied on a regulation that applies to "owners" of firms, and because the male employee relied on by Mrs. Wood was not an owner, that rule did not apply. The court also held that technical

[299] 441 A.2d 660 (D.C. App. 1982).

[300] *Id*. at 668.

[301] 715 So. 2d 297 (Fla. App. 1998).

[302] 49 C.F.R. § 26.69(e) (2000).

[303] *Id.*

[304] 715 So. 2d at 298.

[305] 64 Fed. Reg. at 5118 (comment to 49 C.F.R. § 26.69(g)(2)).

[306] 49 C.F.R. § 26.69(h) (2000).

[307] *Id*.

[308] 12 F. Supp. 2d 25 (D.D.C. 1998).

[309] *Id*. at 27 (citing 49 C.F.R. § 23.53(a)(3)–(4) (1987)).

[310] *Id*. at 28 (quoting 49 C.F.R. § 23.53(a)(2)–(3) (1987)).

[311] *Id*. at 28.

expertise alone was not enough to determine who has control.[312] USDOT had always had a policy of requiring that a DBE owner "must have an overall understanding of, and managerial or technical competence and experience directly related to the type of business in which the business is engaged."[313] The court interpreted this policy as requiring that the owner have technical *or* managerial competence, but not both. Mrs. Wood clearly had managerial competence, having been involved in all corporate decision-making for 30 years, including what jobs to bid and at what price, and equipment acquisition. Her reliance on an employee to handle technical aspects of bid preparation was no different than what was done in other companies.

USDOT clarified its rule in 1999 to address this issue. The most significant change with regard to the *Wood* case is the change from "technical *or* managerial competence" to "technical *and* managerial competence."[314] At the same time, the rule acknowledges that technical tasks may be delegated, or that others may be relied on for some technical expertise:

> The socially and economically disadvantaged owners are not required to have experience or expertise in every critical area of the firm's operations, or to have greater experience or expertise in a given field than managers or key employees. The socially and economically disadvantaged owners must have the ability to intelligently and critically evaluate information presented by other participants in the firm's activities and to use this information to make independent decisions concerning the firm's daily operations, management, and policymaking. Generally, expertise limited to office management, administration, or bookkeeping functions unrelated to the principal business activities of the firm is insufficient to demonstrate control[315]

Whether Mrs. Wood would have qualified as a DBE under this regulation is unclear from the opinion. However, clearly there was a difference of opinion between USDOT and the court as to whether she did even under the previous rule. The new rule was intended to prevent a woman from claiming that she controls a business where her role in running the business has been limited to managerial and accounting functions, rather than actual construction-related work.

iii. Uniform Certification Program.—No Interstate reciprocity requirement exists that obligates one state to honor certifications of another state. USDOT has had a concern that a reciprocity requirement would lead to "forum shopping" by ineligible businesses.[316] However, the 1999 rule requires that states set up a Unified Certification Program (UCP) within each state by March 2002, with the goal being a system of "one-stop shopping" for certification with all recipients within a given state.[317] The rule also allows two or more states to form regional UCPs, and allows UCPs to enter into written reciprocity agreements with other states or other UCPs.[318]

b. Determining Social and Economic Disadvantage

The individual or individuals qualifying the business as a DBE must be both socially and economically disadvantaged. Certain defined minorities are rebuttably presumed to be socially and economically disadvantaged, including African Americans, Hispanic Americans, Native Americans, Asian-Pacific Americans, and Asian-Indian Americans.[319] In addition, other minorities or individuals found to be disadvantaged by the SBA under Section 8(a) of the Small Business Act are included. The states must accept and cannot challenge an 8(a) certification except through SBA.[320]

Apart from 8(a) certifications, the specified minorities are not presumed to be economically and socially disadvantaged. For example, a wealthy minority would not be economically disadvantaged, as he or she would not meet the requirements for limits on personal net worth.[321] Likewise, the qualifying individual must actually be a member of one of the defined minority groups to establish social disadvantage. The rules set out a standard for evaluating whether one is actually part of a minority group, including "whether the person has held himself out to be a member of the group over a long period of time" and "whether the person is regarded as a member of the group by the relevant community."[322]

As to eligible minorities who are presumptively disadvantaged, the states are not burdened with the obligation of inquiring into the actual social and economic situation to make determinations for every firm seeking certification. Disadvantaged status is presumed. However, if a third party challenges this status the state

[312] *Id*. at 29.

[313] *Id*.

[314] 49 C.F.R. § 26.71(g) (2000).

[315] *Id*.

[316] 64 Fed. Reg. at 5122.

[317] 49 C.F.R. pt. 26, subpt. E § 26.81 et seq. (2000); *see also* CalTrans Web site for a description of its Uniform Certification program and application, www.dot.ca.gov (Doing Business with CalTrans, Civil Rights Program).

[318] 49 C.F.R. § 26.81(e) (2000).

[319] 49 C.F.R. § 26.5 (2001).

[320] 49 C.F.R. § 26.67 (2000).

[321] 49 C.F.R. § 26.67 sets this limit at $750,000, excluding the assets of the firm being certified.

[322] 49 C.F.R. § 26.63 (2000).

must follow the challenge procedures and make a determination from the facts presented by all sides.[323]

The states are authorized to make individual determinations of social and economic disadvantage regarding individuals who are not part of a presumptive group. Appendix E to 49 C.F.R. Part 26 provides guidance and standards for making social and economic disadvantage determinations. Three elements must be shown to support a finding of social disadvantage: (1) social disadvantage arising from color, national origin, gender, physical handicap, or long-term isolation from mainstream American society; (2) demonstration that the individual personally suffered substantial and chronic disadvantage in American society and not in other countries; and (3) demonstration that the disadvantage must have negatively affected the individual's entry into or advancement in the business community. Evidence of social disadvantage to establish these points can include denial of equal access to employment opportunities, credit or capital, or educational opportunities, including entry into business or professional schools.

Economically disadvantaged individuals are usually socially disadvantaged as well because of their limited capital and credit opportunities. Therefore, the guidelines direct that a determination first be made as to social disadvantage based on factors other than economic considerations. If social disadvantage is found in accordance with the described elements, an economic determination is made.[324]

c. Certification Denials, Challenges, and Appeals

The regulations provide that a denial of certification must be in writing.[325] The recipient is expected to establish a time period of no more than 12 months that the firm must wait to reapply.[326]

The applicant may appeal a denial of certification to USDOT.[327] Only USDOT has jurisdiction to consider such a denial of certification by a recipient agency.[328] Any firm that believes that it was wrongfully denied certification must file its appeal with USDOT within 90 days after denial of certification unless the time period is extended by USDOT for good cause.[329] USDOT is required to make its decision based on the recipient's administrative record; it does not conduct a de novo review and does not hold a hearing. USDOT will affirm the recipient's decision unless it is not supported by substantial evidence in view of the entire administrative record, or unless it is inconsistent with the regulations regarding certification.[330]

If a recipient is considering removing a firm's DBE status, it must hold an informal hearing and give the firm an opportunity to respond to the agency's reasons for removing its eligibility.[331] The agency must maintain a complete record of the hearing; this facilitates USDOT's review on the administrative record. The agency's decision to remove a firm's eligibility must be made by separate agency personnel from those who originally sought to remove the firm's certification.[332]

9. Counting DBE Participation

As discussed in Section 4(A)(1)(a)(vii), above, counting DBE participation is governed by USDOT regulations 49 C.F.R. Part 26 Subpart C.[333] Readers are referred to that section for a discussion of current (as of the 2011 update to this volume) USDOT requirements governing the counting of DBE certification, which have been revamped in recent years. The following discussion of counting DBE participation is retained from prior editions of this volume, but should be considered primarily for historical purposes, including case law that may have influenced the development of the USDOT regulations over time, rather than for practical application at this point.

The comment to the rules notes:

> In a narrowly tailored program, it is important that DBE credit be awarded only for work actually being performed by DBEs themselves. The necessary implication of this principle is that when a DBE prime contractor or subcontractor subcontracts work to another firm, the work counts toward DBE goals only if the other firm is itself a DBE.…[334]

Under the former regulations, if the prime contractor was a DBE, then the entire contract counted as 100 percent DBE participation. Under the 1999 rules, the DBE prime contract counts only to the extent that the DBE does the work itself or subcontracts with DBE subcontractors. Along the same lines, the rule requires that DBE bidders meet the same contract goals or good faith efforts required of non-DBE bidders.[335] Section 26.55 addresses in detail what types of work, equipment rental, and purchase of materials count toward the DBE goal.[336]

If a DBE joint ventures with a non-DBE, only the portion of the work that the DBE joint venturer performs with its own forces may be counted toward the DBE goal.[337]

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[323] 49 C.F.R. § 26.87 (2000).

[324] 49 C.F.R. pt. 26, app. E.

[325] 49 C.F.R. § 26.85(a) (2000).

[326] 49 C.F.R. §26.85(b) (2000)

[327] 49 C.F.R. §§ 26.85(c), 26.87 (2000).

[328] Mabin Constr. Co. v. Missouri Highway and Transp. Comm'n, 974 S.W.2d 561 (Mo. App. 1998) (state court lacked subject matter jurisdiction to consider state agency's denial of DBE certification, because regulations required that appeal be made to USDOT, whose decision was reviewable only by the federal courts).

[329] 49 C.F.R. § 26.89(c) (2000).

[330] 49 C.F.R. § 26.89(e) (2001).

[331] 49 C.F.R. § 26.87(d) (2000).

[332] 49 C.F.R. § 26.89(e) (2000).

[333] 49 C.F.R. § 26.41 et seq.

[334] 64 Fed. Reg. at 5115.

[335] 64 Fed. Reg. at 5115.

[336] 49 C.F.R. § 26.55 (2000).

[337] 49 C.F.R. § 26.55(b) (2000).

a. The Captive DBE and the Mentor–Protégé Program

As discussed in Section 4(A)(1)(a)(4) of this current volume, above, DBE mentor protégé programs are governed by USDOT regulations 49 C.F.R. Part 26 Subpart B.[338] Readers are referred to that section for a discussion of current USDOT requirements governing mentor protégé programs, which have been revamped in recent years. The following discussion of mentor protégé programs is retained from prior editions of this volume, but should be considered primarily for historical purposes, including case law which may have influenced the development of the USDOT regulations over time, rather than for practical application at this point.

One of the most difficult areas of enforcement for state highway agencies has been the "captive" DBE. A prime contractor may aid, assist, or encourage a female or minority member of the contracting firm to establish another contracting business to take on subcontracting work for the prime contractor. Usually the individual has gained competence and experience in the prime contractor's business and is assured of future continuing business from the mentor. Characteristically these new firms become closely identified with the prime contractor. Equipment, workers, and even working capital may be supplied by the prime contractor, and the prime may own a financial interest in the fledgling firm.

FHWA has recognized that these arrangements can be beneficial to the program to bring new minorities and women into the mainstream of construction contracting. This assumes that they are not used as fronts but are permitted to grow in independence as they gain business experience to supplement their technical competence. FHWA included guidelines for the mentor protégé program in the 1999 rules. It permits established firms to assist fledgling firms in providing specialized assistance to satisfy a mutually beneficial special need.[339]

Only firms that have already been certified as DBEs are eligible to participate in a mentor protégé program. This is intended to prevent the use of "captive" protégé s that are set up by contractors to help them in meeting DBE goals.[340] The mentor and the protégé must enter into a written development plan to be approved by the state highway agency. The protégé firm must remain responsible for management of the new firm, and the two firms must remain separate and independent business entities. The development plan must be of limited duration and contain developmental benchmarks that the protégé should achieve at successive stages of the plan. This is to permit proper monitoring of the development of the DBE firm to be certain that progress is being achieved toward a goal of independence.

The mentor protégé program is not intended to be a substitute for the DBE program. The 1999 rule requires that a mentor may count only one-half of the work done by a protege firm toward its DBE goal.[341]

b. "Commercially Useful Function"

A particular concern regarding counting DBE participation involves the application of the requirement that each DBE subcontractor perform a "commercially useful function."[342] The rules define the performance of a commercially useful function as follows:

A DBE performs a commercially useful function when it is responsible for execution of the work of the contract and is carrying out its responsibilities by actually performing, managing, and supervising the work involved…To determine whether a DBE is performing a commercially useful function, you must evaluate the amount of work subcontracted, industry practices, whether the amount the firm is to be paid under the contract is commensurate with the work it is actually performing and the DBE credit claimed for its performance of the work and other relevant factors.[343]

In addition, FHWA has suggested additional elements that a state agency may use to determine whether the DBE subcontractor is performing a commercially useful function. These include (1) the DBE's management of the work; (2) whether the DBE is using its own work force; (3) whether it rents or leases equipment, or owns its own equipment; and (4) whether it is using its own materials.[344]

c. Monitoring Contract Compliance

As discussed in Section 4(A)(1)(a)(viii) and Section 4(A)(6), above, compliance and enforcement aspects of DBE programs are governed by USDOT regulations 49 C.F.R. Part 26 Subpart F.[345] Readers are referred to those sections for discussions of current (as of the 2012 update of this volume) USDOT requirements governing compliance and enforcement aspects of DBE programs, an area in which both the USDOT regulations and USDOT and state DOT administrative practices have been revamped extensively in recent years. The following discussion of compliance is retained from prior editions of this volume, but should be considered primarily for historical purposes, including case law which may have influenced the development of the USDOT regulations over time, rather than for practical application at this point.

Contract compliance involves monitoring each project to be certain that the contractor continues with its good-faith efforts to achieve the contract goals. The monitoring and enforcement requirements of the 1999

[338] See especially 49 C.F.R. § 26.35.

[339] 49 C.F.R. § 26.35 and pt. 26, app. D (2000).

[340] 64 Fed. Reg. at 5107.

[341] 49 C.F.R. § 26.35 (b)(2)(i) (2000).

[342] 49 C.F.R. § 26.55(c) (2000).

[343] 49 C.F.R. § 26.55(c)(1) (2000).

[344] *See* FHWA Web page entitled "Contract Administration Core Curriculum, Participant's Manual and Reference Guide 2001, Chapter II B," found at http://www.fhwa.dot.gov/programadmin/contracts/cor_IIB.htm.

[345] 49 C.F.R. § 26.101 et seq.

rules are intended to verify that the work committed to DBEs at contract award is actually performed by them.[346]

As part of the recipient's DBE program, the recipient must require that the prime contractor not terminate a DBE subcontractor for convenience and then perform the work with its own forces.[347] Further, when a DBE subcontractor is terminated for default or fails to complete its work for any reason, the prime contractor is required to make good-faith efforts to find another DBE to substitute for the terminated DBE.[348] The same actions cited as good-faith efforts in preparing a bid should also be required for substitution. Substitution is required for at least the same amount of work on the contract, but it need not be for exactly the same item of work.

The rules do not provide for specific enforcement mechanisms, stating only that recipients must implement appropriate mechanisms to ensure compliance with the program requirements, "applying legal and contract remedies available under Federal, state and local law."[349] Some organizations and states have advocated the use of liquidated damage provisions as an enforcement device to ensure goal achievement. This appears to be a convenient and effective means to ensure results, but actually poses problems.[350] Liquidated damages have worked well for owners and contractors in controlling timely completion of the work. However, they have not worked well in other areas to compel performance. They may be challenged as unenforceable penalties, except where actual out-of-pocket damages are quantified. Also, a stipulated damage provision in the contract for failure to achieve the goal could be used by a contractor as an invitation to incur the penalty as a cost of doing business, and include its cost in the bid price rather than employ the good-faith efforts that were promised.

10. Administrative Aspects of Management of DBE Issues by State DOTs

As discussed in Section 4(A)(1)(a)(iv), above, administrative aspects of the DBE program are governed by USDOT regulations 49 C.F.R. Part 26 Subpart B.[351] Readers are referred to that section for a discussion of current (as of the 2011 update of this volume) USDOT requirements governing USDOT requirements for state and municipal DOT administration of DBE requirements, which have been revamped in recent years.

The TRB considered administration of DBE programs by state and municipal DOTs and other recipients of federal aid for transportation projects to be of sufficient interest that the TRB's NCHRP commissioned a study, which was published in 2005.[352] While about 6 years old at the time of the 2011 revision of this volume, and not reflecting the significant amendments to the Federal DBE regulations enacted by USDOT's 2011 rulemaking, that publication remains the best general-purpose study available of state DOT administration of Federal DBE requirements. State and municipal DOT personnel involved in the administration of Federal DBE requirements on federal-aid highway and bridge projects would almost certainly find that publication worth consulting for its discussions of general administrative practices and contract administration practices involved in management of DBE requirements on transportation projects.

11. Bidder Preferences

Bidder preference statutes were adopted in many states during the Great Depression to preserve job opportunities for state residents. Decades later, many states still give statutory preferences to resident contractors and require hiring of local workers, citing to the same need to provide employment opportunities to state residents. Even where these statutes have stood for years, they may still be challenged on constitutional grounds where they have been more recently amended. In other cases, challengers may argue that economic conditions no longer justify the preference. Challenges have alleged violations of the Commerce Clause, the Privileges and Immunities Clause, and the Equal Protection Clause.

a. The Commerce Clause

The Commerce Clause prohibits the states from unduly burdening Interstate commerce in their regulatory activity.[353] Generally, a preference statute will not be found to have violated the Commerce Clause if it applies only to actions in which the agency is acting as a market participant rather than as a regulator.

The U.S. Supreme Court upheld a City of Boston preference in *White v. Massachusetts Council of Construction Employers.*[354] The Court stated in that case:

> If the city is a market participant, then the Commerce Clause establishes no barrier to conditions such as these which the city demands for its participation. Impact on out-of-state residents figures in the equation only after it is decided that the city is regulating the market rather than participating in it, for only in the former case need it be determined whether any burden on interstate commerce is permitted by the Commerce Clause.[355]

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[346] 49 C.F.R. § 26.37 (2000).

[347] 49 C.F.R. § 26.53(f)(1) (2000).

[348] 49 C.F.R. § 26.53(f)(2) (2000).

[349] 49 C.F.R. § 26.37(a) (2000).

[350] *See* DiMambro-Northend Assoc. v. Blanck-Alvarez, Ind., 251 Ga. 704, 309 S.E.2d 364 (1983).

[351] 49 C.F.R. § 26.21 et seq.

[352] GARY SMITH, MANAGEMENT OF DISADVANTAGED BUSINESS ENTERPRISE ISSUES IN CONSTRUCTION CONTRACTING—A SYNTHESIS OF HIGHWAY PRACTICE (NCHRP Synthesis 343, Transportation Research Board, 2005).

[353] U.S. CONST. ART. I § 8, cl. 3; Huron Portland Cement Co. v. City of Detroit, 362 U.S. 440, 80 S. Ct. 813, 4 L. Ed. 2d 852 (1960).

[354] 460 U.S. 204, 103 S. Ct. 1042, 75 L. Ed. 2d 201 (1983).

[355] *Id.* at 210.

In a later case, the Court of Appeals of Wisconsin upheld the DOT's bid requirement that contractors supplying road salt stockpile the salt at locations within the state, finding that it did not violate the Commerce Clause.[356] Relying on *White*, the court found that the department was not acting as a regulator:

> The department is not attempting to control any transactions other than the one in which it is involved: the purchase of road salt for state and municipal use. It is not employing its regulatory powers to dictate who may, or may not, buy or sell road salt in Wisconsin; nor is it requiring that Glacier, or any other businesses, do anything other than have the purchased salt in specified locations at a specified time—hardly an unusual or oppressive provision in a purchase contract. And, as we have said, Glacier is free to contract with other municipalities and counties on its own terms. The department is simply a party to a contract for the purchase of road salt and, when acting as a proprietor, a government shares the same freedom from the Commerce Clause that private parties enjoy.[357]

b. The Privileges and Immunities Clause

The Privileges and Immunities Clause prohibits discrimination by a state against citizens of other states, unless noncitizens are a "peculiar source of evil" at which the statute is directed and the remedy is narrowly tailored.[358]

In *Hicklin v. Orbeck*, the United State Supreme Court struck down a state statute known as the "Alaska Hire" statute, which contained a residential hiring preference for all employment arising out of oil and gas leases.[359] The Court held that it violated the Privileges and Immunities Clause, because it required private employers to discriminate against nonresidents, and there was no showing that out-of-state hiring was the cause of unemployment in the state. First, the State did not show that the influx of out-of-state workers was the cause of unemployment; rather, lack of adequate education and training and the remoteness of some Alaska residents was more likely the cause.[360] Second, the remedy was not narrowly tailored in that it gave a preference to all Alaska residents, regardless of their qualifications.[361] Lastly, the discriminatory effect went beyond the area in which the State had a proprietary interest, and applied to private employers as well. The only basis for application of the statute was the state ownership of oil and gas resources.[362]

In *United Building and Construction Trades Council v. The Mayor and Council of the City of Camden*, the U.S. Supreme Court held that Camden's AAP discriminated against residents of other states, and thus violated the Privileges and Immunities Clause.[363] The Court stated that a law preferring local workers for public construction projects burdens a fundamental right and is covered by the Privileges and Immunities Clause. However, the Court noted that the clause is not absolute:

> [The Privileges and Immunities Clause] does not preclude discrimination against citizens of other States where there is a "substantial reason" for the difference in treatment. "[The] injury in each case must be concerned with whether such reasons do exist and whether the degree of discrimination bears a close relation to them."…As part of any justification offered for the discriminatory law, nonresidents must somehow be shown to "constitute a peculiar source of the evil at which the statute is aimed."[364]

In *People ex rel. Bernardi v. Leary Construction Co.*, the Illinois Supreme Court used this to create a two-part test to determine when state actions violated rights protected by the Privileges and Immunities Clause.[365] First, the state must identify nonresidents as being a "peculiar source of evil" at which the statute is directed. Second, the discrimination must bear a substantial relationship to the evil that nonresidents present. In a municipal painting contract, the court found that nothing in the record established a relationship between nonresident employment on public works projects and resident unemployment. Accordingly, nonresident laborers could not be considered a "peculiar source" of the evil of unemployment, and so there was not a sufficient reason to interfere with the right of a citizen to cross state lines to work.[366]

Applying this standard, the Wyoming Supreme Court in *State v. Antonich* ruled that the State's Preference for State Laborers Act did not violate the Privileges and Immunities Clause of the United States Constitution.[367] This statute required contractors to employ available Wyoming laborers for public works projects in preference to nonresident workers, with provision for certification by the State employment office if local resident employees possessing the necessary skills are not available. Analyzing the *City of Camden* and the "Alaska Hire" case, the court concluded that the preference did in fact discriminate against nonresidents regarding a fundamental right. At the same time it viewed the statute as narrowly tailored to address a valid state goal of ensuring employment of its citizens, stating that it "precisely fits the particular evil identified by the State."[368] First, the statute's applicability was limited only to qualified state residents. Contractors were required to contact local employment offices for qualified workers, and if none were available could

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[356] Glacier State Distribution Services, Inc. v. Wis. Dep't of Transp., 221 Wis. 2d 359, 585 N.W.2d 652, 658 (1998).

[357] *Id.* 585 N.W.2d at 658–59 (citations omitted).

[358] U.S. CONST. ART. IV § 2, cl. 1; Toomer v. Witsell, 334 U.S. 385 68 S. Ct. 1156, 92 L. Ed. 1460 (1948).

[359] 437 U.S. 518, 98 S. Ct. 2482, 57 L. Ed. 2d 397 (1978).

[360] *Id*. at 526–27.

[361] *Id*. at 527.

[362] *Id*. at 530–31.

[363] 465 U.S. 208, 104 S. Ct. 1020, 79 L. Ed. 2d 249 (1984).

[364] 465 U.S. at 222 (citations omitted).

[365] 80 Ill. Dec. 36, 102 Ill. 2d 295, 464 N.E.2d 1019 (1984).

[366] *Id.* at 1022.

[367] 694 P.2d 60 (Wyo. 1985).

[368] *Id*. at 63.

hire from out of state. Second, it applied in the State's proprietary role in carrying out government-funded projects. Third, it specifically addressed unemployment in the construction industry.[369]

c. The Equal Protection Clause

When challenged under the Equal Protection Clause of the Fourteenth Amendment, a bidder preference statute must pass only minimal scrutiny as economic legislation. While the right of an individual to employment is considered a fundamental right, the right of a company to bid on public works is not.[370]

A bidding preference statute was upheld against an equal protection challenge in *Equitable Shipyards v. Washington State Department of Transportation.*[371] In considering bids for new state ferries, the WSDOT was authorized by statute to add a 6 percent "penalty" to the bids of out-of-state shipbuilding companies when determining the lowest responsible bidder. When this action was challenged by the otherwise low bidder as being arbitrary and capricious, and thus unconstitutional, the court found that a reasonable basis existed for the preference that was sufficient to withstand constitutional attack. The court's inquiry involved a three-part test: "(1) Does the classification apply alike to all members of the designated class? (2) Does some basis in reality exist for reasonably distinguishing between those within and without the designated class? (3) Does the classification have a rational relation to the purpose of the challenged statute?"[372]

The court noted that ferry construction was exempt from the state sales tax and that lost revenues from the tax exemption would be partially offset if the shipbuilding occurred in Washington, because the work would generate secondary economic activity. The court also pointed out that construction out-of-state would increase the state's administrative costs for inspecting the work, and that there was a greater potential for delay.[373] The court concluded: "We are convinced that a rational relation exists between the purposes of RCW 47.60.670 and its classifications of in-state and out-of-state shipbuilding firms."[374]

The Alaska Supreme Court found a regional preference law that benefited residents of economically distressed zones to be unconstitutional under the state constitution's equal protection clause.[375] Acknowledging that the Alaska Constitution's equal protection clause provides greater protection than its federal equivalent, the court determined that "the right to engage in an economic endeavor within a particular industry is an 'important' right for state equal protection purposes."[376] It applied this standard to the regional preference statute, holding that the statute would be scrutinized "closely."[377] The court concluded that the statute essentially benefited one class of workers over another. "We conclude that the disparate treatment of unemployed workers in one region in order to confer an economic benefit on similarly situated workers in another region is not a legitimate legislative goal."[378]

d. Payment of State and Local Taxes as Basis for Preference

The Arizona Supreme Court found unconstitutional a bid preference statute that granted a preference to contractors who had paid state taxes for 2 consecutive years.[379] The court found that the statute did not further any constitutionally permissible state interest in preventing unemployment, or in benefiting contractors who contributed to the state's public funds or the state's economy. The statute did not even require that the contractor have an office or any presence within the state, only that it has paid state taxes for the previous 2 years.[380] It did not require or even encourage contractors to hire state residents. Thus, the court found that the statute created a burden and not a benefit.[381] The court noted the statute's Depression origins, but found that it had been altered to no longer suit its original purpose. One of the original purposes of the statute had been to benefit "resident" contractors, and that requirement had been removed by amendment.[382]

In contrast, the Nevada Supreme Court found a very similar statute constitutional.[383] In that case, the preference statute required that bidders have paid state taxes for 60 successive months counting back from submission of their bids. The court found that the statute created a preference for contractors who had a "permanent and continuing presence" in the state, which benefited residents and the state economy and fostered warranty work.[384] The goal of the statute was in fact to have the contractor establish a presence in the state, and not just to have contributed to the state's tax revenues. The statute had recently been amended to

[369] *Id*.

[370] Note that the Privileges and Immunities Clause applies to "citizens," while the Equal Protection Clause applies to "persons." Thus while a corporation may allege a violation of Equal Protection as a "person," it is not a "citizen" with rights under the Privileges and Immunities Clause.

[371] 93 Wash. 2d 465, 611 P.2d 396 (1980).

[372] *Id*.

[373] 611 P.2d at 404 (citations omitted).

[374] *Id*. (citations omitted).

[375] State, by and Through Dep'ts of Transp. and Labor v. Enserch Alaska Constr., Inc., 787 P.2d 624 (Alaska 1989).

[376] *Id*. at 632.

[377] *Id*. at 633.

[378] *Id*. at 634.

[379] Big D Constr. Corp. v. Court of Appeals for State of Ariz., Division One, 163 Ariz. 560, 789 P.2d 1061 (1990).

[380] *Id*. at 1069.

[381] *Id*.

[382] *Id*. at 1070 (although a rational basis for the privileges granted by the statute may have existed at the time it was enacted in 1933, it has ceased to exist).

[383] City of Las Vegas v. Kitchell Contractors, Inc., 768 F. Supp. 742 (D. Nev. 1991).

[384] *Id*. at 745.

extend the time period from 2 to 5 years, in order to "demonstrate a presence here even more convincingly."[385]

e. Federally Funded Projects

State laws providing for preferential treatment of local contractors in bidding or preferential hiring of local labor or suppliers in performance of a public construction contract may not be used in federally funded work. Under statutory authority to approve methods of bidding used in federally funded contracts,[386] the Secretary of Transportation and Federal Highway Administrator have promulgated regulations requiring the bidding procedure to be nondiscriminatory.[387] They have further required that the selection of labor to be employed by a contractor shall be of its own choosing.[388] Prohibition of discriminatory hiring practices is provided in the Required Contract Provisions for Federal-Aid Contracts.[389]

f. Contract Requirements

Even where there is an adequate justification for the use of a bidder preference, the standards under which the preference will be applied must be established prior to bidding and must be set out in the bid documents. The Ohio Supreme Court addressed this problem in *City of Dayton, ex rel. Scandrick v. McGee*, a case in which the agency was found to have abused its discretion in the use of bidder preferences:

The evil here is not necessarily that "resident" bidders are preferred but that there are absolutely no guidelines or established standards for deciding by how "many percentages" a bid may exceed the lowest bid and yet still qualify as the "lowest and best bid." Absent such standards, the bidding process becomes an uncharted desert, without landmarks or guideposts, and subject to a city official's shifting definition of what constitutes "many percentages…."[390]

B. LABOR STANDARDS

The Secretary of Transportation and the Federal Highway Administrator are responsible for requiring that the states' contracting officers require compliance with federal labor standards in federal-aid highway construction contracts and subcontracts.[391] Failure of a contractor or subcontractor to comply with federal labor standards may constitute a violation of federal law directly by the contractor, and also a violation by the state highway agency of the federal statutes or regulations prescribing the terms on which federal funds are used.

In addition to a violation of federal law, the failure to enforce these labor standards also may place the contractor-employer in an unfair competitive advantage with regard to the unsuccessful bidders, and denies to the employees the benefits of federal labor standards. Similarly, enforcement of the standards beyond their proper scope may infringe on the contractor's rights both under the law and the contract.

1. Minimum Wage Standards

Federal regulations governing minimum wages that are applicable to federally funded highway projects include the Davis-Bacon Act, which mandates payment of prevailing wages, and the Contract Work Hours and Safety Standards Act, which requires payment of minimum wages and adherence to a 40-hour work week.

a. Application of the Davis-Bacon Act to Federal-Aid Highway Projects

The basic federal legislation dealing with wage standards for public construction contracts is the Davis-Bacon Act, enacted in 1931.[392] It requires that federal public works contracts provide for minimum wage rates and payment of laborers and mechanics according to the prevailing rates in the area where the work is performed.[393] The dual purposes of the Davis-Bacon Act are to give local laborers and contractors a fair opportunity to participate in building programs when federal money is involved, and to protect local wage standards by preventing contractors from basing bids on wages lower than those prevailing in the area.[394]

The Act also deals with related matters, including payment of fringe benefits,[395] withholding of contract funds from the contractor to assure compliance with the wage standards,[396] and termination of contracts because of failure to pay wages according to predetermined rates.[397] Additional incentives for compliance are supplied by provisions for direct payment of restitution wages to employees by the Comptroller General of the United States from retained funds under the contract, and disqualification of violators of the law from bidding on future federal contracts.[398]

The Davis Bacon Act applies to all federal-aid construction contracts that exceed $2,000 and to all related subcontracts on federal-aid highways; it does not apply

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[385] *Id*. at 746.

[386] 23 U.S.C. § 112(a).

[387] 23 C.F.R. § 635.107(e).

[388] 23 C.F.R. § 635.124(b), Claim Awards & Settlements; FHWA LABOR COMPLIANCE MANUAL, §§ 208-2, 508-3, app. C-9.

[389] 23 C.F.R. § 633.207.

[390] 67 Ohio St. 2d 356, 423 N.E.2d 1095, 1097 (1981).

[391] Portions of this article are derived from *Labor Standards in Federal-Aid Highway Construction Contracts*, by Ross D. Netherton, published by Transportation Research Board and included in SELECTED STUDIES IN HIGHWAY LAW, vol. 3, at 1295.

[392] 40 U.S.C. §§ 276a-276a-7 now codified at 40 U.S.C. §§ 3141–3144 (2003).

[393] 40 U.S.C. § 3142(b) (2003).

[394] L.P. Cavett Co. v. United States Dep't of Labor, 101 F.3d 1111, 1113 (6th Cir. 1996).

[395] 40 U.S.C. § 3141(2)(B) (2002).

[396] 40 U.S.C. § 3142(c)(3) (2003).

[397] 40 U.S.C. § 3143 (2003).

[398] 40 U.S.C. § 3144 (2003).

to projects on roadways classified as local roads or rural minor collectors.[399] Application of Davis-Bacon to the federal-aid highway program is set out in 23 U.S.C. § 113 (a):

> The Secretary shall take such action as may be necessary to insure that all laborers and mechanics employed by contractors or subcontractors on the construction work performed on highway projects on the Federal-aid highways authorized under the highway laws providing for the expenditure of Federal funds upon the Federal-aid systems, shall be paid wages at rates not less than those prevailing on the same type of work on similar construction in the immediate locality as determined by the Secretary of Labor in accordance with the Act of March 3, 1931, known as the Davis-Bacon Act (40 U.S.C. 276a).[400]

Davis-Bacon requirements are also incorporated in relevant provisions of FHWA regulations, including 23 C.F.R. § 635.117(f), which provides that:

> (f) The advertisement or call for bids on any contract for the construction of a project located on the Federal-aid system either shall include the minimum wage rates determined by the Secretary of Labor to be prevailing on the same type of work on similar construction in the immediate locality or shall provide that such rates are set out in the bidding documents and shall further specify that such rates are a part of the contract covering the project.

FHWA regulations, 23 C.F.R. § 635.309(f) also provide in connection with FHWA authorization for state or municipal DOTs or other federal-aid recipients to advertise federal-aid highway or bridge projects for bid, that: "(f) Minimum wage rates determined by the Department of Labor in accordance with the provisions of 23 U.S.C. 113, are in effect and will not expire before the end of the period within which it can reasonably be expected that the contract will be awarded."

A variety of issues have arisen over the years regarding Davis-Bacon prevailing wage requirements for federal-aid projects. In 2008, the Director of FHWA's Office of Program Administration issued a memorandum to all FHWA Division Administrators, Directors of Field Services, and FHWA's Acting Resource Center Manager providing guidance in this area.[401] The memorandum addressed nine recurrent issues of interpretation. State or municipal DOT personnel involved in administration of Davis-Bacon requirements on federal-aid projects should refer directly to that memorandum for details. In brief, the memorandum indicated the following. FHWA interprets the scope of 23 U.S.C. §113 to include any construction work within the right-of-way of a federal-aid highway, including wetlands, landscaping, or other work that might not appear to be highway construction. FHWA also interprets the scope of 23 U.S.C. § 113, in light of 23 U.S.C. §101, to include arterials and collectors, but not to include highways classified as local roads or rural minor collectors. FHWA takes the position that Davis-Bacon requirements are triggered by use of federal-aid funding for any portion of a construction contract, regardless of the amount of federal-aid participation, but are not triggered by minor construction activities on a roadway which is not a federal-aid highway needed to connect to a federal-aid highway. FHWA further takes the position that emergency highway or bridge repair work performed under contract is subject to Davis-Bacon, but that emergency work involving only debris removal and related cleanup is not subject to Davis-Bacon. Emergency repairs performed by state or municipal agency employees are also not subject to Davis-Bacon. For projects involving railroad and utility relocation or adjustment, work performed by a construction contractor under a highway contract let by a state or municipal DOT is subject to Davis-Bacon, but work performed by railroads, utility companies, or contractors retained by them is not subject to Davis-Bacon. Subsurface utility engineering or location services are not subject to Davis-Bacon. Projects involving the building, alteration, or repair of ferryboats and terminals located on or servicing a federal-aid highway route are subject to Davis-Bacon. For High Priority and other congressionally designated projects located within the right-of-way of a federal-aid highway, Davis-Bacon applies. This includes rail line construction projects located within the right-of-way of a federal-aid highway, but not rail line construction projects located outside such right-of-way. Safe Routes to School and Nonmotorized Transportation Pilot projects are subject to Davis-Bacon. Finally, warranty or repair work is subject to Davis-Bacon if such work is required in the original construction contract.

Because the state highway agency, or local unit of government working in cooperation with the state highway agency, is the contracting agency for federal-aid highway construction, it has the primary responsibility for assuring contractor notification of and compliance with the predetermined prevailing wage rates. In the performance of these responsibilities, several specific steps must be taken by the contracting agency, which include assuring that (1) requests for determina-

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[399] *See* FHWA CONTRACT ADMINISTRATION CORE CURRICULUM MANUAL (hereinafter CACC Manual), § II.A.4, Payment of Predetermined Minimum Wage (2001) (available on FHWA Web site, www.fhwa.dot.gov, Contract Administration Group page).

[400] 23 U.S.C. § 113 (2002). For legislative history of the application of Davis Bacon to highway projects, *see* Appalachian Regional Act of 1965, as amended, 40 U.S.C. App. § 402, for inclusion of federal labor standards in construction contracts for projects on the Appalachian Development Highway System and local access roads; 102 CONG. REC. 9156-9171 (Senate debate in which excerpts from letters from 29 state highway departments were introduced as evidence of how the Davis-Bacon Act would affect highway construction); HOUSE COMM. ON PUBLIC WORKS, FEDERAL HIGHWAY AND HIGHWAY REVENUE ACTS OF 1956, H.R. REP. NO. 2022, 84th Cong., 2d Sess., 12–13, 25–32 (1956); 41 Op. Att'y Gen. 488 (1960).

[401] Dwight A. Horne, Director, FHWA Office of Program Administration, Memorandum, Information: Applicability of Prevailing Wage Rate Requirements to Federal-Aid Construction Projects, June 26, 2008; available at http://www.fhwa.dot.gov/construction/contracts/080625.pdf, last accessed on Nov. 20, 2011.

tion of prevailing wage rates are submitted when required; (2) applicable wage rates and labor standards clauses are incorporated into all contract specifications, and in all contracts and subcontracts; (3) wage rate determinations are posted conspicuously at the jobsite; (4) laborers and mechanics are paid weekly at rates not less than those prescribed for the classes of work that they actually perform; (5) jobs are correctly classified in accordance with standards and procedures of the Department of Labor; and (6) failures on the part of contractors or subcontractors to comply with requirements of either the contract or the law are corrected or adjudicated.[402]

b. Determination of Prevailing Wage Rates

The "prevailing wage" for a specific classification is the wage paid to the majority of those employed in that classification in the area where the proposed work is to be done.[403] If a single rate cannot be identified for the majority of those in the classification, the Secretary is directed to use an average of the wages paid, weighted by the total employed in the classification.[404]

The authority to predetermine wage rates is given by statute to the Secretary of Labor, but it actually is exercised by the Administrator, Wage and Hour Division, Employment Standards Administration.[405] The Administrator carries on a continuing program to compile data and to encourage voluntary submission of wage rate data by contractors, contractor associations, labor organizations, public officials, and other interested parties.[406] In determining a prevailing wage rate, however, the regulations require that the Administrator insure accuracy by giving preference to data that reflect actual conditions in the labor market. Thus the regulations prescribe that wage rates will be determined by reference to (1) statements showing wage rates on specific projects, identifying contractors, locations, costs, dates, types of work, and the like; (2) signed collective bargaining agreements; (3) wage rate determinations for public construction by state and local officials pursuant to state prevailing wage laws; and (4) information furnished by state transportation agencies in consultation with the Administrator.[407]

All agencies using wage determination must furnish the Wage and Hour Division annual outlines of their proposed construction programs, indicating estimated number of projects for which determinations will be needed.[408]

The prevailing wage as paid in the "locality" requires that the wage be calculated based on the average rate paid to workers in the county in which the work is performed, not at a particular plant.[409] Where the employees perform more unusual work, the rate must be based on that paid to other workers for the same or similar work, even if they are considered to be in different classifications. For example, where the rate was being determined for shipyard boilermakers, it was not adequate to look only at what shipyard boilermakers were being paid. Where their work was of the same type and similar in nature to that of pipefitters in the construction industry, the wages paid to pipefitters had to be considered in determining the prevailing wage.[410]

The Davis Bacon Act requires the Secretary of Labor to set wage rates for the various classifications of work.[411] With respect to job classifications for highway work, § 113 of Title 23 U.S.C. sets out further requirements:

> In carrying out the duties of subsection (a) of this section, the Secretary of Labor shall consult with the highway department of the State in which a project on any of the Federal-aid systems is to be performed. After giving due regard to the information thus obtained, he shall make a predetermination of the minimum wages to be paid laborers and mechanics in accordance with the provisions of subsection (a) of this section which shall be set out in each project advertisement for bids and in each bid proposal form and shall be made a part of the contract covering the project.[412]

Because of the nature of the federal-aid highway program and other programs providing federal funds administered by state or local agencies, it is possible for transportation construction contracts to provide that wage rates must comply with both the federal standards in the Davis-Bacon Act and with state standards. The two sets of standards may differ in their language or interpretations such that employers are obligated to pay higher rates under one than under the other. In these instances, courts have taken the position that these minimum wage rates are to be treated as a floor, but not as a ceiling.[413] FHWA will approve state rates that are higher than the federal rates, recognizing the states' abilities to establish their own rates under state law.[414]

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[402] 29 C.F.R. § 5.5(a); 29 C.F.R. § 5.5(a)(7), 5.5(b)(2) (2001); *see also* CACC Manual, § II.4, *supra* note 399.

[403] 29 C.F.R. § 1.2(a)(1) (2001).

[404] 29 C.F.R. § 1.2(a)(1) (2001).

[405] 29 C.F.R. § 1.1(a) (2001).

[406] 29 C.F.R. § 1.3 (2001).

[407] 29 C.F.R. § 1.3(b) (2001).

[408] 29 C.F.R. § 1.4 (2001).

[409] Lockheed Shipbuilding Co. v. Department of Labor and Indus., 56 Wash. App. 421, 783 P.2d 1119 (Wash. App. 1989), *review denied*, 791 P.2d 535, 114 Wash. 2d 1018 (1989).

[410] *Id.* 783 P.2d at 1124.

[411] 40 U.S.C. § 3142(b) (2003).

[412] 23 U.S.C. § 113(b) (2001).

[413] *See* Ritchie Paving, Inc. v. Kansas Dep't of Transp., 232 Kan. 346, 654 P.2d 440 (1982) (applying KAN. STAT. § 44-201, and holding that the higher of either the federal or state would prevail).

[414] *See* CACC Manual, *supra* note 399, at section II.A.4.

i. Requests for Wage Rate Determinations.—There are two processes for obtaining wage determinations from the Department of Labor. Both are initiated with a request from the federal agency that is required to comply with the Davis-Bacon Act.

A federal agency may request that the Secretary make a general wage determination for particular types of construction work in particular areas, when wages are well settled and there is likely to be a significant amount of construction in that area.[415] Notices of wage rate determinations are published in the *Federal Register*. Davis-Bacon wage rates are now available on the Department of Labor's Web site at www.access.gpo.gov/davisbacon.[416]

For determinations on one or more classifications for which there is not a general wage determination, the federal agency may submit a request form to the Department of Labor requesting a determination. The agency must provide a detailed description of the work, indicating the type of construction involved, and must provide any pertinent wage information.[417]

ii. Legal Effects of Wage Rate Determinations and Changes to Determinations.—After prevailing wage rates for job classifications in the area of a construction project are determined, the contracting agency is responsible for seeing that they are inserted in the project advertisement and in the construction contract.[418]

Once the Secretary of Labor has made a wage rate determination, its correctness is not subject to judicial review.[419] It may, however, be challenged in administrative review proceedings. First, an interested party may ask the Administrator for reconsideration, in which case it must provide the Administrator with argument or data to support its position.[420] If the Administrator denies reconsideration, the interested party may appeal the determination to the Administrative Review Board.[421] An "interested person" includes a contractor, subcontractor, or contractor association who is likely to seek work under a contract with the wage determination; a laborer, mechanic, or labor union likely to seek employment under such a contract; or a federal, state, or local agency concerned with administration of such a contract.[422]

A request for review will not interfere with the contract advertisement or award schedule. The Board will "under no circumstances" request postponement of contract action because of the filing of a petition.[423]

The transportation agency is required to incorporate the published applicable wage determinations in federal-aid contracts.[424] An addendum must be circulated if notice of an amendment of a general wage determination is published in the *Federal Register* 10 days or more prior to bid opening.[425]

c. Fringe Benefit Provisions of the Davis-Bacon Act

The Davis-Bacon Act requires that the prevailing wage rate determined for federal and federally assisted construction include not only the basic hourly rate of pay, but also all amounts contributed by the contractor or subcontractor for certain fringe benefits.[426] The statute is specific regarding the items included in this component of the wage rate.

> [F]or medical or hospital care, pensions on retirement or death, compensation for injuries or illness resulting from occupational activity, or insurance to provide any of the foregoing, for unemployment benefits, life insurance, disability and sickness insurance, or accident insurance, for vacation and holiday pay, for defraying costs of apprenticeship or other similar programs, or for other bona fide fringe benefits, but only where the contractor or subcontractor is not required by other federal, state, or local law to provide any of those benefits, the amount of —
>
> (A) the rate of contribution irrevocably made by a contractor or subcontractor to a trustee or to a third person under a fund, plan or program; and
>
> (B) the rate of costs to the contractor or subcontractor that may be reasonably anticipated in providing benefits to laborers and mechanics pursuant to an enforceable commitment to carry out a financially responsible plan or program which was communicated in writing to the laborers and mechanics affected. [427]

The Davis-Bacon Act is open-ended in its coverage of these benefits. By providing for determinations regarding "other bona fide fringe benefits," it contemplates that the Secretary may recognize new fringe benefits as they come into general use and prevalence in an area.

Whether such benefits are provided through conventional insurance programs or trusts, they must be based on voluntary commitments to the employee-beneficiaries rather than an obligation imposed by federal, state, or local law. Accordingly, funds to pay for health benefits, pensions, vacations, and apprenticeship programs are distinguishable from payments made by an employer for workmen's compensation insurance under compulsory or elective state laws.[428]

Under this section, the Secretary is required to make separate findings as to the rates of contribution or costs of fringe benefits to which employees may be entitled.[429] Ordinarily this is an hourly rate; however, it may be

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[415] 29 C.F.R. § 1.5(b) (2001).

[416] CACC Manual, *supra* note 399.

[417] 29 C.F.R. § 1.5(a) (2001).

[418] 29 C.F.R. § 1.6(b) (2001).

[419] Nello L. Teer Co. v. United States, 348 F.2d 533, 539–40, 172 Ct. Cl. 255 (Ct. Cl. 1965).

[420] 29 C.F.R. § 1.8 (2001).

[421] 29 C.F.R. § 1.9; 29 C.F.R. pt. 7 (2001).

[422] 29 C.F.R. § 7.2 (b) (2001).

[423] 29 C.F.R. § 7.4(b) (2001).

[424] CACC Manual, *supra* note 399.

[425] *Id*.; 29 C.F.R. § 1.6(c)(2)(i)(A) (2001).

[426] 40 U.S.C. § 3141 (2003).

[427] 40 U.S.C. § 3141(2)(B) (2003).

[428] *Id.*

[429] 29 C.F.R. § 5.25 (2001).

expressed as a formula or a method of payment that can be converted into an hourly rate.[430] Whatever form is used to describe an employer's contribution, it must show that the contribution is made irrevocably to a trustee or third party not affiliated with the employer.[431] The trust or fund into which the contribution is made must be set up in such a way that the contractor-employer can in no way recapture any of the funds for itself, or have the funds diverted to its benefit.[432]

Determination of contribution rates is facilitated when a regularly established fund, plan, or program is involved.[433] However, a contractor or subcontractor may, through an enforceable commitment, undertake to carry out a financially responsible plan or program for the benefit of its employees.[434] Since this plan or program is financed from general assets of the employer, it is called an "unfunded plan," and the determination is directed to the cost reasonably to be anticipated in providing the benefits. In addition to showing its actuarial soundness, an unfunded plan must meet four basic criteria, namely: (1) it must be reasonably expected to provide the benefits described in the Davis-Bacon Act; (2) it must represent a legally enforceable commitment; (3) it must be carried out under a financially responsible program; and, (4) it must have been communicated in writing to the employees affected.[435] In addition to these criteria, and as a further safeguard against the possible use of "unfunded plans" to avoid compliance with the law, the Secretary is authorized to direct a contractor-employer to set aside in a separate account sufficient funds to meet future obligations under the plan.[436]

The District of Columbia Circuit considered the adequacy of a fringe benefit plan under the Davis-Bacon Act in *Tom Mistick & Sons, Inc. v. Reich*.[437] The contractor had made contributions to an employee benefit plan in an amount that constituted the difference between the prevailing wages paid in the locality and the actual cash wages paid to each employee. This was challenged as not being a "bona fide fringe benefit plan" under Davis-Bacon.[438]

The court noted that under Davis-Bacon, the employer's obligation may be met either solely by payment of cash wages in the prevailing amount, or by a combination of cash wages and irrevocable contributions to an employee fringe benefit plan or program.[439] In *Mistick*, contributions to a fringe benefit plan were made for the contractor's employees for all work covered by Davis-Bacon, and were irrevocable. The funds were placed in individual employee interest-bearing trust accounts managed by a neutral trustee. The cost of administering the accounts was not deducted from the accounts. Only the trustee, at the request of the employee, could make withdrawals from the accounts. Upon termination of their employment, the employees received the balance in the accounts.[440]

The Labor Department requires that "the amount contributed by an employer must bear a reasonable relationship to the actual rate of costs or contributions required to provide benefits for the employee in question."[441] The Administrator of the Wage and Hour Division of the Department of Labor determined that the plan was not bona fide because (1) contributions were greater than and not reasonably related to the costs of benefits, and (2) disbursements had been made for expenses not recognized as fringe benefits under Davis-Bacon. The court then found that the plan did in fact pass the "reasonable relationship" test.[442] The Labor Department had taken the position that it was insufficient that the employee would eventually receive the proceeds of the benefit fund, but rather argued that the employee was entitled to receive the prevailing wage at the time the work was performed. However, Davis-Bacon specifically allows use of the fringe benefit plan in conjunction with the cash wage, which necessarily implies that the employee will not get all payment due at the time of the work. Mistick's plan was essentially a pension plan with added benefits such as medical and disability insurance and vacation and sick leave, and was thus more generous than most employee fringe benefit plans.[443] The court thus found that even though contributions were greater than those required only for the insurance benefits, the plan actually benefited the employees.

i. Whether Plans Are Preempted by ERISA.—The Ninth Circuit found that California's prevailing wage law was not preempted by the Employee Retirement Income Security Act of 1974 (ERISA), even though it "referred to" ERISA plans.[444] The state statute measured the "prevailing wage" as the prevailing cash wage plus the prevailing benefits contribution by employers in a given locality. The statute referred to the benefits plans, which are ERISA plans, but the court found that the statute did not "refer to" them in enough detail to warrant ERISA preemption. Fringe benefit costs were calculated without regard to whether they were contributions to ERISA plans, and the employers' obligations to pay prevailing wages did not depend on the existence of an ERISA plan. The law did not impose any additional burden on an ERISA plan, nor did it require an

[430] 29 C.F.R. § 5.25(b) (2001).

[431] 29 C.F.R. § 5.26 (2001).

[432] *Id.*

[433] 29 C.F.R. § 5.27 (2001).

[434] 29 C.F.R. § 5.28 (2001).

[435] 40 U.S.C. § 3141(2)(B)(ii) (2003); 29 C.F.R. § 5.28(b) (2001).

[436] 29 C.F.R. § 5.28(c) (2001).

[437] 312 U.S. App. D.C. 67, 54 F.3d 900 (D.C. Cir. 1995).

[438] *Id.* 54 F.3d at 902; 40 U.S.C. § 3141(2)(B)(ii) (2003).

[439] *Id.* 54 F.3d at 902.

[440] *Id.*

[441] *Id.* at 903.

[442] *Id*. at 902.

[443] *Id*. at 904.

[444] WSB Elec., Inc. v. Curry, 88 F.3d 788 (9th Cir. 1996), *cert. denied*, 519 U.S. 1109, 117 S. Ct. 945 (1997).

employer to take any action regarding those plans.

d. Classification of Laborers and Mechanics

Proper classification of laborers and mechanics is considered a key factor in successful accomplishment of the goals of the Davis-Bacon Act.[445] This involves categorizing laborers and mechanics according to the work they actually perform, in terms of the comprehensive classification nomenclature adopted by the Secretary of Labor. Construction contract specifications are prepared with this in mind, and the states' standard specifications for highway construction furnish detailed descriptions of the work from which job descriptions can be developed. Traditionally, construction work has been performed by recognized craft classifications—carpenters, surveyors, truck drivers, electricians, heavy equipment operators—for which the regular duties are standardized. Where this situation exists, and the practices of the construction industry and labor organizations agree on correlation of duties and classifications, the craft classifications provide a reliable initial index for classifying work on highway projects. Another well-regarded test for job classification is the employee's use of the "tools of a trade."[446]

No single system of classification has succeeded in listing and assigning distinctive definitions to all construction job classifications. Therefore, differences may arise between the duties actually performed by a worker, his or her payroll designation, and the classification for which the contracting officer has requested a wage rate determination. Incomplete or improper classification may result in over- or under-payment of wages, wage disputes, and possible violation of contract terms. Accordingly, doubtful classifications should be clarified to the greatest possible extent, and contracting officers should minimize the chances for disputes by seeking agreement of all parties concerned with wage rate determinations before they are incorporated into project announcements or contracts.

e. "Site of the Work"

Another issue that has been considered is whether workers whose jobs are mainly located away from the construction site should be covered. The statutory provision refers to "mechanics and laborers employed directly on the site of the work."[447]

The regulations define "site of the work" as "[T]he physical place or places where the building or work called for in the contract will remain; and any other site where a significant portion of the building or work is constructed, *provided* that such site is established specifically for the performance of the contract or project;…."[448]

The definition may include such facilities as batch plants or borrow pits, provided that they are dedicated exclusively, or nearly exclusively, to the project or contract, and also provided that they are adjacent or virtually adjacent to the site of the work defined in § 5.2(l).[449] The "site of the work" does not include home offices, fabrication plants, or other facilities whose location and operation are not determined by the particular contract or project.[450]

The District of Columbia Circuit interpreted that language as not including workers employed at borrow pits and batch plants located about 2 mis away from the project, and overruled a contrary interpretation by the Secretary of Labor.[451] The Sixth Circuit later relied on this decision in *L.P. Cavett Co. v. United States Department of Labor*, where it concluded that truck drivers who drove over 3 mi from a batch plant at a quarry to the job site were not considered "mechanics and laborers employed directly on the site of the work."[452] The court found that the quoted language was not ambiguous, and that it means "only employees working directly on the physical site of the public work under construction."[453] The court also noted that expanding the geographic proximity in the manner being advocated by the Labor Department would create a problem with determining which off-site workers are closely enough "related" to the project to be covered by the statute.

Further, the Sixth Circuit held that the Davis-Bacon language was not modified by the Federal-Aid Highway Act, which does not contain the "site of the work" language, but which refers specifically to the Davis-Bacon Act.[454] The current rules defining "site of the work" were adopted in response to this decision.

f. Use of Apprenticeship Programs

Apprentices and trainees are included within the definition of "laborers and mechanics" in the regulations.[455] However, amendments to the Davis-Bacon Act allow apprentices and trainees to be paid a lower wage provided that they are enrolled in approved programs.

Apprenticeship programs are considered necessary to the effective administration of a prevailing wage program. It is essential to any apprenticeship program that an employer be allowed to pay apprentices a lower wage than what it pays fully trained and qualified journeyman employees.[456] The Davis-Bacon Act and state equivalent statutes allow payment of reduced wages to

[445] CACC Manual, *supra* note 399.

[446] *See,* 29 C.F.R. § 5.2(m) (2001).

[447] 40 U.S.C. § 3142(c)(1) (2003).

[448] 29 C.F.R. § 5.2(l)(1) (2001).

[449] 29 C.F.R. § 5.2(l)(2) (2001).

[450] 29 C.F.R. § 5.2(l)(3) (2001); *see also* CACC Manual, *supra* note 399.

[451] Ball, Ball, & Brosamer, Inc. v. Reich, 24 F.3d 1447 (D.C. Cir. 1994).

[452] 101 F.3d 1111, 1115 (6th Cir. 1996).

[453] *Id.*

[454] *Id.* at 1116; 23 U.S.C. § 113(a).

[455] 29 C.F.R. § 5.2(m) (2001).

[456] Minnesota Chapter of Associated Builders and Contractors, Inc. v. Minnesota Dep't of Labor and Indus., 47 F.3d 975, 981 (8th Cir. 1995), *reh'g denied*.

apprentices so long as the employer uses an apprenticeship program that meets the standard issued under the National Apprenticeship Act, known as the Fitzgerald Act.[457] The Department of Labor determines the adequacy of apprenticeship programs through its Bureau of Apprenticeship and Training.[458] States may apply similar standards to their own apprenticeship programs.[459] Although public works contractors are not required to use apprentices, they are allowed to, and if they do they may pay the reduced apprentice wage only to those apprentices in approved programs.[460]

In addition, there is an exemption for those apprentices and trainees employed in equal opportunity employment programs: "The provisions of the section shall not be applicable to employment pursuant to apprenticeship and skill training programs which have been certified by the Secretary of Transportation as promoting equal employment opportunity in connection with Federal-aid highway construction programs."[461]

The implications of this exception were considered in *Siuslaw Concrete Construction Company v. State of Washington, Department of Transportation*.[462] The contractor argued that the state department of transportation could not require the contractor to pay wages higher than those required by federal regulations. However, the court found that there was insufficient evidence of congressional intent to occupy the field of minimum wages in order to support a finding of preemption.

State apprenticeship programs may not, however, impermissibly discriminate against out-of-state contractors. In a 2011 decision, *Tri-M Group, LLC v. Sharp*, the U.S. Court of Appeals for the Third Circuit affirmed a decision by the U.S. District Court for the District of Delaware, which held that the State of Delaware's refusal to recognize out-of-state registered apprentices discriminated against out-of-state contractors without advancing a legitimate state interest, in violation of the dormant Commerce Clause.[463] Until stopped by the courts, Delaware's Department of Labor had administered its state apprenticeship program requirements to allow in-state public works contractors to pay a reduced apprentice rate to Delaware-registered apprentices, while prohibiting out-of-state contractors from sponsoring an in-state apprenticeship program, and requiring them to pay the higher mechanic's rate to apprentices registered elsewhere than Delaware, unless they set up and maintained a permanent office location within Delaware.

i. Relationship of Apprenticeship Programs to ERISA.—Since the enactment of ERISA, these programs have been challenged in a number of states as being preempted by ERISA. The purpose of ERISA is to promote the interests of employees and their beneficiaries in employee benefit plans.[464] It also serves to protect employers by eliminating the threat of conflicting or inconsistent state and local regulation of employee benefit plans.[465] To this end, ERISA includes a preemption clause.[466] However, it is not intended to preempt areas of traditional state regulation.[467]

Issues arose among courts as to whether the states' requirements for apprenticeship programs were preempted by ERISA.[468] An apprenticeship program that is a joint effort of management and labor, or a "joint apprenticeship committee," is an "employee welfare benefit plan" as defined in ERISA. The problem has been to determine what the state may regulate with respect to apprenticeship programs without encountering the ERISA preemption. Unlike other issues that have been raised with respect to ERISA, such as use of project labor agreements by contracting agencies, the apprenticeship program is considered part of the state's regulatory role rather than its role as a construction project owner.

In *Dillingham Construction, N.A. v. County of Sonome*, the Ninth Circuit held that a program that required state approval of apprenticeship programs before contractors could pay reduced wages conflicted with ERISA and was therefore preempted by it.[469] The court found that the program, which required state approval of what the court considered an employee benefit plan under ERISA, "related to" an employee benefit plan and was therefore preempted. Following that decision, the

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[457] 29 U.S.C. § 50 (1999) authorizes the Secretary of Labor to:

> Formulate and promote the furtherance of labor standards necessary to safeguard the welfare of apprentices, to extend the application of such standards by encouraging the inclusion thereof in contracts of apprenticeship to bring together employers and labor for the formulation of programs of apprenticeship, to cooperate with State agencies engaged in the formulation and promotion of standards of apprenticeship….

[458] *See generally* 29 C.F.R. pt. 29 (1999) for standards and procedures regarding federal approval of apprenticeship programs.

[459] *See* Cal. Division of Labor Standards Enforcement v. Dillingham Constr., N.A., Inc., 519 U.S. 316, 117 S. Ct. 832, 835, 136 L. Ed. 2d 791 (1997).

[460] *Id.*

[461] 23 U.S.C. § 113(c) (2001).

[462] 784 F.2d 952 (9th Cir. 1986).

[463] 638 F.3d 406 (3d Cir. 2011).

[464] WSB Elec., Inc. v. Curry, 88 F.3d 788, 791 (9th Cir. 1996) *cert. denied*, 117 S. Ct. 945 (1997) (quoting Shaw v. Delta Air Lines, Inc., 463 U.S. 85, 90, 103 S. Ct. 2890, 77 L. Ed. 2d 490 (1983)).

[465] *Id*. at 791 (quoting Shaw, 463 U.S. at 99).

[466] ERISA, § 514(a); 29 U.S.C. § 1144(a).

[467] WSB, 88 F.3d at 791 (citing Metropolitan Life Ins. Co. v. Mass., 471 U.S. 724, 740, 105 S. Ct. 2380, 85 L. Ed. 2d 728 (1985).

[468] *See* Inland Empire Chapter of Associated General Contractors v. Dear, 77 F.3d 296 (9th Cir. 1996) (Washington apprenticeship program preempted by ERISA); Minnesota Chapter of Associated Builders and Contractors, Inc. v. Minn. Dep't of Labor and Indus., 47 F.3d 975 (8th Cir. 1995), *reh'g denied* (Minn. apprenticeship program not preempted by ERISA).

[469] 57 F.3d 712 (9th Cir. 1995).

Ninth Circuit came to the same conclusion regarding the State of Washington's apprenticeship program.[470]

In a similar case, the Eighth Circuit held that Minnesota's apprenticeship program was not preempted by ERISA.[471] The only difference in that state program appeared to be that the State of Minnesota program allowed approval of the apprenticeship program by either the state or the federal government. However, the court stated more broadly that the purpose of ERISA in protecting employee benefit plans was not hindered by the state's regulation of wages and labor in state-funded construction. Rather, this was within the scope of the state's traditional police power, which Congress did not intend to preempt with ERISA.[472]

The United States Supreme Court took the opportunity to resolve this issue in its review of the Ninth Circuit's decision in *Dillingham Construction*.[473] Reversing the Ninth Circuit, the Court held that California's prevailing wage law, specifically its apprenticeship program requirements, did not "relate to" employee benefit plans, and thus was not preempted by ERISA.

The Court stated that a state law "relates to" a covered employee benefit plan if it "has a connection with" or if it "references" such a plan.[474] Because the range of apprenticeship programs that were eligible for state approval was broader than just those that arguably qualified as ERISA plans (joint apprenticeship committee plans), the law did not make "reference to" an ERISA plan.[475]

The Court then considered whether the apprenticeship program "had a connection to" ERISA plans. Given that both the federal government and the states regulated apprenticeship programs prior to ERISA, the Court concluded that Congress expected those programs to continue after ERISA's enactment. The Court noted that: "The wages to be paid on public works projects and the substantive standards to be applied to apprenticeship training programs are, however, quite remote from the areas with which ERISA is expressly concerned—'reporting, disclosure, fiduciary responsibility, and the like.'"[476]

Thus the Court refused to find that ERISA preempted the prevailing wage law and apprenticeship standards, which it found to be part of an "area of traditional state regulation."[477]

In a 2004 decision, the U.S. Court of Appeals for the Ninth Circuit followed the U.S. Supreme Court's ruling in *Dillingham*, holding in *Associated Building Contractors of Southern California Inc. v. Nunn et al.*[478] that ERISA did not preempt amendments to California statutes which established minimum wages and benefits on public and private construction projects for state-registered apprentices.

In a 2006 decision, *Oregon-Columbia Brick Masons v. Or. Bureau of Labor & Indus.*, the U.S. Court of Appeals for the Ninth Circuit affirmed a ruling by the U.S. District Court for the District of Oregon that ERISA did not preempt certain Oregon state statutes, regulations, and actions concerning apprenticeship programs.[479] After the Oregon State Apprenticeship and Training Council rejected certain unions' applications to register as apprenticeship programs, on the grounds that they did not offer any programs that satisfied any needs unmet by existing programs, under a state statutory needs provision. Rejecting a claim that federal funding made the state laws, regulations, and actions subject to preemption by ERISA, the court found that the state needs requirement did not distinguish between funded and unfunded plans and was thus not tied to the issue of federal funding.

In a 2008 decision, the U.S. Court of Appeals for the Sixth Circuit revisited a 1992 ruling that ERISA had preempted two state apprentice-training requirements. In *Associated Builders & Contractors, Saginaw Valley Area Chapter, et al. v. Michigan Department of Labor and Economic Growth*,[480] the Sixth Circuit reversed a lower court decision denying a state government motion to dissolve a federal injunction, issued in 1992,[481] which had prevented the state from enforcing two state apprentice-training requirements. The 1992 injunction had been based on a determination that ERISA had preempted the state apprentice-training requirements. The state had complied with the injunction for many years, but sought to dissolve it in light of the U.S. Supreme Court's decision in the *Dillingham* case, discussed above. Overturning a lower court, the Sixth Circuit held that the 1992 injunction had to be dissolved, and the state had to be allowed to enforce its apprentice-training requirements, in light of the *Dillingham* case.

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[470] Inland Empire Chapter of Associated General Contractors v. Dear, 77 F.3d 296 (9th Cir. 1996).

[471] Minn. Chapter of Associated Builders and Contractors, Inc. v. Minn. Dep't of Labor and Indus., 47 F.3d 975 (8th Cir. 1995), *reh'g denied*.

[472] *Id.* at 979.

[473] Cal. Div. of Labor Standards v. Dillingham, 519 U.S. 316, 117 S. Ct. 832, 136 L. Ed. 2d 791 (1997).

[474] *Id.* 117 S. Ct. at 837.

[475] *Id.* at 838. In contrast, the Court had found that a prevailing wage statute was preempted where it expressly referred to an ERISA-covered plan, in which the obligation imposed on the employer was measured by reference to the level of benefit provided by that employer under an ERISA plan. District of Columbia v. Greater Washington Board of Trade, 506 U.S. 125, 128, 132, 113 S. Ct. 580, 121 L. Ed. 2d 513 (1992).

[476] *Id.* at 840 (quoting N.Y. State Conference of Blue Cross and Blue Shield Plans v. Travelers Ins. Co., 514 U.S. 645, 115 S. Ct. 1671, 1680, 131 L. Ed. 2d 695 (1995)).

[477] *Id.* at 842.

[479] 356 F.3d 979 (9th Cir. 2004).

[479] 2003 U.S. Dist. LEXIS 28066 (D. Or. Sept. 18, 2003).

[480] 543 F.3d 275 (6th Cir. 2008.

[481] 817 F. Supp. 49, 54 (E.D. Mich. 1992).

Apprenticeship programs do not stand alone, and interact with other programs as well. In a 2010 decision, *Johnson, et al. v. Rancho Santiago Community College District, et al.*, the U.S. Court of Appeals for the Ninth Circuit affirmed most of a decision by the U.S. District Court for the Central District of California granting summary judgment to defendants in a case filed by nonunion apprentices claiming that a college district's decision to participate in a project labor agreement (PLA) violated their due process and equal protection rights and also violated ERISA and the National Labor Relations Act (NLRA).[482] The PLA required all contractors and subcontractors on covered projects to agree to the PLA, required that contractors use union hiring halls to obtain workers, and required that all workers on covered projects become union members within 7 days of their employment. The Ninth Circuit held that entering into the PLA constituted market participation not subject to preemption by ERISA or the NLRA, reflected an interest in the efficient procurement of goods and services, and did not violate the nonunion apprentices' constitutional rights. The Court noted that there was no law requiring that non-union apprentices remain eligible for all construction projects; and that the PLA did not deprive the nonunion apprentices of the opportunity to pursue careers as electricians because they were free to join a union apprenticeship program supplying workers for the college district's projects. The only regard in which the Ninth Circuit modified the District Court's decision was to dismiss ERISA preemption claims by apprentices who had graduated from their apprenticeship programs, indicating that those claims were moot because they did not have reasonable expectations of being subject to a PLA as apprentices again. The U.S. Supreme Court subsequently denied certiorari.

Considering another aspect of the relationship between apprenticeship programs and ERISA, the U.S. Court of Appeals ruled in a 2009 case, *In Re: Halpin*, upholding decisions by a U.S. bankruptcy court and the U.S. District Court Northern District of New York (NDNY), that after an electrical contractor filed for bankruptcy, the debtor's unpaid contributions to union apprenticeship and other benefit funds were not "assets" within the meaning of ERISA, so the contractor was not a fiduciary over those funds and could not be held personally liable for their nonpayment despite the bankruptcy filing.[483]

ii. Consistency with Competitive Bidding.—Other apprenticeship programs have been challenged as being inconsistent with the requirements of competitive bidding. In *Associated Builders and Contractors v. City of Rochester*, the court struck down an apprenticeship program "precondition," in which the successful bidder had to agree to participate in the state program.[484] The requirement in effect created a bidder preference for those bidders whose employees participated in a state-approved apprenticeship program. The court found that this precondition was not linked to the interests embodied in the competitive bidding statutes. An applicable state statute required that the City utilize competitive bidding.[485] The municipal ordinance that established the apprenticeship program preference was found to be inconsistent with competitive bidding statute, and there was not specific statutory authorization for it. The court pointed out that the main purpose of the competitive bidding law was the protection of the public fisc. The requirement for apprenticeship training, while a desirable goal, was not intended to affect the qualification of an otherwise responsible low bidder.

g. State "Prevailing Wage" Laws

As discussed above, federal-aid highway and bridge projects are subject to federal Davis-Bacon requirements.

The Davis-Bacon Act expressly includes the District of Columbia within its provisions. Thus, while Washington, D.C., may not have its own local prevailing wage law, construction projects within that city are subject to Davis-Bacon requirements.

Aside from the Federal Davis-Bacon Act, 32 of the 50 states in the United States have established their own prevailing wage requirements, which will apply to highway and bridge projects even when such projects are funded entirely with state or municipal funding, and no federal-aid funding is involved which would trigger Davis-Bacon requirements. The states that have done so include Alaska, Arkansas, California, Connecticut, Delaware, Hawaii, Illinois, Indiana, Kentucky, Maine, Maryland, Massachusetts, Minnesota, Michigan, Missouri, Montana, Nebraska, Nevada, New Jersey, New Mexico, New York, Ohio, Oregon, Pennsylvania, Rhode Island, Tennessee, Texas, Vermont, the State of Washington, West Virginia, Wisconsin, and Wyoming.

There are eight states that reportedly have never enacted any state prevailing wage laws: Georgia, Iowa, Mississippi, North Carolina, North Dakota, South Carolina, South Dakota, and Virginia.[486] In addition, there are nine other states that used to have state prevailing wage laws, in which such laws have been repealed or held unconstitutional by state courts: Alabama, Arizona, Colorado, Florida, Idaho, Kansas, Louisiana, New Hampshire, and Oklahoma.[487]

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[482] Johnson et al. v. Rancho Santiago Comm. College Dist., 623 F.3d 1011.

[483] Rahm v. Halpin, 370 B.R. 45, 2007 U.S. Dist. LEXIS 41524 (N.D.N.Y. 2007).

[484] 501 N.Y.S.2d 653, 492 N.E.2d 781, 67 N.Y.2d 854 (1986).

[485] N.Y. GEN. MUN. LAW § 103.

[486] George C. Leef, *Prevailing Wage Laws: Public Interest or Special Interest Legislation*, 30 CATO JOURNAL, No. 1, 137, 139 (2010; available at http://www.cato.org/pubs/journal/cj30n1/cj30n1-7.pdf, last accessed on Nov. 17, 2010.

[487] *Id.*

State and municipal DOTs located in states with prevailing wage laws, and contractors and subcontractors working in those states, should become familiar with the applicable state prevailing wage statutes and regulations, as those will apply even to projects that do not involve any federal-aid funding. Such prevailing wage requirements may vary from state to state, and it is beyond the scope of this current volume to provide a detailed survey of all such provisions. The Associated Builders and Contractors, Inc. (ABC), a trade association of construction contractors, has however established a Web site that provides links to information on the prevailing wage statutes, regulations, and other related requirements in the states with state prevailing wage requirements listed above.[488]

2. Hours and Conditions of Work

Federal legislation prescribing standards for hours of work and conditions of the work environment is contained in the Fair Labor Standards Act of 1938 (FLSA)[489] and the Contract Work Hours and Safety Standards Act of 1962.[490] Both prescribe a standard workweek of 40 hours. Compensation for work in excess of these levels is specified as not less than one and one-half times the basic rate of pay.[491] The Contract Work Hours and Safety Standards Act also provides that employers shall not require their employees to work in surroundings or work conditions that are unsanitary, hazardous, or dangerous to their health or safety, as determined by regulations of the Secretary of Labor.[492]

The language of the FLSA is directed to "persons engaged in commerce, or in the production of goods for commerce."[493] The Contract Work Hours and Safety Standards Act applies to construction projects to which the United States is a party, or which are done on behalf of the United States, or which are wholly or partially financed by grants or loans given or guaranteed by the United States.[494] In the case of federal-aid highway construction projects, the application of the federal law's wage and hour standards is achieved by reading 40 U.S.C. §§ 328 and 329 together. Section 328(b) provides that the 40-hour workweek "shall be a condition of every contract of the character specified in section 329…and of any obligation of the United States…in connection therewith." Section 329, in turn, extends the standards to contracts "financed in whole or in part by loans or grants from…the United States or any agency or instrumentality thereof under any statute of the United States providing wage standards for such work…."

Requirements for adherence to the 40-hour workweek have been incorporated into the Required Contract Provisions for Federal-Aid Construction Contracts:

> No contractor or subcontractor contracting for any part of the contract work which may require or involve the employment of laborers, mechanics, watchmen, or guards (including apprentices, trainees, and helpers described in paragraphs 4 and 5 above) shall require or permit any laborer, mechanic, watchman, or guard in any workweek in which he/she is employed on such work, to work in excess of 40 hours in such workweek unless such laborer, mechanic, watchman, or guard receives compensation at a rate not less than one-and-one-half times his/her basic rate of pay for all hours worked in excess of 40 hours in such workweek.[495]

In recent years, the longstanding requirements described above have been supplemented by the regulations of the U.S. Department of Labor's OSHA under the Contract Work Hours and Safety Standards Act of 1962. In particular, OSHA considers work performed by contractors on highway and bridge construction, reconstruction, rehabilitation, and repair projects to be subject to 29 C.F.R. Part 1926, Safety and Health Regulations for Construction.

At the time of the 2011 update to this current volume, 29 C.F.R. Part 1926 includes 28 subparts, each of which includes multiple sections. Every state and municipal DOT undertaking and exercising construction inspection over federal-aid highway and bridge projects, and every contractor and subcontractor working on such projects, should have personnel thoroughly familiar with the requirements of Part 1926. These regulations are too lengthy and complex to be summarized readily in this volume. It is, however, worth focusing briefly on OSHA regulations applicable to two areas in which fatal or serious personal injury construction accidents occur all too frequently on highway and bridge construction projects.

The first such area involves falls from elevated structures. OSHA safety requirements applicable to work on elevated structures include 29 C.F.R. §§ 1926.28, "Personal protective equipment;" 1926.104, "Safety belts, lifelines, and lanyards;" 1926.105, "Safety nets," 1926.106, "Working over or near water," 1926 Subpart L (§§ 1926.450 *et seq*.), "Scaffolds," 1926 Subpart M (§§ 1926.500 *et seq*.), "Fall protection," 1926 Subpart R (§§ 1926.750 et seq.), "Steel erection," especially § 1926.760, "Fall protection," and 1926 Subpart X (§§ 1926.1050 *et seq*.), "Ladders."

OSHA considers contractors responsible to ensure that construction workers on bridge projects and on highway projects involving work on elevated structures or in elevated locations not only have fall protection equipment in good working condition, but also use such equipment in performing their work. Aside from such personal protective equipment, OSHA also expects that elevated work areas be equipped with scaffolds and/or safety nets complying with OSHA requirements, and

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[488] Associated Builders and Contractors, Inc., State Prevailing Wage Laws, 2008.

[489] 29 U.S.C. §§ 201–19 (2001).

[490] 40 U.S.C. §§ 327–34 (2001).

[491] 29 U.S.C. § 207 *et. seq.* (2001); 40 U.S.C. § 328(a) (2001).

[492] 40 U.S.C. § 333 (2001).

[493] 29 U.S.C. §§ 202(a).

[494] 40 U.S.C. §§ 328–29.

[495] Required Contract Provisions for Federal-Aid Construction Contracts, § IV.7

that equipment for projects involving work on elevated areas over water also includes life preservers or bouyant work vests, ring buoys with at least 90 ft of line spaced no more than 200 ft apart, and at least one life-saving skiff (boat) available for rescuing any employees who fall into the water. Any contractor whose personnel have a fatal or serious personal injury accident involving a fall from structure on a highway or bridge project, where OSHA determines that the safety equipment required by these regulations was not available at the project site, was not in good repair, or was not in use, can expect to incur concerted OSHA enforcement action, beginning with immediate shutdown of the construction project and in all likelihood resulting in very substantial fines.

The second such area involves the collapse of trenches or excavations. The applicable OSHA regulations are found in 29 C.F.R. Part 1926 Subpart P (§§ 1926.650 *et seq*.), "Excavations," particularly § 1926.651, "Specific excavation requirements," and § 1926.652, "Requirements for protective systems." There are a number of detailed requirements in OSHA's excavation regulations that state and municipal DOTs and contractors need to be familiar with, but among the most important are the requirements for adequate sloping or benching systems and shoring of all excavations, except for those made entirely in stable rock or those less than 5 ft deep, to protect employees against cave-ins, which could bury them alive in soil. Any contractor whose personnel have a fatal or serious personal injury accident involving a cave-in of an excavation on a highway or bridge project, and who has failed to employ adequate sloping, benching, and shoring of excavations to protect employees against cave-ins, can expect to incur concerted OSHA enforcement action, beginning with immediate shutdown of the construction project and in all likelihood resulting in very substantial fines.

Both because the protection of construction workers' lives and safety is important, and because the consequences following fatal or serious personal injury accidents can be quite severe for all concerned, state and municipal DOTs and their contractors would be well advised to pay focused and ongoing attention to full compliance with all safety requirements required by OSHA regulations for work on elevated structures and work in excavations. OSHA enforcement personnel generally consider fatal and serious personal injury construction accidents involving falls from elevated structures or cave-ins of excavations to be almost entirely preventable occurrences, consider contractors on whose construction sites such accidents occur to be culpable, and often seek to apply the maximum penalties possible under the circumstances. As OSHA takes such matters very seriously, contractors and state and municipal DOTs or other owners should not have high expectations regarding cooperation about the duration of project shutdowns for OSHA investigations or about leniency in OSHA's selection of administrative charges or penalties against contractors.

3. Compliance with Wage and Hour Requirements

Contractors are required to submit weekly payroll statements documenting the wages paid to laborers and mechanics in the previous weekly payroll.[496] These statements are submitted to the contracting agency.[497] The contracting agency should review these statements for completeness, checking periodically items such as classification, hourly rates, fringe benefits, and overtime pay.[498]

The Required Contract Provisions for Federal-Aid Construction Contracts include a provision for withholding liquidated damages for days on which the contractor did not pay overtime.[499] These liquidated damages of $10 per day per employee are forwarded to the Department of Labor to support their enforcement activities.

The Comptroller General has the ability under the Davis-Bacon Act to withhold funds from payments due the contractor for payment of prevailing wages, and to pay those funds directly to laborers and mechanics who have not been paid the wages due to them.[500] Contractors who have failed to meet their obligations under the Davis-Bacon Act are also subject to debarment for a period of 3 years.[501]

4. Project Labor Agreements

The NLRA allows the formation of PLAs on public works projects.[502] PLAs are collective bargaining agreements entered into by the public agency and a representative union. They provide generally for recognition of that union as the representative of all employees on the project, compulsory union dues, and mandatory use of union hiring halls. Where a project specification calls for a PLA, the successful bidder must agree to be bound by the terms of the PLA as a condition of award. Although several issues of consistency with state and federal law have been raised with respect to PLAs, they have usually been found to be valid when challenged.

a. Executive Order 13502 of 2009

PLAs are the subject of a Presidential EO No. 13502, issued on February 6, 2009. [503] This EO sets forth na-

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[496] 29 C.F.R. § 3.3(b) (2001).

[497] 29 C.F.R. § 3.4(a) (2001).

[498] CACC Manual, *supra* note 399.

[499] Required Contract Provisions, *supra* note 495, § IV.8; 29 C.F.R. § 5.8 (2001).

[500] 40 U.S.C. § 3144 (2003).

[501] *Id.*

[502] 29 U.S.C. §§ 158(e), (f).

[503] Presidential Executive Order No. 13502, issued on Feb. 6, 2009, 74 Fed. Reg. 6985, Feb. 11, 2009. Note that Executive Order No. 13502 of Feb. 6, 2009, rescinds prior Executive Orders Nos. 13202 of Feb. 17, 2001, and 13208 of Apr. 6, 2001, and directs the heads of federal agencies to revoke expeditiously any agency orders, rules, or regulations implementing those prior Executive Orders.

tional policy on the use of PLAs on large-scale federal construction contracts, defined as highway or other construction, repair, rehabilitation, alteration, or improvement projects undertaken by federal agencies through contractors where the total cost of such a project is $25 million or more.[504]

Finding that labor disputes on large projects, especially complex projects involving multiple contractors, can be unusually disruptive, the EO declares it to be the policy of the Federal Government to encourage federal agencies to consider requiring the use of PLAs on large federal projects.[505] EO authorizes federal agencies, when awarding contracts in connection with large-scale projects, to determine on a case-by-case basis whether use of a PLA would help to achieve economy and efficiency in federal procurement, producing labor management stability, and ensuring compliance with laws and regulations governing safety and health, equal employment opportunity, labor and employment standards, and other matters, and be consistent with law.[506] If a federal agency finds that such circumstances exist, the agency is authorized, if appropriate, to require that every contractor or subcontractor on the project agree, for that project, to negotiate or become a party to a PLA with one or more appropriate labor organizations.[507]

If a federal agency decides to use a PLA on a large and complex project, the EO authorizes such a PLA to bind all contractors and subcontractors on the project through the inclusion of appropriate language in all project solicitation and contract documents; to allow all contractors and subcontractors to compete for contracts and subcontracts without regard to whether they are otherwise parties to collective bargaining agreements; to contain guarantees against strikes, lockouts, and similar job disruptions; and to provide effective, prompt, and mutually binding procedures for resolving labor disputes arising during the PLA.[508]

The EO does not, however, require federal agencies to use PLAs on all federal projects or preclude the use of PLAs in circumstances not covered in the EO. It also does not require contractors or subcontractors to enter into PLAs with any particular labor organization.[509]

The EO directs the Federal Acquisition Regulatory Council to amend the FARs to implement the provisions of the Order within 120 days after the date of the Order.[510]

While encouraging federal agencies (including USDOT), EO 13502 does not expressly require state or municipal DOTs or other recipients of federal-aid funding to enter into PLAs on all projects. The EO does, however, direct the head of OMB, in consultation with the Secretary of Labor and others as appropriate, to provide the President with recommendations within 180 days after issuance of the Order concerning whether broader use of PLAs, with respect both to federal construction contracts and "construction projects receiving federal financial assistance," would help to promote the economical, efficient, and timely completion of such projects.[511]

b. FHWA Administrative Guidance to States

On May 7, 2010, just over a year after the issuance of EO 13502, FHWA's Administrator issued a memorandum, "Interim Guidance on the use of Project Labor Agreements," to all FHWA Division Administrators and FHWA Directors of Field Services nationwide, providing FHWA's administrative interpretation of it. [512] He indicated that this memorandum superseded FHWA's prior October 5, 2001, administrative guidance on PLAs. The memorandum was characterized as providing "interim" guidance because OMB had not yet provided the President with recommendations concerning the use of PLAs on federal-aid projects. The Administrator indicated that when OMB did so, he would provide further guidance conforming to OMB's recommendations.

The FHWA guidance memorandum indicates that a state DOT wishing to obtain FHWA consent to require a contractor on a federal-aid project to use a PLA may submit a written appliucation to the appropriate FHWA Division Office. The application must assert that the use of a PLA for the particular federal-aid project involved will advance the interest of the government, describing the basis for that determination and providing reasonable documentation demonstrating its factual underpinnings; and that the PLA will be consistent with law. While the EO applies only to large-scale projects costing $25 million or more, the memorandum indicates that FHWA will consider state DOT requests for use of PLAs on federal-aid projects of less than $25 million if the project would otherwise comply with FHWA's guidance.

The FHWA guidance memorandum indicates that, to satisfy the requirement that the use of a PLA will advance the interest of the government, the state DOT must make a reasonable showing that the use of a PLA on the project will advance the interest of the government in reducing construction costs and achieving economy and efficiency, producing labor management stabuility, and assure compliance with laws and regulations governing safety and health, equal employment opportunity, labor and employment

[504] Presidential Executive Order No. 13502, at § 2 (b) through (e).

[505] Presidential Executive Order No. 13502, at § 1(b) of that Order.

[506] Presidential Executive Order No. 13502, at § 3(a).

[507] Presidential Executive Order No. 13502, at § 3(b).

[508] Presidential Executive Order No. 13502, at § 4.

[509] Presidential Executive Order No. 13502, at § 5.

[510] Presidential Executive Order No. 13502, at § 6.

[511] Presidential Executive Order No. 13502, at § 7.

[512] FHWA Memorandum, Interim Guidance on the use of Project Labor Agreements, May 7, 2010; available at http://www.fhwa.dot.gov/construction/contracts/100507.cfm, most recently accessed on Nov. 19, 2011.

standards, and other matters as appropriate. The memorandum lists factors which state DOTs may consider in doing so, including, but not limited to the size and complexity of the project; the importance of the project and the need to adhere to a certain timeline; the risk of labor unrest on the project and any circumstances that may lead to a heightened risk of labor disruption (providing several examples omitted here); the impacts of a labor disruption to the users, the operation of the facility, and the region; the costs of delay should a labor disruption occur; and the available labor pool relative to the particular skills required to complete the project. In addition to stating that any one or more of these factors may be adequate to justify the use of a PLA, the memorandum indicates that this is not an exclusive list, and that other factors may also reasonably permit a state to conclude that the use of a PLA is appropriate. If the state DOT provides evidence that FHWA's Division Office considers reasobly adequate, the Division Office may consider the requirement for advancing government interest satisfied, unless it has some reason for concern that the state DOT's conclusion or evidence is incomplete or inadequate.[513]

In reviewing PLAs, FHWA Division Offices will also check to ensure that they are in compliance with law. Among other things, PLAs must be used and structured in such a manner as to be effective in securing competition. They must not prohibit any contractor from bidding for or working as a subcontractor on the project and must lead to a cost-effective use of federal funds.[514] The latter requirement can be satisfied by the same evidence showing that the PLA is in the interest of the government. PLAs must be in compliance with DBE requirements,[515] FHWA restrictions on the use of labor employment preferences,[516] EEO requirements,[517] and all other applicable Title 23 U.S.C. and C.F.R. requirements.

In considering state PLA requests, FHWA Division Offices will also review the terms of the PLAs, which must meet a series of requirements to be valid. They must bind all contractors and subcontractors on the project through inclusion of appropriate specifications in all solicitations and contract documents. They must allow all contractors and subcontractors to compete for contracts and subcontracts without regard to whether they are otherwise parties to collective bargaining agreements. They must include guarantees against strikes, lockouts, or other job disruptions. They must incorporate procedures for resolving labor disputes on the project which are mutually binding, prompt, and effective. They must also provide mechanisms for labor management cooperation on productivity, quality of work, safety, health, and other issues of mutual concern. Finally, they must also fully conform to all statutes, regulations, and EOs.[518]

As the EO does not make PLAs mandatory, and FHWA's guidance memorandum makes the process for PLA review and approval dependent upon a state DOT first submitting a request for such approval, current federal policy grants state DOTs discretion over whether to request the use of PLAs on their projects or not. In actual practice, their use will depend upon the policy perspectives of the various state governments regarding the usefulness and appropriateness of PLAs. If a state DOT chooses to use PLAs on major projects, however, the EO and FHWA's guidance memorandum provide clear procedures and guidelines for them to follow in doing so. Following the federal procedures and guidelines and obtaining FHWA approval should, in turn, make PLAs more defensible if challenged through judicial review.

c. Consistency with Federal Law

i. Consistency with NLRA.—In *Building and Construction Trades Council v. Associated Builders and Contractors*, the United States Supreme Court considered whether PLAs are consistent with the requirements of the NLRA.[519] The Massachusetts Water Resources Authority (MWRA) had been ordered to clean up Boston Harbor in part by adding treatment facilities for sewer discharges that entered the harbor. The project manager negotiated a PLA with the Building and Construction Trades Council (BCTC), which was designed to assure labor stability over the length of the project. MWRA then included a specification in its bid package that each successful bidder must agree to abide by the terms of the PLA.

Associated Builders first filed a complaint with the National Labor Relations Board (NLRB). The NLRB found that the PLA was valid under Section 8(e) of the NLRA, which contains the exception allowing PLAs. Associated Builders then sought to enjoin the use of the specification on the grounds that it violated the NLRA. The district court denied the injunction, but the First Circuit reversed, finding that the specification was preempted under NLRA. The appeals court found that the PLA was barred by the preemption doctrine set out in *San Diego Building Trades Council v. Garmon*, in which the Court held that the NLRA preempted state or local regulation that constituted a pervasive intrusion into the bargaining process, but not "peripheral regulation."[520] The First Circuit also considered the PLA to be preempted under *International Ass'n of Machinists v. Wisconsin Employment Relations Comm'n*, which held that the State could not regulate activities that Congress intended to be unrestricted by government.[521] The

[513] *Id.* at 2–3.

[514] 23 C.F.R. § 112.

[515] 49 C.F.R. pt. 26.

[516] 23 C.F.R. § 635.117(b).

[517] 23 C.F.R. pt. 230.

[518] FHWA, *supra* note 513, at 3.

[519] 507 U.S. 218, 113 S. Ct. 1190, 122 L. Ed. 2d 565 (1993).

[520] 113 S. Ct. at 1194 (citing 359 U.S. 236, 79 S. Ct. 773, 3 L. Ed. 2d 775 (1959)).

[521] *Id*. (citing 427 U.S. 132, 96 S. Ct. 2548, 49 L. Ed. 2d 396 (1976)).

Supreme Court reversed the First Circuit, holding that the NLRA does not preempt the enforcement by a state agency, acting as an owner of a construction project, of an otherwise lawful pre-hire collective bargaining agreement, such as the PLA in this case.[522]

The Court held that the preemption doctrines of *Garmon* and *Machinists* apply only to state labor *regulation*. The State may act without the effect of preemption when it is acting as a proprietary, not as a regulator or policy-maker.[523] As support for its conclusion, the Court cited to the 1959 amendments to the NLRA. Sections 8(e) and 8(f) had previously prohibited this type of agreement by prohibiting agreements that require an employer to refrain from doing business with anyone who does not agree to be bound by a pre-hire agreement. However, the amendments specifically allowed pre-hire collective bargaining agreements in construction contracts. These amendments were intended to accommodate conditions specific to the construction industry, both public and private.[524] These conditions include the short-term nature of employment in the construction industry, which makes post-hire collective bargaining difficult, and the contractor's need for a steady supply of labor and predictable costs. Further, pre-hire agreements had been a long-standing custom in the construction industry.[525]

In this particular use of a PLA, the Court noted that the agency had been ordered pursuant to the Clean Water Act to undertake the harbor cleanup.[526] Compliance with this court order required construction to proceed without interruption, and made no allowance for delays caused by labor strikes. The project manager had been hired by MWRA to advise the agency on labor relations, and suggested the use of a PLA. The project manager then negotiated the PLA, which included terms such as (1) recognition of the BCTC as exclusive bargaining agent for all craft employees on the project; (2) use of specified methods of resolving all labor-related disputes; (3) a requirement that all employees be required to become union members within 7 days of employment; (4) primary use of BCTC's hiring halls to supply the project's craft labor force; (5) a 10-year no-strike commitment on the part of the union; and (6) requirements that all contractors and subcontractors agree to be bound by the PLA.[527]

The Court noted that NLRA does not contain a specific preemption. A statute or state activity is not preempted by federal law unless it actually conflicts with federal law, or would frustrate a federal scheme, or unless the Court discerns that "Congress sought to occupy the field to the exclusion of the States."[528] *Garmon* holds that the NLRA preempts state regulation, even of activities that NLRA only arguably prohibits or protects.[529] A state cannot establish standards that are inconsistent with NLRA, or provide regulatory or judicial remedies. For example a state could not debar a contractor based on NLRA violations.[530] However, this doctrine applies only to the state's role as a regulator, and not to its activities as a construction project owner.[531]

Thus, under the amendments to Sections 8(e) and (f) of the NLRA, the Court found that the use of a project labor agreement to prohibit an emploer from hiring contractors unless they agree to abide by the PLA was valid. However, the Court noted that Sections 8(e) and (f) are not specifically applicable to the states, as "state" is excluded from the definition of "employer."[532] Still, the Court considered the general goals of Sections 8(e) and (f) to be relevant in determining the intent of Congress with respect to the states.[533]

In *Minnesota Chapter of Associated Builders and Contractors v. County of St. Louis*, the court held that a PLA was not a "state law" that was preempted by ERISA.[534] Because it applied to only one project and not to all of the agency's projects generally, it was not a "state law" of general application, even though it specified particular benefits that must be paid by contractors to employees.

[522] *Id*. at 1198.

[523] *Id*. at 1197.

[524] *Id*.

[525] *Id*. at 1198.

[526] United States v. Metropolitan District Comm'n, 757 F. Supp. 121, 123 (D. Mass. 1991), *rev'd* Associated Builders and Contractors, Inc. v. Mass. Water Resources Auth., 935 F.2d 345 (1st Cir. 1991).

[527] 113 S. Ct. at 1193.

[528] *Id*. at 1194 (quoting Metropolitan Life Ins. Co. v. Mass., 471 U.S. 724, 747–48, 105 S. Ct. 2380, 85 L. Ed. 2d 728 (1985)).

[529] *Id*. at 1195 (citing San Diego Building Trades Council v. Gorman, 359 U.S. 236, 79 S. Ct. 773, 3 L. Ed. 2d 775) (1959).

[530] *Id.*

[531] *Id.* at 1196.

[532] 29 U.S.C. § 152(2).

[533] 113 S. Ct. at 1198.

[534] 825 F. Supp. 238 (D. Minn. 1993); Employee Retirement Income Security Act of 1974, 29 U.S.C. § 1144.

ii. Former Executive Order 13202.—President Obama's EO No. 13502 of 2009 (discussed above), the EO governing the use of PLAs on federal-aid projects at the time the 2012 update to this volume was being prepared, replaced two prior EOs concerning the same subject.

In June 1997, President Clinton issued a Presidential Memorandum entitled "Use of Project Labor Agreements for Federal Construction Projects." This memorandum prohibited the requirement of PLAs in direct federal contracts.[535] However, it did not prohibit their inclusion in contracts for federally assisted projects.

President George W. Bush issued EO 13202 in February 2001, which rescinded President Clinton's memorandum and extended the PLA prohibition to federally assisted projects.

EO 13202 required that "neither the awarding Government authority nor any construction manager acting on behalf of Government shall, bid specifications, project agreements, nor other controlling documents for construction contracts" that were awarded by recipients of federal funds might

> (a) Require or prohibit bidders, offerors, contractors, or subcontractors to enter into or adhere to agreements with one or more labor organizations, on the same or other related construction projects(s); or
>
> (b) Otherwise discriminate against bidders, offerors, contractors, or subcontractors for becoming or refusing to become or remain signatories or otherwise to adhere to agreements with one or more labor organizations, on the same or other related construction project(s).[536]

EO 13202 allowed an exemption for "special circumstances…in order to avert an imminent threat to public health or safety or to serve the national security."[537] However, it also provided that the possibility of a labor dispute is not such a "special circumstance."[538]

EO 13202 did not prohibit voluntary agreements between contractors or subcontractors and labor unions.[539] FHWA, under EO 13202, did not consider such an agreement to be a PLA where it was not required by the owner agency in the construction contract.[540]

EO 13202 was challenged by labor unions in *Building and Construction Trades Department, AFL-CIO v. Allbaugh*.[541] The plaintiffs challenged the president's authority to issue the EO, and contended that it was preempted by the NLRA. The district court granted the plaintiffs' request for a preliminary injunction. The D.C. Circuit reversed, holding that the President has constitutional authority to issue EOs, and that the NLRA did not preempt the EO where it applied only to federal government contracts, and was not regulatory in nature.[542]

In a 2011 ruling in *Idaho Building and Construction Trades Council, AFL-CIO, et ano., v. Wasden*, the U.S. District Court for the District of Idaho, ruling on cross motions for summary judgment, has granted two unions summary judgment and denied the Attorney General of Idaho's motion for summary judgment, holding two amendments to Idaho's Right To Work Act, the Open Access to Work Act and the Fairness in Contracting Act, to interfere with and be preempted by the NLRA.[543] The Open Access to Work Act prohibited state and municipal agencies in Idaho from entering into project labor agreements or otherwise requiring contractors to pay any specified wage scale or provide specified employee benefits except as required by federal wage laws applicable to federally-funded public works projects, and imposed state criminal penalties for any violations. The Fairness in Contracting Act prohibited certain conduct related to what unions refer to as "job targeting programs," prohibiting contractors and subcontractors from receiving any wage subsidies on behalf of its employees, prohibiting unions from paying any wages subsidies to its members in order to subsidize a contractor or subcontractor, and prohibiting any funds derived from wages and collected by unions to subsidize contractors or subcontractoras. In attempting to defend the statutes, the State Attorney General was supported by amicus briefs filed by a contractors; trade association and by the National Right to Work Legal Foundation. Discussing federal case law concerning NLRA preemption of state regulation of labor unions under *Garmon, Machinists, Boston Harbor*, and subsequent leading federal precedents, the Court found both statutes preempted by the NLRA under multiple federal precedents.

In another 2011 ruling, in *Building Industry Electrical Contractors Association et ano. v. City of New York et ano.*, the U.S. District Court for the Southern District of New York held, in the face of a challenge by contractors' trade associations, that certain PLAs entered into by New York City agencies under the provisions of a New York State statute enacted in 2008, State Labor Law Section 222, which exempted municipal projects from compliance with the requirements of New York State's Wicks Law (Section 101 of the General Municipal Law) where the municipal agencies pursuing the projects were operating under a PLA. In late 2009, the Mayor of New York City anounced that the City had entered into three major PLAs covering rehabilitation and renovation of City-owned structures, eight specified new construction projects for the City Department of Design and

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[535] *See* FHWA Contract Administration Core Curriculum Participant's Manual and Reference Guide 2001, available on FHWA's Web site at http://www.fhwa.dot.gov/programadmin/contracts/cor_V.htm, for a summary of the applicability of the memorandum and executive order to FHWA and federally assisted contracts.

[536] E.O. 13202.

[537] E.O. 13202 § 5.

[538] *Id.*

[539] *Id.*; *see also* CACC Manual, *supra* note 535.

[540] *Id.*

[541] 295 F.3d 28 (D.C. Cir. 2002).

[542] *Id*.

[543] 836 F. Supp. 2d 1146 (U.S. Dist. Ct. Idaho 2011).

Construction, and three new projects for the City Department of Sanitation. The contractors' trade associations claimed that the PLAs were preempted by the NLRA and that they violated contractors' rights under 42 U.S.C. § 1983. They also sought for the court to exercise supplemental jurisdiction over state law claims challenging the PLAs as arbitrary, capricious, and an abuse of discretion under New York State's Civil Practice Law and Rules Article 78. Following a detailed analysis, the court found the PLAs in question to represent proprietary rather than regulatory conduct by the City, and therefore held that the PLAs were not preempted by the NLRA or violative of § 1983. The court also declined to exercise supplemental jurisdiction to determine state law Article 78 claims, which it said would be more appropriately heard in state court.

d. Consistency with State Law

i. Consistency with Competitive Bidding.—The most significant question regarding the use of PLAs under state law is whether the use of a PLA is consistent with the statutes, regulations, and policies of competitive bidding. Contractors have also raised constitutional questions, such as whether the requirement of abiding by a PLA violates the contractor's right to equal protection.

The New Jersey Supreme Court considered whether the use of a PLA violated the state constitution's guarantee of equal protection in *George Harms Construction Company v. New Jersey Turnpike Authority*.[544] The contractor had alleged that the state had improperly coerced construction workers in their choice of bargaining representatives by favoring one group of unions over others. Although identifying the petitioner's constitutional claims, the court did not resolve them.

Rather, the court decided the case on the issue of whether the requirement for a PLA violated the state's statutes requiring competitive bidding of public works projects. The court compared the PLA requirement to a "sole source" specification, and questioned whether the agency could choose a sole source for labor, citing to a New Jersey statute that prohibits the use of sole sources.[545]The court found that the specification requiring the PLA had the effect of lessening competition, and was thus contrary to public bidding requirements. The specification was not "'drafted in a manner to encourage free, open and competitive bidding'" as required by New Jersey law.[546] The court thus concluded that the agency needed specific statutory authority to use a PLA to overcome the conflict with competitive bidding requirements.

Other states' courts have examined the *Harms* decision in light of their own public bidding statutes and the general policies underlying competitive bidding, and have concluded that PLAs are consistent with both. In *New York State Chapter, Inc., Associated General Contractors v. New York State Thruway Authority*, the contractors had sought a declaratory ruling that the use of a PLA on a bridge refurbishment contract was illegal, and asked for an order to halt the bidding process.[547] Following the *Harms* decision, the New York Supreme Court ruled in the contractors' favor, concluding that the "policy of using PLA's contravenes two of the purposes of [the competitive bidding statutes] in discouraging competition by deterring non-union bidders, and postering favoritism by dispensing advantages to unions and union contractors."[548] In reversing the trial court, the Appellate Division assumed that the use of a PLA discourages competition in the bidding process.[549] The court concluded, however, that this does not necessarily mean that it is inconsistent with competitive bidding. The purpose of public bidding statutes is not to have "unfettered competition," but to get the best work at the lowest price and to guard against favoritism, extravagance, fraud, and corruption. Specifications are not necessarily illegal because they might tend to favor one contractor or manufacturer over another. Rather, they may be found to be illegal when they are drawn for the benefit of one contractor or manufacturer, and not in the public interest.[550] A specification that has the impact of reducing competition must be based on a public interest, and not for the benefit of a particular contractor.

The court concluded that the agency's decision to use a PLA was rationally based on reasons that were well-grounded in the public interest. These included the need to accommodate conditions unique to the construction industry, noted by the Supreme Court in *Building and Construction Trades Council* as the short-term nature of employment in the construction industry, which makes post-hire collective bargaining difficult, and the contractor's need for a steady supply of labor and predictable costs.[551] Further, the court determined that the use of a PLA advanced the goal of obtaining the best product at the lowest price. The court concluded that the PLA was also consistent with the policy of avoiding favoritism and corruption in that it applied to union and non-union contractors alike, and prohibited discrimination against union members or non-union members in hiring.[552] The court stated that the decision should not be considered a blanket approval of all PLAs, only a holding that the state's competitive bidding statutes do not prohibit PLAs.[553]

[544] 137 N.J. 8, 644 A.2d 76 (1994).

[545] 644 A.2d at 94; N.J.S.A. 40A:11-13.

[546] *Id*. at 95; N.J.S.A. 40A:11-13.

[547] 88 N.Y.2d 56, 643 N.Y.S.2d 480, 486, 666 N.E.2d 185 (1996).

[548] *Id*.

[549] 207 A.D. 2d 26, 620 N.Y.S.2d 855, 857 (1994).

[550] *Id.* 620 N.Y.S.2d at 857.

[551] Citing Building and Construction Trades Council, 113 S. Ct. at 1198.

[552] *Id*. at 858.

[553] *Id*.

ii. Standard of Review and Necessity of Agency Record.—In a decision affirming the Appellate Division in this case, the New York Court of Appeals further stated that PLAs are neither absolutely prohibited nor absolutely permitted by competitive bidding laws.[554] Rather, the court held that the use of a PLA is by its nature anti-competitive, but will be sustained for a particular project where the record supports the agency's determination that a PLA is justified by interests that are consistent with the policies underlying competitive bidding.[555]

The Court of Appeals noted that the PLA included the typical requirements that all bidders (1) hire workers through union hiring halls; (2) follow specified dispute resolution procedures; (3) comply with union wage, benefit, seniority, and apprenticeship requirements; and (4) contribute to union benefit funds, together with the union's promise of "labor peace" throughout the life of the contract. The court then concluded that by requiring bidders to conform to a variety of union practices and limiting each bidder's autonomy in negotiating its own employment terms with a labor pool that includes non-union workers, PLAs do have an anticompetitive impact on the bidding process. As such, they are unlike the usual bid specification. However, PLAs also provide efficiencies to be gained by the public project.[556]

In examining the anticompetitive nature of the PLA specification, the court looked at *Gerzof v. Sweeney*, a New York case that examined the use of narrowly drawn specifications that limit who might bid on a project. In that case, the bid specification required experience constructing three generators of a specific type, and had the effect of eliminating all but one manufacturer.[557] While such a specification is not illegal per se, there must be a clear showing that its use is in the public interest. Based on the ruling in *Gerzof*, the court concluded that New York Competitive Bidding statutes "do not compel unfettered competition, but do demand that specifications that exclude a class of would-be bidders be both rational and essential to the public interest."[558]

The two central purposes of New York's competitive bidding statutes were pointed out as (1) protection of the public fisc by obtaining the best work at the lowest possible price, and (2) prevention of favoritism, improvidence, fraud, and corruption. If an agency uses a specification that impedes competition to bid on its work, then the use must be rationally related to these two purposes. If not, it may be found invalid.[559]

Although the practical effect of the test by the court is that a rational basis must be established by the record, the court noted that "more than a rational basis" must be shown because of the broad scope of PLAs. The court placed the burden on the agency of showing that the decision to use a PLA "had as its purpose and likely effect the advancement of the interests embodied in the competitive bidding statutes."[560] The court refused to allow agencies to approve PLAs in a "pro forma" manner.

In this particular case, the court considered the following information from the agency's record. The PLA was being used for a toll bridge refurbishment project that would take 4 years to complete, including deck replacement under traffic. The agency determined that efficiency in completing the project was important to protect a major revenue-producing facility, maximize public safety, and minimize the inconvenience to the traveling public.[561]

The agency further considered that in the history of work on this particular bridge, union contractors had performed over 90 percent of the work. Based on the size and complexity of the project, it would subject to the jurisdiction of 19 local unions, all of whom would have separate labor contracts setting out different standard hours of work and different benefits requirements. The last time that the Thruway Authority had awarded a contract to a nonunion contractor, a labor dispute had erupted that required police assistance, and the bridge was picketed.[562] The court found that the Thruway Authority had assessed the specific project needs and demonstrated on the record that a PLA was directly tied to competitive bidding goals. The PLA could not be said to promote favoritism because it applied whether a contractor was union or nonunion. The fact that nonunion contractors may be disinclined to submit bids did not amount to preclusion of competition like that identified in *Gerzof* as violative of competitive bidding laws. The agency's detailed record documented the likely cost savings, the fact that toll revenues would not be interrupted, the size and complexity of the project, and a history of labor unrest. This record was sufficient to support the court's determination that the PLA was adopted in conformity with public bidding laws.[563]

While there is a need that a record be created by an agency contemporaneously with its decision to use a PLA, that record need not be formal or extensive. In

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[554] N.Y. State Chapter, Associated General Contractors v. N.Y. State Thruway Auth., 88 N.Y.2d 56, 643 N.Y.S.2d 480, 482 666 N.E.2d 185 (1996).

[555] *Id.* 643 N.Y.S.2d at 482–83.

[556] *Id*. at 483.

[557] *Id*. at 484 (citing 16 N.Y.2d 206, 264 N.Y.S.2d 376, 211 N.E.2d 826 (1965)).

[558] *Id*.

[559] *Id.* at 485.

[560] *Id.*

[561] *Id*.

[562] *Id*.

[563] *Id*. at 486. On the contrary, the court found in a companion case involving the Dormitory Authority of the State of New York that there was no contemporaneous record to support the use of a PLA. There was no documentation of potential cost savings, nor any documented history of labor unrest. Post hoc rationalization cannot substitute for the agency's consideration of the goals of competitive bidding prior to signing the PLA. *Id.* 643 N.Y.S.2d at 487–89.

Albany Specialties, Inc. v. County of Orange, the construction manager had analyzed the potential advantages of a PLA in a letter to the agency, including the prior high use of union labor, the fact that other jobs in the area had had significant delays due to labor disruptions, and that avoiding these delays would also avoid their associated costs.[564] The court found that this met the requirements for an adequate record set out in the *New York State Ch., AGC v. Thruway Authority* case.

The Alaska Supreme Court came to a very similar conclusion on the use of PLAs in *Laborers Local # 942 v. Lampkin*.[565] The Borough of Fairbanks had required a PLA for a school renovation project, and approved a resolution to support the mayor's use of a PLA in the project. The resolution set out the rationale for the PLA, including general justifications based on other agencies' experience, benefit to the school renovation project, and economic and financial interests.[566] The school renovation project was the largest and most complex project in the borough's history, involving work on a school of over 1400 students. There was a significant interest in assuring that it was completed on time and within its budget. Failure to complete it on time would be harmful to all residents, particularly students. The court found this record sufficient to support the use of the PLA. The court adopted the rationale of the New York cases in finding that the PLA did not violate the applicable procurement code.[567]

e. Constitutional Issues

Constitutional issues have been raised with respect to PLAs based on both federal and state constitutional provisions guaranteeing equal protection. The main argument is that the requirement violates equal protection by favoring union contractors and union employees. However, courts have rejected that argument on the grounds that the PLAs considered applied equally to all, union and nonunion contractors alike. Further, they have prohibited any discrimination against union or nonunion employees on that basis or their union status.[568]

A federal district court in Missouri considered whether the PLA violated the associational rights of contractors.[569] In upholding the use of the PLA, the court found that the agency had a rational basis in its desire to have an efficient, productive, and harmonious workforce without work stoppages or delays. Applying the rational basis test, the court found that the PLA requirement did not "'directly and substantially interfere'" with the contractor's associational rights.[570]

The contractor in *Enertech Electrical v. Mahoning County Commissioners* argued that it was entitled to damages under § 1983 for the agency's refusal to award it a contract after the contractor refused to sign the PLA.[571] Enertech, the low bidder, alleged that it was deprived of its right to the award of the contract without due process. It also alleged abuse of discretion by the county and demanded its lost profits.

To support a claim for damages under § 1983, a bidder must demonstrate that it had a constitutionally protected property interest in a publicly bid contract.[572] This can be accomplished by showing either that the contract was awarded and then withdrawn, or that the agency abused its discretion in the award. Enertech argued that the county did not have discretion to condition the award of the contract on the bidder's willingness to sign the PLA. However, the court noted that the Ohio Supreme Court has held that under the language of Ohio's public bidding statute, which requires award to the "lowest and best bidder," that agencies are not limited to acceptance of the lowest dollar bid.[573] The agency therefore has the discretion to make a qualitative determination as to the lowest and best bid.

The court then concluded that the county did not abuse its discretion by determining that the "best" bidder would be one who was willing to ratify the PLA. The contract terms requiring the PLA had been included in the contract to secure labor harmony, and were not inconsistent with the competitive bidding statute's policy to provide for open and honest competition in bidding and protect the public from favoritism and fraud.[574] Because Enertech was never the lowest *and best* bidder, it could not show that it was deprived of a right to the contract without due process; it had no constitutionally protected interest in the contract.

f. Standing to Challenge a PLA

The Ohio court considered the issue of standing to challenge a PLA, and concluded that an individual contractor must have submitted a bid on that project to have standing. Further, it held that a contractor's association must have a member who submitted a bid for the association to have standing.[575]

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[564] 240 A.D. 2d 739, 662 N.Y.S.2d 773 (1997).

[565] 956 P.2d 422 (Alaska 1998).

[566] *Id.* at 427 n.2.

[567] *Id*. at 432–33.

[568] *See, e.g*., State ex rel. Associated Builders and Contractors, Central Ohio Chapter v. Jefferson County Board of Comm'rs, 106 Ohio App. 3d 176, 665 N.E.2d 723, 725–26 (1995), *review denied*, 74 Ohio St. 3d 1499, 659 N.E.2d 314 (1996); Laborers Local # 942 v. Lampkin, 956 P.2d 422, 436 (Alaska (1998)).

[569] Hanten v. School District of Riverview Gardens, 13 F. Supp. 2d 971 (E.D. Mo. 1998).

[570] *Id*. at 976.

[571] 85 F.3d 257 (6th Cir. 1996).

[572] *Id.* at 260.

[573] *Id*. at 260 (citing Cedar Bay Constr., Inc. v. City of Fremont, 50 Ohio St. 3d 19, 552 N.E.2d 202, 205 (1990)).

[574] *Id*. (citing Cedar Bay Constr., 552 N.E.2d at 204).

[575] State ex rel. Associated Builders and Contractors, Central Ohio Chapter v. Jefferson County Board of Comm'rs, *supra* note 409.

SECTION 5

CONTRACT MODIFICATIONS AND DELAY

A. THE CHANGES CLAUSE

1. Introduction

Virtually all construction contracts contain a "Changes" clause that allows the owner to modify the scope of the work, or the time of performance, without the contractor's consent, when the owner and the contractor cannot agree on the terms of the change. Under the common law, an attempt by one party to modify the contract without the consent of the other party was a breach of contract.[1] Thus, without a Changes clause, an owner could not modify the contract unless the contractor agreed to the change.

By empowering the owner to change the contract unilaterally, the clause gives an owner the flexibility it needs to administer the contract. Changes may be necessary for various reasons. A change order may be necessary to correct a design error, or deal with unanticipated site conditions that materially affect the cost of performance, or alter the time allowed for completion of the contract.

While the clause provides operating flexibility for the owner, it may also produce controversies that lead to disputes.[2] The clause is probably the most frequently litigated provision in construction contracts. The legal problems raised by the clause vary depending upon how the clause is worded and the nature of the change. The problems may vary from the enforceability of an oral directive to perform extra work, to the effect of an unprotested bilateral change as an accord and satisfaction, barring a later claim for additional compensation for changed work.

These and other related issues are discussed in this subsection. Part 2 begins this discussion with an overview of some standard clauses used by the Federal Government and some state transportation agencies. Part 3 reviews the law relating to unauthorized change orders. Part 4 discusses the requirement found in most Changes clauses that changes must be ordered in writing to be enforceable and exceptions to this requirement based on waiver and estoppel. Part 4 also discusses constructive changes. Parts 5 and 6, respectively, focus on "cardinal changes" and notice requirements. The remaining parts of this subsection deal with bilateral changes, as an accord and satisfaction, barring claims for additional compensation beyond the amount agreed to in the change order, and exceptions to the rule of an accord and satisfaction based on economic duress, mistake, and the Cardinal Change doctrine. Variations in estimated quantities in unit price contracts complete this subsection.

2. Standard Clauses

The clause has been used in Federal Government construction contracting for over 100 years.[3] While its use spans over a century, the wording of the clause has not remained static. The clause has been revised, from time to time, to reflect both the experiences gained in the administration of contracts and the views expressed by federal courts in numerous decisions. Similar revisions have taken place in standard clauses used by state transportation agencies in their construction contracts.[4]

No attempt is made, however, to trace the various changes that have taken place, over the years, in federal and state clauses. Instead, it is the intent of this subsection to compare the current federal clause[5] with representative clauses used by various state transportation agencies,[6] including the AASHTO Guide Specifications for Highway Construction.[7]

The standard changes clauses used by the Federal Government and state agencies have certain basic elements in common beyond empowering the owner to make unilateral changes to the contract. An analysis of the clauses shows that all of them identify the person who is authorized to issue change orders for the owner. Most clauses require change orders to be in writing to be binding on the owner, but some allow oral change orders and a few allow constructive change orders. All of the clauses specify, either generally or with particularity, the extent of changes that are permitted and impose limitations on the power to order changes by

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[1] Tondevoid v. Blaine School Dist., 91 Wash. 2d 632, 590 P.2d 1268, 1270–71 (Wash. 1979). The common law rule requiring mutual assent to make contractual changes applies to government contracts with private parties. Hensler v. City of L.A., 124 Cal. App. 2d 71, 268 P.2d 12, 18 (Cal. App. 1954); Clark County Constr. Co. v. State Highway Comm'n, 248 Ky. 158, 58 S.W.2d 388, 2390-91 (1933).

[2] Typically, the dispute provisions of the contract require the contractor to keep working, with the resolution of the dispute deferred until later. WALLEY & VANCE, *Legal Problems Arising From Changes, Changed Conditions and Disputes Clauses in Highway Construction Contracts*, SELECTED STUDIES IN HIGHWAY LAW, vol. 3, at 1441–42. This allows the owner to keep the project on schedule, or at least moving forward, instead of coming to a standstill if the contractor stopped working. *Id*.

[3] General Dynamics v. United States, 585 F.2d 457 (Ct. Cl. 1978).

[4] WALLEY & VANCE, *supra* note 2.

[5] 48 C.F.R. ch. 1, pt. 52.243-4, Changes (1987).

[6] AASHTO Guide Specifications 104.03 (1998); Alaska Department of Transportation and Public Facilities Standard Specification 104.1.02 (1998); Arizona Standard Specification 104.02 (2000); California Department of Transportation Standard Specification 4-1.03 (1995); Florida Department of Transportation Standard Specification 4.3.2.1 (1996); Iowa Department of Transportation Standard Specification 1109.16C.1; Michigan Department of Transportation Standard Specification 103.02.B (1996); New Jersey Department of Transportation, Standard Specification 104.02 (1996); New York Department of Transportation Standard Specification 109-05 (1995); Texas Department of Transportation Standard Specification 4.2 (1995); Washington State Department of Transportation Standard Specification 1-04.4 (1996).

[7] AASHTO Guide Specification 104.03 (1998).

requiring that they must be within the general scope of the original contract work. All allow changes to be made without the consent of the performance and payment bond surety or sureties.

All clauses require the owner to compensate the contractor for its additional costs in performing changed work and to grant time extensions when appropriate. The federal clause allows impact costs for the effect of the change upon unchanged work. Most states allow compensation when the changed work affects other work, causing such work to become significantly different in character. Parenthetically, the DSC clauses used by the states and the federally mandated clause,[8] for use in federally aided Interstate highway construction contracts, do not allow a price adjustment for the effects of a DSC on unchanged work,[9] but permit states to delete this prohibition. All clauses require the contractor to give notice of claims. Most provide for increases and decreases in quantities, where the contract quantities are based on unit prices. The key elements of the standard clauses are discussed in this subsection.

The AASHTO Guide Specifications contain sample clauses that have been adopted in whole or part by many state transportation agencies. In addition, many states have their own unique standard clauses. By way of example, the Standard Specification for CalTrans contains standard contract provisions supplemented by provisions for underutilized business enterprises (2.16.18), small business and nonsmall business subcontractors (2.16.18), and California companies (2.1.27; does not apply to federally aided projects). CalTrans also gives special attention to detailed Value Engineering (VE) proposals (4-1.07 B), contractor licensing (3-1.06), alternate dispute resolution (5.1.43 E), and time-related overhead (9.1.11).[10]

3. Authority To Order Changes

A change order must be issued by someone with actual authority to change the contract. In federal construction contracting, that person is the contracting officer. The Standard Changes Clause provides in part that, "the Contracting Officer may…make change in the work within the general scope of the contract…."[11] This is further emphasized by a federal regulation that "[o]nly Contracting Officers acting within the scope of their authority are empowered to execute modifications on behalf of the Government."[12]

In many state highway construction contracts, the person empowered to execute change orders on behalf of the agency is the "Engineer."[13] For example, the Texas Department of Transportation Standard Specification states in part that, "the Engineer reserves the right to make…such changes in quantities and such alterations in the work as are necessary to satisfactorily complete the project."[14] The Guide Specifications issued by AASHTO state in part that "[d]uring the course of the Contract, the Engineer can make written changes in quantities or make other alterations as necessary to complete the work."[15] Some other state specifications are couched in similar language.[16]

The identity of the person authorized to modify the contract is important because a government agency is not bound by the unauthorized acts of its agents. This rule is strictly enforced in public contracting.[17] It protects the government from the potential liability of employees who, without authorization, purport to alter the terms of the written contract.[18] Thus, government agencies are not bound by changes ordered by a project inspector,[19] or by a consulting engineer.[20]

The Doctrine of Apparent Authority—which allows private owners to be bound by the unauthorized acts of their representatives, who are clothed with apparent authority to act the way they did—cannot be invoked against government agencies.[21] The contractor's good faith belief concerning the authority of government agencies to make changes to the contract is irrelevant. Contractors who perform changed work that is unauthorized do so at their peril.[22]

4. Requirement That Change Orders Be in Writing

a. Waiver and Estoppel

Public construction contracts usually require that changes to the contract must be authorized in writing. A typical clause, used by state transportation agencies, authorizes the "Engineer" to make changes, "in writing"…"as are necessary to satisfactorily complete the project."[23] Some specifications may be even more explicit. For example, California's Standard Clause provides that,

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[8] This topic is discussed in Subsection B, Differing Site Conditions.

[9] 48 C.F.R. ch. 1 pt. 52.243-4(a).

[10] See Standard Specification, Caltrans, 2010.

[11] 48 C.F.R. 52.243-4(a).

[12] 48 C.F.R. pt. 43, § 43.102(a).

[13] The "Engineer" is usually defined in the Contract.

[14] Texas DOT Standard Specification 4.2 (1995).

[15] AASHTO Guide Specification for Highway Construction 104.03 (1998).

[16] For some examples, see the specifications listed in note 6.

[17] ECC Int'l Corp. v. United States, 43 Fed. Cl. 359, 367–68 (1999); United States v. Christensen, 50 F. Supp. 30, 32–33 (E.D. Ill. 1943); Noel v. Cole, 98 Wash. 2d 375, 655 P.2d 245, 249–50 (Wash. 1982); 10 MCQUILLIAN, MUNICIPAL CORPORATIONS, § 29.04 (3d ed.).

[18] County of Brevard v. Miorelli Eng'g, Inc., 703 So. 2d 1049, 1051 (Fla. 1997).

[19] Elastromeric Roofing Assocs. v. United States, 26 Fed. Cl. 1106 (1992).

[20] Dillingham Constr. N.A., Inc. v. United States, 33 Fed. Cl. 495, 503 (1995), *aff'd*, 91 F.3d 167 (1996).

[21] Johnson Drake & Piper, Inc., ASBCA 9824 and 10199, 65-2 BCA 4868 180 (1965).

[22] ECC Inter Corp v. United States, *supra* note 17.

[23] Iowa DOT Standard Specification 1109.16 C1 (2001); Texas DOT Standard Specification 4.2 (1993).

> Those changes will be set forth in a contract change order which will specify, in addition to the work to be done in connection with the change made, adjustment of contract time, if any, and the basis of compensation for that work. A contract change order will not become effective until approved by the Engineer.[24]

Generally, provisions of this kind are judicially enforced unless the owner is found to have waived the requirement that changes must be ordered in writing.[25] In *Foster Wheeler Enviresponse v. Franklin County Convention Facilities Auth.*,[26] the Ohio Supreme Court said:

> It is universally recognized that where a building or construction contract, public or private, stipulates that additional, altered, or extra work must be ordered in writing, the stipulation is valid and binding upon the parties, and no recovery can be had for such work without a written directive therefor in compliance with the terms of the contract, unless waived by the owner or employer…(citations omitted).

This rule is based on the notion that a person who has authority to change the contract may waive its provisions.[27] Acts or conduct that may constitute waiver include: (1) the owner's knowledge of the change and its acquiescence in allowing the extra work to proceed,[28] and (2) a course of dealing between the owner and the contractor disregarding the requirement that changes be in writing.[29] This waiver principle is applicable to construction contracts.[30] The Parol Evidence Rule does not bar this kind of extrinsic evidence. The rule does not apply to evidence regarding a subsequent modification of a written contract, or to the waiver of contractual terms by language or conduct.[31]

A number of jurisdictions require clear and convincing evidence to prove that the owner waived the written change order provision.[32] In *Powers v. Miller*, the court gave several reasons why an oral modification to a written contract requiring that changes be in writing must be proven by clear and convincing evidence:

> [W]e believe that the higher standard of proof is appropriate in order to avoid the type of ambiguous situation that occurred in this case, in which one party thought the contract had been modified and the other did not think a modification had occurred. We further believe that requiring proof by clear and convincing evidence is an appropriate balancing of the principles of freedom of contract against the sanctity of written contracts. That standard reduces the risk that the parties' intent as set forth in the contract will not prevail.[33]

Estoppel is another theory that is used to avoid the preclusive effect of a written change order requirement. When the owner's words or conduct constitute a waiver of the written change order requirement, the owner may be estopped from asserting that requirement as a defense to a claim for extra work.[34] The court is likely to apply estoppel as another reason why the written change order requirement does not bar an oral change order, when the owner has acted unfairly.[35] Estoppel, like waiver, must be proved with clear and convincing evidence.[36]

Some courts, for policy reasons, have refused to enforce an oral modification to a public works construction contract when the contract provides that modifications must be made in writing. In *County of Brevard v. Miorelli Engineering*, the court held, as a matter of law, that waiver and estoppel cannot be applied to the government in any dispute arising out of a contractual relationship.[37] The court said:

> MEI asserts that the County waived the written change order requirement by directing work changes without following its own formalities. We decline to hold that the doctrines of waiver and estoppel can be used to defeat the express terms of the contract. Otherwise, the requirement

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[24] California DOT Standard Specification 4-1.03 (1995).

[25] *See generally* 64 AM. JUR. 2D *Public Works and Contracts*, § 189–198 (2d ed. 1972), Annotation, *Effect of Stipulation, in Public Building or Construction Contract, That Alterations or Extras Must Be Ordered In Writing*, 1 A.L.R. 3d 1273, 1281–1282 (1965). *See also*, Sentinel Indus. Cont. v. Kimmins Indus. Service Corp. 74 So. 2d 934, 964 (Miss. 1999).

[26] 78 Ohio St. 3d, 353, 678 N.E.2d 519, 525 (Ohio 1997).

[27] Clark County Constr. Co. v. State Highway Comm'n, 248 Ky. 158, 58 S.W.2d 388, 390–91 (Ky. 1933); Hempel v. Bragg, 856 S.W.2d 393, 297 (Ark. 1993); 13 AM. JUR. 2D; *Building and Construction Contracts*, § 24 *et seq.* (1964); Gilmartin Bros. v. Kern, 916 S.W.2d 324, 329 (Mo. App. 1995); Weaver v. Acampora, 229 A.D. 2d 727, 642 N.Y.S.2d 339, 341 (N.Y. A.D. 1996); Bonacorso Constr. Corp. v. Commonwealth, 41 Mass. App. Ct. 8, 668 N.E.2d 366, 368 (Mass. App. 1996); Austin v. Barber, 227 A.D. 2d 826, 642 N.Y.S.2d 972, 974 (N.Y. A.D. 1996); Todd Shipyards Corp. v. Cunard Line Ltd., 943 F.2d 1056, 1061 (9th Cir. 1991); D.K. Meyer Corp. v. Bevco, Inc., 206, Neb. 318, 292 N.W.2d 773, 775 (1980); Morango v. Phillips, 33 Wash. 2d 351, 205 P.2d 892, 894 (1949); Annotation, 2 A.L.R. 3d 620.

[28] State v. Eastwind, Inc., 851 P.2d 1348, 1351 (Alaska 1993).

[29] Gilmarten Bros. v. Kern, 916 S.W.2d 324, 329 (Mo. App. 1995); Menard & Co. Masonary Bldg. Contractors v. Marshall Bldg. Systems, Inc., 539 A.2d 523, 526–27 (R.I. 1988).

[30] *See* 13 AM. JUR. 2D *Building and Construction Contracts* § 24 (2d ed. 2000).

[31] 29 AM. JUR. 2D *Evidence* § 1133 (2d ed. 1994).

[32] City Nat'l Bank of Fort Smith v. First Nat'l Bank and Trust, 22 Ark. App. 5, 732 S.W.2d 489, 492 (1987); Kline v. Clinton, 103 Idaho 116, 645 P.2d 350, 355 (1982); Duncan v. Cannon, 204 Ill. App. 3d 160, 561 N.E.2d 1147, 1149, 149 Ill. Dec. 451 (1990); Glass v. Bryant, 302, Ky. 236, 194 S.W.2d 390, 393 (1946); Jenson v. Olson, 144 Mont. 224, 395 P.2d 465, 469 (1964); Nicolella v. Palmer, 248 A.2d 20, 23 (Pa. 1968).

[33] 127 N.M. 496, 984 P.2d 177, 180 (1999) (citation omitted).

[34] Harrington v. McCarthy, 91 Idaho 307, 420 P.2d 790, 793 (1966); Northern Improvement Co. v. S.D. State Hwy Comm'n, 267 N.W.2d 208, 213 (S.D. 1978).

[35] W.H. Armstrong & Co. v. United States, 98 Ct. Cl. 519, 528–29 (1941); Griffith v. United States, 77 Ct. Cl. 542, 556–57 (1933); Bignold v. King County, 65 Wash. 2d 817, 54 Wash. 2d 817, 399 P.2d 611, 616 (Wash. 1965).

[36] 28 AM. JUR. 2D *Estoppel and Waiver* § 148 (2d ed. 2000).

[37] 703 So. 2d 1049 (Fla. 1997).

> of Pan Am that there first be an express written contract before there can be a waiver of sovereign immunity would be an empty one. An unscrupulous or careless government employee could alter or waive the terms of the written agreement, thereby leaving the sovereign with potentially unlimited liability.[38]

In a similar view, the court in *State Highway Commission v. Green-Boots Construction Co*.[39] said:

> The stipulation in construction contracts that compensation for extra work should be agreed upon prior to the performance of the work is not an unusual provision in this class of contracts. The reason therefore, no doubt, arises because of the frequent claims made by contractors for this so-called extra work. 'Municipal Corporations have so frequently been defrauded by exorbitant claims for extra work under contracts for public improvements that it has become usual to insert in contracts a provision that the contractor shall not be entitled to compensation for extra work unless it has been ordered in a particular manner.' Mr. Justice Clarke, in the Wells Brothers Case (citation omitted), said: 'Men who take $1,000,000 contracts for government buildings are neither unsophisticated nor careless.' We think that statement applies to this present situation. Contractors engaged in the nature of the work here performed are neither 'unsophisticated nor careless.' It would have been a simple matter for the plaintiff to have agreed in writing with the commission for this extra work prior to the performance thereof. This provision of the contract is not an unreasonable provision, and we know of no reason why it should not be given effect.…[40]

The rule requiring written authorization for changes as a condition precedent to recovery by a contractor for the cost of performing the change is designed to protect owners. This was explained by the Ohio Supreme Court in *Foster Wheeler Enviresponse, Inc. v. Franklin County Convention Facilities Auth.*:

> The primary purpose of requiring written authorization for alterations in a building or construction contract is to protect owners against unjust and exorbitant claims for compensation for extra work. It is generally regarded as one of the most effective methods of protection because such clauses limit the source and means of introducing additional work into the project at hand. It allows the owner to investigate the validity of a claim when evidence is still available and to consider early on alternative methods of construction that may prove to be more economically viable. It protects against runaway projects and is, in the final analysis, a necessary adjunct to fiscal planning.[41]

While denying recovery to the contractor, the court noted that, "under proper circumstances, the refusal of a public entity to give a contractor a written order for alterations, in accordance with a contract stipulation therefor, may constitute a breach of the contract or amount to a waiver of written orders." Moreover, "'proof of waiver, however must either be in writing, or by such clear and convincing evidence as to leave no reasonable doubt about it.'"[42]

b. Constructive Changes

A "constructive change" occurs when the clause provides that the contract may be modified by an oral order, or determination by the owner, which causes the contractor to perform work beyond contract requirements.[43] The standard clause used by the Federal Government incorporates the constructive change concept.[44] The clause provides in part that, "(b) any other written or oral order (which, as used in this paragraph (b), shall include direction, instruction, interpretation or determination) from the Contracting Officer that causes a change shall be treated as a change order under the clause…." This language, which was adopted in l968,[45] has been an express provision of the clause for more than 30 years, and has allowed contracting officers to deal administratively with disputes involving extra work under the changes clause where no formal change order had been issued.[46] This has allowed claims to be dealt with more expeditiously than resolving them through litigation.[47]

To establish a constructive change for extra work, "the contractor must show the performance of work in addition to or different from that required under the contract (the change component) either by express or implied direction of the Government or by Government fault (the order/fauth component)…."[48] The "change component" includes defective contract specifications and misinterpretation of the specifications by the Government, requiring the contractor to perform extra work.[49]

A state court has held that a constructive change occurred where the contract contained language identical to that used in part (B) of the federal clause.[50] But the

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[38] *Id*. at 1051.

[39] 199 Okla. 477, 187 P.2d 209 (Okla. 1947).

[40] *Id*. at 220 (citations omitted).

[41] 78 Ohio St. 3d 353, 678 N.E.2d 519, 527–28 (Ohio 1997) (citations omitted).

[42] *Id.* 678 N.E.2d at 528.

[43] District of Columbia v. Organization for Envtl. Growth, 700 A.2d 185, 203 (D.C. App. 1997); Miller Elevator Co. v. United States, 30 Fed. Cl. 662, 677 (1994); Global Constr. v. Mo. Highway and Trans. Comm'n, 963 S.W.2d 340, 343 (Mo. App. 1997); Youngdale & Sons Constr. Co. v. United States, 27 Fed. Cl. 516 (1993).

[44] 48 C.F.R. § 52.243-4.

[45] 32 Fed. Reg. 16269 (Nov. 29, 1967).

[46] Incorporation of the constructive change concept into the clause allows the Contracting Officer to deal with claims under the terms of the contract rather than for breach of contract.

[47] United States v. Utah Constr. & Mining Co., 384 U.S. 394, 405 (1966).

[48] Miller Elevator Co. v. United States, 30 Fed. Cl. 662, 679 (1994).

[49] *Id*. at 678.

[50] Roger J. Au & Sons, Inc. v. Northeast Ohio Regional Sewer Dist., 29 Ohio App. 3d 284, 504 N.E. 1209 (Ohio App. 1986). *See also* Julian Speer Co. v. Ohio State Univ., 83 Ohio Misc. 2d 88, 680 N.E.2d 254, 257 (Ohio Ct. Cl. 1997) (oral instruction to change specifications created a constructive change order), and R.J. Wildner Contracting Co. v. Ohio Turnpike

constructive change theory has been rejected where the contract provides only for written change orders.[51] Massachusetts reached a similar result, holding that the constructive change theory is inconsistent with an express contract requirement that changes must be ordered in writing.[52] Under this view, the written change order requirement will be enforced unless the changes clause expressly allows constructive changes or the owner, by its acts or declarations, has waived the requirement. The contractor has a greater burden of proof in establishing waiver or estoppel than in proving a constructive change.[53]

5. Changes Within the General Scope of the Contract—Cardinal Changes

The power to order changes, under a changes clause, is not unlimited. In general, a contractor is not contractually obligated, under the disputes clause, to perform a unilateral change order when the changed work results in a contract that is substantially different from the one the contractor agreed to perform when it signed the contract.[54]

Most clauses contain language limiting the power to order changes. Some clauses limit changes to those that are "within the general scope of the contract.[55] Some clauses allow changes that are "necessary to satisfactorily complete the contract,"[56] or "to satisfactorily complete the project."[57] The clause may permit the engineer to make changes "required for the proper completion or construction of the whole work contemplated."[58] Most clauses allow the owner to increase or decrease the quantity of an item in the contract or delete any item or portion of the work.[59] Some clauses specify the types of changes that the clause covers. For example, the Federal Changes clause covers changes within the general scope of the contract, including changes: "(1) in the specifications (including drawings and designs); (2) in the method or manner of performance of the work; (3) in the government-furnished facilities, equipment, materials, services or site; or (4) directing acceleration in the performance of the work."[60]

Drafting the clause too narrowly may limit the owner's authority to make changes. For example, in *General Contracting & Construction Co. v. United States*, the deletion of a building from a hospital construction contract was held to be beyond the scope of the contract, even though the value of the building that was deleted was about 10 percent of the contract price.[61] The standard changes clause that was used by the Federal Government prior to 1968 was limited to changes "in the drawings and specifications."[62] The 1968 revision to the clause[63] expanded the authority to modify the contract.[64] The criterion for determining whether the change is authorized is whether it is within the "general scope of the contract."[65] That determination is governed by the magnitude of the change and whether the change is of the type that would be within the contemplation of the parties when the contract was let.[66]

A contractor who believes that a change ordered by the Government is beyond the scope of the contract has a choice. It may perform the change and sue later for damages, or it may refuse to perform the change and sue for breach of contract.[67] The contractor cannot

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Comm'n, 913 F. Supp. 1031 (N.D. Ohio 1996) (unjust enrichment claim based on superior knowledge).

[51] Sentinel Indus. Contracting Corp. v. Kimmins Indus. Service, 743 So. 2d 954 (Miss. 1999).

[52] Bonacorso Constr. Corp v. Commonweath, 41 Mass. App. Ct. 8, 668 N.E.2d 366, 368 (Mass. App. Ct. 1996).

[53] Summerset Community Hosp. v. Allen B. Michell & Assocs., 454 Pa. Super. Ct. 188, 685 A.2d 141, 146 (Pa. Supp. 1996) (written contract for architectural services to renovate hospital modified orally, even though contract required modifications to be in writing, where clear and convincing evidence showed the hospital's intent to waive the requirement that modifications be made in writing).

[54] *See* L. K. Comstock & Co. v. Becon Constr. Co., 932 F. Supp. 906 (E.D. Ky. 1993) (extensive discussion of the "Cardinal Change" doctrine).

[55] 48 C.F.R. ch. 1, 52.243-4(a); Alaska DOT Specification 104.02.

[56] AASHTO Guide Specification 104.03; Florida DOT Specification 4.3.1.

[57] Arizona DOT Specification 104.02. (D)(1); Michigan DOT Specification 103.02; New Jersey DOT Specification 104.02; New York DOT Specification 109-05(A).

[58] California DOT Specification 4-1.03.

[59] *Id*. Most clauses allow the owner to make "such changes in quantities and such alterations in the work as are necessary to satisfactorily complete the project." *See, e.g.,* Texas DOT Specification 4.2.

[60] 48 C.F.R. ch 1, 52.243-4 (a)(1), (2), (3), (4).

[61] 84 Ct. Cl. 570 (1937).

[62] Article 3 of the contract provided that, "The Contracting Officer may at any time, by written order…make changes in the drawings and (or) specifications of this contract and within the general scope thereof…" *Id*. at p. 579.

[63] *See* note 45.

[64] 48 C.F.R. 52.243-4.

[65] *Id*.

[66] Dittmore-Freimuth Corp. v. United States, 182 Ct. Cl. 507 (1968), 290 Fed 664; ThermoCor, Inc. v. United States, 35 Fed. Cl. 480, 492 (1996); Albert Elia Building Co. v. New York State Urban Dev. Corp., 338 N.Y.S.2d 462 (App. Div. 1976); Freund v. United States, 260 U.S. 60, 68–69 (1922). Work can be deleted as a partial termination under a termination for convenience clause. Whether work is deleted under the changes clause or as a partial termination under a termination for convenience clause does not matter if the amount of the equitable adjustment would be the same in either case. J.D. Hedin Constr. Co. v. United States, 171 Ct. Cl. 70, 347 F.2d 235 (Ct. Cl. 1965). If the deletion would result in a cardinal change, the owner should delete the work as a partial termination under the termination for convenience clause. Krygoski Constr. Co. v. United States, 94 F.3d 1537, 1543 (Fed. Cir. 1996).

[67] L.K. Comstock & Co. v. Becon Constr. Co., 932 F. Supp. 906, 945 (E.D. Ky. 1992); Hensel Phelps Constr. Co. v. King County, 59 Wash. App 170, 787 P.2d 58, 65 (1990); United

hedge by seeking a declaratory judgment as to whether the change is beyond the scope of the contract.[68] Faced with these choices, and the consequences if the change is later determined not to be cardinal, most contractors will elect to perform the change and sue later for damages.

The doctrine that contractors cannot be contractually compelled to perform changes beyond the scope of the contract developed as part of federal procurement law. The rule had two purposes. First, it was designed to protect contractors from being compelled to perform work substantially different from the work the contractor agreed to perform when it signed the contract.[69] Second, the rule prevented government agencies "from circumventing the competitive procurement process by adopting drastic modifications beyond the original scope of a contract."[70] The doctrine developed at the state level for similar reasons,[71] and has been referred to in various ways: "fundamental changes,"[72] radical changes,"[73] and "abandonment."[74] The Cardinal Change doctrine, however, has not been universally accepted.[75]

The Cardinal Change doctrine is fact-dependent.[76] "No rule of thumb exists to measure what constitutes a cardinal change."[77] Each case must be analyzed on its facts, considering the magnitude or quantity of the change and its affect upon the project as a whole.[78] At the end of the day, the basic question is whether the contractor has been ordered to perform changes that are substantially different from what the contractor agreed to do when it accepted the contract.[79] For example, adding a tunnel by change order to connect a building that the contractor was constructing to an adjacent site owned by the developer was a cardinal change, because the change was not the same type of work the contractor agreed to perform when the contract was awarded.[80] In transportation contract law, the Cardinal Change doctrine has not gained universal acceptance in many states. In states such as New York, it is now less important due to the widespread implementation of the federally mandated changed-condition provisions. These authorize administrative contract adjustments for significant changes in the character of the work, quantity variations, and different site conditions.

A change that causes a substantial increase in the cost of the work by making it more difficult to perform may constitute a cardinal change.[81] However, a substantial increase in the cost of the contract, standing alone, does not constitute a cardinal change where the change "entails the same nature of work as contemplated under the original contract (albeit of a different scope)."[82] Similar reasoning applies to the number of changes made by the owner. A changes clause does not limit the number of changes that the owner can order. Changes only become cardinal when they exceed the reasonable number of changes that should be expected

States v. Spearin, 248 U.S. 132, 138, 39 S. Ct. 59, 63 L. Ed. 166 (1918).

[68] Valley View Enters., Inc. v. United States, 35 Fed. Cl. 378, 383–84 (1996).

[69] General Dynamics Corp. v. United States, 585 F.2d 457 (Ct. Cl. 1978); ThermoCor Inc. v. United States, 35 Fed. Cl. 480 (1996); Wunderlich Contracting Co.v. United States, 173 Ct. Cl 80, 351 F.2d 956 (1965); L.K. Comstock & Co. v. Becon Constr. Co., 932 F. Supp. 906 (E.D. Ky. 1993).

[70] Cray Research, Inc. v. Department of Navy, 556 F. Supp. 201, 203 (D.D.C. 1982), *quoted with approval in* Miller Elevator Co. v. United States, 30 Fed. Cl. 662, 677 (1994).

[71] Albert Elia Building Co. v. N.Y. State Urban Dev. Corp., 388 N.Y.S.2d 462, 468 (App. Div. 1976); C. Norman Peterson Co. v. Container Corp. of America, 172 Cal. App 3d 628, 218 Cal. Rptr. 592 (Cal. App. 1985); Blum v. City of Hillsboro, 183 N.W.2d 47, 50 (Wis. 1971); State Highway Comm'n v. J.H. Beckman Constr. Co., 84 S.D. 337, 171 N.W.2d 504, 506 (S.D. 1969). *See* Annotation, *Statute Requiring Competitive Bidding for Public Contract as Affecting Validity of Agreement Subsequent to Award of Contract to Allow the Contractor Additional Compensation for Extras or Additional Labor and Material Not Included in the Written Contract*. 135 A.L.R. 1265. The Alaska DOT Standard Specification (104-1.02) provides that, "Changes that are determined to be outside the general scope of the original Contract will be authorized only by Supplemental Agreement."

[72] Hensel Phelps Constr. Co. v. King County, 57 Wash. App. 170, 787 P.2d 58 (1990).

[73] McHugh v. Tacoma, 76 Wash. 127, 135 Pac. 1011, 1015 (1913).

[74] C. Norman Peterson Co. v. Container Corp. of America, 172 Cal. App. 3d 628, 218 Cal. Rptr. 592, 598 (Cal. App. 1985) (changes so numerous that they constituted an abandonment of the contract).

[75] Claude DuBois Excavation v. Town of Kittery, 634 A.2d 1299, 1301–02 (Me. 1993); Jackson v. Sam Finley, Inc., 366 F.2d 148, 155 (5th Cir. 1966).

[76] Air-A-Plane Corp v. United States, 187 Ct. Cl. 269, 408 F.2d 1030, 1033 (Ct. Cl. 1969).

[77] Miller Elevator Co. v. United States, 30 Fed. Cl. 662, 677 (1994).

[78] L.K. Comstock & Co. v. Becon Constr. Co., 932 F. Supp. 906, 909 (E.D. Ky. 1992).

[79] Alliant Techsystems, Inc. v. United States, 178 F.3d 1260, 1276 (Fed. Cir. 1999).

[80] Albert Elia Building Co. v. N.Y. State Urban Dev. Corp., 54 A.D. 2d 337, 388 N.Y.S.2d 462, 467 (App. Div. 1976).

[81] Merrill Eng'g Co. v. United States, 47 F.2d 932, 933–34 (S.D. Miss. 1931) (change in design of a brick pavement on a bridge reduced bricklaying production from 1000 square yards per day to 200 square yards per day and increased the amount of asphalt needed by 66 percent); Luria Bros. & Co. v. United States., 177 Ct. C. 676, 369 F.2d 701, 707–08 (Ct. Cl. 1966) (change lowered depth of footings for columns from 9 feet to 19 feet).

[82] Miller Elevator Co. v. United States, 30 Fed. Cl. 662, 677 (1994) (an adjustment of $75,615.21 contract to $212,900.00 contract not a cardinal change); General Dynamics Corp. v. United States, 218 Ct. Cl. 40, 585 F.2d 457 (Ct. Cl. 1978) (An increase of $100 million in a $60 million contract not a cardinal change); Peter Kiewit Sons Co. v. Summit Constr. Co., 422 F.2d 242, 255 (8th Cir. 1969) (a treble rise in the cost of the contract was beyond the scope of the contract).

for the type of work specified in the contract. This can be proven through expert testimony. For example, an expert can testify as to the usual and customary number of changes as a percentage of the contract price.[83]

A change outside the scope of the contract is not governed by the changes clause.[84] Whether the change is an "in-scope" change that the contractor is contractually obligated to perform or an "out-of-scope" breach depends upon whether the change is reasonable and necessary to complete the work specified in the original contract. While it may be difficult, at times, to define the boundaries of an allowable change—since each case depends upon its own set of facts—there are, however, some guidelines. Is the work, as changed, essentially the same work called for in the original contract? Are the total number of changes reasonable for the type of work specified in the contract? And finally, are the changes normally associated with the type of work called for in the contract?

If the change is reasonable, and necessary to complete the contract, and does not have an unreasonable impact on the contractor, the change should be within the general scope of the contract. If the change does not meet this test, it is a breach of contract, giving the contractor a choice: perform the change and sue later for damages, or stop work and sue for damages. Most cases involve the former situation rather than the latter because of the consequences that the contractor may face if the change is found by a court to be an allowable change under the change clause.[85]

The STURAA of 1987 required FHWA to develop standardized changed-condition clauses that were to be included in all federal aid construction projects. The adoption of these provisions was thought to result in reduced contractor bids and provide for new contract adjustment provisions. The standardized changed-conditions clauses statutorily required by 23 U.S.C. 112(e), and implemented by FHWA regulations, 23 C.F.R. 635.109, must be included verbatim in all contracts unless prohibited by state statutes. An alternate clause that conforms to state statutes must be approved for inclusion by the FHWA Adminstrator. With the implementation of the federal changed-condition clauses, which began in 1987, transportation contracts now contain three federally mandated provisions that provide for contract adjustments for significant changes in the character of work, suspension of work, and different site conditions.

The significant change clause provides two definition of significant change. Firstly, instances where the character of the work is changed or altered and differs materially from that of the original; and secondly, where a major item of work, as defined in the contract, is increased or decreased by more than 25% of the original contract bid quantity. Either party may initiate the adjustment. The clause provides for adjustment in time and additional cost, and is is wide use by state transportation agenicies across the nation.

6. Notice and Recordkeeping Requirements

"A typical clause requires the contractor to give the owner written notice when it believes that it is performing extra work. The clause specifies that notice must be given within a specified number of days from the event that gave rise to the claim."

The Federal Changes clause[86] requires written notice of any oral order, as defined in the clause, which the contractor regards as a change order.

> If any change under this clause causes an increase or decrease in the Contractor's cost of, or the time required for, the performance of any part of the work under this contract, whether or not changed by any such order, the Contracting Officer shall make an equitable adjustment and modify the contract in writing. However, except for an adjustment based on defective specifications, no adjustment for any change under paragraph (b) of this clause shall be made for any costs incurred more than 20 days before the Contractor gives written notice as required. In the case of defective specifications for which the Government is responsible, the equitable adjustment shall include any increased cost reasonably incurred by the Contractor in attempting to comply with the defective specifications.[87]

The Contractor must assert its right to an adjustment under this clause within 30 days after (1) receipt of a written change order under paragraph (a) of this clause or (2) the furnishing of a written notice under paragraph (b) of this clause, by submitting to the Contracting Officer a written statement describing the general nature and amount of proposal, unless this period is extended by the Government. The statement of proposal for adjustment may be included in the notice under paragraph (b) above.[88]

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[83] In a case involving a building construction contract for the State of Washington, the architect testified that it was normal to expect changes of about 5 percent of the contract price for that type of construction. The contractor's claim for quantum meruit was based on what it considered to be an excessive number of changes. The trial court disregarded the number of changes and looked to the dollar value of the changes. The court found that the dollar value of the changes was not excessive and not a cardinal change and dismissed the quantum meruit claim. However, where there are numerous changes due to poor design, the changes may be cardinal. *See, e.g.*, Slattery Contracting Co. v. New York, 288 N.Y.S.2d 126, 129 (N.Y. Ct. Cl. 1968); Housing Auth. of Texarkana v. E.W. Johnson Constr. Co., 264 Ark 523, 573 S.W.2d 316 (Ark. 1978); General Contracting and Constr. Co. v. United States, 84 Ct. Cl. 570, 580 (1937).

[84] Miller Elevator Co. v. United States, 30 Fed. Cl. 662, 677 (Ct. Cl. 1994).

[85] Under the "dispute" provisions of the contract, a contractor is contractually obligated to perform a unilateral change order that is within the scope of the contract. Refusal to perform such a change is a material breach of contract by the contractor, establishing grounds for a default termination. Discount Co. v. United States, 213 Ct. Cl. 567, 554 F.2d 435, 440 (Ct. Cl. 1977).

[86] *See, e.g.*, 48 C.F.R. § 52.243-4 (1987).

[87] *Id.* at § 52.243-4(d).

[88] *Id.* at § 52.243-4(e).

Some Changes clauses require the contractor to give notice, before it begins work, that it regards it as a change.[89] Other clauses require notice, within a specified time, after the contractor believes that any work ordered by the owner is extra work and not original contract work. An example is a specification used by the New Jersey Department of Transportation, which requires that "the contractor shall promptly notify the Engineer in writing, on forms provided by the Department, within five days from the date that the Contractor identifies any actions or state conduct including, inactions, and written or oral communications, which the Contractor regards as a change to the Contract terms and conditions."[90]

Some contractors have stamps that they use to protest unilateral change orders. The stamp is worded to allow the contractor to reserve its increased costs for performing unchanged work, as well as any additional time needed for performing the changed work. Reservation of the right to assert a claim is usually based on the contention that the contractor is unable to determine, in advance of performing the work, the extra costs and time that may result from the change. When faced with a reservation or notice of a claim, an owner may wish to determine whether the change is really necessary in order to perform the original contract work. In some instances, the owner could withdraw the change order, avoid a dispute, and add the work to a future contract or perform the work with its own employees after the contract is completed.

The notice requirement serves several purposes. Notice enables the owner to investigate the claim while the facts are still fresh to determine its validity. Notice allows the owner to keep records of the costs of an operation that the contractor asserts is extra work. Notice allows the owner to take remedial action to mitigate damages, or take other steps that are in the owner's best interests. Notice also protects the owner from claims for changes that the owner never ordered.[91] The public policy considerations that underlie notice requirements in public works contracts were recently articulated by the New York Court of Appeals:[92]

> Strong public policy considerations favor scrutiny of claims of bad faith when offered by contractors to excuse noncompliance with notice and reporting requirements in public contracts. These provisions, common in public works projects, provide public agencies with timely notice of deviations from budgeted expenditures or of any supposed malfeasance, and allow them to take early steps to avoid extra or unnecessary expense, make any necessary adjustments, mitigate damages and avoid the waste of public funds. Such provisions are important both to the public fisc and to the integrity of the bidding process. Respondent's accumulation of $1,000,000 in undocumented damages—a full 20% over the combined contract price—is precisely the situation that the cited provisions are intended to prevent.[93]

Generally, notice requirements are strictly enforced.[94] However, as with most general rules, there are exceptions. Written notice may be waived if the owner had actual knowledge that extra work was being performed.[95] Also a consideration of the claim, on its merits, may waive lack of timely notice as a defense.[96] And some courts follow the rule that strict compliance with notice requirements will not bar a claim if the court finds that the owner is not prejudiced by lack of notice. Under federal case law, lack of notice will not bar the claim unless the government can show that it was prejudiced, or put at a disadvantage due to the contractor's failure to provide notice.[97] In other jurisdictions, lack of prejudice will not prevent notice requirements from being enforced.[98]

The question of notice often turns on whether the information provided is sufficient to inform the owner that the contractor has a problem for which it intends to hold the owner responsible.[99] The form of the notice

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[89] *See, e.g.*, Connecticut DOT Standard Specification § 1.04-04(3) (2000); Oregon DOT Standard Specification § 00140.40 (2002).

[90] New Jersey Standard Specifications 104.09 (1996).

[91] 3 JOHN C. VANCE, *Enforceability of the Requirement of Notice in Highway Construction Contracts*, SELECTED STUDIES IN HIGHWAY LAW 1542-N2, *et seq*.; Clark-Fitzpatrick, Inc./Franki Foundation Co. v. Gill, 652 A.2d 440, 447 (R.I. 1994); Plumley v. United States, 226 U.S. 545, 548, 33 S. Ct. 139, 57 L. Ed. 342 (1913).

[92] A.H.A. General Constr., Inc. v. N.Y. Housing Auth., 92 N.Y.2d 20, 699 N.E.2d 368, 677 N.Y.S.2d 9 (N.Y. 1998).

[93] *Id*. at 376.

[94] *Supra* note 92; Risser & McMurry Co. v. Sheridan Area Water Supply Joint Powers Bd., 929 P.2d 1228, 1232–33 (Wyo. 1996); Sime Constr. Co. v. Wash. Pub. Power Supply Systems., 28 Wash. App. 10, 621 P.2d 1299, 1302–03 (1980); Allen-Howe Specialties Corp. v. United States Constr., Inc., 611 P.2d 705, 707–08 (Utah 1980).

[95] Harrington v. McCarthy, 91 Idaho 307, 420 P.2d 790 (1966); Frederick Snare Corp. v. Maine-New Hampshire Interstate Bridge Auth., 41 F. Supp. 638, 645 (D. N.H. 1941) (failure to give written notice did not bar claim—owner was reasonably conversant with all the facts that written notice would have provided); Hoel-Steffen Constr. Co. v. United States, 456 F.2d 760, 766 (Ct. Cl. 1972) (actual notice of claim satisfies notice requirement).

[96] Dittmore-Freimuth Corp. v. United States, 390 F.2d 664, 667 (Ct. Cl. 1968) (owner should obtain agreement from the contractor that consideration of the claim in settlement negotiations will not waive the defense of lack of timely notice in litigation if the claim is not settled).

[97] Fru-Con Constr. Corp. v. United States, 43 Fed. Cl. 306, 328–29 (Fed. Cl. 1999); Eggers & Higgins & Edwin A. Keeble Assocs., Inc. v. United States, 185 Ct. Cl. 765, 403 F.2d 225, 233 (Ct. Cl. 1968) (prejudiced established—claim barred).

[98] *Supra* note 91, at 368, 374. 677 N.Y.S.2d. 9 (N.Y. 1998); Absher Constr. Co. v. Kent School Dist., 77 Wash. App. 137, 890 P.2d 1071, 1096 (Wash. App. 1995).

[99] State Highway Dep't v. Hall Paving Co., 127 Ga. App. 625, 194 S.E.2d 493, 496 (1972); Department of Transp. v. Fru-Con Constr. Corp., 206 Ga. App. 821, 426 S.E.2d 905, 908 (Ga. App. 1992) (knowledge that grading work was behind schedule did not waive the agency's right to notice that the contractor would seek a time extension).

is not important if the notice alerts the owner to the problem and gives the owner an opportunity to investigate and take steps to protect itself.[100] The case law dealing with notice requirements has established the following propositions: First, contract provisions that require written notice of intention to make a claim for extra work before starting work are enforceable, absent circumstances constituting waiver, and in a few jurisdictions, lack of prejudice to the owner. Second, in those jurisdictions where waiver has been applied to avoid the defense of lack of notice, certain facts have been identified as being significant. These facts include: extra work orally ordered by the owner,[101] or a course of conduct and dealing between the parties establishing a continuing disregard for the provision relating to notice,[102] or remaining silent, knowing that the contractor is performing extra work.[103]

In general, most courts are disinclined to allow an owner to avoid payment for extra work because the contractor failed to provide written notice when the owner had actual knowledge that extra work was being performed and did nothing to stop it. Some jurisdictions, however, require strict compliance with notice provisions when public contracts are involved.[104]

For example, in *Perini Corp. v. City of New York*, the City's construction contract was funded by the EPA and contained the Federal Changes clause required by EPA regulations.[105] The contractor's claim for extra work was denied by the City because of the contractor's failure to give written notice that it was performing what it considered to be extra work. The contract required such notice before the contractor could begin work.

The question before the court was whether state law or federal law applied in determining what type of notice was sufficient. Under federal law construing notice provisions, lack of notice will bar the claim only if the Government can show prejudice. Under state law, strict compliance with notice requirements was a condition precedent to payment for extra work. The court held that New York law applied, and that the contractor's failure to provide notice as required by the contract barred its claim.[106]

Section 104-04 of the NYSDOT Standard Specifications eliminates the lack of prejudice argument and provides:

> Failure of the Contractor to provide such written notice in a timely fashion will be grounds for denial of the dispute and the Department does not have to show prejudice to its interest before such denial is made. In the event the Contractor fails to provide written notice within the time limit established, and or in the event the Contractor fails to maintain and sumbmit such specified records, the dispute for compensation shall be deemed waived, *notwithstanding the fact that the Department may have actual notice of the facts and circumstances which comprise such dispute and is not prejudiced by said failure.*

The courts in New York have enforced this provision.

Similar provisions are contained in Washington DOT Standard Specifications 104.5. In Washington State, the court in *Mike Johnson, Inc. v. City of Spokane*[107] strictly enforced the contract notice provision even though the owner had actual knowledge of the claim.

a. Notice for Significant Change in Character of Work

Special attention should be focused on the notice provisions for significant changes in the character of the work. As set forth above, a significant change can be a change in character of work or a quantity variation of 25 percent increase or decrease. The AASHTO Guide Specifications recommend that " Before performing significantly changed work, reach agreement with the Agency concerning the basis for the adjustment…."[108] Either party wishing to make a contract adjustment should not wait until the end of construction, but provide prompt notice and request a price and/or time of performance adjustment as soon as it becomes aware of the significant change in the character of the work.

NYSDOT addresses this situation, and provides that either party must provide notice of the existence of an apparent significant change to the character of the work if that party wishes to adjust the contract prices or time of performance. Such notice shall be given within 10 work days of the time at *which the party had knowledge or should have had knowledge of an event,* matter, or occasion which results in a significant change in the character of the work. Section 104-4 provides "the Department will have no liability and no adjustment will be made for any damages which accrued more than 10 work days prior to such filing of such a notice with the Engineer."

A typical Changes clause does not require the owner to obtain the consent of the payment and performance bond surety. Without language of this kind, the owner may discharge the surety's obligations under its bonds for changes made without the surety's approval.[109]

Most clauses do not require the owner to give the surety notice of the change. For example, the clause may provide that, "Such changes in quantities and al-

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[100] Gilmarten Bros. v. Kern, 916 S.W.2d 324, 329 (Mo. App. 1995).

[101] Reif v. Smith, 319 N.W.2d 815, 817 (S.D. 1982).

[102] *Supra* note 100*;* DeNiro v. Gasvoda, 1999 Mont. 129, 982 P.2d 1002, 1004 (1999).

[103] Zook Bros. Constr. Co. v. State, 171 Mont. 64, 556 P.2d 911, 915 (Mont. 1976).

[104] D. Federico Co. v. Commonwealth, 11 Mass. 248, 252, 415 N.E.2d 855, 857–58 (1981) *See, e.g.*, cases cited in note 98.

[105] 18 F. Supp. 2d 287 (S.D. N.Y. 1998), *aff'd without published opinion*, 182 F.3d 901 (2d Cir. 1999), *cert. denied*, 120 S. Ct. 615 (1999).

[106] 18 F. Supp. 2d at 295.

[107] 150 Wash. 2d 375, 391, 78 P.3d 161, 169 (Wash. 2009).

[108] AASHTO Guide Specifications, at 18.

[109] Gritz Harvestore, Inc. v. A.O. Smith Harvestore Products, Inc., 769 F.2d 1225, 1230 (7th Cir. 1985) (material alteration without consent of guarantor discharges guarantor); National Sur. Corp. v. United States, 118 F.3d 1542, 1546 (Fed. Cir. 1997).

terations do not invalidate the contract nor release the contract surety…."[110] However, a clause may require the contractor to obtain surety consent for substantial changes.[111] The standard form performance bond used by some agencies incorporates by reference all of the provisions of the construction contract. The surety, by signing the bond, agrees to the waiver provisions in the Changes clause or the limitations on notice as provided in the construction contract.

7. Effect of Changes on Other Work

The Federal Changes clause allows the contractor to recover, as part of an equitable adjustment, the contractor's increased costs of performing unchanged work.[112] This was not necessarily so prior to 1968 because of the so-called *Rice* doctrine.[113] Under this doctrine, the contractor could recover for performing the change, but not for the effect that the change had on unchanged work. The increased cost of performing unchanged work caused by the change was held to be "consequential."[114] In 1968, the *Rice* doctrine was eliminated from federal construction law when the Changes clause was revised.[115] Today, at the federal level, changes that affect unchanged work are compensable. This has been true for over 30 years.

In general, the same is true at the state level. The clause used by the NYSDOT provides in part that,

> if the alterations or changes in quantities significantly change the character under the contract whether such alterations or changes are in themselves significant changes to character of the work, or by affecting other work, cause such other work to become significantly different in character, an adjustment excluding anticipated profit, will be made to the contract.[116]

The Florida[117] and Texas[118] specifications provide that, "if the alterations or changes in quantities significantly change the character of the work under the contract, whether or not changed by any such different quantities or alterations, an adjustment, excluding loss of anticipated profits, will be made to the contract." The standard specifications used by Arizona,[119] Michigan,[120] and Iowa[121] have similar language. They provide that, "If the alterations or changes in quantities significantly change the character of the work under the contract, whether such alterations or changes are in themselves significant changes to the character of the work, or by affecting other work, cause such other work to become significantly different in character, an adjustment excluding anticipated profit, will be made to the contract." The Changes clause mandated by 23 U.S.C. § 112 contains similar provisions.[122]

8. Variations in Estimated Quantities

Highway construction contracts based on fixed unit prices for estimated quantities typically contain a variation in estimated quantities (VEQ) clause. The VEQ clause used in federal contracts is based upon variations in estimated quantities that exceed 115 percent, or are less than 85 percent of the estimated plan quantities.[123] The VEQ clauses typically used in state transportation contracts provide for a price adjustment from the contract unit price when the actual quantity used exceeds or is less than 25 percent of the estimated contract quantity.[124] The federally mandated Changes clause also uses 25 percent.[125]

The VEQ clause has several purposes: First, it affords protection to the contractor by providing a remedy for excessive overruns or underruns from estimated contract quantities.[126] Second, it affords protection to

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[110] AASHTO Guide Specifications § 104.03, Texas DOT Specification 4.2. The Alaska DOT Changes Clause (104-1.02) allows changes to be made, "without notice to the sureties and within the general scope of the contract."

[111] Surety consent required for changes that increase the total cost of the project by more than 25 percent. WSDOT Standard Specification, 1-04.4.

[112] 48 C.F.R. ch. 1 § 52.243-2(b).

[113] United States v. Rice, 317 U.S. 61 (1942).

[114] *Id.*

[115] The elimination of the Rice doctrine was accomplished by adding the phrases "any part of the work" and "whether or not changed" to the clause. Appendix to 32 Fed. Reg. 16269 (Nov. 29, 1967).

[116] Standard Specification 109-16A(3)(ii).

[117] Standard Specification 4.3.2.1.

[118] Standard Specification 4.2.

[119] Standard Specification 104.02(D)(2).

[120] Standard Specification 103.02 B.

[121] Standard Specification 1109.16 C2.

[122] 23 C.F.R. § 635.109(a)(3)(ii), "Significant Changes in the Character of the Work" provides:

> If the alterations or changes in quantities significantly change the character of the work under the contract, whether such alterations or changes are in themselves significant changes to the character or work or affecting other work cause such work to become significant different in character an adjustment, excluding loss of anticipated profits, will be made to the contract.

[123] 48 C.F.R. § 52.211-18.

[124] Arizona DOT Standard Specification (104.2(D)(4)). California DOT Standard Specifications 4-1.03B(1) (1995), (Increases); 4-1.03 B(2) (1995), (Decreases). Michigan DOT Standard Specification 103.02B2 (1996), Florida DOT Standard Specification 4.3.2.1 (B). Texas DOT Standard Specification 4.2 (b).

[125] 23 C.F.R. § 635.109(a)(3)(iv)(B). A "significant change" includes:

> When a major item of work, as defined elsewhere in the contract, is increased in excess of 125 percent or decreased below 75 percent of the original contract quantity. Any allowance for an increase in quantity shall apply only to that portion in excess of 125 percent of original contract item quantity, or in case of a decrease below 75 percent, to the actual amount of work performed.

This clause and the other clauses mandated by 23 C.F.R. 635, *et. seq*., do not apply to federally-aided state transportation projects if a state has a similar clause, or if state law prohibits their use. 23 U.S.C. § 112.

[126] "The object is to retain a fair price for the contract as a whole in the face of unexpectedly large variations from the

the owner from claims when the quantities vary from estimated contract quantities within a specified percentage.[127] The clause may also entitle the owner to a downward adjustment in the unit contract price when the contractor's actual cost is reduced by an overrun in excess of the specified percentage.[128] An overrun of less than 125 percent or an underrun of less than 75 percent in the case of the state clauses is a risk that the contractor assumes. Agencies, however, are required to use reasonable care in preparing estimated quantities. Where information is available to quantify the estimate with more precision and the owner neglects to use that information, the 25 percent variance may not limit recovery.[129]

The adjustment in the unit contract price for overruns or underruns that exceed or differ from the estimated contract quantities is determined by the language of the VEQ clause and the contractor's costs for performing that item of work. In the case of overruns, the adjustment is based on the actual unit cost for performance of the item minus the unit contract price for 115 percent (Federal VEQ) or 125 percent (state VEQ) of the estimated plan quantity. Where the variation is less than 85 percent (Federal VEQ) or 75 percent (state VEQ) of the original bid quantity, the adjustment is based on any increase in costs due solely to the variation.[130]

The VEQ clause applies only to errors in estimated quantities. In this sense, it supplements the Changes clause by allowing the overrun or underrun to differ from the original quantity estimate up to or less than the specified percentage, without any adjustment in the contract price, when the overrun or underrun is due to an estimating error, and not a change ordered by the owner or some other cause.[131] When the variation in quantity is due to a change ordered by the owner, the Changes clause applies and any increase in the cost of performance resulting from the change is governed by that clause.[132]

Standard VEQ clauses should contain clear notice provisions. These can promote early dispute resolution and afford all parties the ability to mitigate future damages.

9. Accord and Satisfaction

An accord and satisfaction is a means of discharging an existing right.[133] In a change order setting, an accord occurs when the owner and the contractor agree upon the terms of a contract modification and express those terms in a bilateral change order. The satisfaction occurs when the contractor performs the change and is paid for it by the owner.[134] A typical change order provision provides that a change order that is not protested by the contractor is full payment and final settlement of all claims for time, and for costs of any kind, including delays related to any work either covered or affected by the change, and constitutes a waiver of any future claims arising out of the change order.[135]

An accord and satisfaction will bar any claim arising within the scope of the accord.[136] There are, however, exceptions to this rule. One frequently litigated exception is whether the contractor and the owner reached an accord. In *Safeco Credit v. United States*, the court said: "As in many contract cases where accord and satisfaction is the government's asserted defense, 'this case requires the court to rule on whether there was a meeting of the plaintiff's and the Government's minds. Without agreement the parties did not reach an accord…'"[137] (citations omitted).

In a construction dispute in Vermont, the State transportation agency processed a change order for extra costs occasioned by past delays on the contract. The change order provided for release of all claims up to the date of execution. The contractor asserted a claim that included the release time periods established in the change order. Vermont successfully maintained that there was accord and satisfaction which released all claims as of a certain date, and was able to arrive at a favorable settlement.

This determination is a question of law that requires the court to determine whether the parties intended the change order to be an accord.[138] In making this determination, the court will not consider parol evidence of prior negotiations to create a genuine issue of material fact when such evidence would vary or contradict the plain and unambiguous language of the change order.[139]

Another theory that a contractor may advance to avoid the preclusive effect of a bilateral change order is economic duress. To establish economic duress, the contractor must prove that the contractor's assent was in-

estimated quantities on which bids are based." Bean Dredging Corp., 89-3 ENGBCA 22,034 (1989) ¶ 110, 816 at 110,824 (concurring opinion).

[127] Burnett Constr. Co. v. United States, 26 Ct. Cl. 296, 302 (1992); Farub Found. Corp. v. City of N.Y., 183 Misc. 636, 49 N.Y.S.2d 922, 923 (N.Y. Sup. Ct. 1944).

[128] Foley Co. v. United States, 11 F.3d 1032 (Fed. Cir. 1993).

[129] Travis T. Womack, Jr. v. United States, 182 Ct. Cl. 399, 389 F.2d 793 (Ct. Cl. 1968).

[130] Burnett Constr. Co. v. United States, 26 Ct. Cl. 296, 302 *et. seq*. (1992); Foley v. United States, *supra* note 128.

[131] Reliance Ins. Co. v. United States, 931 F.2d 863, 866 (Fed. Cir. 1991).

[132] ThermoCur v. United States, 35 Fed. Cl. 480, 486 (1996).

[133] 6 CORBIN, CORBIN ON CONTRACTS, § 1276 (rev. ed. 1993).

[134] Brock & Blevins Co. v. United States, 170 Ct. Cl. 52, 343 F.2d 951, 955 (Ct. Cl. 1965); C. & H. Commercial Contractors, Inc. v. United States, 35 Fed. Cl. 246, 252 (1996).

[135] *See* Safeco Credit v. United States, 44 Fed. Cl. 406, 419–20 (Fed. Cl. 1999), for examples of this type of clause.

[136] Transpower Contractors v. Grand River Dam Auth., 905 F.2d 1413, 1419 (10th Cir. 1990).

[137] Safeco Credit v. United States, *supra* note 132, at 419.

[138] McLain Plumbing & Elec. Serv., Inc. v. United States, 30 Fed. Cl. 70, 78 (Fed. Cl. 1993).

[139] Safeco Credit v. United States, *supra* note 135, at 420-21.

duced by an improper threat that left the contractor with no reasonable alternative, other than to sign the change order without protest.[140] Economic pressure, and even the threat of considerable financial loss, do not constitute duress. The act must be coercive and violate notions of fair dealing.[141] For instance, when the owner induces the contractor to sign because of an improper threat, the change order is voidable.[142]

Because a change order induced by duress is voidable and not void, the contractor must act promptly to repudiate the change order or be deemed as having waived the right to do so.[143] A contractor may also be deemed as having ratified a change order executed under duress when the contractor accepts payment for the change, and then remains silent for a period of time after the contractor has had an opportunity to repudiate the change order.[144]

Another theory for avoiding the preclusive effect of an unprotested change order is the Cardinal Change doctrine. This exception is based on the premise that a contractor should not be bound by a change order as an accord and satisfaction when the contractor was unable to assess the cumulative effect of the change order on the overall performance of the contract,[145] or determine how the changes would ultimately impact the work.[146] The Cardinal Change doctrine will not apply, however, where the contractor clearly waives future claims. For example, in *In re Boston Shipyard Corp*.,[147] the contractor signed a change order settling all of its claims for delay and disruption. The contractor later attempted to avoid the change order by claiming that the changes were so extensive that they amounted to a cardinal change. The court found that the change order barred the contractor's claim for quantum meruit. The court observed that the change order clearly served as a release of claims, and once the contractor accepted payment, the parties had reached an accord and satisfaction on all possible claims, including those for delay and disruption. The court also noted that the contractor's assertion that it did not intend to waive its claim when it signed the change order was insufficient to raise a genuine issue of material fact so as to preclude summary judgment for the Government.

A claim cannot be reserved on the basis of the contractor's subjective intent.[148] To avoid the preclusive effect of a bilateral change order, the contractor must show that the mistake was mutual, not unilateral, and that the change order did not reflect what the contractor and the owner intended.[149] The Parol Evidence rule prevents the contractor from creating a contractual ambiguity based on its intentions.[150]

10. Value Engineering

State transportation contracts often contain provisions that encourage contractors to submit VE proposals and share the resulting cost savings with the state transportation agency. The AASHTO Guide Specifications describe the basic VE provisions, which require that the contractor and agency share equally in the savings resulting from approval of the VE proposal. The agency will consider VE proposals that may potentially result in savings without damaging the essential function and characteristics of the project, which may include such things as service life, economy of operation, ease of maintenance, desired appearance, and safety. The provisions outline the submittal requirements, which include discussion of the proposed advantages and disadvantages, a timeframe within which the agency must make a decision, a plan showing the proposed revisions, and a statement of effect on completion time. If the VE proposal is accepted, payment is made for the cost of the redesigned work in its entirety, excluding the cost to develop and design the proposal.[151] The agency in its review should also focus on any potential deviation from approved environmental plans and permits which could cause potential problems.

11. Observations

The Changes clause is a powerful and necessary tool in the administration of construction contracts. Yet, the clause should be used sparingly insofar as practicable. Changes to the contract increase the cost of the work and the potential for delay. In addition, they often lead to disputes and ultimately to litigation. Thus, the goal of every owner should be to reduce change orders. Owners may wish to consider better subsurface site investigations when the contract contains a DSC clause. Also, when the work is novel or extremely complex, the owner may wish to employ constructibility reviews to assure that the design is reasonably constructible within accepted industry standards.

A balance should be struck by weighing the cost of such investigations and reviews against the potential cost and delay that can result when design errors and

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[140] Systems Technology Assocs. v. United States, 699 F.2d 1383, 1386–87 (Fed Cir. 1983); David Nassif Assocs. v. United States, 644 F.2d 4, 12 (Ct. Cl. 1981).

[141] David Nassif Assocs. v. United States, *supra* note 137.

[142] Willms Trucking Co. v. JW Constr. Co., 314 S.C. 170, 442 S.E.2d 197 (S.C. App. 1994) (citing the RESTATEMENT OF CONTRACTS, § 175(1)) (2d 1981) (contractor needed payment provided by change order to pay subcontractors and suppliers and avoid litigation).

[143] In re Boston Shipyard Corp., 886 F.2d 451, 455 (lst Cir. 1989).

[144] *Id*. at 455.

[145] Atlantic Dry Dock Corp. v. United States, 773 F. Supp. 335, 399 (M.D. Fla. 1991).

[146] Saddler v. United States, 152 Ct. Cl. 557, 287 F.2d 411, 413 (Ct. Cl. 1961).

[147] In re Boston Shipyard Corp., *supra* note 140.

[148] *Id.*

[149] H. L. C. & Assocs. Constr. Co. v. United States, 367 F.2d 586, 591 (Ct. Cl. 1966).

[150] Denver D. Darling v. Controlled Env'ts Constr., Inc., 89 Cal. App 4th 1221, 1235, 108 Cal. Rptr. 2d 213 (2001).

[151] AASHTO Guide Specifications, at 22–24.

inadequate investigations have to be corrected through the change order process.

The Changes clause provides all parties with tools, mechanisms, and opportunities to make appropriate contract adjustments to price and time of performance and thus reduce contractor bid contingencies. In addition to requiring clear notice provisions, it provides opportunities to mitigate damages, promote prompt issue resolution, and help reduce if not eliminate end-of-project disputes.

B. DIFFERING SITE CONDITIONS

1. Introduction

Under common law, a contractor who agreed to build some improvement assumed the risks ordinarily associated with performing that kind of work.[152] The fact that the work was actually more difficult and costly than the contractor anticipated did not entitle the contractor to additional compensation or excuse its performance. This principle of construction law was succinctly stated in *United States v. Spearin*:[153] "Where one agrees to do, for a fixed sum, a thing possible to be performed, he will not be excused or become entitled to additional compensation, because unforeseen difficulties are encountered."

This principle applies to unknown subsurface or latent physical conditions at the work site. These are risks that the contractor assumes, unless the contract shifts those risks to the project owner.[154] It was generally understood that contractors, faced with the risk of adverse, unknown site conditions, would include some amount in their bids as a contingency against encountering such conditions.[155] Some project owners, particularly large institutional owners such as the Federal Government, realized that if they assumed the risk of adverse site conditions, bids would be lower and the overall cost of their construction projects would be reduced. This realization was based on three assumptions: First, by shifting the risk of adverse conditions to the owners, the contractor would not have to include a contingency in its bid to guard against the risk of unforeseen site conditions. Second, on fixed-price contracts that are competitively bid, contractors must be competitive to obtain work. Third, it was cheaper to pay the occasional DSC claim than to pay the contingency as part of the price of each contract. Thus, the competitive process would force contractors to exclude those contingencies from their bids if they wished to be competitive and obtain contracts.

The desire of owners to reduce construction costs led to the development of the Federal "Changed Conditions" clause, and in 1968, its successor, the "Differing Site Conditions" (DSC) clause. This clause, which is now codified in the FAR,[156] is required in direct, fixed-price construction contracts. For state transportation projects funded with Federal Aid, the provisions are called "Changed Condition Contract Clauses." The use of the standardized Changed Conditions clause takes the risk of subsurface conditions out of the bidding process. Theorectically, contractors wll not receive a windfall or suffer the repercussion of a changed condition.[157] The purpose of the clause is to take some of the gamble out of bidding with regard to subsurface conditions. That purpose was stated by the Court of Claims in *Foster Construction C.A. and Williams Brothers v. United States*:

> The starting point of the policy expressed in the changed conditions clause is the great risk, for bidders on construction projects, of adverse subsurface conditions…Whenever dependable information on the subsurface is unavailable, bidders will make their own borings or, more likely, include in their bids a contingency element to cover the risk. Either alternative inflates the costs to the Government. The Government, therefore, often makes such borings and provides them for the use of the bidders, as part of a contract containing the standard changed conditions clause.[158]

Bidders are thereby given information on which they can rely in making their bids, and are at the same time promised an equitable adjustment under the changed conditions clause if subsurface conditions turn out to be materially different than those indicated in the logs. The purpose of the changed conditions clause is thus to take at least some of the gamble on subsurface condi-

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[152] Ashton Co. v. State, 9 Ariz. App. 564, 454 P.2d 1004, 1008 (Ariz. App. 1969); 3 A. CORBIN, CORBIN ON CONTRACTS § 598; 6 A. CORBIN, CORBIN ON CONTRACTS § 1333 (1962).

[153] 248 U.S. 132, 136, 39 S. Ct. 59, 63 L. Ed. 166 (1918).

[154] "[N]o one can ever know with certainty what will be found during subsurface operations." Kaiser Indus. Corp. v. United States, 169 Ct. Cl. 310, 340 F.2d 322, 329 (Ct. Cl. 1965). "If he [the contractor] wishes to protect himself against the hazards of the soil…he must do so by his contract." White v. Mitchell, 123 Wash. 630, 213 Pac. 10, 12 (Wash. 1923). There can be no claim for "Changed Conditions" when the contract does not contain a "Changed Conditions" clause. Frenz Enters. v. Port of Everglades, 746 So. 2d 498, 503 (Fla. App. 1999) ("[T]he parties' contract contained no 'changed conditions' clause, thus no breach of contract actions would lie for changed conditions."); Dravo Corp. v. Metro Seattle, 79 Wash. 2d 214, 484 P.2d 399, 402 (1971).

[155] Foster Constr. and Williams Bros. Co. v. United States, 193 Ct. Cl, 587, 435 F.2d 873, 887 (Ct. Cl. 1970); Hardwick Bros. Co., II v. United States, 36 Fed. Cl. 347, 405 (1996); H.B. Mac, Inc. v. United States, 36 Fed. Cl. 793, 819 (1996); Department of General Services v. Harmans Assoc., 987 Md. App. 535, 633 A.2d 939, 947 (Md. App. 1993); Sornsin Constr. Co. v. State, 190 Mont. 248, 590 P.2d 125, 130 (1978), P.T.L. Constr. v. Department of Transp., 531 A.2d 1330 (N.J. 1987).

[156] 48 C.F.R. ch. 1 § 52.236-2. In 1968, the title of the clause was changed from "Changed Conditions" to "Differing Site Conditions." 32 Fed. Reg. 16269 (Nov. 29, 1967).

[157] *See* FHWA, CONTRACT ADMINISTRATION CORE CURRICULUM MANUAL (hereinafter CACC Manual) 36 (2001), available online at http://www.fhwa.dot.gov/programadmin/contracts/cacc.pdf, last accessed on June 27, 2012.

[158] Foster Constr., *supra* note 155, at 887. *See also* Annotation, *Construction and Effect of "Changed Conditions" Clause in Public Works or Construction Contract With State or its Subdivision*, 56 A.L.R. 4th 1042 (1987).

tions out of bidding. Bidders need not weigh the cost and ease of making their own borings against the risk of encountering an adverse subsurface, and they need not consider how large a contingency should be added to their bid to cover the risk.

Some state transportation agencies have developed their own DSC clauses. Those clauses differ from the standard clause used by the Federal Government in its construction contracts. Some states have adopted the Changed Conditions clause contained in the AASHTO Guide Specifications for Highway Construction.[159] This subsection discusses those differences and the legal problems ordinarily associated with this type of clause.

In the absence of a DSC clause, the contractor assumes the risk of subsurface conditions unless the contractor can shift that risk to the owner under one of several common law theories. One such theory is misrepresentation. This theory imposes liability on an owner for adverse site conditions when the contractor can prove that it was mislead by erroneous information in the contract documents that caused the contractor to submit a bid lower than it would have otherwise made. Liability is based on the theory that furnishing misleading plans and specifications constitutes a breach of an implied warranty of their correctness.

Alternatively, a contractor may claim that the owner failed to disclose information about site conditions that was vital in preparing the bid. Liability for nondisclosure may be imposed where the contractor could not reasonably obtain such information without resort to the owner.

This subsection also discusses impossibility of performance as an excuse for nonperformance where unforeseen, adverse site conditions make performance physically impossible or commercially impracticable. Subcontractor pass-through claims are also discussed briefly, since subsurface work is often sublet by the general contractor and a DSC clause may be incorporated in the subcontract, either expressly or by implication through a flow-down clause. The subsection concludes with some observations about change orders as admissions when an owner wishes to change the design and keep the project moving, rather than let it languish because of a dispute over whether a DSC has occurred.

2. Contract Clauses—Type I and Type II Conditions

The FAR require inclusion of the standard DSC clause in all fixed-price construction contracts.[160] Some states have similar laws.[161] Other state agencies include DSC clauses under their general authority to develop plans and specifications for their construction projects.[162]

The federal clause differs from most state clauses in how it treats the effect of a DSC on unchanged work. The 1968 revisions to the federal clause not only changed the name of the clause from "Changed Conditions" to "Differing Site Conditions," it also broadened the equitable adjustment provisions of the clause to cover the effect of changed conditions upon the cost of performing unchanged work. Prior to 1968, a contractor was only entitled to the additional cost it incurred in performing the changed work. If the changed condition affected other work by delaying or resequencing that work, the contractor was not entitled to additional compensation. The financial impact that the condition had on other work was considered "consequential" and as such was not compensable.[163] To obviate that result, the 1968 revision added this language: "…that such conditions do materially so differ and cause an increase or decrease in the contractor's cost of, or the time required for, performance of any part of any work under this contract, *whether or not changed as a result of such conditions*" (emphasis added). This language eliminated the *Rice* doctrine.[164]

The standard DSC clauses used by some states contain language disallowing impact costs on unchanged work.[165] The FHWA DSC clause mandated in 23 C.F.R. 635.109 for federally aided highway projects also disallows impact costs but permits the state to eliminate the prohibition. Subsection IV of that clause provides that, "no contract adjustment will be allowed under this clause for any effects caused on unchanged work."

Both the federal and state clauses recognize two types of DSCs: (1) subsurface or latent physical conditions at the site that differ materially from those indicated in the contract (generally referred to as a Type I condition); and (2) physical conditions that are so unusual for the type of work performed that the conditions could not have been reasonably anticipated by an experienced and prudent contractor (generally referred to as a Type II condition). For example, the DSC clause contained in federal construction contracts provides in pertinent part as follows:

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[159] D.W. HARP, *Preventing and Defending Against Highway Construction Claims: The Use of Changes or Differing Site Conditions Clause, Etc.*, SELECTED STUDIES IN HIGHWAY LAW, National Cooperative Highway Research Program Legal Research Digest No. 28.

[160] 48 C.F.R. ch. 1 § 52.236-2.

[161] *See* Sutton Corp. v. Metropolitan Dist. Comm'n, 423 Mass. 200, 667 N.E.2d 838, 842 (Mass. 1996); Metro Sewerage Comm'n of the County of Milwaukee v. R.W. Constr., Inc., 72 Wis. 2d 365, 241 N.W.2d 371, 376 (Wis. 1976); Department of Gen. Services v. Harman Assocs., 98 Md. App. 535, 633 A.2d 939, 948 (Md. App. 1993).

[162] For example, WASH. REV. CODE § 47.28.050 authorizes the WSDOT to include in its highway construction contracts those specifications which in its judgment it deems necessary.

[163] United States v. Rice, 317 U.S. 61, 63 S. Ct. 120 (1942).

[164] 32 Fed. Reg. 16269 (Nov. 29, 1967).

[165] Arizona Standard Specification 104.02(B)(4); California Standard Specification 5-1.116 (1995) ("no contract adjustment allowed…for any effects caused on unchanged works."); Iowa Standard Specification 1109.16 A.4.; New York Standard Specification 109-16A(1)(iv); Texas Standard Specification 9.7. Florida's DSC clause, however, allows for an increase or decrease in the cost required for the performance of any work under the contract. Florida Standard Specification 4-3.4.

> The Contractor shall promptly, and before the conditions are disturbed, give a written notice to the Contracting Officer of (1) subsurface or latent physical conditions at the site which differ materially from those indicated in this contract, or (2) unknown physical conditions at the site, of an unusual nature, which differ materially from those ordinarily encountered and generally recognized as inhering in work of the character provided for in the contract.166

The AASHTO Guide Specification defines differing site conditions similarly: "Surface or latent physical conditions differing from those indicated in the contract or an unknown physical condition of an unusual nature differing materially from those ordinarily encountered and generally recognized as inherent in the work provided for in the contract."[167]

For example, in *Foster Construction Co.*,[168] the contractor claimed that it had encountered a Type I DSC in constructing bridge pier footings at three of the six bridge pier locations. The court found that the contract led the contractor to believe, when it prepared its bid, that dry soil could be expected at all six pier conditions. The actual soil conditions at three of the piers were highly permeable, causing the cofferdams to fill with water and requiring the use of seals and tremie concrete[169] to pour the footings. The court held that a Type I changed condition had occurred at those three piers.

a. Type I DSC

The fact situations that constitute Type I conditions vary. Rock obtained from a quarry designated in the contract as an approved source was a Type I condition when the rock could not be used. The court held that by designating the quarry in the contract as an approved source, the government indicated that the quarry would produce suitable material.[170] A Type I condition was established when the contractor encountered numerous boulders while driving sheet pile. The contract indicated that sheet pile could be driven without extraordinary efforts.[171] Wet soil conditions have produced their share of Type I claims. Type I conditions were established where the moisture content was far greater than indicated in the contract;[172] where the site contained dense, nondraining soil, rather than free-draining sands and gravel;[173] and where the site contained perched water instead of dry soil as indicated in the contract documents.[174] The possibility that actual conditions may vary from those indicated in the contract is almost unlimited. "[N]o one can ever know with certainty what will be found during subsurface operations."[175]

There are six elements which the contractor must prove, by a preponderance of the evidence, to establish a Type I DSC claim. These six elements are:

> (1) the contract documents must have affirmatively indicated or represented the subsurface or latent physical conditions which form the basis of plaintiff's claim; (2) the contractor must have acted as a reasonably prudent contractor in interpreting the contract documents; (3) the contractor must have reasonably relied on the indications of subsurface or latent physical conditions in the contract; (4) the subsurface or latent physical conditions actually encountered within the contract area must have differed materially from the conditions indicated in the same contract area; (5) the actual subsurface conditions or latent physical conditions encountered must have been reasonably unforeseeable; and (6) the contractor's claimed excess costs must be shown to be solely attributable to the materially different subsurface or latent physical conditions within the contract site. To prove these six elements, the contractor is only required to use a simple logical process in evaluating the information in the contract documents to determine the expected subsurface or latent physical conditions….176 (citations omitted).

The term contract documents, as used in a typical Type I DSC clause, includes not only the documents furnished to bidders, but also materials referenced in those documents. There cannot be, however, a Type I condition when there is nothing in the documents indicating what the contractor could expect to encounter in the way of site conditions.[177] For example, a Type I condition was denied where there was nothing in the contract about the density or type of soil that the contractor could expect to encounter in driving sheet pile.[178] A similar result was reached where there was no indication in the contract as to the size of boulders where large boulders were encountered.[179]

Even where there are indications in the contract, the contractor must show that its reliance upon those indi-

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[166] 48 C.F.R. pt. 1 § 52.243.2(A).

[167] AASHTO Guide Specifications 104.02B.

[168] 435 F.2d 873, *supra* note 155.

[169] Tremie is a means of placing concrete under water by using a pipe or "elephant trunk."

[170] Kaiser Indus. Corp. v. United States, 169 Ct. Cl 310, 340 F.2d 322 (Ct. Cl. 1965).

[171] Kit-San-Azusa v. United States, 32 Fed. Cl. 647, 658 (1995); Thomas M. Durkin & Sons, Inc. v. Department of Transp., 742 A.2d 233, 238 (Pa. Commw. 1999) (encountering unanticipated rock in constructing highway ramps).

[172] Ray D. Bolander Co. v. United States, 186 Ct. Cl. 398, 408 (1968).

[173] H.B. Mac, Inc. v. United States, H.B. Mac, Inc. v. United States, 36 Fed. Cl. 793, 819 (1996); Ragonese v. United States, 128 Ct. Cl. 156, 120 F. Supp. 768 (Ct. Cl. 1954) (subterranean water where boring showed no water).

[174] Appeal of R.D. Brown Contractors, ABSCA No. 43973, 93-1 BCA ¶ 25, 368 (1992).

[175] Kaiser Indus. Corp. v. United States, 340 F.2d 322, 329 (Ct. Cl. 1965), *supra* note 170.

[176] H.B. Mac, Inc. v. United States, 36 Fed. Cl. 793, 820 (1996); (citing Youngdale & Sons Constr. Co. v. United States, 27 Fed. Cl. 516 (1993)).

[177] Fru-Con Constr. Corp. v. United States., 43 Fed. Cl. 306, 318 (Fed. Cl. 1999) (defining contract documents); Olympus Corp. v. United States, 98 F.3d 1314 (1996) (no Type I condition when contract is silent about the condition).

[178] Appeal of PK Contractors, Inc., ENGBCA 92-1 BCA, ¶ 24, 583.

[179] T.F. Scholes, Inc. v. United States, 357 F.2d 963 (Ct. Cl. 1966).

cations was reasonable. If the inference that the contractor draws from the documents is not reasonable, there is no Type I condition. This principle was applied in *Stuyvesant Dredging Co. v. United States*, where the contractor claimed it encountered a Type I condition when it dredged materials that were denser than indicated in the technical provisions of the contract.[180] The court denied the claim because the contract stated that the density readings were the average value of all the readings. The contractor was not entitled to rely on the average density since it should have known that the average density represented densities both greater and less than the average. A contractor's claim for a Type I condition for encountering hardpan[181] was denied where the hardpan amounted to 11 percent of the material excavated, and the contract warned the contractor that some hardpan could be expected.[182] A similar result was reached where the contract contained indications that the subsurface soil would be wet.[183] This principle was applied by a Washington DOT disputes review board in denying a claim for a Type I condition. The contractor claimed that it encountered a DSC when it was unable to drive piling at a bridge pier using the same driving methods that were successfully used at other piers. The board denied the claim, finding that the contract warned the contractor that it might be necessary to use certain predriving techniques to loosen the soil and make driving easier.[184]

A Type I condition must be physical in nature. This is so because both the federal clause and the clauses used by some states refer to subsurface or latent physical conditions at the site.[185] The DSC must exist before the contract is awarded. This is so because the DSC clause requires that the conditions differ materially from those indicated in the contract. This was explained by the New Jersey Supreme Court in *P. T. & L Construction v. State, Department of Transportation*, when it said:

Bidders are thereby given information on which they may rely in making their bids, and are at the same time promised an equitable adjustment under the changed conditions clause, if subsurface conditions turn out to be materially different than those indicated in the logs. The two elements work together; the presence of the changed conditions clause works to reassure bidders that they may confidently rely on the logs and need not include a contingency element in their bids. Reliance is affirmatively desired by the Government, for if bidders feel they cannot rely, they will revert to the practice of increasing their bids.[186]

A Type I DSC (as well as a Type II DSC, which is discussed next) must be material. Both the federal and state clauses refer to conditions at the site that differ *materially* from those indicated in the contract. To be material, the condition must affect the contractor's costs and/or the time for performance. And the extra costs and/or delays claimed by the contractor must be solely attributable to the DSC.[187] Whether the condition is material is a question of fact. "We think that whether the changed conditions are 'conditions…differing materially from those in the contract' under § 104.03 is a question of fact regardless of whether the claimed changes result in quantitative or qualitative changes to the work to performed."[188]

b. Type II DSC

The Federal DSC clause defines a Type II condition as: "(2) unknown physical conditions at the site, of an unusual nature, which differ materially from those ordinarily encountered and generally recognized as inhering in work of the contractor provided for in the contract."[189]

Most DSC clauses used by state transportation agencies follow the AASHTO Guide Specifications in providing for a Type II condition.[190] The Guide Specification defines DSCs in part as those that:

- Differ materially from conditions normally encountered or from those conditions generally recognized as inherent in the nature of the work required.
- Present unknown or unusual physical conditions.

A Type II DSC exists when the conditions at the work site differ materially from those normally encountered in performing the work specified in the contract. To prevail on a claim for a Type II condition, the contractor must show: (1) that it did not know about the condition; (2) that it could not have reasonably anticipated the condition after a review of the contract documents, a site inspection, and the contractor's general experience in that area; and (3) that the condition was unusual because it varied from the norm in similar construction work.[191]

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[180] 834 F.2d 1576 (Fed. Cir. 1987).

[181] A very dense, cemented material, often clay, which is difficult to excavate.

[182] R.C. Huffman Constr. Co. v. United States, 100 Ct. Cl. 80 (1943).

[183] Leal v. United States, 149 Ct. Cl. 451, 276 F.2d 378 (Ct. Cl. 1960).

[184] I-90 Bridge Approach Spans, Third Lake Washington Floating Bridge Project.

[185] The same requirement applies to Type II conditions, as discussed in Part B *infra*.

[186] 108 N.J. 539, 531 A.2d 1330, 1334–35 (N.J. 1987) (quoting Foster Constr. Co. C.A. Williams Bros. Co. v. United States, 435 F.2d 873, 887, 193 Ct. Cl 587 (1970).

[187] Fruin-Colnon Corp. v. Niagara Frontier, 180 A.D. 2d 222, 585 N.Y.S.2d 248, 251 (N.Y. A.D. 1992) (citing federal cases).

[188] Asphalt Roads & Materials Co. v. Commw., DOT, 257 Va. 452, 512 S.E.2d 804, 807 (Va. 1999).

[189] 48 C.F.R. pt. 1 § 52.243.2(A).

[190] AASHTO Guide Specification for Highway Construction § 101.03 (1998).

[191] Fru-Con Constr. Corp. v. United States, 44 Fed. Cl. 298, 311 (Fed. Cl. 1999); Lathan Co. v. United States, 20 Cl. Ct. 122, 127 (1990). Information in boring logs available to the

The condition does not have to be a "geological freak" to qualify as unusual.[192] Nevertheless, the contractor's burden in establishing a Type II site condition is heavy.[193] The key is whether the site condition is physical, preexisting, unknown, and unusual. If these elements are satisfied the condition may qualify as a Type II DSC.[194] But conditions that do not satisfy these criteria are not covered by the clause.[195] A Type II condition may be proven by expert testimony.[196] Proving a Type II condition is usually more difficult when the condition is natural. Generally, it is more difficult to prove that a natural condition was unexpected because of the variations and kinds of earth materials found in subsurface work.[197]

Generally, the DSC clause encompasses only those site conditions that existed prior to the time the contract was awarded.[198] Site conditions that are created after the contract has been awarded are not covered by the clause, although there are some exceptions to this rule.[199] In addition, changes to the work that are nonphysical in nature do not qualify as DSCs since the clause refers only to physical conditions at the site.[200]

States must use the DSC clause in 23 C.F.R. 635.109(a)(1) for federal-aid highway projects unless the agency has an acceptable[201] DSC clause of its own or use of the clause is prohibited by state law.[202] The federally-mandated clause reads as follows:

> (i) During the progress of the work, if subsurface or latent physical conditions are encountered at the site differing materially from those indicated in the contract or if unknown physical conditions of an unusual nature, differing materially from those ordinarily encountered and generally recognized as inherent in the work provided for in the contract, are encountered at the site, the party discovering such conditions shall promptly notify the other party in writing of the specific differing conditions before they are disturbed and before the affected work is performed.
>
> (ii) Upon written notification, the engineer will investigate the conditions and if it is determined that the conditions materially differ and cause an increase or decrease in the cost or time required for the performance of any work under the contract, an adjustment, excluding anticipated profits, will be made and the contract modified in writing accordingly. The engineer will notify the contractor of the determination whether or not an adjustment of the contact is warranted.
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> (iii) No contract adjustment which results in a benefit to the contractor will be allowed unless the contractor has provided the required written notice.
>
> (iv) No contract adjustment will be allowed under this clause for any effects caused on unchanged work. (This provision may be omitted by the SHA's at their option).

3. Site Investigation

Most construction contracts contain site inspection clauses. These clauses require bidders to bid on condi-

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contractor that provided notice of the condition precluded recovery for a Type II claim. Youndale & Sons Constr. Co. v. United States, 27 Fed. Cl. 516, 537 (1993).

[192] Western Well Drilling Co. v. United States, 96 F. Supp. 377, 379 (N.D. Cal. 1951).

[193] Charles T. Parker Constr. Co. v. United States, 433 F.2d 771, 778 (Ct. Cl. 1970); Youndale & Sons, *supra* note 191, at 537–39 (discussing contractor's burden of proof).

[194] Type II conditions established when contractor encountered: James Julian, Inc. v. Comm'rs of Town of Elkton, 341 F.2d 205 (4th Cir. 1965) (buried wharf during construction of a sewer); Reliance Ins. Co. v. County of Monroe, 198 A.D. 2d 871, 604 N.Y.S.2d 439, 440 (N.Y. 1993) (hazardous waste); Appeal of Panhandle Constr. Co., DOTCAB 79-1 BCA ¶ 13576 (1979) (buried animal bones); Kit-San Azusa v. United States, 32 Fed. Cl. 647 (1995) (encountering boulders that impeded driving sheet pile).

[195] Type II conditions were not established in the following cases. Condition visible from site inspection: Walsh Bros. v. United States, 107, Ct. Cl. 627, 69 F. Supp. 125 (Ct. Cl. 1947) (foundations from old buildings visible); Appeal of Basic Construction Co., ASBCA 77-2 BCA 2738 (1977) (roadway cuts revealed rock outcroppings); Sergent Mech. Sys., Inc. v. United States, 34 Fed. Cl. 505, 527 (1995) (encountering heavy rains preventing compaction not a Type II condition at airforce base project). Not preexisting: Olympus Corp. v. United States, 98 F.3d 1314, 1317 (Fed. Cir. 1996) (damage to work caused by another contractor after contract award). Weather: Donald B. Murphy Contractors, Inc. v. State, 40 Wash. App. 98, 696 P.2d 1270 (Wash. App. 1985); Annotation, *Construction and Effect of a "Changed Conditions" Clause in Public Works or Construction and Effect of a "Changed Conditions" Clause in Public Works or Construction Contract with State or its Subdivision*, 56 A.L.R. 4th 1042, 1066 (1987) (heavy rain); contracts, 56 A.L.R. 4th 1042, 1066 (heavy rain); Turnkey Enterprises v. United States, 220 Ct. Cl. 199, 597 F.2d 750 (Ct. Cl. 1977) (drought). Difficulty in performing work due to alleged unusual site condition: Fru-Con Constr. Corp v. United States, 44 Fed. Cl. 298, 311–12 (Fed. Cl. 1999) (concrete removal).

[196] T. Brown Constr., Inc., DOTCAB, 95-2 BCA ¶ 27,870 (1995) (expert testified that it was unusual for clay to adhere to rock); Charles T. Parker Constr. Co. v. United States, 193 Ct. Cl. 320, 433 F.2d 771, 778 (Ct. Cl. 1970) (expert testified to the amount of garnet encountered in excavating rock and its affect on drilling the rock).

[197] Charles T. Parker, *supra* note 80; Hardwick Bros. Co. II. v. United States, 36 Fed. Cl. 347, 409–10 (Ct. Cl. 1996) (ground water conditions not a Type II condition).

[198] Arundel Corp. v. United States, 96 Ct. Cl. 773 (Ct. Cl. 1942); Olympus Corp. v. United States, 98 F.3d 1314, 1317 (Fed. Cir. 1996).

[199] John A. Johnson Contracting Corp. v. United States, 132 F. Supp. 698, 702 (Ct. Cl. 1955) (unusual soil conditions combined with rains and early thaw damaged haul roads); Phillips Constr. Co. v. United States, 184 Ct. Cl. 249, 394 F.2d 834 (1968) (flooding of site due to heavy rainfall exacerbated by defective drainage system); Donald B. Murphy Contractors, Inc. v. State, 40 Wash. App. 98, 696 P.2d 1270, 1273 (Wash. App. 1985) (changed conditions claim based on defective drainage system and heavy rains denied).

[200] Olympus Corp. v. United States, *supra* note 197, at 1318 (labor strike not a DSC); Bateson-Stolte, Inc. v. United States, 145 Ct. Cl. 387, 172 F. Supp. 454 (1959) (change in wage rates during contract performance not a changed condition).

[201] The substitute clause is subject to FHWA approval.

[202] 23 U.S.C. § 112.

tions, as they appear, based upon a reasonable investigation of the physical conditions at the site that could affect the work. The site investigation clause, when coupled with a DSC clause, encourages more accurate bidding as to the true cost of performing the work.[203]

The Federal "Site Investigation" clause[204] is typical of the type of clause used in construction contracts. That clause provides as follows:

> (a) The Contractor acknowledges that it has taken steps reasonably necessary to ascertain the nature and location of the work, and that it has investigated and satisfied itself as to the general and local conditions which can affect the work or its cost, including but not limited to (1) conditions bearing upon transportation, disposal, handling, and storage of materials; (2) the availability of labor, water, electric power, and roads; (3) uncertainties of weather, river stages, tides, or similar physical conditions at the site; (4) the conformation and conditions of the ground; and (5) the character of equipment and facilities needed preliminary to and during work performance. The Contractor also acknowledges that it has satisfied itself as to the character, quality, and quantity of surface and subsurface materials or obstacles to be encountered insofar as this information is reasonably ascertainable from an inspection of the site, including all exploratory work done by the Government, as well as from the drawings and specifications made a part of this contract. Any failure of the Contractor to take the actions described and acknowledged in this paragraph will not relieve the Contractor from responsibility for estimating properly the difficulty and cost of successfully performing the work, or for proceeding to successfully perform the work without additional expense to the Government.
>
> (b) The Government assumes no responsibility for any conclusions or interpretations made by the Contractor based on the information made available by the Government. Nor does the Government assume responsibility for any understanding reached or representation made concerning conditions which can affect the work by any of its officers or agents before the execution of this contract, unless that understanding or representation is expressly stated in this contract.

A typical state site investigation clause is contained in the AASHTO Guide Specifications. It provides that the contractor must carefully examine the contract documents and perform a reasonable site investigation before submitting a bid proposal. Submitting a proposal is considered an affirmative statement that the bidder has examined the site and is satisfied as to the character, quality, quantities, and conditions to be encountered in performing the work. A reasonable site investigation includes investigating the project sites, borrow pits, and all other locations related to the performance of the work. When available the Agency may include in the contract documents or make available to bidders for review at the designated Agency location, one or more of the following: A. all agency boring logs and other records of subsurface investigation, B. record drawings, or C. results of other preliminary investigations. A reasonable site inspection includes review of these documents. Such information is for the bidder's general knowledge only and is not a substitute for the bidder's own investigation, interpretation, or judgment.[205] Similar provisions are contained in the Ohio Construction Specification Manual, Section 102.4-2.04.

The knowledge that a reasonable site inspection would disclose is imputed to the contractor.[206] A contractor who fails to make a reasonable site inspection may not recover for a DSC if the condition would have been observed by a reasonably prudent contractor.[207]

As a general rule, a contractor is not obligated to verify representations in the contract about subsurface site conditions through independent tests when the contract contains a DSC clause and the accuracy of the information, such as test borings, is not specifically disclaimed. The presence of the DSC clause is intended to assure bidders that they may rely on the soils information and need not incur the expense of their own tests, or include a contingency element in their bids.[208]

DSC clauses cannot be overridden by general exculpatory clauses.[209] In *Asphalt Roads & Materials v. Commw. DOT*,[210] the State argued that the exculpatory provisions in the contract relating to site investigation and bid submittal[211] precluded the contractor's claim for

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[203] Foster Constr. Co., 435 F.2d at 887.

[204] 48 C.F.R. pt. 1 § 52-236-3.

[205] AASHTO Guide Specifications 102.05 0 11.

[206] Hardwick Bros. v. United States, 36 Fed. Cl. 347, 406 (Ct. Cl. 1996).

[207] Gene Hock Excavating, Inc. v. Town of Hamburg, 227 A.D. 2d 911, 643 N.Y.S.2d 268 (App. Div. 1996); Umpqua Riv. Nav. Co. v. Cresent City Harbor Dist., 618 F.2d 588 (9th Cir. 1980); "The conditions actually encountered must have been reasonably unforeseeable based on all the information available to the contractor at the time of bidding." Fur-Con Constr. Corp. v. United States, 44 Fed. Cl. 298, 309 (1999) (quoting A.S. McGaughan Co. v. United States, 24 Cl. Ct. 659 (1991) *aff'd*, 980 Fed. 2d 744 (Fed. Cir. 1992) and referring also to CIBINIC & NASH, ADMINISTRATION OF GOVERNMENT CONTRACTS 508 (3d ed. 1995)). Contractor charged with knowledge that reasonable site inspection would disclose. Beltrone Constr. v. State, 256 A.D. 2d 992, 682 N.Y.S.2d 299, 301 N.Y. A.D. 1998).

[208] H.B. Mac, Inc. v. United States, 36 Fed. Cl. 793, 819 (1996); Foster Constr. C.A. & Williams Bros. Co. v. United States, 93 Ct. Cl. 589, 435 F.2d 873, 887 (1970); Asphalt Roads & Materials Co. v. Commw. DOT, 257 Va. 452, 512 S.E.2d 804, 807–08 (Va. 1999).

[209] Sutton Corp. of Metro. Dist. Comm'n, 423 Mass. 200, 667 N.E.2d 838, 843 (Mass. 1996); Metro Sewerage Comm'n of the County of Milwaukee v. R.W. Constr., Inc., 72 Wis. 2d 365, 241 N.W.2d 371, 382 (Wis. 1976); United Contractors v. United States, 177 Ct. Cl. 151, 368 F.2d 585, 598 (Ct. Cl. 1966). These cases involve DSC clauses that were required by law to be included in construction contracts. Contracting agencies lack authority to negate DSC clauses through the use of exculpatory provisions. *See, e.g.,* Department of General Services v. Harmans' Assocs., 98 Md. App. 535, 633 A.2d 939, 945 (Md. App. 1993).

[210] 257 Va. 452, 512 S.E.2d 804 (Va. 1999).

[211] *Id*. at 808. "The submission of a bid will be considered conclusive evidence that the bidder has examined the site…and

a DSC. The court, in rejecting this contention, said that giving effect to the exculpatory provisions, "…would render meaningless the language of sections like 104.03 [Differing Site Condition clause] and negate their salutary purposes."[212]

A contractor must conduct the site inspection in a reasonable and prudent manner. A contractor is not required or expected to discover conditions that would only be observed by a geologist or a geotechnical engineer. The standard is what a reasonably prudent and experienced contractor would learn from a reasonable pre-bid site investigation.[213]

Occasionally, contractors try to avoid the consequences of not conducting a site investigation by arguing that the time between the advertisement for bids and bid opening was too short to allow for a reasonable inspection. How this argument fares depends upon several considerations. First, was the time really too short to permit a reasonable inspection of the project site? Second, is the clause mandated by a statute or regulation? If the answer to these questions is "yes," the contractor's failure or inability to conduct a reasonable site inspection will not bar a claim for a DSC.[214] However, the claim may be barred where the information that would be gleaned from a site investigation could be obtained from other sources, available to the contractor when it prepared its bid.[215]

Where there is no DSC clause in the contract, failure to investigate the site may bar a claim for misrepresentation[216] of site conditions even though the time allowed for the investigation is insufficient. The risk of unanticipated soil conditions should be considered by the contractor in formulating its bid.[217]

4. Notice Requirements

All DSC clauses require the contractor to provide prompt written notice to the owner when it encounters what it considers to be a DSC. Notice must be given before the condition is disturbed.[218] Prompt notice allows the owner to investigate the condition while the facts are fresh and determine whether a DSC occurred. If the owner determines that a DSC has occurred, it can consider design changes or other alternatives to reduce costs and keep the project on schedule. This is particularly important to public agencies that operate under tight budgetary restrictions.[219] Notice also allows the owner the opportunity to document costs caused by the condition as they are incurred by the contractor.[220]

Generally cases involving notice issues range from strict enforcement[221] to no enforcement, unless the owner can show that it was prejudiced by lack of notice.[222] Jurisdictions that require strict compliance with notice requirements regard them as substantive rights that the owner is entitled to enforce as a condition precedent to any recovery, by the contractor, for a DSC. Failure to satisfy notice requirements will bar a claim for DSC,[223] unless the owner has waived notice or the owner is estopped from asserting lack of notice as a defense. [224] Once notice is given, it is not necessary to continue to give notice when the condition recurs.[225]

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is satisfied as to the conditions to be encountered in performing the work…." VDOT Specification 102.04.

[212] 515 S.E.2d at 808 (citations omitted).

[213] Foster Constr. Bros., 435 F.2d at 886, *supra* note 155; Western Contracting Corp., ENGBCA No. 4066, 82-1 BCA ¶ 15,486 (1982); Gulf Constr. Group, Inc., *supra* ENGBCA 93-3 BCA ¶ 26,040, CCH 25,229 (1993).

[214] Where the DSC clause is required by statute or regulation, an agency cannot frustrate those laws by imposing unreasonable requirements. Department of General Services v. Harmon, 633 A.2d 739 (Md. App. 1993). *See also* Grow Constr. Co. v. State, 56 A.D. 2d 95391 N.Y.S.2d 726, 728 (N.Y. A.D. 1977) (evidence indicated that it would have taken far more time to investigate the site than allowed).

[215] "'[T]he conditions actually encountered must have been reasonably unforeseeable based on all the information available to the contractor at the time of bidding.'" Fru-Con Constr. Corp. v. United States, 44 Fed. Cl. 298, 309 (Fed. Cl. 1999); Fortec Constructors, ENGBCA No. 4352, 80-2 BCA ¶ 14,623 (1980).

[216] Misrepresentation, as a theory of recovery of recovery for adverse site conditions encountered during contract performance, is discussed in Part Five of this subsection.

[217] J.E. Brenneman Co. v. Commw., Dep't of Transp., 56 Pa. Commw. 210, 424 A.2d 592, 595 (Pa. Commw. 1981); Central Penn Indus., Inc. v. Commw., Dep't of Transp., 358 A.2d 445, 448 (Pa. Commw. 1976) (insufficient time for site investigation will not support a claim for unanticipated conditions).

[218] "Notify the Agency…when encountering different site conditions on the project. Unless directed otherwise, leave the site undisturbed and suspend work." AASHTO Guide Specification § 104.02 (1998). "The Contractor shall promptly, and before the conditions are disturbed, give a written notice to the Contracting Officer…." 48 C.F.R. pt. 1 § 52.236.2. *See* "Enforceability of the Requirements of Notice in Highway Construction Contracts," 3 JOHN C. VANCE, SELECTED STUDIES IN HIGHWAY LAW 154 N-1.

[219] Justin Sweet, *Owner Architect Contractor: Another Eternal Triangle*, 47 CAL. L. REV. 645 (1959).

[220] Sutton Corp. v. Metro Dist. Comm'n, 423 Mass. 200, 667 N.E.2d 838, 843 (Mass. 1996); Blankenship Constr. Co. v. N.C. State Highway Comm'n, 28 N.C. 593, 222 S.E.2d 452, 459–60 (N.C. 1976).

[221] A.H.A. General Constr., Inc. v. Housing Auth., 241 A.D. 2d 428, 661 N.Y.S.2d 213, 215 (A.D. 1997); Blankenship Constr. Co. v. State Highway Comm'n, *supra* note 218 (strict compliance with notice requirements required).

[222] Hoel-Steffen Constr. Co. v. United States, 197 Ct. Cl. 561, 456 F.2d 760, 767–8 (Ct. Cl. 1972); Fru-Con Constr. Corp. v. United States, 44 Fed. Cl. 298, 313 (Fed. Cl. 1999); T. Brown Contractors, Inc., DOTCAB 95-2 BCA ¶ 27870 (1995); New Pueblo Constructors, Inc. v. State, 144 Ariz. 95, 696 P.2d 185, 191 (Ariz. 1985). Contra: Absher Constr. Co. v. Kent Sch. Dist., 77 Wash. App. 137, 890 P.2d 1071, 1073 (Wash. App. 1995) (showing of prejudice not required to enforce notice provision).

[223] A.H.A. General Constr., Inc. v. N.Y. City Housing Auth., 92 N.Y.2d 20, 699 N.E.2d 368, 374, 677 N.Y.S.2d 9, 15 (N.Y. 1998).

[224] Reif v. Smith, 319 N.W.2d 815, 817 (S.D. 1982) (waiver); Thorn Constr. Co. v. Utah Dep't of Transp., 598 P.2d 365, 370 (Utah 1979) (estoppel; work ordered by project engineer); Northern Improvement Co. v. State Highway Comm'n, 267 N.W.2d 208, 214 (S.D. 1978) (estoppel). There is authority,

Courts that do not require strict compliance with notice requirements view notice from the standpoint of why notice is required. Under this approach, written notice is excused if the owner knew about the condition early enough to take steps to protect its interests.[226] This "substantial compliance" approach to notice often leads to arguments over who told what to whom, requiring a trial or hearing to resolve those kinds of factual disputes. The contractor must prove that the alleged oral notice of a DSC was "sufficiently forceful to anyone to replace the contractual requirement of clear written notice." Failure to make that showing will bar a claim for DSCs.[227]

Under federal contract law, lack of notice by the contractor that it encountered a DSC will not bar the contractor's claim for the condition, unless the Government can show that it was prejudiced by lack of notice.[228]

5. Misrepresentation of Soil Conditions

Construction contracts may contain language that purports to relieve owners from any responsibility for the accuracy or completeness of soils information and other site data furnished to bidders. Owners who choose not to include DSC clauses in their contracts are reluctant to guarantee this type of information. This is not only understandable, it is prudent. Information of this kind is obtained for design purposes and is furnished to prospective bidders with the caveat that the information is not part of the contract, is not necessarily accurate, was obtained for design purposes, and should not be relied upon by the bidders in making their bids. Bidders are cautioned to make their own site investigation to verify the data and obtain additional information. Often the time allowed for the site investigation is short, and on occasion insufficient. It may be difficult for bidders to discover, in a limited time, information that the owner was unable to discover during its own site investigation—an investigation that may have taken months, even years.[229] The bidders are given the site data that the owner obtained for design purposes, but told not to rely on the data. Faced with this dilemma, bidders can choose not to bid, or to bid and include an amount in their bids to cover site investigations of their own (if they so choose) and a contingency for unforeseen site conditions. The DSC clause, as discussed earlier, is designed to obviate this dilemma.

As a general rule, a broad exculpatory clause will not override the DSC clause; otherwise the purpose of the DSC clause would be negated.[230] When a DSC clause is required to be in the contract by a statute or regulation, an agency cannot avoid the clause by omitting it from the contract. A DSC clause that is physically omitted will be read into the contract and enforced as if it were part of the contract.[231] Where the DSC clause in the contract is not mandated by statute or regulation, a disclaimer concerning site conditions must be specific, clear, and unambiguous, otherwise it will not be enforced.[232] But what are the rules when there is no DSC clause in the contract, and the agency is not legally obligated to include one as part of its procurement policy?

In the absence of a DSC clause in the contract, the contractor assumes the risk of unforeseen site conditions.[233] The contractor may attempt to shift this risk to the owner under several legal theories. The contractor may claim that the owner failed to disclose information about the site that would have been important to the contractor in preparing its bid. This theory is advanced when the contract documents are silent about the condition that was encountered.[234] A more common situation is where the contract contains information about the site but the information was inaccurate. When this occurs, the claim for adverse site conditions is based on misrepresentation.[235]

Misrepresentation has its roots in actions for damages based on fraud and deceit.[236] The theory has

however, that lack of notice may be waived as a defense when the claim is considered on the merits. Blount Bros. Corp. v. United States, 191 Ct. Cl. 784, 424 F.2d 1074, 1076 (Ct. Cl. 1970); T. Brown Contractors, Inc., DOTCAB 95-2 BCA ¶ 27,870 (1995).

[225] Fru-Con Constr. Corp. v. United States, 43 Fed. Cl. 306, 328 (Fed. Cl. 1999).

[226] Neal & Co. v. City of Dillingham, 923 P.2d 89, 92 (Alaska 1993); New Pueblo Constructors, Inc. v. State, 144 Ariz. 93, 696 P.2d 185, 191 (Ariz. 1985); Zook Bros. Constr. Co. v. State, 177 Mont. 64 556 P.2d 911, 914–15 (Mont. 1976); Lindbrook Constr. Co. v. Mukilteo Sch. Dist., 76 Wash. 2d 539, 458 P.2d 1 (Wash. 1969).

[227] Neal & Co. v. City of Dillingham, *supra* note 227, at 92–93.

[228] Fru-Con Constr. Corp; 43 Fed. Cl., *supra* note 226, at 324–25. But where prejudice is shown the claim will be barred. Schnip Building Co. v. United States, 227 Ct. Cl. 148, 645 F.2d 950, 958–59 (Ct. Cl. 1981) (lack of notice prevented Government from determining whether problems with rock were due to a DSC or the contractor's blasting methods); Eggers & Higgins v. United States, 185 Ct. Cl. 765, 403 F.2d 225, 293 (Ct. Cl. 1968) (late notice prejudiced Government's ability to evaluate DSC claim).

[229] 3 WALLEY & VANCE, *Legal Problems Arising From Changes, Changed Conditions, and Disputes Clauses in Highway Construction Contracts*, SELECTED STUDIES IN HIGHWAY LAW 1441.

[230] Asphalt Roads & Materials v. Com. DOT, 757 Va. 452, 512 S.E.2d 804, 808 (Va. 1997).

[231] District of Columbia v. Organization for Envtl. Growth, Inc., 700 A.2d 185, 198–99 (D.C. App. 1999); Department of General Services v. Harman Assocs., 98 Md. App. 535, 633 A.2d 939, 947 (Md. App. 1993).

[232] United Contractors v. United States, 177 Ct. Cl. 151, 368 F.2d 585, 598 (Ct. Cl. 1966); Bignold v. King County, 65 Wash. 2d 817, 399 P.2d 611, 614 (1965).

[233] *See* note 151 *supra*.

[234] This theory is discussed next in the part dealing with nondisclosure.

[235] 3 VANCE & JONES, *Legal Effect of Representations as to Subsurface Conditions*, SELECTED STUDIES IN HIGHWAY LAW 1471–77.

[236] L. PROSSER & KEETON, HANDBOOK ON THE LAW OF TORTS, ch. 18, at 525, *et seq*. (5th ed. 1984).

evolved in construction law, so that today a contractor may recover for adverse conditions if it can prove that the owner misrepresented the conditions at the site. The general rule is that when statements of fact made by an owner in the contract documents cause a contractor to make a lower bid than it otherwise would have made, the owner is liable for the increased costs caused by those conditions.[237] This rule has been expressed in various ways:

> [W]here plans or specifications lead a public contractor reasonably to believe that conditions represented therein do exist and may be relied upon in bidding, he (contractor) is entitled to compensation for extra expense incurred as a result of the inaccuracy of those representations….[238]

> A contractor…who, acting reasonably, is misled by incorrect plans and specifications issued by public authorities as the basis for bids and who, as a result, submits a bid which is lower than he would have otherwise made may recover in a contract action for extra work or expenses necessitated by the conditions being other than as represented. This rule is mainly based on the theory that furnishing of misleading plans and specifications by the public body constitutes a breach of an implied warranty of their correctness…(citations omitted).[239]

The rule articulated in these cases is a fundamental principle of construction law,[240] and is based on reliance. This was observed by Professor Williston when he said,

> The real issue which should be discussed is this constantly obscured by the terminology of the subject. The real issue is no less than this: When a defendant has induced another to act by representations false in fact although not dishonestly made, and damage has directly resulted from the action taken, who should bear the loss?[241]

The answer is the owner when the following elements are proven:[242]

- Positive representations about physical conditions at the project site. The representations must be material, i.e., basic to the work called for in the contract.
- The contractor must rely on the representations in making its bid. Its reliance must be reasonable.
- The actual conditions that the contractor encounters must differ materially from those represented in the contract.
- The difference between the actual conditions encountered and those represented in the contract must result in damages suffered by the contractor.

An application of these elements is illustrated in the following case. In *Christie v. United States*, there was a representation as to the type of materials that the contractor would excavate in constructing a dam.[243] The representation was material because the excavation was necessary in building the dam. The contractor relied on the representation in figuring its bid. The reliance was justified because there was insufficient time to verify the information by personal investigation. The material encountered was substantially different from that described in the contract and more costly to excavate than the material the contractor expected to encounter. Since these elements were proved, the contractor was able to recover its additional costs.

Recovery, however, has been denied where the court found that there was no factual misrepresentation. For example in *L-J Inc. v. South Carolina State Highway Department*, the court said that each soil boring "was a true revelation of the content of the earth at the 33 sites. The Contractor's problem arises because the borings were misinterpreted. It was assumed that rock lay on a level plane and this assumption was simply erroneous."[244]

A similar result was reached in *Codell Construction v. Commonwealth of Kentucky*, which involved a contract for the construction of 8 miles of Interstate 71.[245] Among the documents provided by the state to prospective bidders was a profile showing the line where rock would be encountered. Printed on the plans and contained in other contract documents were specific disclaimers stating that the information about the rock was solely for the information of the state, and was not to be taken as an indication of classified excavation or the quality of rock that would be encountered. The contractor brought suit claiming an overrun of rock and alleging misrepresentation by the state as to subsurface conditions. In denying recovery, the court said:

> The record does not disclose any misrepresentations of facts or withholding of material information in connection with the drawings, plans, specifications or other data furnished by the Department. The Highway Department, for its own purposes, made tests of the soil conditions and published the results with an express and unqualified disclaimer as to any guarantee of their accuracy. Clearly,

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[237] United States v. Spearin, 248 U.S. 132, 135–36, 395 S. Ct. 59, 63 L. Ed. 166 (1918); E.H. Morrill Co. v. State, 65 Cal. 2d 787, 791, 423 P.2d 551, 56 Cal. Rptr. 479 (1967). Morris Inc. v. State ex rel DOT, 1999 S.D. 95, 598 N.W.2d 525, 523 (S.D. 1999); *Changed Conditions as Misrepresentation in Government Construction Contracts*, 35 GEO. WASH. L. REV. (1967).

[238] Nelson Constr. Co. of Ferndale, Inc. v. Port of Bremerton, 20 Wash. App. 321, 582 P.2d 511, 515 (Wash. App. 1978).

[239] Souza & McCue Constr. Co. v. Superior Court, 57 Cal. 2d 508, 370 P.2d 338, 339–40, 20 Cal Rptr. 634 (Cal. 1962); Fairbanks North Star Borough v. Kandik Constr. & Assoc., 795 P.2d 793, 797 (Alaska 1990); Vinnell Corp. v. State Highway Comm'n, 85 N.M. 311 512 P.2d 71, 77 (N.M. 1973); Jack B. Parson Constr. Co. v. State, 725 P.2d 614, 616 (Utah 1986); Ideker, Inc. v. Mo. State Highway Comm'n, 654 S.W.2d 617 (Mo. App. 1982); P.T. & L. Constr. Co. v. Department of Transp., 108 N.J. 539, 531 A.2d 1330, 1335 (N.J. 1987).

[240] Nelson Constr.*, supra* note 238. Annotation, *Right of Public Contractor to Allowance of Extra Expenses Over What Would Have Been Necessary if Conditions Had Been as Represented by the Plans and Specifications,* 76 A.L.R. 268 (1932).

[241] WILLISTON ON CONTRACTS § 1510, at 462 (3d ed. 1970).

[242] *Supra* note 235.

[243] 237 U.S. 234, 35 S. Ct. 565, 59 Ed. 733 (Ct. Cl. 1915).

[244] 270 S.C. 413, 242 S.E.2d 656, 665 (S.C. 1978).

[245] 566 S.W.2d 161 (Ky. App. 1977).

> this put any bidder on notice as to its obligation to make its own private investigation to determine the classification and quantities of the materials to be excavated.…
>
> The express and unqualified disclaimer…clearly put the bidders on notice of their obligation to make a private investigation. In a situation where the information and representations are intended to be suggestive of construction conditions, or the contract provides that they are to be taken as estimates only, then the governmental agency is not to be held accountable for variances which may be encountered on the job when there is no deliberate misrepresentation or fraud involved. (citations omitted).[246]

The element paramount to recovery is reliance. The contractor must show that it was mislead by the representations. If a reasonably prudent contractor would not have relied on the information in preparing its bid, there can be no recovery for misrepresentation. The question is this: Were the disclaimers about the accuracy of the data sufficiently specific to warn a reasonable contractor not to rely on them in formulating its bid?[247] This question is discussed further in Part Seven (Exculpatory Provisions) of this subsection.

6. Nondisclosure

Generally, the law holds an owner liable for failing to impart its knowledge about the difficulties a contractor may encounter in performing the work.[248] The rule requiring disclosure has been described in various ways. For example, in *Warner Construction Corp. v. City of Los Angeles*, the court said:

> A fraudulent concealment often composes the basis of an action in tort, but tort actions for misrepresentation against public agencies are barred by Government Code section 818.8. Plaintiff retains, however, a cause of action in contract. "It is the general rule that by failing to impart its knowledge of difficulties to be encountered in a project, the owner will be liable for misrepresentation if the contractor is unable to perform according to the contract provisions. This rule is mainly based on the theory that the furnishing of misleading plans and specifications by the public body constitutes a breach of an implied warranty of their correctness. The fact that a breach is fraudulent does not make the rule inapplicable."[249]

In *Hardeman-Monier-Hutcherson v. United States*, the court said: "[W]here the government possesses special knowledge, not shared by the contractor, which is vital to the performance of the contract, the government has a affirmative duty to disclose such knowledge. It cannot remain silent with impunity."[250]

Similarly, the Alaska Supreme Court, in referring to decisions by the United States Court of Claims concerning disclosure, said that:

> We read these cases as establishing the following test for imposing a duty to disclose upon the state: did the state occupy so uniquely-favored a position with regard to the information at issue that no ordinary bidder in the plaintiff's position could reasonably acquire that information without resort to the state? Where resort to the state is the only reasonable avenue for acquiring the information, the state must disclose it, and may not claim as a defense either the contractor's failure to make an independent request or exculpatory language in the contract documents.…[251]

An owner, however, does not have a duty to disclose information that the contractor could reasonably obtain for itself. The contractor "cannot thereafter throw the burden of his negligence (in failing to obtain information) upon the shoulders of the state by asserting that the latter was guilty of fraudulent concealment in not furnishing him with information which he made no effort to secure for himself."[252] In one case, for example, the court held that the State had no duty to disclose information that it obtained from other bidders concerning the feasibility of hydraulic dredging at the project site. The court observed that the contractor could have performed its own tests at the site like other bidders.[253]

In addition to proving that the information that the agency failed to disclose was not reasonably available, the contractor must also prove that it was prejudiced by

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[246] *Id.* at 164.

[247] J.A. Constr. Corp v. Department of Transp., 591 A.2d 1146 (Pa. Commw. 1991); Wunderlich v. State, 65 Cal. 2d 777, 423 P.2d 545, 548–50, 56 Cal. Rptr. 473 (Cal. 1967) ("The crucial question is one of justified reliance."); Joseph F. Trionfo & Sons, Inc. v. Board of Educ., 41 Md. App. 103, 395 A.2d 1207, 1209 (Md. App. 1979).

[248] GAF Corp. v. United States, 932 F.2d 947, 949 (Fed. Cir. 1991); Hercules, Inc. v. United States, 24 F.3d 188, 196 (Fed. Cir. 1994); J. A. Jones Constr. Co. v. United States, 390 F.2d 886 (Ct. Cl. 1968); Warner Constr. Corp. v. City of L.A., 2 Cal. 3d 285, 466 P.2d 996, 1001, 85 Cal. Rptr. 444 (Cal. 1970); Nelson Constr. Co. of Ferndale, Inc. v. Port of Bremerton, 20 Wash. App. 32, 582 P.2d 511, 514–15 (Wash. App. 1978); Hardwick Bros. II v. United States, 36 Fed. Cl. 347, 386 (Ct. Cl. 1996); R.J. Wildner Contracting Co. v. Ohio Turnpike Comm'n, 913 F. Supp. 1031, 1042 (N.D. Ohio 1996); Annotation, *Public Contracts: Duty of Public Authority to Disclose to Contractor Information Allegedly in its Possession, Affecting Cost or Feasibility of Project*, 86 A.L.R. 3d 182 (1978). McDonnell Douglas Corp. v. United States, 182, 3d 1319, 1329 (Fed. Cir. 1999).

[249] 2 Cal. 3d 285, 466 P.2d 996, 1001 85 Cal. Rptr. 444 (Cal. 1970) (citation omitted).

[250] 198 Ct. Cl. 472, 458 F.2d 1364, 1371–2 (Ct. Cl. 1972) (citations omitted).

[251] Morrison-Knudson Co. v. State, 519 P.2d 834, 841, 86 A.L.R. 3d 164 (Alaska 1974).

[252] Wiechmann Eng'rs v. State, 31 Cal. App. 3d 741, 753, 107 Cal. Rptr. 529 (1973); *see also* Nelson Constr., *supra* note 238 (agency not required to provide soils report concerning glacially consolidated soils containing boulders where information about harbor bottom was reasonably available from other sources); Comprehensive Bldg. Contractors, Inc. v. Pollard Excavating, Inc., 251 A.D. 2d 951, 674 N.Y.S.2d 869 (N.Y. A.D. 1998) (depth of sewer available to excavation contractor from subdivision plat).

[253] Morrison-Knudson Co. v. State, 519 P.2d at 842 (Alaska 1974); *but see* Howard Contracting, Inc. v. G. A. MacDonald Constr. Co., 71 Cal. App. 4th 38, 56, 83 Cal. Rptr. 2d 590 (Cal. App. 1998) (city liable for failure to direct bidder to examine permits issued by regulatory agencies, even though bidder knew that agency would impose restrictions on the project).

the nondisclosure. In other words, the contractor must show that its bid would have been different had it seen the information. Failure to make that showing will bar the claim.[254]

Whether there was a failure to disclose vital information, entitling the contractor to recover damages is a jury question.[255] The use of special interrogatories to the jury should be considered. This technique was used successfully by the State in a case where the contractor alleged, among other things, that the State failed to disclose test reports about a pit that the State furnished to the contractor.[256]

7. Exculpatory Provisions

Unless an agency is required by a statute[257] or a regulation[258] to include a DSC clause in its contracts, it may choose to let the risk of unforeseen site conditions remain with the contractor.[259] In making this choice an agency may decide that it would rather pay a contingency for unforeseen conditions than pay for such conditions through litigation. This policy determination is driven by considerations such as budget predictions, the number and size of its projects, and the availability of potential bidders who are willing to assume the risk of unforeseen conditions and factor that risk into their bids. At times, there may be situations where the agency does not know what will be encountered and prefers that the contractor assume those risks and price them competitively as part of its bid. "But once a policy determination is made, it should be enforced by the courts."[260]

When a DSC clause is included in the contract, an agency cannot undermine the clause by also including broad exculpatory provisions that purport to shift the risk of unanticipated conditions to the contractor. Generally, broad exculpatory provisions will simply not be enforced.[261] Most courts view broad exculpatory language, disclaiming liability for DSCs, as contradictory. General statements, which are inconsistent with the intention of the parties as expressed in the DSC clause, will not be enforced.[262] The key to making exculpatory clauses effective is specificity. Specific warnings telling the contractor not to rely on certain information about site conditions should be enforced.

In the absence of a DSC clause, an agency is not liable for unforeseen site conditions unless the contractor was misled by the information provided to prospective bidders,[263] or the agency failed to disclose information about the site that should have been disclosed.[264] To insulate itself from liability for unforeseen site conditions, the agency should: (1) disclose information in its possession about site conditions or tell the prospective bidders where the information can be obtained, and (2) include clear and specific exculpatory clauses in the contract disclaiming responsibility for unforeseen conditions. This latter point is supported by case law, particularly the leading case of *Wunderlich v. State*.[265] *Wunderlich* was a breach of warranty claim by a highway contractor when a state-furnished pit did not provide sufficient material for the project. The contract indicated that there would be certain base material "of satisfactory quality" available for the contractor's use from a private pit that the state had obtained. The specifications disclaimed responsibility for the quantity of suitable material that could be produced from the pit. The contractor claimed that the material was too sandy, requiring the contractor to bring in more equipment and finally to import material from other pits. The contractor claimed the State had misrepresented the actual conditions encountered in the pit and was liable for the

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[254] A.S. Wikstrom, Inc. v. State, 52 A.D. 2d 658, 381 N.Y.S.2d 1010, 1012 (App. Div. 1976) (contractor failed to prove that its bid would have been different had it seen the test borings); Wm. A. Smith Contracting Co. v. United States, 188 Ct. Cl. 1065, 412 F.2d 1325, 1338 (Ct. Cl. 1969) (contractor not misled by failure to disclose information); *see also* Hendry Corp. v. Metro Dade County, 648 So. 2d 140, 142 (Fla. App. 1994).

[255] Horton Indus., Inc. v. Village of MoweAqua, 142 Ill. App. 3d 730, 492 N.E.2d 220, 226, 97 Ill. Dec. 17 (Ill. App. 1986).

[256] Ledcor Indus., et al. v. State of Wash. Dep't of Transp., Thurston County Superior Court No. 92-200085-4.

[257] *See* Department of Gen. Services v. Harmans, 98 Md. App. 535, 633 A.2d 939, 947 (1993) (DSC clause required by statute); 23 U.S.C. § 112 (requiring use of a DSC clause in certain federally-funded state highway construction contracts).

[258] 48 C.F.R. ch. 1, pt. 52.236-2.

[259] Most state agency DSC clauses provide that, "No contract adjustments will be allowed under this clause for any effects caused by unchanged work." *See, e.g.*, Iowa Standard Specifications 1109.16A.4. When procurement laws require that a particular clause be included in a contract, the contract is read as though it contained that clause irrespective of whether the clause was actually written in the contract. G.L. Christian & Assocs. v. United States, 160 Ct. Cal. 1, 312 F.2d 418, 424 (Ct. Cl. 1963); S.J. Amoroso Constr. Co. v. United States, 26 Cl. Ct. 759, 764 (1992); Department of Gen. Services v. Harmans, 98 Md. App 535, 633 A.2d 939, 949 (1993).

[260] P.T. & L. Constr. v. Department of Transp., 108 N.J. 539, 531 A.2d 1330, 1331 (N.J. 1987); S&M Contractors, Inc. v. City of Columbus, 70 Ohio St. 2d 69, 434 N.E.2d 1349, 1351 (Ohio 1982) (argument that enforcing disclaimer is bad public policy rejected); HARP, *supra* note 159. Mr. Harp notes that a "no claims specification" had mixed reviews by the TRB Task Force on Innovative Contracting. The Task Force expressed concern that "no claims" specifications generate additional litigation and greater conflict between the contractor and the agency, and result in an adverse working relationship that could affect the quality and progress of the work. These observations could be urged as additional reasons, besides eliminating contingency bidding, for having a DSC clause in contracts.

[261] Sornsin Constr. Co. v. State, 180 Mont. 248, 590 P.2d 125, 129 (1978); Morris, Inc. v. State ex rel DOT, 1999 S. D. 95, 598 N.W.2d 520, 523 (S.D. 1999); Mass. Bay Trans. Auth. v. United States, 129 F.3d 1226, 1231 (Fed. Cir. 1997).

[262] Morrison-Knudson Co. v. United States, 184 Ct. Cl. 661, 686, 397 F.2d 826 (Ct. Cl. 1968); Haggart Constr. Co. v. Highway Comm'n, 149 Mont. 422, 427 P.2d 686, 689 (Mont. 1967).

[263] *Id*.

[264] 86 A.L.R. 3d 182 (1978).

[265] 65 Cal. 2d 777, 423 P.2d 545, 548 (Cal. 1967).

extra costs incurred in processing material at the pit and in hauling material from more distant sources. The State claimed that what was represented in the contract was accurate based on the tests it had performed. The trial court's decision in favor of the contractor was reversed by the California Supreme Court which, said:

> The crucial question is thus one of justified reliance. If the agency makes a "positive and material representation as to a condition presumably within the knowledge of the government, and upon which…the plaintiffs had a right to rely" the agency is deemed to have warranted such facts despite a general provision requiring an onsite inspection by the contractor. (Citation omitted.) But if statements "honestly made" may be considered as "suggestive only," expenses caused by unforeseen conditions will be placed on the contractor, especially if the contract so stipulates…(citations omitted).

The court concluded that the boring data from the test holes were only indicative of the general area of the pit. There were no positive representations about the quantity of material that could be obtained from the pit. The court emphasized the importance of specific exculpatory language disclaiming any state responsibility for the quantity of acceptable material and requiring the contractor to determine whether there was enough material in the pit for the project.

Briefly stated, the court held that the contractor could not justifiably rely on the information about the sufficiency of suitable material in view of the specific nature of the statements about the quantity of material, the specificity of the exculpatory provisions, and the absence of any misrepresentations about factual matters. Thus, where the statements are not positive representations and the contractor is warned to determine conditions for itself, there is no warranty.

Other states have followed the *Wunderlich* rule, focusing on the lack of positive representations and the specificity of the disclaimer.[266] For example, in *Ell-Dorer Contracting Co. v. State*, the specifications required the contractor:

> [T]o ascertain for himself all the facts concerning conditions to be found at the location of the Project including all physical characteristics above, on, and below the subsurface of the ground, …and to make all necessary investigations….
>
> Borings, test excavations and other subsurface investigations, if any, made by the Engineer prior to construction of the project…are made for use as a guide for design. Said borings, test excavations and other subsurface investigations are not warranted to show the actual subsurface conditions. The contractor agrees that he will make no claims against the State if in carrying out the project he finds that the actual conditions encountered do not conform to those indicated by said borings, test excavations and other subsurface investigations.[267]

The court found that the disclaimers were so specific that the contractor could not justifiably rely on the soils data provided to the bidders. A similar result was reached in *Joseph F. Trionfo & Sons, Inc. v. Board of Education*, where the court enforced an exculpatory clause that provided that the soils information was: (1) not part of the contract, (2) not guaranteed, (3) obtained by the agency for design purposes only, (4) was not to be relied upon by the contractor, and (5) that the contractor should make its own site investigation. [268] The clause also provided that the owner was not responsible if the actual conditions differed from what the contractor expected or from what the soils data indicated.

Other examples are *Biolota Construction Corp. v. Village of Mamaroneck*, in which the specifications stated that the grade elevations shown on the plans were approximate, their accuracy not guaranteed, and that the contractor should make its own site investigation;[269] and *Air Cooling & Energy, Inc. v. Midwestern Construction Company*, in which no implied warranty was found where the boring logs were not part of the contract and the contractor was required to make its own site investigation and told not to rely on the boring logs.[270]

It is important that the specifications specifically disclaim responsibility for the accuracy of the soils data provided to bidders. If this is not done, the disclaimer may not be enforced even though the test borings are not part of the contract.[271] It is also important for the exculpatory clause to disclaim any intention on the part of the owner that bidders should use the soils information in preparing the bid. Absent a disclaimer specifically disclaiming any such intention, a court may find that "the government performs certain basic tests in order to provide each bidder with some information on which he may make his bid."[272]

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[266] Nelson Constr. Co. v. Port of Bremerton, 20 Wash. App, 321, 582 P.2d 511, 515 (Wash. App. 1978); Bilotta Constr. Corp. v. Village of Mamaroneck, 199 A.D. 2d 230, 604 N.Y.S.2d 966 (N.Y. App. Div. 1993); Air Cooling & Energy, Inc. v. Midwestern Constr. Co. of Missouri, Inc., 602 S.W.2d 926, 930 (Mo. App. 1980); L-J, Inc. v. S.C. Highway Dep't, 280 S.C. 413, 242 S.E.2d 656 (S.C. 1978); Joseph F. Trionfo & Sons v. Board of Ed., 395 A.2d 1207, 1213 (Md. App. 1979); S&M Contractors, Inc. v. City of Columbus, 434 N.E.2d 1349, 1353 (Ohio 1982); Gene Hock Excavating, Inc. v. Town of Hamburg, 227 A.D. 2d 911, 643 N.Y.S.2d 268 (N.Y. App. Div. 1996); Sasso Contracting Co. v. State, 173 N.J. Super. 486, 414 A.2d 603, 606, *cert. denied*, 85 N.J. 101, 425 A.2d 265 (N.J. 1980); J.A. Thompson & Sons, Inc. v. State, 51 Haw. 529, 465 P.2d 148, 155 (1970); Frontier Founds., Inc. v. Layton Constr., 818 P.2d 1040, 1042 (Utah App. 1991).

[267] 197 N.J. Super. 175, 484 A.2d 356, 359 (App. Div. N.J. 1984).

[268] 41 Md. App. 103, 395 A.2d 1207, 1209 (Md. App. 1979).

[269] 199 A.D. 2d 230, 604 N.Y.S.2d 966, 967–68 (N.Y. App. Div. 1993).

[270] 602 S.W.2d 926, 930 (Mo. App. 1980).

[271] City of Columbia v. Paul N. Howard Co., 707 F.2d 338, 340 (8th Cir. 1983) (court construed contract to mean that contractor could rely upon the data shown in the borings, but not upon interpolations between borings).

[272] Robert E. McKee, Inc. v. City of Atlanta, 414 Supp. 957, 959 (N.D. Ga. 1976); Morris, Inc. v. State ex rel. DOT, 1999 S.D. 95, 598 N.W.2d 520, 523 (S.D. 1999); Haggart Constr. Co. v. State, 149 Mont. 422, 427 P.2d 686, 687 (Mont. 1967) (State

There are, of course, decisions that decline to enforce exculpatory provisions. The specifications may be viewed as conflicting[273] or ambiguous[274] or unfair because insufficient time was allowed for a reasonable site investigation. With respect to the latter point, there is a split of authority as to the enforceability of exculpatory provisions when insufficient time is allowed for a contractor to conduct its own site investigation. One view is that an agency cannot enforce exculpatory clauses, particularly those requiring a contractor to make its own site investigation, when the time allowed is insufficient.[275] There is authority, however, that insufficient time does not preclude enforceability.[276] This latter view is premised on the notion that contractors are not compelled to bid. If they believe that the time allowed for an adequate site investigation is not sufficient, they can decline to bid, or they can factor the lack of an adequate site investigation into their bids.[277]

In preparing contracts that do not contain DSC clauses, care should be taken to avoid the pitfall of non-disclosure. Care should also be taken to avoid presenting information to bidders in a way that can be construed as positive assertions of fact. Data should be qualified by using words like "approximate" or "estimated" or "for design purposes only," or words of like import. Exculpatory provisions should say in clear and plain language that:

- The soils information is not part of the contract.
- The accuracy or completeness of the soils information is not guaranteed.
- The soils information was obtained only for design purposes.
- The soils information should not be relied upon by bidders in making their bids.
- Bidders should make their own investigations of site conditions. If a bidder believes that the time allowed for the investigation is insufficient, that should be taken into consideration in preparing the bid.
- The owner will not be responsible in any way for additional compensation based on any claim that soils information obtained solely for design purposes and furnished to bidders differed from what the contractor expected to encounter or differed in any way from what the soils information indicated to the contractor concerning subsurface conditions.

Disclaimers that are specific should be enforced.[278] Specific contract provisions trump general provisions.[279] Thus, where the specific disclaimer conflicts with other general contract provisions, the disclaimer should be enforced. Where the disclaimer is clear, unambiguous, and specific, a court may hold that the contractor's reliance on site data was not justified, and that its claim for misrepresentation of site conditions may be dismissed as a matter of law.[280]

8. Subcontractor Claims

Claims for DSCs often originate with subcontractors. This occurs because earth work, such as excavation, embankment construction, pile driving, and site preparation may be sublet by the general contractor. Typi-

admitted at trial that one purpose in furnishing soils data to bidders was to obtain lower bids).

[273] Young-Fehlahaber v. State, 265 A.D. 61, 37 N.Y.S.2d 928, 929 (N.Y. A.D. 1942) (conflict between representation in the plans and the disclaimer in the specifications, resolved in favor of the contractor under the rule that plans take precedence over specifications); Millgard Corp. v. McKee/Mays, 49 F.3d 1070, 1073 (5th Cir. 1995) (specific disclaimer with respect to underground water took precedence over the more general language in the DSC clause). "[G]eneral disclaimers will not absolve defendant for positive and material representations upon which the contractor had a right to rely." Morris, Inc. v. State el rel DOT, 598 N.W.2d 520., 523 (S.D. 1999) (quoting Western States Mech. Contractors, Inc. v. Sandin Corp, 110 N.M. 676, 798 P.2d 1062, 1065 (N.M. App. 1990)).

[274] Ambiguous specifications are construed against the drafter. Metric Constructors, Inc. v. National Aeronautics and Space Admin., 169 F.3d 747, 751 (Fed. Cir. 1999); Van-Go Transport Co. v. N.Y. City Bd. Of Educ., 53 F. Supp. 2d 278, 283 (E.D. N.Y. 1999); Haggart Constr. Co. v. State, 149 Mont. 422, 427 P.2d 686, 689 (1967) (soils data and general disclaimer conflicted, making the contract ambiguous; contract was construed against the State because the State had drafted it).

[275] Kiely Constr. Co. v. State, 154 Mont. 363, 463 P.2d 888, 890 (1970); Yonkers Contracting Co. v. N.Y. State Thruway Auth., 45 Misc. 2d 763, 257 N.Y.S.2d 781, 784 (N.Y. Ct. Cl. 1964); Peter Salvucci & Sons, Inc. v. State, 110 N.H. 136, 268 A.2d 899, 906 (1970); Alpert v. Commonwealth, 357 Mass. 306, 258 N.E.2d 755, 764 (1970) (adequate site investigation would require 2 ½ to 3 months, but only 21 days allowed).

[276] J.E. Brenneman Co. v. Commonwealth, Dep't of Transp., 56 Pa. Commw. 210, 424 A.2d 592, 595 (1981); Central Penn Indus. v. Commonwealth, 358 A.2d 445, 448 (Pa. Commw. 1976). "Insufficiency of the allowed for investigation by bidders, standing alone, will not support a claim for extra compensation for unanticipated site conditions."

[277] Codell Constr. Co. v. Commonwealth, 566 S.W.2d 161, 165 (Ky. App. 1977); Scherrer v. State Highway Comm'n, 148 Kan. 357, 80 P.2d 1105, 1110 (Kan. 1938); McArthur Bros. Co. v. United States, 258 U.S. 6, 42 S. Ct. 225, 66 L. Ed. 433 (1922).

[278] P.T.& L. Constr. v. State Dep't of Transp., 108 N.J. 539, 531 A.2d 1330, 1334 (N.J. 1987). The court acknowledged that the State, for policy reasons, may require the contractor to assume the risk of unforeseen site conditions.

[279] "It is a maxim of interpretation that when two provisions of a contract conflict, the specific trumps the general." Millgard Corp. v. McKee/Mays, 49 F.3d 1070, 1073 (5th Cir. 1995); (specific disclaimer concerning underground water given precedence over more general language in DSC clause). *See also* Vaughn v. Gulf Copper, 54 F. Supp. 2d 688, 690 (E.D. Tex. 1999); Transitional Learning v. United States, 220 F.3d 427, 432 (5th Cir. 2000); Chantilly Constr. Corp. v. Department of Highways, 6 Va. App. 282, 369 S.E.2d 438, 445 (Va. App. 1988).

[280] Frontier Founds., Inc. v. Layton Constr., 818 P.2d 1040, 1041–42 (Utah App. 1991) (where disclaimer is effective as a matter of law, owner is entitled to judgment); Joseph F. Trionfo, 395 A.2d 1207 (Md. App. 1979).

cally, claims for DSCs are presented by the subcontractor to the general contractor who, in turn, passes them on to the owner for resolution. This process was described by the California Court of Appeals in *Howard Contracting v. G.A. MacDonald Construction Co.*

As a matter of law, a general contractor can present a subcontractor's claim on a pass-through basis. When a public agency breaches a construction contract with a contractor, damage often ensues to a subcontractor. In such a situation, the subcontractor may not have legal standing to assert a claim directly against the public agency due to a lack of privity of contract, but may assert a claim against the general contractor. In such a case, a general contractor is permitted to present a pass-through claim on behalf of the subcontractor against the public agency…(citations omitted).[281]

To recover for a DSC (subcontractor versus general contractor), there must be a DSC clause in the subcontract,[282] either expressly or by implication.[283] The *Severin* doctrine, which prevents a general contractor from recovering for its subcontractor against the owner when the prime contractor is not liable to the subcontractor, is discussed in the next section.

9. Impossibility

A contractor is not excused from performing its contract when unforeseen circumstances make performance burdensome.[284] To excuse performance, the contractor must prove that performance was impossible. "Impossibility excuses a party's performance only when the destruction of the subject matter of the contract or the means of performance makes performance objectively impossible. Moreover, the impossibility must be produced by an unanticipated event that could not have been foreseen or guarded against in the contract."[285] (citations omitted).

Impossibility can be either actual or practical. Actual impossibility exists when it is physically impossible for anyone to perform the contract. If another contractor could perform the work, the contractor's own inability to perform is not excused.[286] Practical impossibility exists when the cost of performance is so great that it becomes economically senseless.[287] Impossibility may be raised as a defense by a contractor in an action brought by an owner for breach of contract for the contractor's nonperformance.[288]

To prove practical impossibility, the contractor must show that the cost of performance would be so extreme that it would render further performance economically senseless. Because courts are reluctant to excuse performance, this is usually difficult to prove.[289] Whether an unanticipated event rendered the contract impossible to perform is a factual question.[290]

10. Admissions

Occasionally, a dispute over whether a DSC occurred may threaten to delay the work. To expedite construction, the owner may wish to change the design or make some other modification to allow the work to proceed. If this happens, the change order should be carefully worded to prevent the change order from being used by the contractor as an admission by the owner that a DSC had occurred.[291]

If the contractor will not agree, in a bilateral change order, that the design change is not an admission of a DSC, and if the owner still wishes to make the change, the unilateral change order should be couched in language indicating that the owner denies that a differing site occurred, that it reserves all defenses, waives nothing, and makes the change solely to move the project along rather than have the project delayed because of the dispute. The stronger and more self-serving the language, the less likely the change order will be offered in a lawsuit or arbitration as an admission.

C. DELAY

1. Introduction

Construction work is more susceptible to delay than many other forms of contracting. Variables such as ad-

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[281] 71 Cal. App. 4th 38, 60, 83 Cal Rptr. 2d 590 (1998); *see also* Buckley & Co. v. State, 140 N.J. Super., 289, 356 A.2d 56, 73–74 (N.J. Super. 1975) (cases cited from other jurisdictions holding that lack of privity between the subcontractor and the owner does not bar the subcontractor's pass-through claim when the prime contractor is liable to the subcontractor for damages for which the owner ultimately assumes responsibility).

[282] Dravo Corp. v. Metro Seattle, 79 Wash. 2d 214, 484 P.2d 399 (Wash. 1971).

[283] A flow-down clause in a subcontract incorporates by implication an express DSC clause in the prime contract.

[284] United States v. Spearin, 248 U.S. 132, 135–36 39 S. Ct. 59, 63 L. Ed. 166 (1918); Comprehensive Bldg. Contractors v. Pollard Excavating, Inc., 251 A.D. 2d 951, 674 N.Y.S.2d 869, 871 (N.Y. App. 1998).

[285] Comprehensive Bldg. v. Pollard Excavating, 674 N.Y.S.2d at 871.

[286] Mineral Park Land Co. v. Howard, 172 Cal. 289, 156 P. 458, 459 (1916); Tripp v. Henderson, 158 Fla. 442, 28 So. 2d 857 (1947).

[287] Blount Bros. Corp. v. United States, 872 F.2d 1003, 1007 (Fed. Cir. 1989).

[288] Annotation, *Modern Status of the Rules Regarding Impossibility of Performance as a Defense in an Action for Breach of Contract*, 84 A.L.R. 2d 12 (1962).

[289] Large cost overruns do not necessarily excuse further performance. Campeau Tool & Die Co., ASBCA No. 18,436, 76-1 BCA ¶ 11,653 (1975) (cost overrun of $600,000 on a $1.2 million contract did not amount to commercial impossibility).

[290] Silverite Constr. Co. v. Town of North Hempstead, 259 A.D. 2d 745, 687 N.Y.S.2d 434 (N.Y. A.D. 1999) (Hazardous waste encountered at construction site); Interstate Markings, Inc. v. Mingus Constructors., Inc., 941 F.2d 1010, 1014 (9th Cir. 1991); (jury found that it was not possible to do the work).

[291] Foster Constr. and Williams Bros. C.A. v. United States, 193 Ct. Cl. 587, 435 F.2d 873 (Ct. Cl. 1970).

verse weather conditions, the division of work between the general contractor and its numerous subcontractors, changes to the work ordered by the owner, DSCs, strikes, and other events can delay the original contract completion date.

Most construction contracts contain clauses that deal with delay. The "suspension of work" clause[292] and time extension clauses allow the time for contract completion to be extended when the event that caused the delay is excusable.[293] The "changes" clause and the "differing site conditions" clause (discussed earlier) also provide for time extensions as part of an equitable adjustment.[294]

Determining whether a time extension should be granted can be important. If the delay is not excused, the contract completion date will not be extended and the contractor may be assessed liquidated damages. If, however, it is later determined that the delay was excusable, the owner may face a claim for constructive acceleration for costs incurred by the contractor in making up a delay that should have been excused.

This subsection discusses how delay is usually classified in analyzing delay claims made by a contractor. It also discusses the use of time related clauses, such as a "suspension of work" clause, and the use of "no-pay-for-delay" clauses to minimize exposure for delay damages.[295] Acceleration claims and owner's remedies for delay (liquidated damages and termination for default) complete this subsection.

2. Types of Delay

Some events that may cause delay are usually classified in the contract as excusable, subject to the caveat that the delay was beyond the control or responsibility of the contractor.[296] Acts of God, unavoidable strikes, acts of government, and other *Force Majeure* events are examples.[297] If a delay is not classified in the contract, the delay will be determined as excusable or inexcusable by the law of the jurisdiction that governs the contract.[298]

Contract clauses allocating risk of possible delay between the contractor and the owner provide benefits to owners similar to those provided by a "differing site conditions" clause. Contractors who are promised time extensions, and in some instances monetary relief for specific kinds of delay,[299] will be deterred (if contractors wish to be competitive in bidding work) from including contingencies in their bids for delays that may or may not occur during contract performance.[300] Whether a time extension is warranted is usually determined by analyzing the critical path method (CPM) schedule furnished by the contractor.[301] In general, only delays to work shown on the critical path affect the completion date of the contract,[302] although there is authority to the contrary.[303]

a. Excusable But Noncompensable Delay

Simply put, this type of delay allows a time extension but no monetary relief. To be excusable, the contractor must show that (1) the delay was not foreseeable when the contract was let, (2) the delay was not caused by any act or neglect by the contractor, and (3) the contractor could not have reasonably prevented the delay.[304] If the contractor can establish these criteria, the

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[292] *See, e.g.,* 48 C.F.R. 52.242-14, Suspension of Work Clause.

[293] E. M. Freeman v. Department of Highways, 253 La. 105, 217 So. 2d 166 (La. 1968) (delay excusable, contractor entitled to a time extension). "The grant of an extension of time by the contracting officer carries with it an administrative determination (admission) that the delays resulted through no fault of the contractor." J.D. Hedin Constr. Co. v. United States, 347 F.2d 235, 245 (Ct. Cl. 1965).

[294] These clauses require the owner to grant time extensions, when appropriate, for added or changed work.

[295] How delay damages are computed is discussed in Section Six, which deals with construction claims.

[296] PYCA Indus., Inc. v. Harrison County Waste Water Management Dist., 177 F.3d 351, 361 (5th Cir. 1999).

[297] 3 D.W. HARP, *Liability for Delay in Completion of Highway Construction Contracts*, SELECTED STUDIES IN HIGHWAY LAW, at 1495, 1515-17; J. D. Hedin Constr. Co. v. United States, 408 F.2d 424, 428 (Ct. Cl. 1969).

[298] Highland Constr. Co. v. Stevenson, 636 P.2d 1034, 1037 (Utah 1981) (delay caused by utility relocation not excusable; contractor knew that utility relocation would be carried on simultaneously with its own work); Mount Vernon Contracting Corp. v. State, 56 A.D. 2d 952, 392 N.Y.S.2d 726, 727 (N.Y. A.D. 1977) (delay due to work stoppage caused by court order, where contractor, aware of pending litigation when bids were submitted, not changeable to State.); Arrowhead, Inc. v. Safeway Stores, Inc., 179 Mont. 510, 587 P.2d 411, 413–14 (1978) (severe weather that was normal for winter construction was not a basis for further extension of time beyond that already granted); Reichenbach v. Sage, 13 Wash. 364, 43 Pac. 354, 356 (1896) (delay caused by its subcontractor not excusable); Cooke Contracting Co. v. State, 55 Mich. App. 479, 223 N.W.2d 15, 17–18 (1974) (delay to contractor caused by other state contractors not excusable).

[299] Delay to unchanged work caused by a DSC is compensable under the federal DSC clause but not under most state clauses. See Subsection B.

[300] Foster Constr. C.A. and Williams Bros. Co. v. United States, 193 Ct. Cl. 587, 435 F.2d 873, 887 (Ct. Cl. 1970).

[301] The use of CPM schedules in analyzing claims is discussed in Section Six, *infra*.

[302] Morrison-Knudsen Corp. v. Fireman's Fund Ins. Co., 175 F.3d 1221, 1232 (10th Cir. 1999); Haney v. United States, 230 Ct. Cl. 148, 676 F.2d 584, 595 (Ct. Cl. 1982); Neal & Co., Inc. v. United States, 36 Fed. Cl. 600, 645 (1996).

[303] Howard Contracting, Inc. v. G. A. MacDonald Constr. Co., 71 Cal. App. 4th 38, 83 Cal. Rptr. 2d 590, 597 (Cal. App. 1999) (declining to apply federal rule that only delay to work on the critical path affects the project's completion date).

[304] Carnegie Steel Co. v. United States, 240 U.S. 156, 165, 36 S. Ct. 342, 60 L. Ed. 576 (1916); Morrison-Knudsen Corp v. Fireman's Fund Insurance Co., 175 F.3d 1221-7 (10th Cir. 1999).

contractor is entitled to a time extension. The contractor, however, is not entitled to delay damages unless it can also show that the delay, while excusable, is also compensable.[305]

The most common example of excusable but noncompensable delay is unusually severe weather. Weather is considered as unusually severe when the weather was unforeseeable. If it was foreseeable when the contract was let, it is not unusual and therefore not excusable.[306] When severe weather is not unusual for the time and place where the work is performed, the contractor is required to anticipate severe weather and account for it in its bid.[307] Whether severe weather encountered during construction was normal and to be expected is usually determined by comparing what occurred with weather conditions in prior years.[308]

Proving unusually severe weather is just the first step in seeking a time extension. The contractor must also show that the weather affected the progress of the work and that the effect of the weather on the work could not have been avoided by taking reasonable care to protect the work.[309] In addition, the contractor is usually required to show that the weather affected work on the critical path, causing the contract completion date to be extended.[310]

As a general rule, delay caused by third-party actions that were not foreseeable and could not have been reasonably avoided is normally excusable but not compensable unless the owner has assumed responsibility for such actions in the contract. For example, an owner is not liable for delays to its contractor caused by its other contractors unless the contract imposes a duty upon the owner to coordinate and control the work of other contractors. [311] Thus, where, under the contract, the engineer completely coordinates construction and controls the work, a court may find that the agency has assumed a contractual duty to coordinate the project.[312] A similar result may be reached where the contract is ambiguous with respect to the owner's duty to coordinate the work of multi-prime contractors.[313] The rule that an owner is not vicariously liable for its various contractors applies to utility relocation work. Generally, an owner does not owe a duty to its prime contractor to ensure timely relocation of utilities while the prime is performing its contract.[314] The specifications, however, should clearly provide that any costs resulting from utility relocation, adjustment, or replacement, including delays resulting from such work, shall be at the contractor's expense, and the only remedy for such costs or delay shall be a time extension.[315] If the specification is not clear, it will not be enforced.[316] The rule that the owner is not vicariously liable for third-party actions that delay contract performance applies to labor strikes. Unavoidable strikes are excusable but not compensable.[317]

NYSDOT Standard Specifications provide a listing of noncompensable delays. The provision indicates that "the Contractor agrees to make no monetary request for and has included in his bid prices for the various items of the contract, any extra, addional costs attributable to any delays, inefficiencies or interferences in the performance of the contract caused or attributable to the items set forth below." The provision lists the following noncompensable events:

1. The work of or presence on the contract site of any third party.

2. Delays in processing the work by third parties as indicated in the contract or generally encountered as

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[305] Morrison-Knudsen Corp., *supra* note 302, at 1234 n.8 (to establish excusable delay, the contractor need only prove that the delay was not foreseeable, not within its control, or due to its fault; to show that the delay is also compensable, the contractor must prove that the delay was the government's fault).

[306] Annotation, *Construction Contract Provision Excusing Delay Caused By "Severe Weather,"* 85 A.L.R. 3d 1085.

[307] Arrowhead, Inc. v. Safeway Stores, Inc., 179 Mont. 510, 587 P.2d 411, 414 (1978); McDevitt & Street Co. v. Marriott Corp., 713 F. Supp. 906, 911–12 (E.D. Va. 1989).

[308] Experts usually use a 10-year base for comparison purposes, although the base may be longer or even shorter than 10 years. National Oceanic and Atmospheric Administration (NOAA) records may be used. Robert L. Rich, DOTCAB No. 1026, 82-2 BCA ¶ 15,900 (1982). Other records such as airport records may be used if they are not too far from the project site and reliable. University meteorology professors may make excellent expert witnesses on weather issues.

[309] Titan Pacific Constr. Corp., ASBCA No. 24,148, 87-1 BCA ¶ 19,626 (1987) (light rain had little effect on steel erection in constructing a bridge, but the same weather could have a serious, adverse effect on painting the bridge).

[310] CPM schedules discussed in Section Six, *infra*.

[311] Department of Transp. v. Fru-Con Constr. Corp., 206 Ga. App. 821, 426 S.E.2d 905, 906 (Ga. App. 1992) (DOT was not vicariously liable for delay caused by its various contractors); Cooke Contracting Co. v. State, 55 Mich. App. 479, 223 N.W.2d 15 (Mich. App. 1974) (contractor not entitled to recover damages for delays caused by other contractors).

[312] Department of Transp. v. APAC-Georgia, Inc., 217 Ga. App. 103, 456 S.E.2d 668 (1995). Regarding the duty to coordinate multi-prime construction contractors, *see* Goldberg, *The Owner's Duty to Coordinate Multi-Prime Construction Contractors, a Condition of Cooperations*, 28 Emory L.J. 377 (1979); United States v. Blair, 321 U.S. 730, 737, 64 S. Ct. 820, 88 L. Ed. 1039 (1944).

[313] E.C. Nolan, Inc. v. State, 58 Mich. App. 294, 227 N.W.2d 323, 327 (1975); *Liability for Delay in Completion of Contract*, 3 SUPPLEMENTARY MATERIAL, SELECTED STUDIES IN HIGHWAY LAW 1524-S4-S5.

[314] White Oak Corp. v. Department of Transp., 217 Conn. 281, 585 A.2d 1199, 1204 (1991); Cooke Contracting Co. v. State, 223 N.W.2d at 18.

[315] Highland Constr. Co. v. Stevenson, 636 P.2d 1034, 1037 (Utah 1981).

[316] Peter Kiewit & Sons Co. v. State Highway Comm'n, 184 Kan. 737, 339 P.2d 267, 273–74 (1959); HARP, *supra* note 297.

[317] Olympus Corp. v. United States, 98 F.3d 1314, 1318 (Fed. Cir. 1996). The contract may list "unavoidable strikes" as an excusable delay. PYCA Indus. v. Harrison County, 177 F.3d 351, 361 (5th Cir. 1999).

inherent in the work.

3. Existence of facilities of third parties.

4. Failure to act by any public or governmental bodies.

5. Restraining orders, injunctions caused by contractor's submission, action, or inaction.

6. Labor boycotts or strikes.

7. Shortage of materials or supplies.

8. Climate conditions, storms, floods.

9. Extra work that does not significantly affect overall completion, delays in issuing orders on contract.

10. Any situation within the contemplation of the parties.

11. Award of the contract beyond the 45-day letting date.

The contractor shall be solely compensated by an extension of time, with or wthout engineering charges as appropriate, to complete the performance of the work in accordance with the provisions of 108.02.

b. Excusable and Compensable Delay

Delay is often equated with money. The adage "Time is Money" may have its origin in construction work. When a project is delayed, although work is unchanged, it may be more costly to perform. For those costs to be compensable, the delay must be caused by the owner, and result from an event that is either covered by a contract clause or by the common law dealing with remedies for breach of contract.[318]

The "suspension of work" clause is one of the more significant clauses dealing with delay. The clause was adopted by the Federal Government in 1960,[319] and is currently codified in the FAR.[320] Under this clause, the contractor may be awarded compensation for "*government caused* delays of an unreasonable duration."[321] The clause disallows compensation, however, to the extent that, "other causes" attributable to the contractor "would have simultaneously suspended, delayed, or interrupted contract performance."[322] The delay, however, need not be a government-ordered work stoppage to be compensable. Any unreasonable delay attributable solely and directly to the government will be considered a constructive suspension of work under the clause.[323]

The FHWA requires a "suspension of work" clause in state highway construction contracts that receive federal aid. The federally mandated clause, like the clause used in direct federal contracts (FAR 52.242-14), allows the agency to suspend work without breaching the contract. The suspension does not entitle the contractor to compensation for the delay unless, "the work is suspended or delayed…for an unreasonable period of time (not originally anticipated, customary or inherent in the construction industry)…."[324] What constitutes an "unreasonable" delay is a question of fact based on the circumstances of each case.[325] Under the federal clause (FAR 52.242-14) the delay, to be compensable, must be attributable solely and directly to the government.[326] The federally mandated clause appears to allow compensation for third-party delays, something which the federal clause does not allow. Part (iii) of the federally mandated clause provides for an adjustment (excluding profit) when the suspension was caused by "conditions beyond the control of and not the fault of the contractor, its suppliers, or subcontractors at any approved tier, and not caused by weather…."

Another notable feature is the language in Part (iv) of the federally mandated clause. Delay damages that are excluded under another provision of the contract are not recoverable under this clause.[327] For example, delay to unchanged work caused by a DSC is not compensable under the federally mandated DSC clause (but may be deleted by state transportation agencies). Thus, recovery for such damages would also be excluded under the "suspension of work" clause.

To recover under the federal "suspension of work" clause, the contractor must show that (1) contract performance was delayed, (2) the delay was caused by the government, (3) the delay was for an unreasonable period of time (delay that is not unreasonable in duration is not compensable), and (4) the contractor incurred additional expense because of the delay.[328] The contractor is entitled to an equitable adjustment for both written and constructive (oral) suspended work orders under the federal clause. The concept of a "constructive suspension," however, has been rejected by one court as inconsistent with a contract requirement that an order delaying or suspending work must be in writing and signed by an authorized representative of the owner.[329]

The Changes clause and the DSC clause provide for time extensions in addition to compensation for changes to the work ordered by the owner, or caused by a DSC. Whether delays resulting from such changes are compensable depends upon how the contract is written. The federal clauses provide for an equitable adjustment in the contract price for an increase in the cost of performing unchanged work resulting from the change or the

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[318] Jensen Constr. Co. v. Dallas County, 920 S.W.2d 761, 770 (Tex. App. 1996); Morrison-Knudsen Corp. v. Fireman's Fund Ins. Co., 175 F.3d 1221, 1232 (10th Cir. 1999).

[319] Hoel-Steffen Constr. Co. v. United States, 197 Ct. Cl. 561, 456 F.2d 760, 763 n.2 (Ct. Cl. 1972).

[320] 48 C.F.R. 52.242-14.

[321] Beauchamp Constr. Co. v. United States, 14 Ct. Cl. 430, 436–37 (1988) (emphasis original).

[322] *Id*. at 437.

[323] John A. Johnson & Sons v. United States, 180 Ct. Cl. 969, 984–85 (Ct. Cl. 1967); Mega Constr. Co. v. United States, 29 Fed. Cl. 396, 424 (1993).

[324] *Id.*

[325] Commercial Contractors, Inc. v. United States, 29 Fed. Cl. 654, 662 (1993).

[326] Beauchamp Constr. Co., *supra* note 321, at 437.

[327] See Subsection B of this Section.

[328] Melka Marine, Inc. v. United States, 38 Fed. Cl. 545, 546 (Fed. Cl. 1997).

[329] Bonacorso Constr. Corp. v. Commonwealth, 41 Mass. App. Ct. 8, 668 N.E.2d 366, 367 (1996).

DSC. Most DSC clauses used by the states and the federally-mandated DSC clause[330] bar delay damages. Those clauses provide that no contract adjustments will be allowed for any effects on unchanged work.

The possible claims that a contractor may have against an owner for delay damages vary. The claim may be based on a specific contract clause entitling the contractor to additional compensation because of owner delay. The Changes clause is one example. The claim, in the absence of a specific, controlling contract clause,[331] may be based on breach of contract for the owner's failure to perform some express contract obligation, or for the owner's actions or inactions that hinder or delay performance. Claims based on the latter theory may result from a myriad of situations.

The NYSDOT provision permits delay compensation arising from differing site conditions, significant change in the character of the work, and suspension of the work and for situations not referenced in the noncompensable items listed in 109.04 B and not within the contemplation of the parties at the time the contract was entered into.[332]

As a matter of law, there is an implied covenant in every contract that the parties will deal fairly and in good faith.[333] Equally basic is the principle that the owner will not hinder or delay the contractor in performing the contract.[334] This principle is almost universally accepted as a matter of general contract law.[335] An owner's failure to provide the contractor with the work site, or an owner's interference with the use of the work site, are examples of acts or omission that hinder or delay the contractor, resulting in delay that is excusable and compensable.[336]

c. Inexcusable Delay

Inexcusable delays are delays for which the contractor assumes sole responsibility. Generally, inexcusable delay occurs in one of two ways. The first category involves delays caused by the fault or negligence of the contractor. An example of this type of delay is the contractor's failure to provide sufficient resources to perform the work.[337] Another example is delay caused by the contractor's failure to plan and coordinate the work of its subcontractors.[338] The second category involves delays that result from events for which the contractor assumes responsibility. Adverse weather that is not unusually severe is an example of that kind of delay. The law requires the contractor to consider the effects of normal weather, although severe, when it calculates its bid.[339]

A contractor is not entitled to a time extension if the delay is inexcusable.[340] In addition, the contractor may be liable for damages for breach of contract if the delay caused the contract completion date to be postponed.[341] The contractor must also take reasonable steps to avoid or reduce the delay. A contractor who fails to take such steps may be liable for liquidated damages caused by the delay.

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[330] See Subsection B of this Section.

[331] See Subsection A of this Section.

[332] NYSDOT Standard Specifications § 108.04 Delay Provisions, A. Compensable delays (2010).

[333] State v. Transamerica Premier Ins. Co., 856 P.2d 766, 774 (Alaska 1993); Howard Contracting v. McDonald Constr., 71 Cal. App. 4th 38, 83 Cal. Rptr. 2d 590, 596 (Cal. App. 1998) (implied coverant to provide timely access and facilitate performance); United States v. Metric Constructors, Inc., 325 S.C. 129, 480 S.E.2d 447, 450 (S.C. 1997); J&B Steel Contractors, Inc. v. C. Iber & Sons, Inc., 162 Ill. 2d 265, 642 N.E.2d 1215, 1222 (Ill. 1994).

[334] Urban Masonary Corp. v. N&N Contractors, Inc., 676 A.2d 26, 36 (D.C. 1996); Neal & Co. v. United States, 36 Fed. Cl. 631 (Ct. Cl. 1996); SIPCO Services & Marine, Inc. v. United States, 41 Fed. Cl. 196, 216 (Fed. Cl. 1998); Lester N. Johnson Co. v. City of Spokane, 22 Wash. App. 265, 588 P.2d 1214, 1217 (1978).

[335] Maine apparently is an exception. *See* Claude Dubois Excavating, Inc. v. Town of Kittery, 634 A.2d 1299, 1302 (Me. 1993).

[336] Department of Transp. v. Arapaho Constr., 257 Ga. 299, 357 S.E.2d 593, 595 (1987); Southern Gulf Indus., Inc. v. Boca Ciega San. Dist., 238 So. 2d 458, *cert. denied*, 240 So. 2d 813 (Fla. 1970) (failure to provide right of way); Grant Constr. Co. v. Burns, 92 Idaho 408, 443 P.2d 1005, 1011 (1968).

[337] John F. Miller Co. v. George Fichera Constr. Corp., 7 Mass. App. Ct. 494, 7 Mass. App. Ct. 494, 388 N.E.2d 1201 (1979).

[338] Reichenbach v. Sage, 13 Wash. 364, 43 Pac. 354, 356 (Wash. 1896); Space Communications Etc., ASBCA No. 9805, 65-1 BCA ¶ 4726 (1965).

[339] *See* "Excusable But Noncompensable Delay," *supra* note 305.

[340] Morrison Knusen Corp. v. Fireman's Fund Ins. Co., 175 F.3d 1221, 1234 n.8 (10th Cir. 1999) (only delays that are not foreseeable, not within the contractor's control, or not due to its fault are excusable).

[341] 3 D.W. HARP, *Liability for Delay in Completion of Highway Construction Contracts*, SELECTED STUDIES IN HIGHWAY LAW 1495, 2495, 1508-9. *See generally* Annotation, *Contractual Provisions for Per Diem Payment for Delay in Performance as One for Liquidated Damages or Penalty*, 12 A.L.R. 4th 891 (1982).

d. Concurrent Delay

Concurrent delay occurs when two or more independent events take place at the same time during contract performance, causing an activity or activities on the critical path to be delayed and resulting in a single, overall delay to project completion.[342] Where both the owner and the contractor contribute to the delay, neither can recover damages from the other, unless there is a clear apportionment of the delay attributable to each party.[343]

There is some authority that a court should approximate the delay in the nature of a jury verdict. The trial court, however, cannot guess at apportionment—delay must be apportioned in a way that is not too speculative and is supported by some evidence.[344] The modern trend is to segregate delays using a CPM analysis and allocate the delay to the party responsible for the delay.[345] But if the delays are so intertwined that they cannot be apportioned without resorting to speculation, then the general rule proscribing apportionment will apply. "The general rule is that 'where both parties contribute to the delay, neither can recover damages, unless there is in the proof a clear apportionment of the delay and expense attributable to each.'"[346]

3. Early Completion

A contractor may claim damages for delay contending that the owner prevented it from completing the contract earlier than scheduled. As a general rule, an owner has no implied duty to aid the contractor in completing its contract prior to the completion date specified in the contract.[347] However, an owner does have a duty not to hinder or prevent the contractor from completing its contract earlier than scheduled.[348] In *Metropolitan Paving Co. v. United States*, the court said:

> While it is true that there is not an "obligation" or "duty" of defendant to aid a contractor to complete prior to completion date, from this it does not follow that defendant may hinder and prevent a contractor's early completion without incurring liability. It would seem to make little differences whether or not the parties contemplated an early completion…Where defendant is guilty of "deliberate harassment and dilatory tactics" and a contractor suffers damages as a result of such action, we think that defendant is liable.[349]

A "no-damage-for-delay" clause should bar an early completion delay claim unless the delay falls within one of the exceptions to enforceability of the clause discussed next in Part 4. For example, New York State has a provision that provides that:

> In the event the Contractor completes the work prior to the contract completion date set forth in the proposal, even if he informs the Department of his intention to complete early or submits a schedule depicting early completion, the Contractor hereby agrees to make no claim for extra costs due to delays, interferences or inefficiencies in the performance of the work….[350]

Most construction contracts require the contractor to submit a schedule showing how the project will be completed on time. Occasionally, contractors submit schedules showing a completion date earlier than required by the contract. There is a desire to accept a schedule showing early completion, since it is usually in the owner's interest to have the project completed early. This can also be a concern. By accepting a schedule showing early completion, the owner implies that the schedule is realistic. This can come back to haunt an owner when faced with an early completion delay claim. To avoid this dilemma, owners may consider including a "no-damage-for-delay" clause like the one quoted earlier. The owner may also reject schedules that are patently unreasonable.

The Ohio DOT has developed a process to approve early completion schedules via a change order, which also revises the contract completion date and the date liquidated damages may commence. The Ohio provision, ODOT Construction and Material Specifications (CMS) 2010, 108.02.B, provides:

> 2. Early Completion Schedule. An Early Completion Schedule is defined as a baseline schedule or update schedule which anticipates completion of all work prior to the Completion Date established by the contract documents and the Contractor submits as an Early Completion Schedule. In the event that an Early Completion Schedule is accepted, the Engineer will initiate a change order amending the Completion Date to the finish date shown on the accepted Early Completion Schedule. The amended Completion Date will be effective upon execution of that change order and all contract provisions concerning the Completion Date such as incentives, disincentives, excusable delays, compensable delays, and

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[342] Mega Constr. Co. v. United States, 29 Fed. Cl. 396, 424 (Fed. Cl. 1993).

[343] William F. Klingensmith, Inc. v. United States, 731 F.2d 805, 809 (Fed. Cir. 1984); Buckley & Co. v. State, 40 N.J. Super., 289, 356 A.2d 56, 71 (N.J. 1975); L.A. Reynolds Co. v. State Highway Comm'n, 155 S.E.2d 473, 482 (N.C. 1967); Mega Constr. Co. v. United States, 29 Fed. Cl. 396, 424 (1993).

[344] Grow Constr. Co. v. State, 56 A.D. 2d 95, 391 N.Y.S.2d 726, 729, "Liability of building or construction contractor for liquidated damages for breach of time limit whose work is delayed by contractee or third persons" (App. Div. 1977); Annotation, 152 A.L.R. 1349, 1359–78 (1944).

[345] District of Columbia v. Kora & Williams Corp., 743 A. 2d 682, 691–92 (1999).

[346] Mega Constr. Co. v. United States, 29 Fed. Cl. 396, 424 (1993) (quoting William F. Klingensmith, Inc. v. United States, *supra* note 343); Blinderman Constr. Co. v. United States, 695 F.2d 552, 559 (Fed. Cir. 1982); Coath & Gass, Inc. v. United States), 101 Ct. Ct. 702, 714–15 (1944).

[347] United States v. Blair, 321 U.S. 730, 64 S. Ct. 820, 88 L. Ed 559 (1944).

[348] Housing Auth. of City of Texarkana v. E. W. Johnson Constr. Co., 1039, 264 Ark. 523, 573 S.W.2d 316, 323 (1978); Grow Constr. v. State, 56 A.D. 2d 95, 391 N.Y.S.2d 726, 729 (N.Y. A.D. 1969); State v. Cherry Hill Sand & Gravel Co., 51 Md. App. 29, 443 A.2d 628, 634 (1982).

[349] 163 Ct. Cl. 420, 325 F.2d 241 (1963).

[350] New York DOT Standard Specifications 102-17, art. 13 (1995).

liquidated damages will be measured against the amended Completion Date. The Contractor may elect not to execute the change order amending the Completion Date; however, in so doing, the Contractor waives its rights to delay damages in meeting the projected early Completion Date.

4. Delay Compensation, "No-Damage-for-Delay" Clauses, and Case Law

In an effort to reduce claims, owners will often include "no-damage-for-delay" clauses in their construction contracts. These exculpatory clauses preclude damages for owner-caused delay, limiting the contractor's sole remedy to a time extension. Generally, such clauses are valid and enforceable.[351] A typical clause provides that a contractor's sole remedy for delay is a time extension, and that the contractor is not entitled to any compensation from the owner for any damages caused by the delay.[352] The "no-damage-for-delay" clause may be combined with a clause providing for time extensions.

> If delays are caused by acts of God, acts of Government, unavoidable strikes, extra work, or other causes or contingencies clearly beyond the control or responsibility of the Contractor, the Contractor may be entitled to additional time to perform and complete the Work…The Contractor agrees that he shall not have or assert any [sic.] claim for, nor shall he be entitled to any additional compensation or damages on account of such delays.[353]

The law on the validity of "no-pay-for-delay" clauses varies from state to state. All jurisdictions agree that, because such clauses are exculpatory in nature and have harsh results, they will be strictly construed.[354] Therefore, in drafting this type of clause it is important to make sure that the clause is clear and unambiguous.[355] It is also important to make sure that the clause

The rule that "no-damage-for-delay" clauses are enforceable is subject to the following exceptions: (1) where the delay was not contemplated by the parties to the contract; (2) where the delay was caused by fraud, gross negligence, or active interference; and (3) where the delay is so unreasonable that it is tantamount to an abandonment of the contract.[356]

a. Delay Not Contemplated by the Parties

Under this exception, delay is not barred by the clause if the delay was not contemplated by the parties. This exception is based on the premise that if the delay was not contemplated, the contractor could not waive a delay that it had not considered in making its bid.[357] "It can hardly be presumed…that the contractor bargained away his right to bring a claim for damages resulting from delays which the parties did not contemplate at the time."[358]

As discussed previously, NYSDOT Standard Specifications provide a laundry list of delays that are contemplated by the parties and categorized as noncompensable.

Other decisions enforcing the clause have not required that the delay be contemplated.[359] Observing that unforeseen delay was the sort of delay that the clause was designed to cover, the court in *City of Houston v. R. W. Ball Const. Co.,* said:

> The clause does not limit its application to those delays and hindrances that were foreseen by the parties when they entered into the contract. Instead, it embraces all delays and hindrances which may occur during the course of the work, foreseen and unforeseen. Indeed, it is the unforeseen events which occasion the broad language of the clause since foreseeable ones could be readily provided for by specific language.[360] (citations omitted)

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[351] Annotation, *Validity and Construction of "No Damage Clause" with Respect to Delay in Building or Construction Contract*, 74 A.L.R. 3d 187 (1976); Beltrone Constr. Co. v. State; 256 A.D. 992, 682 N.Y.S.2d 299, 300 (1998).

[352] L & B Constr. Co. v. Ragan Enters., Inc., 267 Ga. 809, 482 S.E.2d 279, 282 (1997).

[353] PYCA Indus. v. Harrison County Waste Water Mgmt. Dist., 177 F.3d 351, 361 (5th Cir. 1999) (emphasis in original).

[354] Little Rock Wastewater Utility v. Larry Moyer Trucking, Inc., 321 Ark. 303, 902 S.W.2d 760, 765 (1995); WILLISTON ON CONTRACTS, § 602A (3d ed.). Contract provisions aimed at relieving a party from the consequences of its own faults are strictly construed. Such clauses, however, are valid as long as they comply with the rules governing the validity of contracts. 74 A.L.R. 3d 187, 200 at § 2(a) (1976). Such clauses are risk-shifting provisions in which the contractor assumes the risk of owner caused delay. Green Int'l, Inc. v. Solis, 951 S.W.2d 384, 386 (Tex. 1997).

[355] *See, e.g.*, Borden v Phillips, 752 So. 2d 69, 73 (2000).

[356] PYCA Indus. v. Harrison County, *Id.* at 364; Corinno Civetta Constr. Co. v. City of N.Y., 67 N.Y.2d 297, 493 N.E.2d 905, 907–08 502 N.Y.S.2d 681 (N.Y. 1986); United States v. Metric Constructors., Inc., *Id*. at 448; United States ex rel. Evergreen Pipeline v. Merritt-Meridan Pipetime Constr. Corp., 890 F. Supp. 1213, 1221 (S.D. N.Y. 1995) (applying New York law).

[357] Corinno Civetta Constr. Co. v. City of N.Y., *Id*. at 911; United States ex rel. Evergreen Pipeline v. Merritt, 890 F. Supp. 1213 (S.D. N.Y. 1995) (applying New York state law); J & B Steel Contr. v. C. Iber & Sons, 246 Ill. App. 3d 523, 617 N.E.2d 405, 411; 187 Ill. Dec. 97 (Ill. App. 1993), *aff'd*, 162 Ill. 2d 265, 642 N.E.2d 1215, 205 Ill. Dec. 98 (1994); PYCA Indus. v. Harrison County, *Id*. at 362; Department of Transp. v. Arapaho Constr., Inc., 257 Ga. 269, 357 S.E.2d 593, 594 (1987).

[358] Corinno Civetta Constr. Co. v. City of N.Y., 67 N.Y.2d 297, 493 N.E.2d 905, 910 502 N.Y.S.2d 681 (1986).

[359] State Highway Admin. v. Greiner Eng'g Sciences, Inc., 83 Md. App. 621, 577 A.2d 363, 367–68 (Md. App. 1990); John E. Gregory and Son, Inc. v. A. Guenther & Sons Co., 148 Wis. 2d 298, 432 N.W.2d 584, 586–89 (1988); Edward E. Gillen Co. v. City of Lake Forest, 3 F.3d 192, 194 (7th Cir. 1993); Western Eng'rs v. State, 20 Utah 2d 294, 437 P.2d 216, 217–18 (1968). United States v. Metric Constructors, Inc., 325 S.C. 129, 480 S.E.2d 447, 450 (1997).

[360] 570 S.W.2d 75, 78 (Tex. Civ. App. 1978).

b. Delay Caused by Bad Faith, Gross Negligence, or Active Interference

Under this exception, damages for delays are not barred by the clause if the delay is caused by bad faith,[361] gross negligence,[362] or active interference with the contractor's efforts to perform the contract.[363] This exception is based on the principle that such conduct violates the obligation of good faith and fair dealing implicit in the contract,[364] and would allow the owner to avoid the consequences of its wrongful acts.[365]

c. Abandonment

Some courts recognize an exception to a "no-damage" clause where the delays are so unreasonable in length that they amount to an abandonment of the contract by the owner.[366] Other courts do not recognize this exception and enforce the clause,[367] although delays that are unreasonable in duration and prevent the contractor from performing the contract may justify treating the contract as ended.[368] In those jurisdictions where this exception is recognized, the question of whether the delay is of sufficient duration to constitute abandonment is factual.[369]

Contractors, in an effort to avoid the application of a "no-damage" clause, have argued that courts should declare such clauses void and contrary to public policy because they are unfair and inflate bids. Generally, this argument has not been successful. For example, in *Christiansen Bros., Inc. v. State,* the contractor was delayed by design errors and by other contractors performing change orders.[370] The trial court determined the amount of damages caused by the delay, but denied judgment to the contractor because of the "no-damages-for-delay" clause in the contract.[371] On appeal, the contractor argued that such clauses are contrary to public policy because they inflate bids and are unconscionable. The court held that the clause was valid, and that more forceful considerations of public policy outweighed the argument that the clause was unfair and inflated bids. In this regard, the court said:

> In a construction project of the magnitude of the WSU structure, some delays are inevitable. Costs attributable to such delays must be borne by either the owner or the contractor. By allowing the owner to preclude damages at the outset, the contractor may raise the price of his bid so as to take into account delay costs. By this method, the owner is able to know more accurately the total cost of a building at the outset and does not have to worry about "hidden costs" in the form of damages which do not arise until the project is substantially underway. The constituents of a municipality or of the state will also know the costs of a particular project prior to embarking on the construction. The contractor is protected because it knows in advance of bidding that it cannot recover for damages for delay and will bid accordingly….[372]

Following the court's decision in *Christiansen Bros*., the Washington State Legislature enacted a statute prohibiting "no-pay-for-delay" clauses in both public and private contracts.[373] In 1990, Missouri enacted legislation prohibiting such clauses in public works contracts.[374] The prohibition does not apply to contracts

[361] Halloway Constr. Co. v. Department of Transp., 218 Ga. App. 243, 461 S.E.2d 257 (1995); Owen Constr. Co. v. Iowa State Dep't of Transp., 274 N.W.2d 304, 308 (1979); White Oak Corp. v. Department of Transp., 217 Conn. 281, 585 A.2d 1199, 203–04 (1991); State Highway Admin. v. Greiner Eng'g Sciences, Inc., 83 Md. App. 621, 577 A.2d 363 (1990); 74 A.L.R. 3d 187, 215–16 § 7(b). In Kalisch-Jarcho, Inc. v. City of N.Y., 58 N.Y.S.2d 397, 448 N.E.2d 413, 467 N.Y.S.2d 746 (N.Y. 1983), the court approved a jury instruction that required the contractor to prove that, "the city acted in bad faith and with deliberate intent delayed the [contractor] in the performance of its obligation." 448 N.E.2d at 418.

[362] State Highway Admin. v. Greiner Eng'g Sciences, Inc., 577 A.2d 363 (Md. App. 1990); White Oak Corp. v. Department of Transp., 585 A.2d 1199, 1203–04 (Conn. 1991); Gust K. Newberg, Inc. v. Illinois State Toll Highway Auth., 153 Ill. App. 3d 918, 506 N.E.2d 658, 665, 106 Ill. Dec. 858 (1987).

[363] Newberry Square Dev. Corp. v. Southern Landmark, Inc., 578 So. 2d 750, 752 (Fla. App. 1991); Owen Constr. Co. v. Iowa State Dep't of Transp., 274 N.W.2d 304, 307 (Iowa 1979); Christiansen Bros. v. State, 90 Wash. 2d 892, 586 P.2d 840, 844 (1978) (unconscionability defense); United States v. Metric Constructors, Inc., 480 S.E.2d 447, 449 (S.C. 1997) (adopting this exception).

[364] Lewis-Nicholson, Inc. v. United States, 213 Ct. Cl. 192, 550 F.2d 26, 32 (Ct. Cl. 1977).

[365] J & B Steel Contractors, Inc. v. C. Iber and Sons, Inc., 162 Ill. 2d 265, 642 N.E.2d 1215, 1222, 205 Ill. Dec. 98 (1994).

[366] Corinno Civetta Constr. Co. v. City of N.Y., 67 N.Y.2d 297, 493 N.E.2d 905, 912, 502 N.Y.S.2d 681 (1986) ("No-Damage" clause did not apply to delay that was so excessive and unreasonable as to be beyond the contemplation of the parties); United States v. Metric Constructors, Inc., 325 S.C. 1, 480 S.E.2d 447, 449–50 (1997); 74 A.L.R. 3d 187, 226–231, 7(i), (1976).

[367] State Highway Admin. v. Greiner Eng'g Sciences, Inc., 83 Md. App. 621, 577 A.2d 363, 370 (Md. App. 1990) (clause barred delay of over 4 years); Dickinson Co. v. Iowa State Dep't of Transp., 300 N.W.2d 112, 114–15 (Iowa 1981) (2-year delay).

[368] Gust K. Newberg, Inc. v. Illinois State Toll Auth., 153 Ill. App. 3d 918, 506 N.E.2d 658, 665, 106 Ill. Dec. 858 (1987) ("no-damage" clause enforced); Southern Gulf Utils., Inc. v. Boca Ciega San. Dist., 238 So. 2d 458 (Fla. 1970) ("no-damage" clause not enforced); Merritt-Chapman & Scott Corp. v. United States, 108 Ct. Cl. 639, 528 F.2d 1392, 1399 (Ct. Cl. 1976) ("no-damage" not enforced); Buckley & Co. v. State, 140 N. J. Super. 289, 356 A.2d 56, 61–62 (N.J. Super. 1975) ("no-damage" clause not enforced); *see also* United States v. Merritt Meridian Constr. Corp., 95 F.3d 153, 167 (2d Cir. 1996).

[369] Hawley v. Orange County Flood Control Dist., 211 Cal. App. 2d 708, 716–17, 27 Cal. Rptr. 478 (Cal. App. 1983).

[370] 90 Wash. 2d. 872, 586 P.2d 840 (Wash. 1978).

[371] The court determined the amount of damages caused by the delay in case its decision on liability was reversed on appeal. *Id*. at 842.

[372] *Id*. at 844.

[373] WASH. REV. CODE 4.24.360 (1988).

[374] MO. REV. STAT. 34.058 (2001).

between private parties.[375] The Missouri statute provides that:

> Any clause in a public works contract that purports to waive, release, or extinguish the rights of a contractor to recover costs or damages,…for delays in performing such contract, if such delay is caused in whole, or in part, by acts or omissions within the control of the contracting public entity or persons acting on behalf thereof, is against public policy and is void and unenforceable.[376]

Other states have enacted similar legislation as depicted in the following table.

[375] Roy A. Elam Masonary, Inc. v. Fru-Con Constr. Corp., 922 S.W.2d 783, 790 (Mo. App. E.D. 1996).

[376] *Supra* note 374.

State	Applies To Public Contracts	Applies To Private Contracts	Reference
California	Yes	No	CAL. PUB. CONT. CODE § 7102 (1985)
Colorado	Yes	No	COLO. REV. STAT. § 24-91-103.5 (1991)
Kansas	Yes	No	KAN. STAT. ANN. § 16-1907 (2008)
Kentucky	Yes	Yes	KY. REV. STAT. § 371.405 (2)(c) (2007)
Louisiana	Yes	No	LA. REV. STAT. ANN. § 38.2216(H) (1990)
Minnesota	Yes	Yes	MINN. STAT. 15.411 SUB 2 (2013)
Missouri	Yes	No	MO. REV. STAT. 34.0582.2 (2000)
Montana	Yes		MONT. CODE ANN. § 28-1,1301 (2013)
North Carolina	Yes	No	N.C. GEN. STAT. § 143-134.3 (1997)
North Dakota	Yes	No	N.D. CENT. CODE § 9-08-02.1 (1999)
Ohio	Yes	Yes	OHIO CODE ANN. § 4113.62 (C)(1) (1998)
Oregon	Yes	No	OR. REV. STAT. § 279.063 (1985)
Virginia	Yes	No	VA. CODE ANN. § 2.2-4335 (A) (1991)
Washington	Yes	Yes	WASH. REV. CODE § 4.24.360 (1979)

Despite numerous cases to the contrary, these statutes are based on the premise that "no-pay-for-delay" clauses violate public policy. Those who advocate this view argue that such clauses are unfair. Are such clauses unfair? The language used by the Supreme Court in *Wells Bros. Co. v. United States* is instructive.

> Men who take million-dollar contracts for government buildings are neither unsophisticated nor careless. Inexperience and inattention are more likely to be found in other parties to such contracts than the contractors, and the presumption is obvious and strong that the men signing such a contract as we have here protected themselves against such delays as are complained of by the higher price exacted for the work.[377]

5. Subcontractor Delay

A "no-pay-for-delay" clause may be expressly incorporated in a subcontract, or it may be incorporated by reference through the subcontractor's "flow-down" clause.[378] Whatever its form, the clause is subject to the same rules and exceptions that apply to such clauses in contracts between an owner and a general contractor.[379] However, the clause will be enforced between the general contractor and its subcontractor so long as the clause meets the ordinary rules governing contracts and does not fall within one of the exceptions that prevent enforceability. For example, in *L & B Construction Co. v. Ragan Enterprises*, a clause in the subcontract provided that, "[s]hould subcontractor be delayed in the work by contractor then contractor shall owe subcontractor therefor only an extension of time for completion equal to the delay…."[380] The use of the word "only" limited the subcontractor's remedy to an extension of time. Damages for the delay were not allowed.

Clauses precluding subcontractor claims become important to owners when the prime contractor attempts to pass the claim along to the owner for delays that the

[377] 254 U.S. 83, 84, 41 S. Ct. 34, 65 L. Ed. 148 (1920).

[378] Pete Scalamandre & Sons v. Village Dock, 187 A.D. 2d 496, 589 N.Y.S.2d 191 (1992).

[379] Port Chester Elec. Constr. Corp. v. HBE Corp., 894 F.2d 47, 49 (2nd Cir. 1990).

[380] 267 Ga. 809, 482 S.E.2d 279, 280 (1997).

owner caused. If the clause bars the subcontractor's claim against the contractor for delay,[381] the claim cannot be passed through to the owner even though the owner caused the delay.[382] The clause may also extend to and protect the owner's architect/engineer as a third-party beneficiary of the owner's construction contract with the contractor.[383] The limitations on pass-through claims and the *Severin* doctrine are discussed in the next section.

6. Notice of Delay

Most construction contracts contain provisions requiring the contractor to notify the owner, in writing, when the contractor claims that it has been delayed and seeks a time extension, or additional compensation for the delay.[384] Notice serves several purposes. It allows the owner to verify the contractor's claim and document the contractor's costs. It also allows the owner to explore alternatives such as termination for convenience if the delay could be extensive.[385]

There is ample authority that failure to provide written notice, as required by the contract, will bar the claim.[386] There is, however, authority to the contrary. These cases hold that written notice is not required when the owner had actual notice of the delay,[387] or the government was not prejudiced or disadvantaged by lack of notice.[388] These views focus more on the purpose of the clause than on a literal and strict construction of its language.[389]

Whether oral notice was given, or whether the owner knew about the delay is often disputed. Requiring strict compliance with the notice requirements of the contract eliminates those types of disputes. This is of particular importance when the issue of whether oral notice was given, or the owner knew about the delay, is being litigated years after the project has been completed. These are questions of fact.[390] Written notice requirements, like other contract provisions, can be waived.[391] This may occur, for example, by granting time extensions that have not been requested by the contractor and by not assessing liquidated damages.[392]

New York has also developed significant case law on strict enforcement of notice and recordkeeping contract provisions. Following the decision in *A.H.A. Gen. Constr. v. New York City Hous. Auth.,*[393] New York courts have continued the practice of dismissing litigation due to contractor failure to provide notice and submit contemporaneous cost records that are required by the contract. NYSDOT Standard Specifications Section105.14 provides that "Disputes of any nature shall be made in strict accordance with the contract provisions, including the notice and recordkeeping provisions of section 104.06 Notice and Recordkeeping, which are condition precedent for any recovery." The N.Y. Court of Claims, in *Di-Pizio Construction Co. Inc. v. State of New York*, dismissed the claim on the grounds claimant failed to give notice and provide contemporaneous cost records concerning the expenses incurred.[394] Similarly, the N.Y. Court of Claims, in *Baker Heavy Highway Construction, Inc. v. N.Y. State Thruway Authority,* stated that claimants' falure to comply with the reporting provisions of the contract was fatal to its claims for extra work and delay damages. The court cited *A.H.A., supra,* and stated "It is well established that strict compliance with the notice and damage documentation terms of a municipal contract is a condition precedent to recovery for such cause of action."[395]

7. Acceleration

Acceleration in construction parlance means to speed up work through the use of increased labor, additional equipment, or other contractor resources. Acceleration may be used to make up work that is behind schedule or to complete the project earlier than scheduled. There are two types of acceleration: actual and constructive. Both types are based on the changes clause.[396]

Actual acceleration occurs when the owner issues a formal change order directing the contractor to speed

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[381] Green Int'l, Inc. v. Solis, 951 S.W.2d 384, 387 (Tex. 1997).

[382] Frank Briscoe Co. v. County of Clark, 772 F. Supp. 513, 516–17 (D. Nev. 1991).

[383] Bates & Rogers Constr. Corp. v. Greeley & Hanseon, 109 Ill. 2d 225, 486 N.E.2d 902, 906, 693 Ill. Dec. 369 (Ill. 1985).

[384] Under the Severin doctrine, the contractor must be liable to the subcontractor in order to pass the subcontractor's claim through to the owner. Severin v. United States, 99 Ct. Cl. 435 (1943).

[385] It may be prudent for the owner to terminate the contract for convenience and pay an "equitable adjustment" under the termination for convenience clause rather than pay damages for a prolonged delay.

[386] *See supra* note 220 and accompanying text.

[387] *Id.*

[388] Hoel-Steffen Constr. Co. v. United States, 197 Ct. Cl. 561, 456 F.2d 760, 768 (Ct. Cl. 1972); APAC-Georgia, Inc. v. Department of Transp., 221 Ga. App. 604, 472 S.E.2d 97, 101 (1996) (any recovery limited to desgn errors); New Pueblo Constrs. v. State, 144 Ariz. 95, 696 P.2d 185, 193 (1985).

[389] Fru-Con Constr. Corp. v. United States, 43 Fed. Cl. 306, 324–25 (Fed. Cl. 1999).

[390] New Pueblo Constrs. v. State, *supra* note 388; State v. Eastwind, Inc., 851 P.2d 1348, 1351 (Alaska 1993).

[391] Reif v. Smith, 319 N.W.2d 815, 817 (S.D. 1982).

[392] APAC-Georgia, Inc. v. Department of Transp., *supra* note 389, at 99–100.

[393] 92 N.Y.2d 20, 699 N.E.2d 368, 677 N.Y.S.2d 9 (N.Y. 1998).

[394] 2004 N.Y. Misc. LEXIS 3149 (N.Y. Ct. Cl. Feb. 4, 2004).

[395] Baker Heavy Highway Constr., Inc. v. N.Y. State Thruway Auth., N.Y. Ct. Cl., Claim 105620, Judge Michael E. Hudson; 26 Misc. 3d 1204A; 906 N.Y.S.2d 777 (2006).

[396] In the absence of a changes clause authorizing the owner to order acceleration, the contractor is not contractually obligated to accelerate. If the contractor agrees to accelerate, the acceleration may be authorized by a supplemental agreement, which is in effect a new contract, not a change to the existing contract. See Subsection A, "Changes," *supra.*

up the work.[397] Constructive acceleration, as the name implies, does not involve a formal change order. Generally, it occurs when a contractor encounters an excusable delay,[398] and the owner refuses to grant an extension of time for the delay and directs the contractor to meet the original contract completion date.[399]

a. Constructive Acceleration

The vast majority of cases recognizing constructive acceleration are federal decisions.[400] There are, however, some state court decisions where constructive acceleration has been recognized as a theory of entitlement in public works contracts[401] and private contracts.[402] In the absence of precedent, state courts may look to federal law for the elements necessary to establish constructive acceleration.[403]

To prove constructive acceleration under federal law, five elements must be established.

First, there must be an excusable delay. Second, the Government must have knowledge of the delay. Third, the Government must act in a manner which reasonably can be construed as an order to accelerate. Fourth, the contractor must give notice to the Government that the "order" amounts to a constructive change. Fifth, the contractor must actually accelerate and thereby incur added costs.[404]

An order to accelerate, to be effective, need not be couched in terms of a specific command to speed up the work. In *Department of Transportation v. Anjo Construction Co.*, the court observed that

> An order to accelerate need not be expressed as a specific command by the government unit, but may be constructive. A constructive acceleration order may exist, when the government unit merely asks the contractor to accelerate or when the government expresses concern about lagging progress. Whether a constructive acceleration order was given to a contractor is a question of law. (citations omitted)[405]

To guard against constructive acceleration claims, an owner may wish to include a clause in its construction contracts prohibiting such claims unless the order to accelerate is in writing and signed by the engineer, or another person authorized to sign change orders. An example of this type of clause is the NYSDOT Standard Provision governing acceleration claims:

> The Contractor may not maintain a dispute for costs associated with acceleration of the work unless the Department has given prior express written direction by the Engineer to the Contractor to accelerate its effort. The Contractor shall always have the basic obligation to complete the work in the time frames set forth in the contract. For purposes of this Subsection, lack of express written direction on the part of the Department shall never be construed as assent.[406]

This acceleration provision was discussed in *Di-Pizio Construction Co. Inc.*, where the contractor asserted a claim for acceleration of its labor to ensure it completed the "B" portion of the work in a timely manner.[407] Clamant asserted it did not get an answer to its request to extend the contract time, and it was forced to accelerate the "B" portion of the work to ensure timely completion. The court noted that the contract requires the contractor to provide written notice to the Commissioner with 10 days, but instead of filing such notice, the contractor chose to unilaterally accelerate the project and expend resources. The court noted the aforementioned contract provision that prohibited claimant from unilaterally accelerating, noting that no prior written direction was given and that claimant ignored the notice provisions at its own peril.

This type of clause, absent a waiver by the owner, should bar constructive acceleration claims in those jurisdictions where written change order requirements are strictly enforced. Also, clauses requiring the contractor to give notice of a constructive acceleration claim may bar the claim if notice is not given.[408] However, as with any contractual provision, notice requirements may be waived by the party attempting to en-

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[397] For example, the Federal Changes Clause in 48 C.F.R. pt. 1, 52.243-4 authorized the contracting officer to make changes, including: "(4) directing acceleration in the performance of the work."

[398] Norair Eng'g Corp. v. United States, 229 Ct. Cl. 160, 666 F.2d 546, 548 (Ct. Cl. 1981) (The delay may be compensable or noncompensable, but in either case the delay must be excusable).

[399] Fru-Constr. Corp. v. United States, 43 Fed. Cl. 306, 328 (Fed. Cl. 1999).

[400] *Id.;* Norair Eng'g Corp. v. United States, *supra* note 398; Tombigee Constructors v. United States, 190 Ct. Cl. 615, 420 F.2d 1037, 1046 (Ct. Cl. 1970); McNutt Constr. Co., 85-3 BCA ¶ 18,397, at 92,279 (1985); Envirotech Corp. v. Tenn. Valley Auth., 715 F. Supp. 190, 192 (W.D. Ky. 1988).

[401] Department of Transp. v. Anjo Constr. Co., 666 A.2d 753, 757 (Pa. Commw. 1995); Siefford v. Housing Auth. of City of Humbolt, 192 Neb. 643, 223 N.W.2d 816, 820 (1974) ("no-damage" clause barred recovery for acceleration damages); Global Constr., Inc. v. Mo. Highway and Transp. Comm'n, 963 S.W.2d 340, 343 (Mo. App. 1997).

[402] S. Leo Harmonay, Inc. v. Binks Mfg. Co., 597 F. Supp. 1014, 1026 (S.D. N.Y. 1984) (general contractor liable to subcontractor for acceleration damages—court applied New York law); Johnson Controls, Inc. v. National Valve & Mfg. Co., 569 F. Supp. 758, 761 (E.D. Okla. 1983) (constructive acceleration claim by subcontractor against general contractor denied because of subcontractor's failure to give notice that it considered a directive from the general contractor to stay on schedule an order to accelerate the work).

[403] For example, the court in Department of Transp. v. Anjo Constr. Co., 666 A.2d 753, followed Norair Eng'g Corp. v. United States, 229 Ct. Cl. 160, 666 F.2d 546 (Ct. Cl. 1981).

[404] Fru-Con Constr, 43 Fed. Cl. at 328.

[405] Anjo Constr., 666 A.2d at 757 (citing Norair Eng'g Corp. v. United States, 666 F.2d 546 (Ct. Cl. 1981)).

[406] New York DOT Standard Specification § 105-148 (1995).

[407] *Di-Pizio Constr. Co.*, 699 N.E.2d 368.

[408] Johnson Controls, Inc. v. National Valve & Mfg. Co., *supra* note 396.

force them.[409] Also, conduct by the owner that amounts to overreaching or bad faith may equitably estop the owner from asserting such clauses as a defense.[410]

A contractor may recover its acceleration costs even if it does not complete the project on time. All that is required is a reasonable and diligent effort to make up the delay.[411] There is also authority that a contractor may recover damages when the owner prevents the contractor from completing the contract earlier than scheduled.[412] Acceleration costs may include added labor costs, including premium pay for overtime and weekend work, lost labor productivity due to overmanning, impacts on subcontractors, stacking of trades, and additional equipment. These costs are usually proved by expert witnesses using CPM scheduling methods. Costs are discussed in more detail in Section Six.

8. Owner's Remedies for Delay

a. Liquidated Damages

A failure to complete a contract on time is a breach of contract unless the delay extending the contract completion date is excusable. The owner, as the injured party, is entitled to damages for the breach. Damages for late completion are usually addressed by including a liquidated damages clause in the contract. The clause authorizes the owner to assess a specified sum of money for each day that the contract completion date is delayed.[413]

Historically, the law did not favor liquidated damages. Clauses providing for liquidated damages were often suspect, with some courts viewing them as more penal in nature than compensatory.[414] When viewed in this matter, the clause was regarded as a penalty because it was being used *in terrorem* to compel performance rather than to quantify damages for delay in completing the contract, and it was invalidated.[415] The modern view favors liquidated damages.[416] As a general rule, courts will enforce a liquidated damages clause unless the party challenging the clause can prove that the clause is unenforceable.[417]

An attack on a liquidated damages clause may be made on several fronts. The most common line of attack is that the amount specified as liquidated damages is so disproportionate to the anticipated loss that it is, in fact, a penalty.[418] The second but less common line of attack is that actual damages can be accurately quantified. This argument is based on the premise that liquidated damages are permissible only when it would be impracticable or extremely difficult to determine actual damages accurately.[419] A third line of attack is that liquidated damages should not be enforced where no actual damages were sustained because of the delay.[420] Under the Restatement of Contracts rule, liquidated damages cannot be recovered if there is no loss.[421] This, however, is not the majority rule. The view taken by most courts is that liquidated damages will be enforced even though no actual damages were suffered.[422] This view is based upon the premise that the reasonableness of the amount specified as liquidated damages is determined as of the date the contract was made, not the date that the breach occurred. In *Gaines v. Jones*, the court said:

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[409] APAC-Georgia, Inc. v. Department of Transp., *supra* note 389.

[410] Bignold v. King County, 54 Wash. 2d 817, 399 P.2d 611, 615–16 (1965); Kohn v. City of Boulder, 919 P.2d 822, 824–25 (Colo. App. 1995).

[411] Appeal of Monterey Mechnical Co., ASBCA No. 51450, 2001 – 1B.C.A. ¶ 31,380 (2001).

[412] Grow Constr. Co. v. State, 56 A.D. 2d 95, 391 N.Y.S.2d 726, 729 (1977).

[413] Usually the sum is set forth in the special provision of the contract. For example, the California DOT Standard Specification 8-1-07 provides that, "the Contractor will pay to the State of California, the sum set forth in the special provisions for each and every calendar day's delay in finishing the work in excess of the number of working days prescribed…." Instead of a specific sum, the clause may include a formula for calculating liquidated damages. For example, WSDOT Standard Specification 1-08.9 contains the following formula:

LIQUIDATED DAMAGES FORMULA

$$LD = \frac{0.15C}{T}$$

where: LD = liquidated damages per working day (rounded to the nearest dollar)

C = original contract amount

T = original time for physical completion

[414] *Contractual Provisions for Per Diem Payments for Delay in Performance as One for Liquidated Damages or Penalty*, 12 A.L.R. 4th 891 (1982); DARRELL W. HARP, 3 *Liability for Delay in Completion of Highway Construction Contract*, SELECTED STUDIES IN HIGHWAY LAW 1495, 1510–11.

[415] S. L. Rowland Constr. Co. v Beall Pipe & Tank Co., 14 Wash. App. 297, 540 P.2d 912, 921–22 (1975).

[416] RESTATEMENT OF CONTRACTS 2d, § 356 (1979); 12 A.L.R. 4th 891 (1982).

[417] APAC-Carolina v. Greensboro-High Point, Airport Auth., 110 N.C. App. 664 431 S.E.2d 508, 516 (N.C. App. 1993); Reliance Ins. Co. v. Utah Dep't of Transp., 858 P.2d 1363 (Utah 1993).

[418] RESTATEMENT OF CONTRACTS 2d, § 356 (1979). *See also* State Highway Dep't v. Milton Constr. Co., 586 So. 2d 872 (Ala. 1991) (disincentive payment of $5,000.00 for each day the contract overran in addition to liquidated damages held to be an unenforceable penalty).

[419] 12 A.L.R. 4th 891; New Pueblo Constructors v. State, 144 Ariz. 95, 696 P.2d 185 (Ariz. 1985).

[420] RESTATEMENT OF CONTRACTS 2d, § 339, 356 (1979).

[421] Lind Bldg. Corp. v. Pacific Bellevue Dev., 55 Wash. App. 70, 776 P.2d 977, 983 (Wash. App. 1989).

[422] 34 A.L.R. 1336 (1925) "Right to amount stipulated in contract for breach, where it appears there were no actual damages, or there was no proof of such damage," (1982); *see* Wallace Real Estate Inv., Inc. v. Groves, 881 P.2d 1010, 1017 (Wash. 1994).

> It is not unfair to hold the contractor performing the work to such agreement if by reason of later developments damages prove to be less or non-existent. Each party by entering into such contractual provision took a calculated risk and is bound by reasonable contractual provisions pertaining to liquidated damages. 423

If the liquidated amount is determined to be a penalty, the clause will be stricken and actual damages may be recovered. The court cannot reform the contract by substituting an amount of liquidated damages that the court believes to be reasonable, but it can determine the actual damages incurred as a result of the delay.[424] An owner's recovery for delay is limited to the liquidated amount even though its actual damages are greater.[425] However, a liquidated damages clause does not preclude recovery for actual damages that are not covered by the clause,[426] or where the right to recover actual damages is reserved in the contract. In *VanKirk v. Green Construction Co*., the state was entitled to liquidated damages for the contractor's delay and to indemnification from the contractor for damages that the state paid to another contractor because of the delay.[427]

Occasionally, construction contracts will contain milestone completion dates.[428] Failure to meet these dates is a breach of contract. Liquidated damages are assessed unless it is clear that when the contract was made that no damages could possibly result from a breach. If so, the clause serves no compensable purpose; its only function is to compel performance by "an exaction of punishment for a breach which could produce no possible damage…."[429]

The fact that the clause induces performance does not invalidate liquidated damages, if it were reasonable to expect that delays in contract completion would result in damages to the owner. A liquidated damage clause is not invalid because it also has the effect of encouraging prompt performance.[430] In *Robinson v. United States*, the court said that a provision in a construction contract "giving liquidated damages for each day's delay is an appropriate means of inducing due performance, or of giving compensation, in case of failure to perform…."[431]

Where both the contractor and the owner contribute to the delay, and neither can establish the extent to which the other is responsible for the delay, neither can recover delay damages from the other.[432] This is simply the rule of apportionment that was discussed earlier. The authorities also differ regarding the enforcement of a liquidated damage provision for delay that accrues after the contractor abandons the contract. The majority rule is that only actual delay damages can be recovered after the contract has been abandoned.[433] This includes damages for the delay in completing the contract.[434] The majority rule is based on the notion that abandonment of the contract constitutes abandonment of the liquidated damages clause, limiting the owner to those damages that it can actually prove. The minority view holds that the abandonment should not deprive the owner of the benefit of the liquidated damage clause.[435]

Liquidated damages are not assessed after substantial completion of the project.[436] Once substantial completion is achieved, further overruns in contract time are assessed on the basis of direct engineering costs until actual physical completion has occurred.[437] Problems occur when the contractor is dilatory in completing punch list work, and the amount assessed for direct engineering costs is not enough to be an incentive to complete the work promptly. If the situation becomes too bad, default termination may be an option, coupled with recovery for costs incurred by the owner in completing punch list items.[438]

Liquidated damages save the time and expense of attempting to prove delay damages. This may have particular significance when the specified sum includes damages for inconveniences to the state and the travel-

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[423] 486 F.2d 39, 45 (8th Cir. 1973) (quoting Southwest Eng'g Co. v. United States, 341 F.2d 998, 1002–03 (8th Cir. 1965)).

[424] Kingston Contractors, Inc. v. Washington Metro. Area Transit Auth., 930 F. Supp. 651, 656 (D.D.C. 1996).

[425] Brower Co. v. Garrison, 2 Wash. App. 424, 468 P.2d 469 (Wash. App. 1970).

[426] Meyer v. Hansen, 373 N.W.2d 392, 395–96 (N.D. 1985).

[427] 195 W. Va. 714, 466 S.E.2d 782, 787 (1995).

[428] Milestone dates refer to dates when certain portions of the project are required to be completed; for example, in opening the highway to traffic. Department of Transp. v. Anjo Constr. Co., 666 A.2d 753, 756 (Pa. Commw. 1995).

[429] Priebe & Sons, Inc. v. United States, 332 U.S. 407, 413, 68 S. Ct. 123, 92 L. Ed 32 (1947); DJ Mfg. Corp. v. United States, 86 F.3d 1130, 1136 (Fed. Cir. 1996).

[430] DJ Mfg. Corp., 86 F.3d at 1135.

[431] 261 U.S. 486, 488, 43 S. Ct. 420, 67 L. Ed. 760 (1923).

[432] Buckley v. State, 140 N. J. Super. 289, 356 A.2d 56, 69, 71 (1975); *but see* Nomeollini Constr. Co. v. State of Cal. ex rel. Dep't of Water Resources, 19 Cal. App. 3d 240, 245–46, 96 Cal. Rptr. 682 (1971) (court said that apportioning delay was an "uncomplicated fact finding process").

[433] Six Companies v. Joint Highway Dist., 311 U.S. 180, 185, 61 S. Ct. 186, 85 L. Ed 114 (1940).

[434] L. Romano Co. v. Skagit County, 148 Wash. 367, 268 Pac. 898, 901 (Wash. 1928).

[435] Pacific Employers Ins. Co. v. City of Berkeley, 158 Cal. App. 3d 145, 155–56, 204, Cal. Rptr. 387 (1984).

[436] Phillips v. Ben Hogan Co., 267 Ark. 1104, 594 S.W.2d 39, 49 (1980).

[437] Olympic Painting Contractors, ASBCA No. 15,773, 72-2, BCA ¶ 9549 (1972). Substantial completion has been defined as

> [w]hen the contract work has progressed to the extent that the Contracting Agency has full and unrestricted use and benefit of the facilities, both from the operational and safety standpoint, and only minor incidental work, replacement of temporary substitute facilities, or correction or repair remains to physically complete the total contract…"

Washington State Standard Specification 1-08.9 (2000).

[438] F&D Constr. Co., ASBCA No. 41,441, 91-1 BCA ¶ 23, 983(1991) ("If a contractor refused to complete punch list work or the corrections are unduly prolonged, the contractor may be deemed to have abandoned the contract.").

ing public.[439] Liquidated damages are generally viewed with favor by the courts and will be enforced if they are reasonable. All an owner has to do, to enforce the clause, is introduce the clause in evidence and prove the number of days of delay that are inexcusable. The burden is on the contractor, as the defaulting party, to prove that the clause is not enforceable.[440] There are caveats, however. Care should be taken in drafting liquidated damage clauses for particular projects. Liquidated damages that are too high may be unenforceable and discourage other contractors from bidding, thus reducing competition. Worse yet, those who do bid may include a contingency in their bids to cover the assessment of liquidated damages. When liquidated damages are too low, some contractors may decide to accept liquidated damage assessment rather than take more expensive steps to avoid delay.

Historically, liquidated damages assessed by state highway departments were equated with increased engineering and administration costs. The AASHTO *Guide Specifications for Highway Construction* included tables representing an estimate of the nationwide average of construction engineering (CE) costs. State agencies were left on their own in setting rates for projects. For years, the FHWA regulations referred to, and included, these tables for guidance. [441] Currently, FHWA regulations allow liquidated damage sums to include daily CE costs and such other additional amounts as liquidated damages in each contract, "to cover other anticipated costs of project related delays or inconveniences to the SHA or the public. Costs resulting from winter shutdown, retaining detours for an extended time, additional demurrage, or similar costs as well as road user delay costs may be included."[442]

The modern view is that liquidated damages should not only reflect daily CE costs applicable to the project, but also the more intangible, but equally real, impacts on the traveling public caused by the delay in completing an urgently needed public facility. The liquidated damage rates may be project specific, or they may be in the form of a table or schedule developed for a range of projects based on project costs or project types.[443]

[439] The state transportation agencies may, with FHWA concurrence (for federally-aided projects), include amounts as liquidated damages to cover user benefit losses caused by delay. 23 C.F.R. ch. 1, 635.127(c).

[440] DJ Mfg. Corp. v. United States, 86 F.3d 1130, 1134 (Fed. Cir. 1996).

[441] O.F. FINCH, *Legal Implications in the Use of Penalty and Bonus Provisions of Highway Construction Contracts: The Use of Incentive and Disincentive Clauses as Liquidated Damages for Quality Control and for Early Completion*, SELECTED STUDIES IN HIGHWAY LAW 1582 - N63.

[442] 23 C.F.R. ch. 1 § 635.127(c).

[443] 23 C.F.R. ch. 1 § 635.127(a). Subsection (f) of the regulation also authorizes the use of incentive provisions for early completion.

b. Termination for Default: Practice, Case Law, and Developments

Construction contracts usually contain a termination for default clause. The clause specifies events that constitute contractor default. One of the events specified in the clause is the contractor's inability to meet the contract schedule.[444] The default provision allows the owner to terminate the contract when it becomes reasonably apparent that the contractor's lack of progress has reached a point where it is unlikely that the contractor can complete the contract on time.[445] When this occurs, the owner may demand a revised progress schedule showing how the contractor intends to complete the project on schedule.[446]

Federal regulations provide that federally aided transportation contracts exceeding $10,000 must contain a termination provision.[447] Prior to termination of a federally aided project, the state highway agency must receive concurrence of the FHWA Division Administrator if the Division Adminstrator concurred in the original award. Further federal participation in a contract previously terminated for default is limited to the lesser of the original contract amount, or the sum of the new contract plus the payments on the old contract.[448]

The AASHTO Guide Specifications provide a representative default termination provision which provides for termination for the following contractor events:

1. Fails to begin work in the time period specified.
2. Fails to perform work with sufficient resources.
3. Fails to meet contract work requirements.
4. Stops work.
5. Fails to resume stopped work after receiving notice to proceed.
6. Becomes insolvent or bankrupt or makes an assignment for the benefit of creditors.
7. Fails to comply with minimum wage payments or

[444] McDonnell Douglas Corp. v. United States, 182 F.3d 1319, 1328 (Fed. Cir. 1999) (contractor's ability to meet the contract schedule is a fundamental obligation of a government contract).

[445] The owner's determination that the contractor is in default may be reviewed under one of two standards. The majority rule is that the owner determination should be based on whether a reasonable person in the owner's position would be satisfied with the contractor's performance or believe that the work could not be timely completed. Burton, *Breach of Contract and the Common Law Duty to Perform in Good Faith*, 94 HARV. L. REV. 369, 383 (1980). The other standard is whether the owner's determination that the contractor would not complete on time was made in good faith. Action Eng'g. v. Martin Marietta Alum., 670 F.2d. 456, 458–60 (3d Cir. 1982) (applying California law).

[446] Construction contracts usually contain a provision requiring a supplemental progress schedule when the contractor is behind schedule. Refusal to provide a supplemental schedule may be further proof of the contractor's unwillingness or inability to complete the project on time.

[447] 23 C.F.R. § 635.125.

[448] FHWA CACC Manual, *supra* note 157, at 45.

EEO contract requirements.

8. Is a party to a fraud.

ODOT Standard Specifications 108.08 provides termination default provisions which include the following additional events:

1. The contractor abandons, or fails or refuses to complete, the work.

2. The contractor is not performing the work properly.

3. Any other reason the ODOT Director believes jeopardizes completion of the work by the completion date.

Typical termination provisions require notice to the contractor and surety of the default considerations, and give the parties an opportunity to respond before final action is taken. After termination the parties are governed by the contract provisons and the provisons in the performance bond.

> Courts and administrative bodies have upheld contract terminations based upon the contractor's failure to complete the contract by the completion date. In *Thomas Lee*[449] the Board of Contract Appeals held that the contractor's failure to complete by the specified date permitted the contract to be terminated. Similarly, the contractor is required to prosecute the work with such diligence that will ensure its timely completion. In *Square Construction Co. and La Fera Contracting Co.*, U.S. Army Corps of Engineers Board of Contract Appeals No. 2996, the Board of Contract Appeals approved a termination where the contractor failed to prosecute the work with "due diligence." Similarly, where the contractor indicates he cannot and will not render further performance, termination is appropriate.[450]

An owner has several options under the default clause when the contractor defaults. The owner may tender the work to the performance bond surety to complete the project. If the surety "accepts the tender," it will retain a completion contractor and enter into a takeover agreement with the owner.[451] If the surety refuses the tender, the owner can sue the surety and the defaulting contractor for increased costs in completing the project, including damages for late completion.[452]

There are limitations on the owner's power to terminate. For example, the owner may waive the contractor's failure to complete the work on time by establishing a new completion date and by not assessing liquidated damages.[453] Another example is the effect of a Chapter 11 bankruptcy filing while the contract is ongoing. An unfinished contract is an executory contract, and as such, an asset of the debtor's (contractor's) estate. The owner must obtain an order from the bankruptcy court granting relief from the automatic stay imposed when the bankruptcy petition is filed. A termination, in violation of the automatic stay, is null and void.[454] A third limitation is substantial completion. Once substantial completion is achieved, the contract cannot be terminated for default.[455] Substantial completion occurs when the agency has full and unrestricted use of the facility, both from an operational and safety standpoint.[456]

The burden of proving that the contractor could not complete on time rests with the owner.[457] A wrongful default termination is a breach of contract entitling the contractor to damages, unless the contract contains a termination for convenience clause.[458] When the contract contains a termination for convenience clause (most contracts do), a wrongful termination is automatically converted to a termination for the owner's convenience. This eliminates a breach of contract claim, including recovery for lost profits on uncompleted work, and restricts the contractor's recovery to the remedy provided in the clause.[459]

c. Termination for Convenience

The right of the government to terminate a contract when completion is no longer in the best interests of the government, even in the absence of a termination for convenience provision, is extremely broad and provides the contracting officer full discretion to end the work.[460]

When a termination for convenience is issued, the contractor's right to continue the work ceases, as does the government's obligation to compensate the contractor for further work. A more detailed discusssion of termination of convenience provisions is contained in Section 1 of this study.

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[449] *VACAB*, No. 1161, 7502 BCA 11, 539.

[450] David R. Levine, Trustee for Rosedale Dairy Co., Inc., ASBCA No. 5077, 59-1 BCA 2061.

[451] La. Ins. Guaranty Ass'n v. Rapides Parish Police Jury, 182 F.3d 326 (5th Cir. 1999).

[452] *See* discussion in Part A of the preceding Subsection.

[453] APAC-Georgia, Inc. v. Department of Transp., 221 Ga. App. 604, 472 S.E.2d 97, 100 (1996); Sun Cal, Inc. v. United States, 21 Cl. Ct. 31, 38–40 (1990) (waiver of liquidated damages and negotiation of new liquidated damages clause, even without execution of new agreement, waived right to terminate).

[454] 11 U.S.C. § 362; Harris Products, Inc., ASBCA 30426, 87-2 BCA ¶ 19,807 (1987).

[455] Olson Plumbing & Heating Co. v. United States, 602 F.2d 950 (Ct. Cl. 1979); *but see* note 438 concerning contractor's refusal to complete punch list work.

[456] *See* note 437 *supra*.

[457] Lisbon Contractors, Inc. v. United States, 828 F.2d 759, 763 (Fed. Cir. 1987).

[458] Morrison Knudson Corp. v. Fireman's Fund Ins. Co., 175 F.3d 1221 (10th Cir. 1999).

[459] District of Columbia v. Organization for Envtl. Growth, 700 A.2d 185, 199–200 (D.C. App. 1997); A.J. Temple Marble & Tile, Inc. v. Long Island R.R., 172 Misc. 2d 442, 659 N.Y.S.2d 412, 414 (N.Y. Sup. 1997) (contractor terminated for convenience on a fixed-price contract could not receive more than the contract price.); *see also* Best Form Fabricators, Inc. v. United States, 38 Fed. Cl. 627, 637 (Ct. Cl. 1997).

[460] Nolan Bros., Inc. v. United States, 186 Ct. Cl. 623 (1969).

d. Recovery of Engineering Charges

In addition to liquidated damages, NYSDOT contract provisions provide for the assessment of engineering charges against the contractor for failure to complete the contract by the completion date. Engineering charges include engineering and inspection expenses incurred by the state, its consultants and inspection agencies, and by railroad companies. Before assessing the engineering charges, the department will give due to consideration to any extenuating circumstances beyond the control of the contractor, as limited to circumstances provided in Section 108.03 of the Standard Specifications.

e. Recovery Against Design Professionals

Many state transportation agencies have been able to negotiate substantial settlements with design professionals occasioned by their design errors and omissions. Generally, this has occurred after in-depth discussion with design professionals regarding their design performance. Standard practice in transportation agencies is to put the designer on notice of the potential design claim being asserted by the contractor, and incorporate the designer into the defense team if appropriate. Subsequently, the agency would negotiate an appropriate settlement with the contractor, and then proceed to negotiate and reach resolution with the design professional over his or her design responsibility. If negiotiations are not successful, lititgtion may ensue. Our research and discussions with state transportation officials indicate that most if not all such matters are settled administratively, thus resulting in little if any reported case law.

SECTION 6

CONSTRUCTION CLAIMS AND LITIGATION

This Section focuses on construction claims brought by contractors against state transportation agencies. The Section is arranged into four subsections. The first subsection deals with contract claims procedures. The next two subsections discuss the major liability and damage issues that are usually presented in a large construction claim. The last subsection concludes with a discussion of the trial strategies and considerations that may be used in preparing and defending a construction claim in a typical litigation setting.

A. CLAIM PROCEDURES

1. Introduction

In deciding whether a claim brought by a contractor should be settled administratively or litigated, the agency must be able to evaluate the claim. Is it likely that the contractor will be successful if the case is tried? If so, what kind of monetary exposure is the agency facing? What will it cost to defend the case in terms of money and agency resources? Will an adverse result create a bad precedent, or conversely, will an unwarranted settlement just encourage more claims? [1]

To assess these concerns, an agency must have information about the claim. The agency must understand the contractor's theory on entitlement or liability, the provisions in the contract on which the contractor relies, and what the contractor has in the way of documentation supporting its position. The owner must know how much is sought, how that amount was calculated, and the facts that support those calculations.

Claim procedures allow an owner to investigate the claim and document the facts while they are still fresh. Early notice of a potential claim also allows an owner to evaluate the impact that the claim could have on the owner's construction program. This can have real significance to a public agency that is operating under tight budgetary constraints.

Generally, it is also in the contractor's interest to submit a well-documented claim. A poorly documented claim, in all likelihood, will be rejected, leaving litigation or arbitration as the only means available to the contractor for resolving the dispute.

Contract claims that are not settled by the parties must be referred to a neutral third party for resolution. In the case of state transportation agencies, the "final remedy" for resolving claims can vary widely. They can range from litigation to arbitration conducted by the American Arbitration Association. Some states have created boards and commissions to decide claims, subject to some judicial review. Several states use a mix of litigation and arbitration, specifying arbitration as the sole remedy for claims under a specific dollar amount and providing for litigation for claims over that amount. The administrative procedures used by the states to review claims, and the final remedies available to the contractor if the claims are not settled, are listed in a Table in Part 3 of this Subsection.

The variations in the methods used by the states as final remedies stem from their policy on sovereign immunity as a bar to contract claims. Many states have judicially recognized that immunity from suit is waived through contracting. Other states have statutorily waived or abolished sovereign immunity for breach of contract claims. The Table in Part 3 of this Subsection contains a summary showing how each state has dealt with sovereign immunity as a defense against parties seeking redress from a state for breach of contract.

2. Immunities from Suit

a. Sovereign Immunity

Sovereign immunity, unless waived, protects a state, its agencies, and officers from lawsuits,[2] and applies to contract claims against a state.[3] The doctrine of sovereign immunity is based on the ancient common law maxim that, "the King can do no wrong," and therefore, he cannot be held liable for his acts or omissions.[4] The modern justification for the doctrine has been characterized as a means of protecting the public purse: "Sovereign immunity protects the public fisc, and therefore, the public welfare by limiting assaults on the public fisc."[5]

Generally, sovereign immunity can be impliedly waived by conduct, or expressly by legislation.[6] A number of states have judicially recognized that a state waives its immunity from suit for breach of contract by contracting for goods and services.[7] The rationale supporting this view was explained by the Delaware Supreme Court.

It must be assumed that the General Assembly, in granting the State Highway Department the power to contract intended that it should have the power to enter into only valid contracts. A valid contract is one which has mutuality of obligation and remedy between the

[1] While an early resolution of the claim is usually in the owner's best interest, claims that lack merit should not be settled simply to make them go away. A policy of settling everything and litigating nothing often encourages more claims.

[2] S.J. Groves & Sons v. State, 93 Ill. 2d 397, 444 N.E.2d 131, 67 Ill. Dec. 92 (Iowa 1982); 72 AM. JUR. 2D, *States, Territories and Dependencies*, §§ 92 & 93 (2d ed. 2001), Stone v. Ariz. Highway Comm'n, 93 Ariz. 384, 381 P.2d 107 (Ariz. 1963).

[3] Federal Sign v. Tex. So. Univ., 951 S.W.2d 401, 412 (Tex. 1997) (dismissing claim for breach of contract based on sovereign immunity).

[4] Stone v. Highway Comm'n, *supra* note 2, at 109; Jaffe, *Suits Against Governments and Officers: Sovereign Immunity*, 77 HARV. L. REV. 1 (1963).

[5] Hocking, *Federal Facility Violations of the Resource Conservation and Recovery Act and the Questionable Role of Sovereign Immunity*, 5 ADMIN. L. J. 203 (1991).

[6] Stone v. Highway Comm'n, *supra* note 2, at 111.

[7] The Table in Part 3.b *infra* lists those states that have taken that position, including case citations.

parties to it (citations omitted). It follows therefore, that in authorizing the State Highway Department to enter into valid contracts the General Assembly has necessarily waived the State's to suit immunity for breach by the State of that contract.[8]

In Wisconsin, contract claims require passage of enabling legislation before a claim can be filed.[9]

Other states have enacted legislation that waives or abolishes sovereign immunity as a defense to lawsuits for breach of contract.[10] Not all states, however, permit private parties to litigate their contract claims in courts of general jurisdiction. Some states, for example, have a state claims board or Court of Claims to determine claims against the state that arose from contracts entered into by the state.[11] In Vermont, claims are referred to the transportation board.[12] In Texas, sovereign immunity for breach of contract is not waived by the act of contracting.[13] The court, however, noted that, "There may be other circumstances where the State may waive its immunity *by conduct* other than simply executing a contract so that it is not always immune from suit when it contracts," (emphasis added).[14]

In *Aer-Aerotron v. Texas Department of Transportation,*[15] the court held that the Department's immunity from suit was waived by conduct that went beyond the mere act of contracting. In that case, the Department contracted with Aerotron to supply radios for a total contract amount of $468,550. In the first year of the contract, the Department increased the number of radios from 125 to 300, raising the total contract price to $993,900. Aerotron alleged, in its complaint, that it had shipped the radios and the Department had accepted them, but failed to pay, forcing Aerotron into bankruptcy. Aerotron further alleged that the State, by accepting goods and services, increasing its order, requesting and receiving technical assistance, and by twice promising to pay the balance due, waived its immunity from suit for breach of contract. The court held that the State waived its immunity from suit by engaging in actions that "fully implicated it in the performance of the contract."[16]

In *Texas Department of Transportation v. Jones Bros. Dirt & Paving Contrs.*,[17] the court held that the contractor's petition for breach of contract must allege facts showing that immunity from suit was waived by conduct that goes beyond the act of contracting. The contractor's failure to make this showing deprived the trial court of jurisdiction over the contractor's breach of contract claim.

b. Eleventh Amendment Immunity

The Eleventh Amendment to the United States Constitution provides: "The judicial power of the United States shall not be construed to extend to any suit in law or equity, commenced or prosecuted against one of the United States by citizens of another state, or by citizens or subjects of any foreign state."

While the Amendment, by its terms, does not bar suits against a state by its own citizens, the Supreme Court has consistently held that an unconsenting state is immune from suits brought in federal courts by the state's own citizens, as well as citizens of another state.[18]

Eleventh Amendment immunity applies even though a state is not named as a party to the lawsuit, when it is clear that the state is the real party in interest and the state officials are only nominal defendants.[19]

Abrogation of Eleventh Amendment immunity can occur in two ways. First, a state may expressly waive its immunity.[20] Second, Congress may abrogate the immunity, but only if Congress expresses an intent to do so and the legislation is pursuant to a valid exercise of Congressional power.[21]

Unless Congress abrogates a state's immunity, any suit by private parties in federal court seeking to impose a liability that must be paid from public funds in the state treasury is barred by the Eleventh Amendment.[22]

3. Administrative Claim Procedures and Remedies

The administrative procedures used by state transportation agencies to resolve claims are governed by the standard specifications in the agencies' construction contracts. This subpart examines the claims specifica-

[8] George & Lynch Co. v. State, 57 Del. 158, 197 A.2d 734, 736 (Del. 1964).

[9] Wis. Stat. 16.007.

[10] The Table in Part 3.b *infra* lists those states that have enacted legislation waiving sovereign immunity.

[11] New York, for example, has a State Court of Claims to determine contract claims, N.Y. Court of Claims Law § 9. Pennsylvania has similar legislation creating a Board of Claims to determine breach of contract claims against the Commonwealth, 62 PA. CONS. STAT. § 1724. Other states that have adopted similar approaches are listed in the Table in Part 3 of this Subsection.

[12] 18 VT. STAT. ANN. 5.

[13] Federal Sign Co. v. Tex. So. Univ., 951 S.W.2d at 408–09.

[14] *Id.* at 408 n.1.

[15] 997 S.W.2d 687 (Tex. App. 1999).

[16] *Id.* at 691.

[17] 24 S.W.3d 893, 901 (Tex. App. 2000).

[18] Hans v. La., 134 U.S. 1, 16, 10 S. Ct. 504, 33 L. Ed. 842 (1890); Duhne v. N.J., 251 U.S. 311, 40 S. Ct. 154, 64 L. Ed. 280 (1920); Employees v. Department of Public Health and Welfare, 411 U.S. 279, 93 S. Ct. 1614, 36 L. Ed. 2d 251 (1973); Edelman v. Jordan, 415 U.S. 651, 663, 94 S. Ct. 1344, 39 L. Ed. 2d 662 (1974).

[19] Ford Motor Co. v. Department of Treasury, 323 U.S. 459, 464, 65 S. Ct. 347, 89 L. Ed. 389 (1945). Edelman v. Jordan, 415 U. S. at 663.

[20] Edelman v. Jordan, *id*. at 673.

[21] Green v. Mansouer, 474 U.S. 64, 68, 88 L. Ed. 2d 371, 106 S. Ct. 423 (1985).

[22] Edelman v. Jordan, 415 U.S. at 674.

tions used by several state transportation agencies,[23] and the AASHTO Guide Specifications. These specifications illustrate the elements that a claims specification should contain. In this regard, much of the discussion focuses on the Florida Department of Transportation,[24] New York, and California, although elements from other state specifications are also examined as part of this discussion.

This subpart also summarizes the internal administrative review practices employed by the states in dealing with contract disputes and the final remedies available to contractors who are dissatisfied with the agencies' decisions.

a. Claims Specifications

A typical claims specification contains the following elements: (1) notice of the claim, and waiver of the claim if notice is not provided; (2) furnishing of sufficient information to enable the agency to evaluate the claim; (3) an internal administrative process; and (4) a certification stating that the claim is made in good faith and reflects what the contractor believes it is owed. Each of those elements are discussed below.

The first element requires notice of a potential claim. Failure to provide such notice waives the claim. For example, the AASHTO Guide Specification provides in part that the contractor must "[n]otify the Engineer in writing of any intent to file a claim for additional compensation."[25] This specification also provides that "the Contractor waives any claim for additional compensation if the Engineer is not notified or is not given sufficient access to obtain a strict accounting of the Contractors's actual costs and afforded proper facilities for strict accounting of actual costs."

Prompt notice of a potential claim before any disputed work is performed serves several public purposes. Prompt notice allows the agency to take early steps to change the work, as necessary, to mitigate damages and avoid extra or unnecessary expenses.[26] It also allows the agency to keep track of the costs associated with the disputed extra work.[27] Notice provisions for failure to comply with claim filing procedures are judicially enforced.[28]

The second function of a claims specification is to allow the owner to obtain sufficient information about the claim so that it can determine whether to settle or reject the claim. This function requires the contractor to explain the basis of its claim and the amount of additional compensation sought, including time extensions, if any. The specification also requires the contractor to submit documentation supporting the claim. The language used in the specification to implement this function can be specific or generalized.

The AASHTO Guide Specifications, which serve as a model for many state transportation agencies, provide that the contractor is to provide sufficient detail to enable the engineer to understand the basis for entitlement and resulting costs. They require the following information:

1. Detailed statement providing all necessary dates, locations, and work items affected.
2. The date on which actions or conditions resulting from the claim occurred or became evident.
3. A copy of potential claim forms.
4. Name, title, and activity of each agency employee familiar with the facts of the claim.
5. Name, title, and activity of contractor employees familiar with the facts that are the basis of the claim.
6. Specific contract provisions that support the claim and a statement of why they support it.
7. Identification of writings and documents and the substance of any material oral communications relating to the claim.
8. Statement as to whether additional compensation or time extension is based on contract provisions or breach of contract.
9. For time extension requests, an analysis of contruction schedule.
10. Amount of specific compensation sought.

The AASHTO Guide Specifications further provide that failure to submit a claim before final payment constitutes a waiver of the claim.[29]

The Florida claims specification[30] is another good example of a specification that is very specific in enumerating what the claim must contain. This specification requires that the claim contain the following information:

[23] Arizona, California, Florida, New York, Oregon, Pennsylvania, South Dakota, and Washington.

[24] Florida Department of Transportation Standard Specifications for Road and Bridge Construction (2000).

[25] AASHTO Guide Specification § 105.18 (2007); *see also* California Specification 9-1.04; Pennsylvania Specification 9.105-14; South Dakota Specification 5.17.

[26] A.H.A. Gen. Constr., Inc. v. N.Y. City Housing Auth., 92 N.Y.2d 2D, 699 N.E.2d 368, 376, 677 N.Y.S.2d 9 (N.Y. 1998).

[27] *Id*.

[28] Blankinship Constr. Co. v. State Highway Comm'n, 222 S.E.2d 442 (N.C. 1976); Main v. Department of Highways, 206 Va. 143, 142 S.E.2d 524, 530 (Va. 1965); Absher Constr. Co. v. Kent Sch. Dist., 78 Wash. App. 137, 890 P.2d 1071, 1073 (1995); Ritangela Constr. Corp. v. State, 183 A.D. 2d 817, 584 N.Y.S.2d 108, 110 (1992); Glynn v. Gloucester, 21 Mass. App. Ct. 390, 487 N.E.2d 230, 233 (1986); PYCA Indus. v. Harrison County, 177 F.3d 351 (5th Cir. 1999).

[29] AASHTO Guide Specifications 105.18.

[30] Specification 5-12 (2000). The California Standard Claims Specification is more generalized. Section 9-1.04 (1999) requires the contractor to submit notice of a potential claim on a standard form (CEM-680). When the affected work is completed, the contractor must submit substantiation of its actual costs. Failure to do so waives the claim.

• A detailed factual statement of the claim, including the items of work affected and pertinent dates.

• An identification of all pertinent documents and the substance of any material oral communications relating to the claim, and the identity of the persons involved in the communications.

• An identification of the provisions of the contract that support the claim, and the reasons why such provisions support the claim, including the provisions of the contract that allegedly have been breached and the actions constituting such breach.

• The amount of additional compensation sought, with a breakdown of the amount showing: 1) job site labor expenses; 2) additional materials and supplies together with invoices and receipts establishing such costs; 3) a list of additional equipment costs claims, including each piece of equipment and the rental rate claimed for it; 4) any other additional direct costs or damages, and all documentation in support thereof; 5) any direct costs or damages and all documentation in support thereof; and 6) a list of the specific dates and the exact number of days sought for a time extension and the basis for entitlement to time for each day for which a time extension is sought, including a detailed description of the events or circumstances that caused the delay.

Under the Florida claims specification, submittal of a written claim containing this type of information is a condition precedent to the contractor bringing any circuit court action, arbitration, or other formal claims resolution proceeding against the Department for additional compensation or time.[31]

The Florida Standard Specifications provide for Notice of Claim for extra work and delay. Generally for extra work, the Florida Standard Specifications require that the contractor submit to the engineer a notice of intention in writing to make a claim for additional compensation before beginning the work on which the claim is based and submit full and complete documentation of the claim as required in the contract within 90 calendar days after final accceptance of the project with an original contract amount of $3 million or less, or within 180 calendar days after project acceptance for projects greater than $3 million, thus allowing the contractor sufficient time to document its claim.[32]

Notification of claims for delay, differing site conditions, or breach of contract requires the contractor to submit written notice to the engineer within 10 days after commencement of the delay to a controlling work item and to provide a reasonably complete description as to the cause and nature of the delay and possible impacts to the contractor's work. If requesting a time extension, notice is required within 30 days after elimination of the delay. For projects under $3 million, complete documentation required by the contract is required within 90 days after final acceptance; if the contract is greater than $3 million, it is required within 180 days.[33]

To guard against the contractor revising its claim after the claim has been submitted, the Specification prohibits the contractor from increasing the amount of the claim or the basis for entitlement. The Specification provides that:

> The Contractor shall be prohibited from amending either the basis of entitlement or the amount of any compensation or time stated for any and all issues claimed in the contractor's written claim submitted hereunder, any circuit court, arbitration or other formal claims resolution proceeding should be limited solely to the basis of entitlement and the amount of any compensation or time stated for any and all issues claimed in the Contractor's written claim submitted hereunder. This shall not, however, preclude a contractor from withdrawing or reducing any of the basis of entitlement and the amount of any compensation or time stated for any and all issues claimed in the contractor's written claim submitted hereunder at any time.[34]

Florida's Specifications also provide that the Engineer shall respond within 90 days of receipt of contractor's claim submittal on contracts with an original contract amount of $3 million or less, and within 180 days if the original contract amount is more that $3 million. Failure to repond within the 90- or 180-day time period is considered a denial of the claim by the engineer.[35]

The audit provisions of the Florida Standard Specifications are also specific.[36] They enumerate in detail the types of records that may be audited. These include, but are not limited to, daily time sheets, foreman's daily reports, diaries, payroll records, material invoices and purchase orders, lists of company owned equipment, subcontractor payroll certificates, job cost reports, general and subsidiary ledgers used to record costs, and cash disbursement journal and financial statements for all years reflecting the operations on the project, including income tax returns for those years.[37] A further discussion of audit provisions is contained in Section 6(A)(6)(b) of this study.

Also subject to audit are all documents reflecting the contractor's actual profit and overhead during the years the contract was being performed, and for each of the 5 years prior to the commencement of the contract. Aside from defending against a total cost claim,[38] the question of whether a contractor makes or loses money on a

[31] Florida Standard Specification for Road and Bridge Construction at pp. 5-12 (2010).

[32] *Id*. at 5-12.2.1.

[33] *Id.* at 5-12.4.

[34] *Id*. at 5-12.3.

[35] Florida Standard Specification, 5-12.4.

[36] *Id.* at 5.12.14.

[37] The Specification used by the Washington State Department of Transportation allows the agency to audit financial statements for 3 years preceding execution of the contract and 3 years following final acceptance of the contract, in addition to auditing financial statements for all years reflecting operations relating to the contract. Standard Specification 1-09.12 (2000).

[38] Claims based on the total cost method are discussed in Subsection C.4 of this Section.

fixed-price, competitively bid contract is ordinarily not legally relevant. An exception may apply where there are large profits and defective work.[39] But beyond legal relevance is practical relevancy. Did the contractor or subcontractor make or lose money? This type of information can be useful in formulating negotiation strategies, particularly when the contractor has pass-through claims from subcontractors who have suffered large losses and may be on the verge of bankruptcy.[40]

The Florida Specification also requires the contractor to make its bid documents available for audit[41] and all worksheets used to evaluate the cost components of the claim, including all documents that establish the specific time periods and individuals involved and the hours and wage rates for such individuals.

In addition, a specification should permit the owner to audit depreciation records on all company equipment irrespective of whether those records are maintained by the contractor, its accountant, or others. This should include any other source documents used by the contractor for internal purposes in establishing the actual cost of owning and operating its equipment.[42] Computer software used to prepare the claim should also be subject to audit.[43]

The audit specifications should provide that, as a condition precedent to recovery on any claim, the contractor, subcontractors, and suppliers must keep sufficient records to support and document their claims. The specification should also provide full access to such records to allow the auditors to verify the claim and make copies of such records, as determined necessary by the auditors. Finally, the specification should provide that failure to retain sufficient records to verify the claim, and failure to provide full and reasonable access to such records, waives the claim or any portion of the claim that cannot be verified.[44]

One final consideration: Care should be taken in selecting the auditor. The auditor may be called upon to testify to his or her findings if the claim is not settled. Thus, consideration should be given not only for the auditor's professional competence, but also for his or her ability as an expert witness.

The third element of a typical claims specification is the administrative process that the agency will follow in reviewing the claim. In general, many transportation agencies utilize a three-step process wherein the initial review is made by the resident engineer. If the claim is not resolved at this level, it will be reviewed at a higher level. For example, Arizona follows a three-step process: (1) review by the resident engineer, (2) review by the district engineer, and (3) review by the state engineer.[45] Oregon has a four-step process with the stated purpose of resolving claims at the lowest possible level in the agency.[46] The administrative review process used by the states is illustrated in the Table shown later in this subpart.

The agency is required to act in good faith in evaluating the claim,[47] and moreover, the law presumes that public officials act in good faith in carrying out their duties.[48] Thus, a claim should not be rejected for minor defects. But what should the agency do when the claim is materially defective? This question can be important because failure to comply with claim procedures may waive the claim. Sending the claim back for more information, however, may waive any defense that the claim is barred because of the contractor's failure to comply with the claim procedures specified in the contract.

To preserve this defense, the letter should specify why the claim is deficient, and that the claim is waived. However, if the agency is willing to leave the door open for future negotiations, the letter may state that the agency is willing to engage in further negotiations, but only with the understanding that to do so will not prejudice the agency's waiver defense, and that the defense will be asserted if the claim is litigated or arbitrated.[49]

The administrative review aspect of a claims specification specifies when the agency will respond to the claim.[50] Failure to respond constitutes a denial of the

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[39] Defective work may explain why the profits are so large. The counter argument is that admission of large profits may be too prejudicial. *See* Federal Evidence Rule 403.

[40] Pass-through claims are discussed in Subsection C.4 of this Section.

[41] Escrow bid documentation specifications are discussed later in this Subsection.

[42] WSDOT Standard Specification C1-09.12(3)(20) (2000).

[43] *Id*. 1-09.12(3)(22) (2000).

[44] Florida Standard Specification, *supra* note 24.

[45] Arizona Standard Specification 105.21 (2000).

[46] Oregon Standard Specification 00199.40 (1996).

[47] Sutton Corp. v. Metro. Dist. Comm'n, 423 Mass. 200, 667 N.E.2d 838 (1996).

[48] D.C. v. Organization for Envtl. Growth, Inc., 700 A.2d 185, 201 (D.C. App. 1997).

[49] Whether the claim will be deemed as waived may depend upon whether the owner can show that it was prejudiced by the contractor's failure to comply fully with the notice of claim requirements. A.H.A. General Constr. Co. v. N.Y. Housing Auth., 92 N.Y.2d, 20, 699 N.E.2d 368, 374, 677 N.Y.S.2d 9 (1998) (strict compliance with notice requirements required); Absher Constr. Co. v. Kent Sch. Dist., 77 Wash. App 137, 890 P.2d 1071, 1095 (showing of prejudice not required to enforce notice provision); New Pueblo Constructors, Inc. v. State, 144 Ariz. 95, 696 P.2d 185, 188 (1985) (showing of prejudice required—applying federal contract law).

[50] Section 5-12.4 of the Florida Standard Specifications provides for a response within 90 days for claims on contracts having an original amount of $3 million or less and 120 days for contracts having an original amount greater than $3 million. The WSDOT Specification provides for a response based on the size of the claim: 45 calendar days for claims under $100,000 and 90 calendar days for claims of $100,000 or more. The time may be extended if necessary. Standard Specification 1-09.11(2) (2000).

claim.[51] If the claim is not resolved at the project level, the contractor may request further review of the claim until the internal administrative process is exhausted.[52]

The fourth and final element is the format for certifying the claim. While there is no standardized format, the contractor is generally required to certify that the claim is true and fully documented.[53]

The AASHTO Guide Specifications for required certification provide that the contractor must certify that the claim is made on good faith, that supporting data is accurate and complete to the contractor's knowledge and belief, and that the claim amount accurately reflects the contractor's actual cost incurred.[54]

The California specifications require that the claim must be accompanied by a notarized certificate certifying, under penalty of perjury and with specific reference to the California False Claims Act,[55] that the claim for additional compensation and time, if any, is a, "true statement of the actual costs incurred and time sought, and is fully documented and supported under the contract between the parties."[56] The California provisons require the following declaration:

> I declare under penalty of perjury, according to the laws of the State of California, that the foregoing claims, with specific reference to the California False Claims Act (Govt. Code Section 12650 *et. seq*.), and to the extent the project contains federal funding the U.S. False Claims Act (31 USC Sections 3729 et seq.), are true and correct and the declaration was signed on_____ (date) _____,20___at _____ California.[57]

The California Claims Specification[58] requires that any claim for overhead costs must be supported by an audit report of an independent certified public accountant. But the state may, at its discretion, conduct its own audit of overhead costs. The specification further provides that any costs or expenses incurred by the State in reviewing any claim not supported by the contractor's cost accounting or other records shall be deemed to be damages incurred by the state within the meaning of the California False Claims Act.

In addition, the Caltrans Standard Specifications require the contractor to comply with the provisions of the Initial Potential Claim Record, Supplemental Potential Claim Record, and Full and Final Potential Claim Record. The notice requirements of the Initial Potential Claim Record require the Contractor to submit an Initial Potential Claim record within 5 days from the date when a dispute arises due to an act or failure to act by the engineer. The provisions require the engineer to respond within 5 days, and the contractor is required to proceed with the potentially claimed work unless otherwise directed. Thereafter, within 15 days, the contractor is required to submit a Supplemental Potential Claim Record to include the nature and circumstances causing the claim or event, contract specifications supporting the basis of claim, and estimated claim costs and breakdown. The engineer evaluates the information and responds within 20 days. Subsequently, the Contractor is required to submit within 30 days of completion of the claimed work, a Full and Final Potential Claims Record, which provides more detail to include detailed factual account of the events, contract documents supporting the potential claim, itemized breakdown of payment and time adjustments requested, relevant information, copies of cost records, and supporting commnications. The engineer is required to respond within 30 days. If not resolved, the dispute may be elevated to an alternative dispute resolution, which would include a Dispute Resolution Advisor (DRA) if the total bid is from $ 3 million to $10 million, or a Dispute Resolution Board (DRB) if the total bid is over $ 10 million.[59] A detailed discussion of DRBs and their use in transportation projects is contained in Section 7 of this study.

The claims specifications may contain other features that protect the owner's interests. For example, the Florida Specification enumerates the types of consequential damages that are not recoverable.[60] These include, but are not limited to, such damages as loss of bonding capacity, loss of bidding opportunities, interest paid on money borrowed to finance the work, and loss of financing. Claim preparation expenses, attorney fees, expert witness fees, and the cost of litigation are also not recoverable. Acceleration costs are also not allowed, except where the contractor was directed by the agency to accelerate the work at the agency's expense.

The Florida Specification[61] contains two other interesting features. It makes settlement discussions between the contractor and the agency inadmissible in court proceedings or arbitration brought by the contractor. The Specification also provides that no claim can be filed in court or no demand can be made for arbitration until after final acceptance of the contract.[62]

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[51] Florida Specification, *supra* note 44.

[52] The Arizona specification, for example, uses a three-step hearing process. If the contractor does not accept the project engineer decision, the contractor may request a review by the district engineer and then the State Engineer. Standard Specification 105.21 (2000).

[53] South Dakota Standard Specification 5.17 (1998); New York Standard Specification 109.05F (1995). Both specifications require that certifications be made under oath before a notary public.

[54] AASHTO Guide Specification, op. cit., 105.18, Claims for adjustment, at 52–53.

[55] The California False Claims Act is discussed in Subpart 4 of this Subsection.

[56] Standard Specification 9-1.04 (1999).

[57] Caltrans Standard Specifications 9-1.17(D)(2)(c).

[58] *Id.*

[59] Caltrans Standard Specifications 5-1.43

[60] Standard Specification 5-12.10.

[61] Standard Specification 5-12.12.

[62] Standard Specification 5-12.4. Metropolitan Dade County v. Recchi America, Inc., 734 So. 2d 1123 (Fla. App. 1999) (contractor must follow contract claim procedures prior to commencement of suit).

b. State Dispute Resolution Procedures and Remedies

The most common method for resolving state highway construction claims is litigation. Arbitration is a distant second, followed by special courts and boards. These methods vary because of the manner and extent in which the states have waived sovereign immunity.

State transportation agencies use varying methods of dispute resolution, ranging from litigation, mediation, and DRBs to facilitation. A detailed discussion of the alternative dispute provisions is contained in Section 7 of this volume. NYSDOT utilizes a unique process for project closeout called the "gatekeeper" concept wherein the gatekeeper—the chief engineer—at the contractor's request, refers the dispute to a facilitated closeout meeting with the Office of Construction, or to a dispute resolution board, or to the traditional closeout process meeting with NYSDOT's Office of Construction.[63]

The contractor involved in the dispute is required to contact the gatekeeper with a brief decription of the contract work and its preferred method of dispute resolution; to demonstrate that the unresolved dispute involves unique, unusual, and complex construction, engineering, or legal issues; and to demonstrate that the dispute has a monetary value in excess of $50,000. The contractor must also have demonstrated a clear commitment to active participation in partnering during the conduct of the contract.

The following State Sovereign Immunity/Administrative Procedures Table lists each state, summarizes how sovereign immunity was waived, and generally describes the internal administrative processes used by each state in reaching a decision on whether to settle or deny a contractor's claim. The Table also summarizes the final remedy available to a contractor who is unwilling to accept the agency's decision.

[63] NYSDOT Standard Specifications, Sept. 2011, § 102 H.

State Sovereign Immunity/Administrative Procedures		
State	Administrative Procedures	Final Remedy
Alabama sovereign immunity judicially waived. *State Highway Dept. v. Milton Constr. Co.,* 586 So. 2d 872 (Ala. 1991).	Agency decision may be appealed to a Claims Committee composed of agency personnel not involved in the project. The Claims Committee decision may be accepted or rejected by the agency head. Contractor may request a hearing by a Claims Appeal Board. The Board is a standing committee composed of three members, one of whom is appointed by the state, one by a contractor's association, and the third jointly by the state and association. The Board's decision is not binding on the state.	Litigation.
Alaska sovereign immunity waived by statute. Statute 09.50.250 (express authority to contract waived immunity).	Resident Engineer's decision may be appealed to the Contracting Officer, which in turn may be appealed to the Commissioner of Transportation for a final agency decision.	Litigation. Statute 36.30.685. (Trial *de novo* if Commissioner's final decision made without a hearing).
Arizona sovereign immunity judicially waived. *Stone v. Arizona Highway Comm'n*, 93 Ariz. 384, 381 P.2d 107, 109 (Ariz. 1963).	Initial decision by the Project Engineer with final review by the State Engineer or his or her representative.	For claims of $200,000 or less—arbitration pursuant to AAA Construction Industry Rules. Over $200,000—litigation in Maricopa County Superior Court.
Arkansas retains sovereign immunity, but allows claims to be heard by administrative claims commission, Ark. Code § 19-10-201 *et seq*.	Initial decision by the Resident Engineer, with successive appeals to the Chief Engineer.	Appeal to the State Claims Commission, which is composed of five members appointed by the Governor, two of whom must be attorneys. Decisions of the Commission may be reviewed by the Legislature.
California sovereign immunity judicially waived. *Souza & McCue Constr. Co. v. The Superior Court*, 57 Cal. 2d 508, 370 P.2d 338, 20 Cal. Rptr. 634 (1962).	Initial decision by the Project Engineer. Review by District Highway Director. Settlements at the District level may be subject to approval by the Headquarters Construction Department.	Statute makes arbitration the sole remedy. Sections 10240–10240.13, Ch. 1, Div. 2, Public Contract Code. Arbitrator's decision is subject to judicial review for findings of fact not supported by substantial evidence and errors of law.
Colorado sovereign immunity judicially waived. *Ace Flying Service, Inc. v. Colorado Dept. of Agriculture*, 136 Colo. 19, 314 P.2d 278 (Colo. 1957).	Initial decision by Project Engineer, with appeal to the District Engineer and then to the Chief Engineer, who refers the claim to a review board composed of three members: one appointed by the State, one appointed by the contractor, and the third by the two members. Board's recommendation referred to Chief Engineer, who makes the final decision.	Litigation.
Connecticut sovereign immunity waived by statute, Conn. Gen. Stats. § 4-160.	Claim may be submitted to claims commissioner, who may authorize suit against state on claim that presents issue of law or	Action must be brought within 1 year of commissioner's ruling in judicial

State Sovereign Immunity/Administrative Procedures		
State	Administrative Procedures	Final Remedy
	fact under which state would be liable if it were private person.	district in which claimant resides, or in Hartford or district in which claim arose if non-resident.
Delaware sovereign immunity judicially waived. *George & Lynch, Inc. v. State*, 57 Del. 158, 197 A.2d 734, 736 (1964).	Initial decision by the Division Engineer, with an appeal to the Contract Claims Committee and a further appeal to the Secretary of Transportation.	Arbitration by the AAA under the Construction Industry Arbitration Rules.
Florida sovereign immunity waived by statute (FLA. STAT. ANN. § 337.19) (2002).	Initial decision at the District level, with appeal to the Claims Review Committee, which is composed of three agency members. Final decision may be made by the Secretary of Transportation.	Litigation claims under $50,000.00 may be arbitrated.
Georgia State Constitution, Art. 1, Sec. II, Paragraph IX (c) waives sovereign immunity for breach of contract actions.	Initial review by the Project Engineer, with successive appeals to the State Highway Engineer, who has final administrative authority to settle contract claims.	Litigation.
Hawaii sovereign immunity waived by statute. HAW. REV. STAT. § 661.	Initial review by the Resident Engineer, and if not settled, then to the District Engineer. If not settled at that level, then to the Chief Engineer, who has final administrative authority to settle claims.	Litigation.
Idaho sovereign immunity judicially waived. *Grant Constr. Co. v. Burns*, 92 Idaho 408, 443 P.2d 1005, 1009 (Idaho 1968).	Claim filed with the Resident Engineer for determination by the District Engineer. Decision may be appealed to the State Highway Administrator and thereafter to the Transportation Board for a *de novo* hearing. The Board's decision is not binding.	Litigation.
Illinois State Constitution, Art. XIII, Sec. 4, abolished sovereign immunity except as provided by the Legislature.	Claim filed with the Project Engineer for referral to the Engineer of Construction. Claim may be referred to a three-member claims board. The Board makes a recommendation to the Director of Highways, who has final administrative authority.	Three-Judge Court of Claims established by statute (I.R.S. c37 § 439.24 *et seq.*). No appeal from the court's decision.
Indiana sovereign immunity waived by statute. Code § 34-4-16-1.1.	Claim filed with District. Decision may be appealed to Commissioner.	Litigation.
Iowa Code § 613.11 waived immunity to suits against the Department of Transportation for construction contract claims. Judicial waiver. *See Kersten Co. v. Dept. of Social Services*, 207 N.W.2d 117, 120 (Iowa 1973).	Claim filed with Project Engineer. Contractor may request meeting with the agency for review and final agency decision.	Contractor may elect with agency approval to submit the claim to nonbinding arbitration by three-member panel: one member chosen by contractor, one by agency, and the third by the other two arbitrators. Litigation if nonbinding arbitration fails to settle the claim.
Kansas sovereign immunity judicially waived. *Parker v. Hufty Rock Asphalt Co.*, 136 Kan. 834, 18 P.2d 568, 569 (1933).	Claim filed with Area Engineer, with appeal to the Secretary of Transportation, who may either authorize an administrative hearing before a hearing officer or appoint a three-member claims panel. The Secretary may accept or reject the recommendations	Litigation.

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	made by the hearings officer or the panel.	
Kentucky sovereign immunity waived by statute. KY. REV. STAT. § 45A 245.	Claim filed with the Project Engineer. Successive appeals to the Commissioner of Highways, who may authorize an administrative hearing for a nonbinding recommendation. The Commissioner has final administrative authority to settle the claim.	Litigation. Case tried to the court sitting without a jury.
Louisiana State Constitution, Art. 12, Sec. 10(A), waived sovereign immunity.	Claim may be filed with the Project Engineer. Successive appeals to the Chief Engineer, who has the final administrative authority to settle claims.	Litigation.
Maine statute waived sovereign immunity. ME. REV. STAT. tit. 5, § 1510-A.	Claim filed with Project Engineer. Appeal to the Commissioner of Transportation, who has the final administrative authority to settle claims.	Appeal to State Claims Commissioner. Claims heard *de novo*. Appeal to Superior Court hearing *de novo* without a jury.
Maryland sovereign immunity waived by statute. MD. STATE GOV'T CODE § 12-201(a).	Claim filed with District Engineer, with final decision by the Procurement Officer.	State Board of Contract Appeals. Board decisions, other than those decided under the small claims expedited process, are subject to judicial review. A contractor also has the option of bypassing the Board and going directly to state court.
Massachusetts, *M. De Matteo Constr. Co. v. Commonwealth*, 156 N.E.2d 659 (1959) (Interpreting general law giving superior courts jurisdiction for contract claims against state agencies.).	Agency Claims Committee, which makes recommendation to the Chief Engineer, who submits decisions to the Public Works Commission for approval. The contractor can request the Commission to hold a hearing before an administrative law judge.	Litigation. A contractor may bypass the Commission and go directly to court from an unfavorable decision by the Chief Engineer.
Michigan sovereign immunity judicially waived. *Hersey Gravel Co. v. State Highway Dept*., 305 Mich. 333 9 N.W.2d 567, 569 (Mich. 1943).	Claim filed with the District Office. The claim, if not settled, is referred to the Central Office for review and decision. The Chief Engineer/Deputy Director of Highways has final administrative authority to settle the claim.	Court of Claims—One judge sitting without a jury. Court of Claims decisions may be appealed in the same manner as other trial court decisions.
Minnesota sovereign immunity waived by statute. MINN. STAT. §§ 3.751, 161.24.	Claim filed with the Project Engineer. If not settled at that level, it is referred to the Assistant District Engineer–Construction. The Claims Engineer has final administrative authority to settle the claim.	Litigation.
Mississippi sovereign immunity waived by statute. MISS. CODE ANN. § 11-45-1.	Claim filed with Project Engineer, who refers the claim to the District Engineer for review and recommendation and then further referral to the agency Director, who has final administrative authority to settle the claim.	Litigation. Claims of $25,000.00 or less may be submitted to the State Arbitration Board composed of three members: one selected by the State, one selected by a contractor's association, and the third by the other two members. Claims over $25,000.00 may be arbitrated by agreement of the

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		parties.
Missouri judicial recognition that sovereign immunity waived by contracting. *V.S. D'Carlo Constr. Co. v. State*, 485 S.W.2d 52, 56 (Mo. 1972).	Claims filed with the Transportation Commission Secretary and referred to a Claims Committee. The Committee makes a recommendation to the Chief Engineer for determination. The contractor may appeal the Chief Engineer's decision to the Commission or go directly to court.	Litigation. Arbitration may be used under the Uniform Arbitration Act, if the parties agree.
Montana judicial recognition that sovereign immunity waived. *Meens v. State Bd of Educ.*, 127 Mont. 515, 267 P.2d 981, 984 (Mont. 1954).	Agency determination following review by the agency Legal Division and audit of the claim.	Litigation.
Nebraska sovereign immunity waived by statute. NEB. REV. STAT. § 25-21, 201.	Claim filed with Project Manager, who refers the claim to the District Engineer. The Director–State Engineer has final administrative authority to settle the claim.	Litigation.
Nevada sovereign immunity waived by statute. NEV. REV. STAT. § 41.031.	Claim filed with Resident Engineer, who forwards the claim to the Highway Claims Review Board, which is composed of an agency member, a Nevada contractor, and a registered professional engineer from the private sector. Board's recommendation submitted to the Agency Director, who has final administrative authority to resolve the claim.	Litigation.
New Hampshire sovereign immunity waived by statute. N.H. REV. STAT. ANN. § 491.8.	Claim filed with the Engineer, whose determination may be appealed by the contractor to the Transportation Commissioner, who has final administrative authority to resolve the claim.	The contractor has a choice: (1) litigation (court hears case sitting without a jury), or (2) an appeal to the Transportation Appeals Board—a three-member board appointed by the Governor. Board decisions may be appealed directly to the State Supreme Court.
New Jersey sovereign immunity waived by statute. N.J. STAT. ANN. § 59.13-1 to .10.	Claim filed with Regional Director, who may submit claim to the Claims Committee composed of four agency members and a Deputy Attorney General. The Committee submits its recommendation to the Deputy Commissioner for a final determination.	Litigation. A contractor may file suit at any stage in the agency's administrative proceedings. Claims may be submitted to arbitration if the parties agree.
New Mexico sovereign immunity waived by statute. N.M. STAT. ANN. § 57-1-23.	Claim filed with the Project Manager, who refers the claim to the District Engineer. The contractor may appeal to the Secretary, who may assign the claim to the agency's Claims Board, which is composed of retired engineers and consultants. The Board makes a recommendation to the Secretary, who has final administrative authority to settle the claim.	Litigation. Claims of $150,000.00 or less may be arbitrated if the parties agree. Each party appoints an arbitrator and the two choose the third member. The arbitration proceedings are conducted in accordance with the Uniform Arbitration Act.
New York Statute (Ct. Cl. Act., §	Claim submitted to the Engineer, then	16-member Court of

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8) establishes a Court of Claims to hear claims against the State.	Regional Director. Gatekeeper concept—DRB, Construction, or Facilitation. The Commissioner of Transportation has final administrative authority to resolve the claim.	Claims. Claims heard by one judge sitting without a jury.
Oklahoma judicial recognition that sovereign immunity waived. *State Board of Public Affairs v. Principal Funding Corp.*, 1975 OK 144, 542 P.2d 503, 505–6 (1975).	Claim filed with Resident Engineer. Appeal to Division Engineer for a hearing if claim is not resolved. Appeal to a three-member Board of Claims appointed by Director and contractor. Board makes recommendation to Highway Commission, which has final administrative authority to resolve the claim.	Litigation.
Oregon sovereign immunity waived by statute. OR. REV. STAT. § 30.320.	Claim filed with Project Manager, with successive appeals to the State Region Engineer and the State Contract Administration Engineer. If not resolved at those levels, claims between $25,000 to $250,000 must be submitted to a three-member Claims Review Board for nonbinding arbitration. Board members are selected by the State and the contractor from a panel previously developed by the State and the construction industry. Claims over $250,000 may also be submitted to the Board if the parties agree.	For claims under $25,000, there is mandatory arbitration by a single arbitrator, pursuant to AAA Construction Industry Arbitration Rules. Contractor may also demand arbitration if the claim is $250,000 or less. Litigation for claims over $250,000, unless the parties agree to arbitration.
Pennsylvania sovereign immunity waived by statute. 62 PA. CONS. STAT. § 1711.1.	Claim filed with District Engineer. Appeals to the Construction Claims Review Committee.	Three-member Board of Claims appointed by the Governor. The Board's decision may be appealed by the State or the contractor to the Commonwealth Court of Pennsylvania.
Rhode Island sovereign immunity waived by statute. R.I. GEN. LAWS § 37-13.1-1.	Claim filed with agency's construction office. Review by Claims Unit and Claims Board, which submits its recommendation to the Director, who has final administrative authority to settle the claim.	Litigation. Case tried to the court sitting without a jury.
South Carolina sovereign immunity waived by statute. S.C. CODE ANN. § 57-3-620.	Claim must be made on form provided by the agency and filed with the Resident Construction Engineer. Claim may be supplemented as required by the agency. If the claim is not resolved, it is referred to the Claims Committee appointed by the State Highway Engineer. The Committee makes its recommendation to the State Highway Engineer, who has final authority to resolve the claim.	Litigation.
South Dakota sovereign immunity waived by statute. S.D. CODIFIED LAWS ANN., § 31-3-24.	Claim must be filed on an agency form with the Project Engineer. The form requires the contractor to furnish additional information as required by the agency. Claim, if not resolved, may be referred to the agency's Claim Committee, which makes	Litigation.

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	its recommendation to the State Highway Engineer, who has final administrative authority to settle the claim.	
Tennessee sovereign immunity waived by statute. TENN. CODE ANN. § 9-8-101 *et. seq.*	Claim filed with the Project Engineer, with appeals to the Transportation Commissioner, who has final administrative authority to settle the claim.	Three-member Claims Commission appointed by the Governor. The Commission's decision can be appealed in the same manner as any trial court decision.
Virginia sovereign immunity waived by statute. VA. CODE ANN. § 8.01-192, *et. seq*; Specific authorization for suits on highway contract claims. VA. CODE ANN., § 33-1.382, *et. seq.*	Claim filed with Resident Engineer. Review and approval by Chief Engineer. Appeal to Commissioner of Highways. A settlement by the Commissioner is subject to approval by the Attorney General and the Governor.	Litigation. Case tried to the court sitting without a jury.
Washington sovereign immunity waived by statute. WASH. REV. CODE ch. 4.92.010. Specific authorization for suits and highway contracts. WASH. REV. CODE ch. 47.28.120.	Claim filed with Project Engineer. Review and approval by Construction Engineer. If claim denied, an appeal may be made to the Secretary of Transportation.	Arbitration is the sole remedy for claims under $250,000 under AAA rules. Litigation for claims over $250,000 in the Thurston County Superior Court, unless the parties agree to arbitration.
West Virginia sovereign immunity waived by statute. W. VA. CODE § 14-2-1 through 29.	Claim filed with Project Engineer. Successive appeals to Highway Commissioner, who has final administrative authority to settle claims.	Litigation. Three-judge Court of Claims.
Wisconsin sovereign immunity waived by statute. WIS. STAT. ANN. § 775.01 (statute allows suit if claim denied by Legislature).	Claim filed with the Project Engineer. Successive appeals to the Secretary of Transportation.	Five-member Claims Board. The Board's recommendation is submitted to the Legislature. If the Legislature denies the claim, the contractor may sue.
Wyoming sovereign immunity waived by statute. WYO. STAT. § 24-2-101.	Claim filed with Resident Engineer. Appeal to the Superintendent and Chief Engineer, who has final administrative authority.	Litigation.

Generally, the states have a similar administrative approach to the resolution of construction claims: A claim is filed with the engineer in charge of the project, usually the project or resident engineer. If the claim is not resolved at that level, the contractor may appeal to higher administrative authority. If the claim is not resolved by the agency through its internal review process, the contractor may pursue its final remedy. At this point, the types of remedies available to the contractor vary.

The most common final remedy for resolving highway construction claims is litigation.[64] A few states use a mix of litigation and arbitration.[65] Several states specify arbitration as the final remedy for resolving construction claims.[66] Some states provide for boards or commissions with some judicial review.[67] This divergence in remedies is due largely to the extent and manner in which sovereign immunity was waived by the state legislatures.

4. The Federal and California False Claims Acts—An Overview

The U.S. Government, a number of states, and several major municipalities have enacted legislation dealing with fraudulent claims whose applicability extends to include government transportation construction contracts.[68] The Federal FCA was originally enacted in 1863 during the Civil War.[69] The Act was originally aimed at preventing fraud in federal military procurement, a practice that was prevalent during the Civil War.

The Federal FCA contemplates enforcement through federal civil actions and criminal prosecutions and also through state or private civil actions. The Act authorizes the U.S. Attorney General to investigate possible violations, and to commence a civil action on behalf of the government if he or she finds that a person has violated or is violating the Act.[70] Another provision, codified with federal criminal statutes rather than with the Act's civil provisions, authorizes federal criminal prosecutions.[71] The Act also authorizes "a person" to bring a civil action for violation of the Act, for both the person and the U.S. Government, in the name of the government.[72] Such actions are referred to as *qui tam* actions.[73] The persons who bring them are referred to formally as "relators," and less formally as "whistleblowers."

The provision authorizing *qui tam* actions has been one of the most distinctive aspects of the FCA from its inception. Due to a spate of *qui tam* actions during World War II, which were perceived as interfering with the war effort, the Act was amended at that time to discourage such actions. In 1986, however, prompted by new abuses in military procurement, the Act was once again amended[74] to allow employees to bring *qui tam* actions against their employers. It has been interpreted sufficiently broadly to authorize such actions by states, as well as by private parties.

As discussed below, the Federal FCA was extensively amended in 2009. Responding to that legislation, TRB and NCHRP commissioned a study of the federal and state false claims statutes in the transportation construction context, which was published in 2011.[75] This current volume will prevent a brief overview, drawing on that publication; those needing more details are referred to that publication.[76] The NCHRP study revealed, through a detailed survey of State DOTs and interviews with current and former government officials and private sector experts, that there was considerably less likelihood that private whistleblowers would pursue *qui tam* false claims actions in highway or bridge construction cases than in other sectors such as Medicaid and pharmaceutical fraud.[77] Q*ui tam* actions appear destined to play only a relatively limited role in

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[64] Thirty-one states provide for some form of litigation. See Sovereign Immunity/Administrative Procedures Table *supra*.

[65] Arizona, Oregon, and Washington. *See* Sovereign Immunity/Administrative Procedures Table *supra*.

[66] California, Delaware, and North Dakota. *See* Sovereign Immunity/Administrative Procedures Table *supra*.

[67] Idaho, Maryland, Ohio, Pennsylvania, and Tennessee are examples. *See* Sovereign Immunity/Administrative Procedures Table Decisions of the Maryland State Board of Contract Appeals are subject to judicial review, as with other civil cases.

[68] The Federal False Claims Act is codified at 31 U.S.C. §§ 3729 et seq. State false claims statutes are cited and discussed further under subsection (A)(4)(e) below.

[69] 12 Stat. 696, 37 Cong. Ch. 67 (Mar. 2, 1893); United States v. Bornstein, 423 U.S. 303, 309–10, 96 S. Ct. 523, 46 L. Ed. 2d 514 (1976); *see* Evan Caminker, *Comment*, *The Constitutionality of Qui Tam Actions*, 99 YALE L. J. 341 (1989).

[70] The provision authorizing the Attorney General to pursue investigations and civil actions is 31 U.S.C. § 3730(a); such actions may be commenced if the Attorney General finds that a person or persons has violated or is violating 31 U.S.C. § 3729.

[71] 18 U.S.C. § 287.

[72] The provision authorizing "a person" to bring a civil action in the name of himself or herself and the government is 31 U.S.C. § 3730(b)(1); such actions are also based on violations of 31 U.S.C. 3729.

[73] *Qui tam* is an abbreviated Latin phrase meaning one who sues for the King and for himself. *See Comment*, *supra* note 69, at 341 n.1. A *qui tam* action is one brought by an informer pursuant to a statute to recover damages for the government and for himself. Erickson v. Am. Institute of Bio-Sciences, 716 F. Supp. 908 (E.D. Va. 1989).

[74] 31 U.S.C. § 3729 (1986).

[75] ERIC KERNESS & PETER SHAWHAN, IDENTIFICATION, PREVENTION AND REMEDIES FOR FALSE CLAIMS IN HIGHWAY IMPROVEMENT CONTRACTING (NCHRP Legal Research Digest 55, Transportation Research Board, 2011), hereinafter cited as "LRD 55"; available at http://onlinepubs.trb.org/onlinepubs/nchrp/nchrp_lrd_55.pdf.

[76] The authors of the 2012 update to this current volume were also the authors of LRD 55.

[77] *See* LRD 55, *supra* note 75, at 69–71, discussing specific reasons why major factors that may favor *qui tam* litigation for Medicaid and pharmaceutical fraud are much less favorable for using such litigation to combat highway and bridge construction fraud.

future enforcement of the FCA for highway and bridge projects. They are still part of the framework of the FCA, however, and so will be included in this summary of the Act's provisions.

a. 2009 Amendments Redefine the Federal False Claims Act, 31 U.S.C. § 3729

During 2009, Congress approved major new federal expenditures including surface transportation projects as an economic stimulus through enactment of the 2008 ARRA,[78] and sought to enhance the protection of such expenditures against fraud through enactment of the 2009 FERA.[79] As part of this effort, Congress enacted comprehensive amendments to the FCA.[80] Both the terms of the 2009 amendments and statements in legislative history indicated that Congress was responding to, and intended to overrule, recent judicial decisions, including *Allison Engine Co. Inc. v. United States ex rel. Sanders*,[81] a U.S. Supreme Court decision issued in 2008, which members of Congress characterized as being contrary to the legislative intent of the Act.[82] (For a discussion of the ways in which the FERA amendments to the FCA addressed and altered precedents established by prior case law, see the 2011 TRB publication.)[83]

As noted above, the FCA both authorizes the U.S. Government to pursue civil and criminal false claims actions against persons violating the Act's provisions; and authorizes states and private parties to pursue federal civil false claims actions against such persons. As amended by FERA, the FCA, specifically 31 U.S.C. § 3729(a)(1), imposes civil false claims liability, including treble damages plus a civil penalty, upon any person who:

A. Knowingly presents, or causes to be presented, a false or fraudulent claim for payment or approval;

B. Knowingly makes, uses, or causes to be made or used, a false record or statement material to a false or fraudulent claim;

C. Conspires to commit a violation of § 3729(a)(1)(A), (B), (D), (E), (F) or (G);

D. Has possession, custody, or control of property or money used, or to be used, by the government and knowingly delivers, or causes to be delivered, less than all of that money or property;

E. Is authorized to make or deliver a document certifying receipt of property used, or to be used, by the government and, intending to defraud the government, makes or delivers the receipt without completely knowing that the information on the receipt is true;

F. Knowingly buys, or receives as a pledge of an obligation or debt, public property from an officer or employee of the government or a member of the armed forces, who lawfully may not sell or pledge property; or

G. Knowingly makes, uses, or causes to be made or used, a false record or statement material to an obligation to pay or transmit money or property to the government, or knowingly conceals or knowingly and improperly avoids or decreases an obligation to pay or transmit money or property to the government (sometimes referred to as a "reverse false claim").

FERA also amended the FCA in several other important respects. Under Section 4(a)(1) of FERA, the FCA, specifically 31 U.S.C. § 3729(a)(2) and (3) and § 3729(b), now makes any person violating § 3729(a) liable to the U.S. Government for the costs of a civil action brought to recover such damages; encourages even culpable witnesses to cooperate by authorizing courts to reduce to double, rather than treble, damages the liability of any person committing a violation who is not subject to pending criminal charges, furnishes federal officials with all known information about the violation within 30 days after first obtaining it, and cooperates fully with the government investigation; and defines the terms "knowing," "knowingly," "claim," "obligation," and "material" in ways that must be considered in litigating FCA cases.

b. Anti-Fraud Measures by Federal Agencies

Following the Congressional enactment of ARRA and the FERA amendments to the FCA, USDOT and multiple other federal agencies undertook a series of training activities and investigative and enforcement initiatives to deal with false claims and other types of fraud on federal, state, and municipal transportation construction projects, some of which can be expected to have long-term impacts. Agencies pursuing such initiatives included, among others, the USDOT OIG, which conducted nationwide fraud awareness training programs serving state DOT as well as USDOT officials; the Recovery Accountability and Transparency Board created by ARRA; the DOJ Antitrust Division, which joined with the USDOT OIG in conducting fraud-awareness training; ongoing activities by the DOJ's National Procurement Fraud Task Force (NPFTF), established in 2006; and audits by the GAO, which ARRA required to review the use of federal economic recovery funds by

[78] The American Recovery and Reinvestment Act of 2008 (ARRA), Pub. L. No. 111-5, Feb. 17, 2009.

[79] Fraud Enforcement and Recovery Act of 2009 (FERA), Pub. L. No. 111-21, 123 Stat. 1617, May 20, 2009 (FERA); text available at http://www.gpo.gov/fdsys/pkg/PLAW-111publ21/pdf/PLAW-111publ21.pdf (last accessed July 24, 2012).

[80] 31 U.S.C. §§3729 et seq.

[81] 553 U.S. 662, 128 S. Ct. 2123, 170 L. Ed. 2d 1030 (2008).

[82] For a discussion of the prior case law, and of congressional intent in enacting the FERA provisions amending the False Claims Act, *see* LRD 55, *supra* note 75, at 7–12.

[83] LRD 55, *supra* note 75, at 10–15.

states and localities every 2 months and issue reports.[84] It should also be noted that significant amendments to the FAR in late 2008 adopted significant new measures to deter, detect, and prevent fraud affecting federal contracts.[85]

c. What Are False Claims, and Who Can Be Sued?

The FCA, 31 U.S.C. § 3729, provides that any person who knowingly presents or causes to be presented a false or fraudulent claim for payment or approval or knowingly makes or uses or causes to be made a false record or statement material to a false or fraudulent claim is liable to the U.S. Government for a civil penalty of not less than $5,000 and not more than $10,000 plus three times the amount of damages which the government sustains because of the act of that person. The provisions define claim to mean any request or demand, whether under contract or otherwise, for money or property that is presented to an officer, employee, or agent of the United States.

As indicated above, the FCA sets forth seven grounds for liability. The most often used provisions involve conduct involving knowingly presenting false claims, § 3729(a)(1), and knowingly making or using false records or statements, § 3729(a)(2). In general terms, for transportation construction projects, the provisions of the FCA define a false "claim" as any request for payment, final payment, equitable adjustments, and contract adjustments of any type.[86]

The FCA defines "knowingly" to mean that a person, with respect to information, (1) has actual knowledge of the information, (2) acts in deliberate ignorance of the truth or falsity of the information, or (3) acts in reckless disregard to the truth or falsity of the information.[87] Submitting a false claim knowing that the claim is false fits within the definition of "knowingly."[88] Reckless disregard and deliberate ignorance standards are not as easily defined and depend upon an analysis of the specific facts of each case.

Prior to the FERA amendments, some federal courts interpreted the FCA to include a requirement that a false claim had to be presented directly to a federal official, meaning that presentation of a false claim to a state or municipal official was insufficient to trigger the statute's provisions. FERA clarified this by redefining "claim" to include not only a request or demand presented to a federal employee, officer, or agent, but also one presented to a contractor, grantee, or other recipient if the money or property requested was to be spent or used on the government's behalf, and if the government had provided any portion of the money or property or would reimburse the contractor, grantee, or recipient for any portion of it.[89]

Some illustrative examples of false claims involving state or municipal federal-aid transportation construction contracts might include, for example, false certifications of payments to subcontractors, payment of Davis-Bacon prevailing wages, or compliance with "Buy America" requirements; implied certifications in applications for progress payments; inflated invoices, inflated or fabricated demands for contract adjustments or additional payments, or adoption of unreasonable interpretations of contract requirements; disadvantage (D)/M/WBE fraud; or use of bid-rigging, collusive bidding, or kickbacks to obtain contracts by fraudulent means.[90]

Who can be sued for false claims? The FCA, 31 U.S.C. § 3729(a)(1), provides that any "person" who engages in specified types of conduct shall be liable for a false claim. False claims litigation has resulted in liability for contractors, subcontractors, material men, vendors, and suppliers who have submitted false claims and false records. FCA actions are not confined to contractors alone. The federal government funds myriad types of programs. Federal funds find their way to both public and private owners, design professionals, and construction managers, so all of these groups have potential exposure to FCA liability. Corporations, design professionals,[91] and construction managers[92] may also be held liable for damages under the FCA.

Federal government agencies are immune from FCA liability by virtue of sovereign immunity.[93] This exemption also applies to FCA actions against federal employees acting within the scope of their employment. States and state agencies may be held liable by the U.S. Government under the FCA, but the U.S. Supreme Court has held that states may not be held liable to private relators in *qui tam* actions.[94] Unlike federal and state agencies and officials, municipal public agencies and employees acting within their official capacity can be

[84] For a more detailed discussion of these various federal training, investigative, and enforcement initiatives, *see* LRD 55, *supra* note 75, at 15–18.

[85] For a more detailed discussion of the fraud prevention measures included in the 2008 amendments to the FARs, *see* LRD 55, *supra* note 75, at 18–20.

[86] For a more detailed discussion of what constitutes a false claim, *see* LRD 55, *supra* note 75, at 20–22.

[87] *See* 31 U.S.C. § 3729(b), Definitions.

[88] United States v. Advance Tool Co., 902 F. Supp. 1011 (W.D. Missouri 1995) (presenting invoices for tools that were reversed engineered rather than brand names as required).

[89] *See* FERA, *supra* note 79, § 4(a)(2).

[90] For a more detailed discussion of these and other examples of false claims, *see* LRD 55, *supra* note 75, at 22–26.

[91] *See* United States v. Peters, 927 F. Supp. 363 (D. Neb. 1996).

[92] *See* United States *ex re.* Ali v. Daniel, Mann, Johnson & Mendenhall, 355 F.3d. 1140 (9th Cir. 2004).

[93] Galvan v. Fed. Prison Indus., Inc., 339 U.S. App. D.C. 248, 199 F.3d 461, 463 (D.C. Cir. 1999); for a good discussion of who can be sued under the FCA, see Charles M. Sink & Krista L. Pages, eds., *False Claims in Construction Contracts, Federal, State and Local*, American Bar Association, 2007, at 47–67. (Note that an updated version of the Sink and Pages publication was released on CD-ROM in 2010.).

[94] *See* Vt. Agency of Natural Res. v. United States *ex rel.* Stevens, 529 U.S. 765, 120 S. Ct. 1858, 146 L. Ed. 2d 836 (2000).

subject to FCA liability, however, since they are "persons" within the meaning of the FCA.[95]

d. Qui Tam Provisions and the Public Disclosure Bar

While FERA[96] enacted significant amendments to the provisions of governing what a false claim consists of,[97] it retained the existing *qui tam* provisions[98] largely unchanged, with only some limited revisions to the provisions protecting whistleblowers from retaliation,[99] along with some amendments to the provisions on U.S. Government intervention in private *qui tam* actions,[100] jurisdictional provisions,[101] and provisions on civil investigative demands in false claims litigation.[102]

A key provision of the FCA[103] authorizes "a person" to bring a civil action for violation of the Act,[104] for the person and the U.S. Government, in the name of the government. The "person" who is authorized to bring such a civil action in the name of the government is known as a *qui tam* relator. This is an abbreviation of the historical Latin phrase, used in English law, "*qui tam pro domino rege quam pro se ipso in hac parte sequitur*," meaning someone "who sues on behalf of the king as well as himself."[105] As one authority on the FCA has noted, the concept of private *qui tam* actions on behalf of the government has roots in English legal history going back to the fourteenth century, roots in American legal history going as far back as 1692, and forerunners in a variety of state and federal statutes enacted between the Revolutionary War and the Civil War. This concept has been developed further over the course of enactment of the Act during the Civil War and its subsequent amendment.[106]

While the Act does not define the word "person," the concept involves providing an inducement for individual employees of a government contractor with direct knowledge of a concealed fraud by the contractor to come forward with that knowledge, as a so-called "whistleblower." The statute does not limit the term "person" to contractors' employees, however, and individuals who are not employees of the defendant, corporations, and even state governments have brought *qui tam* actions.[107]

The FCA includes a variety of procedural requirements for *qui tam* actions,[108] including the following: The person filing the *qui tam* civil action must do so in the name of the U.S. Government.[109] A *qui tam* action may be filed in any federal district court in any district in which the defendant (or, if there are multiple defendants, any one defendant) resides, transacts business, or can be found, or where any act proscribed by 31 U.S.C. § 3729 occurred.[110] Federal courts shall have pendent jurisdiction over any state or local court actions arising from the same transaction or occurrence as a federal *qui tam* action.[111] *Qui tam* actions must be filed within 6 years after the violation is committed, or within 3 years after a federal official becomes aware of material facts but not more than 10 years after the violation is committed, whichever is later.[112] Once a relator has filed a *qui tam* action, the action cannot be dismissed without the consent of the U.S. Government and the court, regardless of whether the U.S. Government decides to intervene in the case.[113] The complaint must be filed secretly in camera with a federal court and kept under seal for up to 60 days in order to provide the U.S. Government with an opportunity to decide whether or not to intervene in the action. The *qui tam* relator must serve a copy on the government under FRCP Rule 4(d)(4); the government then has 60 days to decide whether to intervene, and the government can obtain extension of the 60-day period for good cause shown. If the government decides to intervene, it conducts (i.e., takes over control and litigates) the action; if not, the *qui tam* relator conducts the action.[114] As between private parties, the first *qui tam* relator to file an action wins the race to the courthouse. Once a person has filed such an action, no person other than the government may intervene or file a related action.[115]

If any state or local government is named as a co-plaintiff with the United States in any state or local court action governed by 31 U.S.C. § 3732(b), the 60-day seal imposed following the filing of a *qui tam* action and

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[95] For a more detailed discussion of the applicability of the FCA with regard to federal, state, and municipal agencies and officials, *see* LRD 55, *supra* note 75, at 26–27.

[96] FERA, *supra* note 79.

[97] 31 U.S.C. § 3729.

[98] 31 U.S.C. § 3730.

[99] 31 U.S.C. § 3730(h).

[100] 31 U.S.C. § 3731.

[101] 31 U.S.C. § 3732.

[102] 31 U.S.C. § 3733.

[103] 31 U.S.C. § 3730(b)(1).

[104] 31 U.S.C. § 3729.

[105] 3 WILLIAM BLACKSTONE, COMMENTARIES ON THE LAWS OF ENGLAND 160, and BLACK'S LAW DICTIONARY 1251 (6th ed.), as cited and quoted in CLAIRE M. SYLVIA, THE FALSE CLAIMS ACT: FRAUD AGAINST THE GOVERNMENT 34–35 nn. 1 and 2 (2d ed., Thomson West 2010).

[106] For an excellent discussion of the historical roots of *qui tam* actions and the False Claims Act, and the evolution of the concept since enactment of the Act, see SYLVIA, *supra* note 105, at 34–64.

[107] Claire M. Sylvia, *Qui Tam* Actions Under the False Claims Act, included as ch. 5 in Sink & Pages, *supra* note 93.

[108] 31 U.S.C. §§ 3730(b) through (g), 3731, 3732, and 3733.

[109] 31 U.S.C. § 3730(b)(1).

[110] 37 U.S.C. § 3732(a).

[111] 37 U.S.C. § 3732(b).

[112] 37 U.S.C. § 3731(b). The statute of limitations provisions of the False Claims Act are discussed in § 9 of LRD 55, *supra* note 75.

[113] *Id*.

[114] 31 U.S.C. § 3730(b)(2), (3), and (4).

[115] 31 U.S.C. § 3730(b)(5).

its service on the U.S. Government shall not prevent the relator and U.S. Government from serving the pleadings and sharing all material evidence with state and local law enforcement authorities involved in such state or local actions, but they too shall be governed by the 60-day renewable seal imposed in connection with the federal *qui tam* action.[116] This provision was added to the FCA by FERA and was the subject of specific comment in its legislative history.[117]

Under another provision enacted by FERA in 2009, if the U.S. Government chooses to intervene in a *qui tam* action, the government may file its own complaint or amend the complaint filed by the *qui tam* relator to clarify or add claims. For statute of limitations purposes, such a new or amended complaint shall be considered to relate back to the filing date of the initial *qui tam* action if it arises from the same conduct, transactions, or occurrences.[118] The legislative history of FERA indicates that this provision was enacted to address potential issues raised by a Second Circuit ruling in 2006, which suggested that the Government might not be able to avail itself of retroactive amendment of a complaint under FRCP Rule 15(c)(2) in FCA litigation.[119] If the U.S. Government files a false claims action or intervenes in a *qui tam* action, it shall be required to prove all essential elements of the cause of action, including damages, by a preponderance of the evidence.[120] Notwithstanding any other provision of law, the defendant in a civil action under the FCA shall be estopped from denying the essential elements of any offense for which the defendant has been convicted at trial, or to which the defendant has pled guilty or *nolo contendere*, in any criminal proceeding charging fraud or false statements.[121] Subpoenas for witnesses in *qui tam* actions may be served at any place in the United States.[122]

The FCA authorizes private *qui tam* relators to commence actions in the name of the government and retain a portion of the damages recovered in order to motivate private parties with knowledge of concealed fraud against the government to come forward. Unless qualified, however, this could create a risk of parasitic actions. For example, a private party having no direct knowledge of a fraud might learn of its existence through news media coverage of an audit report or public testimony and then commence a *qui tam* action on that basis. In such a situation, the private party would contribute no direct knowledge and would not deserve any compensation for coming forward but might nonetheless stand to gain an unmerited recovery.

To protect against parasitic actions, the FCA includes a provision known as the "public disclosure bar," enacted in 1986, which prohibits the filing of *qui tam* actions and states that no court shall have jurisdiction over an action "based upon the public disclosure of allegations or transactions in a criminal, civil, or administrative hearing, in a congressional, administrative or Government Accounting Office report, hearing, audit or investigation, or from the news media."[123] The legislative history of the 1986 enactment indicates clearly that the Senate Judiciary Committee was aware of and sought to address this issue.[124]

The situation would be different where there had been media coverage of an audit report or a hearing, but the private party commencing the *qui tam* action was the original source who came forward with the information and led government auditors or staff to uncover the fraud. In that situation, the private *qui tam* relator would deserve compensation for coming forward. Addressing this, the FCA creates an exception from the public disclosure bar where the action is filed by the government "or the person bringing the action is an original source of the information."[125] The statute goes on to define "original source" as "an individual who has direct or independent knowledge of the information on which the allegations are based and has voluntarily provided the information to the government before filing an action…based on the information."[126] The issue of whether a given *qui tam* relator is or is not an "original source" has been the subject of conflicting judicial

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[116] 31 U.S.C. § 3732(c).

[117] Section 4(e) of FERA, *supra* note 79. *See also* CONG. REC. E1295 to E1300, at E1300 (daily ed. June 3, 2009) (statement of Rep. Berman), available at http://www.gpoaccess.gov/crecord/advanced.html; on advanced search page, check boxes for "2009 CR, Vol. 155" and "Extension of Remarks," specific date on 06/03/2009, search E1295; on results page, click on the underlined letters "pdf" under hit no. 3, Fraud Enforcement and Recovery Act of 2009 (last accessed on Dec. 18, 2011).

[118] 31 U.S.C. § 3731(c), as enacted by § 4(b) of FERA.

[119] United States v. Baylor Univ. Medical Center, 469 F.3d 263 (2d Cir. 2006), cited and discussed in CONG. REC. E1295 to E1300, at E1299 (daily ed. June 3, 2009) (statement of Rep. Berman); text of Rep. Berman's statement, *see* CONG. REC. E1295 to E1300, at E1300 (daily ed. June 3, 2009) (statement of Rep. Berman), available at http://www.gpoaccess.gov/crecord/advanced.html; on advanced search page, check boxes for "2009 CR, Vol. 155" and "Extension of Remarks," specific date on 06/03/2009, search E1295; on results page, click on the underlined letters "pdf" under hit no. 3, Fraud Enforcement and Recovery Act of 2009 (last accessed on Dec. 18, 2011).

[120] 31 U.S.C. § 3731(d).

[121] 31 U.S.C. § 3731(e).

[122] 31 U.S.C. § 3731(a).

[123] 31 U.S.C. § 3730(e)(4)(A). This provision was enacted by § 3 of the False Claims Amendments Act of 1986, Pub. L. No. 99-562, 100 Stat. 3153; and was subsequently amended in 1990 by Pub. L. No. 101-280 and in 1994 by Pub. L. No. 103-272.

[124] S. REP. NO. 99-345 (July 28, 1986), cited and reprinted in SYLVIA, *supra* note 105; *see* SYLVIA, at 59 n.30, and see more generally discussion at 53–60 and App. B-1 of that book.

[125] 31 U.S.C. § 3730(e)(4)(A).

[126] 31 U.S.C. § 3730(e)(4)(B).

interpretations and litigation up to and including the U.S. Supreme Court level.[127]

In a 2011 case with potentially major implications for *qui tam* actions, the U.S. Supreme Court ruled that the public disclosure bar is triggered if the *qui tam* action is based in part on information obtained by a *qui tam* relator or a person associated with the relator, from a federal agency pursuant to the FOIA.[128] In that case, the relator, a Vietnam veteran, had been employed by an elevator manufacturer that held a number of Federal Government contracts subject to a federal statute requiring employers to report to the U.S. Department of Labor concerning how many of their employees were veterans covered by the statute. After the employee resigned from the company based on actions which he perceived as intended to force him out, his wife used FOIA to obtain documents filed by his former employer with the Department of Labor. Asserting that his employer had failed to file many of the required reports, and that many of the reports it filed had included false statements, the employee filed a *qui tam* action. The Court held that a federal agency response to a FOIA request constituted a "report" within the meaning of the public disclosure bar provisions of the FCA. The Court reasoned that the word "report" had a broad ordinary meaning and that this was consistent with the public disclosure bar, which was generally broad in scope. It found no basis in language of the FAC for imposing a narrower definition of the term. Adopting this interpretation did not undercut the other terms used in the public disclosure bar provision. The Court also took the view that holding the public disclosure bar to be triggered by FOIA responses would not "necessarily lead to unusual consequences," such as defendants precluding *qui tam* actions by filing FOIA requests themselves.[129]

The U.S. Supreme Court also ruled in a post-FERA case decided in 2010 that the public disclosure bar is triggered by state as well as federal disclosures.[130]

e. State False Claims and False Statements Statutes

In addition to the U.S. Government, 26 states and at least 3 major municipalities have enacted legislation dealing with fraudulent claims whose applicability extends to transportation construction contracts.[131] There are also 27 states that have enacted Medicaid-only false claims legislation. There is some overlap between the groups, since 14 states have enacted both. There are, however, 13 states having only Medicaid false claims statutes, and no false claims statutes that would apply to transportation construction projects.[132] While less comprehensive than false claims statutes, there are 14 states which have enacted False Statements Acts, which typically authorize prosecution for submission of false written statements to state officials in order to obtain pecuniary or other benefits.[133] Although six of those states have enacted both FCAs and False Statements Acts, there are eight states in which the False Statements Acts appear to be the only state actions authorizing legal action for fraud against state transportation agencies.[134]

The provisions of the state false claims statutes, while generally modeled to some extent on the Federal FCA, vary considerably. Any agency or party engaged in litigation under a false claims statute must research the state statutory provisions and case law directly, rather than relying on assumptions based on the federal statute. NCHRP's 2011 publication provides cita-

[127] *See, e.g.*, Rockwell Int'l Corp. v. United States, 549 U.S. 457, 127 S. Ct. 1397, 167 L. Ed. 2d 190 (2007), and other cases cited and analyzed in Sink & Pages, *supra* note 93, at 102–105; and Seyfarth Shaw LLP, THE GOVERNMENT CONTRACT COMPLIANCE HANDBOOK 20–26 (4th ed., Thomson West 2006).

[128] Schindler Elevator Corp. v. United States *ex rel.* Kirk, 131 S. Ct. 1885; 179 L. Ed. 2d 825 (2011). The case was decided by a 5 to 3 vote, with one abstention. The majority opinion was written by Justice Thomas, in which he was joined by Chief Justice Roberts and Justices Alito, Kennedy, and Scalia. Justice Ginsberg dissented, in which she was joined by Justices Breyer and Sotomayor. Justice Kagan recused herself from participation in the case. The decision reversed a prior decision by the U.S. Court of Appeals for the Second Circuit, United States *ex rel.* Kirk v. Schindler Elevator Corp., 601 F.3d 94 (2d Cir. N.Y. 2010).

[129] *Schindler Elevator Corp.*, 131 S. Ct. 1885 at 1894; and see more broadly discussion at 1894–1896.

[130] Graham County Soil and Water Conservation Dist. v. United States, 559 U.S. 280, 130 S. Ct. 1396, 176 L. Ed. 2d 225 (2010).

[131] The 26 states that have enacted false-claims statutes applicable to transportation construction contracts include Alaska, Arizona, California, Delaware, Florida, Hawaii, Idaho, Illinois, Indiana, Kansas, Louisiana, Massachusetts, Michigan, Minnesota, Montana, Nebraska, Nevada, New Jersey, New Mexico, New York, North Carolina, Ohio, Rhode Island, Tennessee, Virginia, and Wyoming. The municipalities include Chicago, New York City, and Washington, D.C.

[132] The 13 states having only Medicaid false claims statutes, and no false claims statutes that would apply to transportation construction projects, include Colorado, Connecticut, Georgia, Kentucky, Missouri, New Hampshire, Oklahoma, Oregon, Texas, Utah, Washington State, West Virginia, and Wisconsin.

[133] The 14 states that have enacted false statements statutes include Alabama, Arizona, Colorado, Georgia, Illinois, Iowa, Kentucky, Louisiana, Nebraska, North Dakota, Ohio, Pennsylvania, South Dakota, and West Virginia.

[134] The eight states that have false statements statutes, but no false claims statutes applicable to transportation projects, include Alabama, Colorado, Connecticut, Georgia, Iowa, Kentucky, North Dakota, Pennsylvania, South Dakota, and West Virginia.

tions to the state FCAs, brief summaries of their provisions, and further discussion of related issues.[135]

In general terms, while the provisions of state FCAs may not be identical with the Federal FCA or each other, state FCAs typically authorize the state's attorney general (AG) to pursue civil false claims actions and to recover treble damages, plus civil penalties of up to $10,000 to $12,000, plus attorneys' fees, expenses, and costs. A number of states also authorize their AGs to issue civil investigative demands (CIDs), typically modeled on the Federal FCA CID provisions. Most states require that FCA actions be filed within 3 years after discovery and within 10 years after commission of the underlying acts.

It is also typical for state FCAs to authorize private *qui tam* actions for treble damages plus attorneys' fees and expenses (although Kansas expressly prohibits *qui tam* actions); to authorize state AGs to intervene in such actions, and to control the litigation of those cases they intervene in; and to authorize *qui tam* relators to receive 15 to 25 percent of the total recovery, or up to 30 percent if proceeding alone without the intervention of the state AG (Nevada and Tennessee, however, offer terms more generous to relators).

f. Practice Guidance for State DOTs on Prevention and Remediation of False Claims

Based on a survey of state DOT officials, the NCHRP's 2011 report on false claims indicated that most false claim cases encountered by state DOTs involved DBE fronts, false certifications, wage rate and hour violations, inflated invoices, false certification of quantities, falsification of materials quality test results, bid-rigging, Buy America violations, overstated costs, and false requests for extra compensation.[136] The report also found that state DOTs most often addressed potential false claims in reviewing a contractor's submission of a claim during the administration of an active contract or at the contract close-out stage. Approaches to investigating false claims, once identified, ranged from using audit and construction engineering staff, or in-house claim engineers, to using claim consultants or experts to assist in the discovery process in defending claims litigation. It was rare, however, for sState DOTs to have formal written standards or procedures to review and investigate for false claims during the process of reviewing a contractor's claim.[137]

One of the clearest and most striking findings emerging from the NCHRP report's survey of state DOTs was that, while many state DOTs reported problems with false claims or fraud on highway or bridge projects, and agencies had pursued a number of criminal and civil remedies, state DOTs had made only very limited use of either the Federal FCA or state FCAs to seek civil recovery of damages for false claims or fraud on highway or bridge construction projects. The number of *qui tam* False Claims Act lawsuits involving highway and bridge projects was minimal. Only 5 state DOTs reported being aware of any *qui tam* actions involving their projects, and they reported a cumulative total for all 5 states of 13 or fewer *qui tam* cases among them.

The NCHRP's 2011 false claims study did, however, identify a number of potentially promising practices, derived from research and interviews, which state DOTs might wish to consider as methods of detecting, preventing, and deterring false claims. These included:

- Requiring consultants and contractors to establish a Code of Conduct and a Business Ethics Compliance Program, including internal controls.
- Reviewing contractors' records of integrity and business ethics in making responsibility determinations or bid qualification decisions.
- Requiring contractors to disclose involvement in any prior false claims cases in connection with prequalification and bidding responsibility reviews.
- Requiring consultants and contractors with a history of integrity problems to employ IPSIGS or monitors to ensure compliance with relevant law and regulations, and to deter, prevent, uncover, and report unethical and illegal conduct by, within, and against their firms.
- Strengthening claims certification requirements.
- Including failure-to-disclose involvement in prior false claims among the grounds for state suspension, debarment, or findings of non-responsibility.
- Providing fraud awareness training to employees involved in reviewing bids, responsibility issues, contract awards, construction work, requests for payment, requests for orders on contract, construction claims, and compliance with D/M/WBE requirements.
- Pursuing state legislation to conform state false claims statutes to the Federal FCA as amended by FERA.
- Creating a dedicated false claim unit within the state DOT or state AG's office.
- Requiring state DOT attorneys to review all construction claims for potential FCA exposure.
- Incorporating set-off provisions for recovery of false claims investigative costs into the standard terms and provisions of state DOT consultant and construction contracts.
- Pursuing state legislation to adopt a state Contract Disputes Act or other provisions for forfeiture of false claims.
- Dedicating any false claims damage recoveries to supporting future investigations.
- Establishing, maintaining, and publicizing a toll-free telephone hotline to receive allegations of false claims and other waste, fraud, and abuse on a confidential basis.
- Sharing information regarding problem contractors with other state agencies and among state DOTs nationwide.
- Reviewing contract payment requests, contractor requests for orders on contract (change orders), and contract claims on a timely and thorough basis.

[135] *See* LRD 55, *supra* note 75, at 45–58.

[136] *See* LRD 55, *supra* note 75, at 70.

[137] *See* LRD 55, *supra* note 75, at 69–70.

• Enhancing the scrutiny of construction firms experiencing other problems, such as financial problems, major performance delays, or recurrent difficulty in meeting contract specifications, for possible false claims.

• Maintaining records of damages after potential false claims were identified.

• Training and requiring state DOT employees to use Red Flag lists such as those maintained by the USDOT, which list common indicators of fraud, bid-rigging and collusion, material overcharging, time overcharging, product substitution, DBE fraud, quality-control–testing fraud, bribery, kickback, and conflicts of interest.

• Adopting bid escrow provisions.[138]

5. Escrow Arrangements to Preserve Bid Documents

As discussed earlier, the right to audit is an important tool for resolving claims. One area that should be subject to audit is the contractor's bid documents.[139] Such documents, for example, may be relevant in a total cost claim involving the reasonableness of the contractor's estimated costs, or time for performing the work, as reflected in the bid,[140] or as a baseline to measure the cost of changes to the work that occur during contract performance. The contractor's bid anticipation may be relevant to many of the issues in a claim or dispute. The right to audit, however, has little value if there is nothing to audit. Recognizing this, some states have included an escrow bid documentation specification in their construction contracts.[141] This type of specification requires the contractor to place its bid documents with an escrow agent, usually a bank, to ensure that the documents will be available for use by the owner in the event of a claim.[142]

The term "bid documentation" should be broadly defined. The term should include all quantity take-offs, crew size, equipment, and calculations showing estimated rates of production. The bid documents should include quotations from subcontractors and suppliers whose quotations were used to arrive at the prices contained in the bid proposal. The contractor's allocation of equipment costs, indirect costs, contingencies, markup, and any other costs allocated to and included in bid items should also be included. If the bid documents were developed using computer generated software, the specification should require that the information be furnished in hard copy, and that the contractor identify the name and version of the computer software that was used.[143]

The ODOT bid escrow provisions require the low bidder and the second low bidder to submit the bid documents for escrow the next day after the bid opening. Typical escrow provisions contain sample escrow agreement provisons to be executed by the parties. The sample escrow agreements provide for contractor's indemnification of the escrow agent and for notice requirements and release provisions; and are to be signed by the contractor, ODOT, and the escrow agent.[144]

The specification should contain safeguards to assure that the information is complete and legible. The specification should require the contractor to submit an affidavit with the bid documents listing all of the documents in the escrow container. Section 103.08 of the AASHTO Guide Specifications for highway construction provide that that the contractor is required to submit a signed certified affidavit attesting that the affiant has examined the bid documentation, that the affidavit lists all documents used to prepare the bid, and that the sealed container contains all such bid documentation. The AASHTO Specifications provide , "Certifying that the materials in escrow represent all documentation used to prepare the bid waives the contractor's right to use bid documentation other than those in escrow should a contract dispute arise." The affidavit should be signed by the person authorized to execute bid proposals, attesting that the affiant has personally examined the bid documentation, that the affidavit lists all of the documents used in preparing the bid, and that all of the documentation is included in the container placed in escrow.[145]

The ODOT CMS provisions provide that the ODOT will not use the escrowed documents to assess the contractor's or subcontractor's qualifications for performing the work and that the documents will always remain the property of the contractor or subcontractor, subject to joint review by the department and the contractor or subcontractors.[146]

The ODOT provisions provide that the bid documentation will be examined at any time deemed necessary by either the department or the contractor to assist in

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[138] *See* LRD 55, *supra* note 75, at 71–80.

[139] The contract specifications may specifically enumerate "bid documents" as documents that the owner may audit in evaluating the contractor's claim. Florida Standard Specification 5-12.14 and Washington Standard Specification 1-09.12(3)23 are examples.

[140] S. Le Roland Constr. Co. v. Beall Pipe Tank Co., 14 Wash. App. 297, 540 P.2d 912, 917 (1975). Calculating the contractor's damages is discussed in Subpart C of Section 6.

[141] Montana, New Jersey, Oregon, South Carolina, and Washington. *See* DARRELL W. HARP, *Preventing and Defending Against Highway Construction Contract Claims: The Use of Changed or Differing Site Conditions Clauses and New York State's Use of Exculpatory Contract Provisions and No Claims Clauses* (National Cooperative Highway Research Program Legal Research Digest No. 28); Arizona Standard Specification 103.11.

[142] The specification may provide that failure to provide the bid documentation as specified will render the bid nonresponsive. Arizona Standard Specification 103.11(E).

[143] Arizona Standard Specification 103.11(D) (2000).

[144] ODOT PN110 (Apr. 12, 2008) escrow bid documents.

[145] Arizona Standard Specification 103.11(B).

[146] ODOT PN110 (Apr. 12, 2008) escrow bid documents.

the negotiation or settlement of a dispute and claim, and that the contractor and subcontractor and department personnel will be present to review the escrowed documents.[147]

After the documents are placed in escrow, the agency can verify the documents to ensure completeness and legibility. Completeness is assured by comparing the documents to those listed in the affidavit. Incomplete submittals or illegible documents may be corrected by a supplemental submittal. The verification process is a practical requirement. To learn after the project is over that the bid documents in the escrow container are incomplete or illegible may be too late. By then, the original documents may be lost or discarded. If the documents are illegible because of poor copying, they would be of little value. Illegible documents rarely refresh memories in depositions.

The bid documents remain in escrow during the life of the contract or until the contractor submits a claim, at which time the documents may be obtained by the owner for its use in evaluating the claim. The owner will instruct the escrow agent to release the bid document container to the contractor after the project is completed and the contractor has signed a release of all claims.[148]

Confidentiality of the bid documents is of serious concern. The AASHTO provisions provide that the agency will make every reasonable effort to ensure confidentiality of the bid documentation. The ODOT specifications state that the department will safeguard the escrow dDocuments and all information they contain against disclosure to the fullest extent permitted by law.[149] In addition, the cost of the bid escrow is included in contract bid prices, and failure to provide bid documentation renders the bid nonresponsive.

The WSDOT's escrow bid documentation specification was challenged by the Associated General Contractors of Washington in a lawsuit.[150] Because of Washington's liberal public disclosure laws,[151] contractors voiced concern about the confidentiality of bid information. They claimed that the information contained trade secrets, the disclosure of which could undermine their competitive positions.[152] The court upheld the specification.[153]

[147] *Id.*

[148] Arizona Standard Specification 103.11(C).

[149] ODOT PN110 Escrow Bid Documnents.

[150] Associated Gen. Contractors of Wash. v. State, Thurston County Cause No. 86-2-01972-1 (1986).

[151] Ch. 42.17, WASH. REV. CODE.

[152] *Contractors Challenge Bidding Rule*, ENGINEERING NEWS RECORD (Oct. 23, 1986), at 40.

[153] The contractor may, however, seek a protective order to protect information that, if disclosed, could harm its competitive position.

6. State Agency Precautions

a. Inclusion of Risk Allocation Provisions in Contracts

Some state standard contract provisions provide risk allocation provisions specifying that certain risks or occurrences are in contemplation of the parties when the contract is entered into. State agencies use these provisions to help insulate themselves from liability for delays and interference claims.

Florida DOT standard contract provisions contain risk allocation provisions and indicate that the parties anticipate that delays might be caused by and arise from any number of events during the term of the contract, including change orders, supplemental agreements, extra work, differing site conditions, right-of-way issues, permitting issues, actions by third parties, shop-drawing approval delays, etc. The provisions recognize that such delays are specifically contemplated and acknowledged by the parties and shall not be deemed to constitute willful or intentional interference without clear and convincing proof that they were the result of a deliberate act, without reasonable and good faith basis, and specifically intended to disrupt the contractor's performance.[154]

Stronger risk allocation provisions are contained in NYSDOT standard contract provisions, which list 11 instances that are contemplated in the contract and thus serve as ineligible reasons for delay compensation. The contract provides that the contractor has included in its bid for various items any extra or additional costs attributable to any delays, inefficiencies, or interference in the performance of the contract caused or attributable to specified events. Some of the instances of noncompensable delays include extra work that does not significantly affect the overall completion of the project, climatic conditions, restraining orders, injunctions, increase in contract quantities below 25 percent, strikes, presence or work by third parties on the contract site, and award of the contract beyond 45 days. A complete discussion of these provisions is contained in Section 1(B)(5) of this study;[155] however, NYSDOT's Standard Specifications do permit delay compensatrion for differing site conditions, significant changes to the character of the work, and suspension of the work directed by the engineer.

b. Contract Audit Provisions

Several state transportation specifications require contractors to provide access to various accounting and job records, which are necessary for review and analysis of claims and disputes. Providing a list of records in the base contract minimizes record disputes and greatly assists in claim resolutions. The right to audit provisions give owners rights to review various accounting documents and help to deter frivolous undocumented claims. The AASHTO Guide Specifications provide that

[154] FDOT Specification 5.12.6.2.

[155] NYSDOT § 108.04 Delay Provision.

the contractor, subcontractor, or suppliers shall cooperate with the agency and provide access to the following documents: daily time sheets and foreman's daily reports, union agreements, insurance welfare and benefit records, payroll register, earning records, payroll tax returns, material invoices, purchase orders, material cost distribution worksheets, equipment records, vendor rental agreements, subcontractor payment certificates, cancelled checks, job payroll ledger, general ledger and subsidiary ledgers and journals, cash disbursement journals, income tax returns, financial statements, depreciation records, bid preparation documents, all documents reflecting actual profit and overhead during contract performance and each of the 5 years before starting the project, all documents used to develop the contractor's equipment ownership costs for internal purposes, and worksheets used to prepare the claim and establish cost component of claim items.[156]

It should be noted that review of tax returns as to past profits, job cost ledgers as to actual costs, and financial statements as to overhead and equipment costs can have significant impact on damage defense positions.

Florida DOT Standard Specifications Section 5-14, Auditing of Claims, provides that a state audit may be performed by employees of the department or by an independent auditor appointed by the department. The provisions indicate that as a condition precedent to recovery on any claim, the contractor, subcontractor, or supplier must retain sufficient records and provide full and reasonable access to such records. Failure to retain sufficient records of the claim and failure to provide reasonable access to such records shall constitute a waiver of that portion of such claim that cannot be verified and shall bar recovery. The provision further mandates the contractor to make available for copying, at the department's expense, a list of records, which is nearly identical to the AASHTO listing specified above.

NYSDOT Standard Specifications Section 105 G, the right-to-audit provision, contains a similar list of records that are to be made available but does omit income tax returns from the list. The New York provisions provide that failure to maintain and retain sufficient records shall constitute a waiver of that portion of that dispute that cannot be verified and shall bar recovery thereunder and that failure to substantially furnish the required accounting records shall constitute a waiver of that portion of the dispute for payment, other than for payment at contract unit prices for the work perfomed.

[156] AASHTO Guide Specification § 105.18.

B. CONTRACTORS' CLAIMS AGAINST OWNERS AND DESIGN PROFESSIONALS

1. Introduction

Contracts are based on expectations. The law protects those expectations by providing a remedy when they are not fulfilled, due to some default by the other contracting party. "The controlling policy consideration underlying the law of contracts is the protection of expectations bargained for."[157] The expectations that the contractor has bargained for are to complete the project on time and make a profit. Usually, it's when these expectations are not fulfilled that claims arise.

Generally, claims by contractors against owners may be grouped into categories. This Subsection discusses those categories.[158] Before discussing the various theories of liability, mention should be made about some of the differences between public and private construction contracts. In addition to the procedural limitations imposed by sovereign immunity,[159] government contracts may also implement social and economic policies as part of the public works contracting process. Minority and Disadvantaged Business Enterprise Requirements[160] and labor and wage standards[161] are some examples.

Although public and private contracts differ in many respects, generally speaking a state, by entering into a contract with a private party for goods and services, absent a statute or contractual provision to the contrary, waives its sovereign immunity and impliedly consents to the same liabilities as a private party.[162] This Subsection discusses those liabilities.

2. Contract Interpretation

Disputes about what the contract requires are a fertile source for claims by contractors. The contracting parties may disagree about how certain work should be paid for,[163] the scope of the work called for by the con-

[157] Sensenbrenner v. Rust, Orling & Neale, Architects, Inc., 236 Va. 419, 374 S.E.2d 55, 58 (1988).

[158] The law dealing with damages, discussed in Subsection C *infra*, measures how those unfilled expectations may be compensated.

[159] *See generally* Subsection A, *supra* of this Section.

[160] *See generally* Subsection A, of Section 4.

[161] *See generally* Subsection B, of Section 4; *see also* 3 SANDS & LIBONATI, LOCAL GOVERNMENT LAW § 22.05.50 (2000).

[162] Clark County Constr. Co. v. State Highway Comm'n, 248 Ky. 158, 58 S.W.2d 388 (Ky. 1933); Architectural Woods, Inc. v. State, 598 P.2d 1372 (Wash. 1979).

[163] Dick Enterprises, Inc. v. Department of Transp., 746 A.2d 1164, 1168 (Pa. Commw. 2000); (dispute over the rate of pay for certain excavation that the contract required); R.W. Duntleman Co. v. Village of Lombard, 281 Ill. App. 3d 929, 666 N.E.2d 762, 217 Ill. Dec. 93 (1996) (dispute over whether payment should be made under "pavement removal" or "special excavation").

tract,[164] and the responsibility for events occurring during contract performance that affect the work.[165] When the parties disagree about the contractual rights and duties, they may resort to litigation asking the court to interpret their contract.[166]

a. Principles of Contract Interpretation

When parties to a contract dispute the meaning of their agreement and resort to litigation, the court will examine the contract language to determine whether it is ambiguous.[167] The court's basic purpose in interpreting the contract is to give effect to the intention of the parties as it existed when they entered into their contract.[168] Only the objective intentions of the parties, as expressed in their contract, is relevant.

If, however, it were proved by twenty bishops that either party, when he used the words, intended something else than the usual meaning which the law imposes upon them, he would still be held, unless there were some mutual mistake or something else of the sort. Of course, if it appear by other words, or acts, of the parties, that they attribute a peculiar meaning to such words as they use in the contract, that meaning will prevail, but only by virtue of the other words, and not because of their unexpressed intent.[169]

Contract interpretation begins with the plain language of the contract to determine whether the language is ambiguous.[170] In analyzing the language, the court will prefer an interpretation that gives a reasonable and consistent meaning to all parts of the contract, avoiding, if possible, an interpretation that leaves a portion of the contract meaningless, superfluous, or achieves an unreasonable or absurd meaning.[171]

The interpretation of a contract is a matter of law.[172] Only when a contract is ambiguous will extrinsic evidence be considered in interpreting the contract.[173] Usually when the contract language is clear and unambiguous, the court will not consider extraneous circumstances, such as prior negotiations or trade practices for its interpretation.[174] This is generally referred to as the "plain meaning" rule and is applied in most states.[175]

A few states follow the "context" rule of contract interpretation rather than the "plain meaning" rule.[176] Under the "context" rule, an ambiguity in the meaning of the contract need not exist before evidence of the circumstances surrounding the making of the contract is admissible to ascertain the parties' intent. The Parol Evidence rule is not violated because the evidence is not offered to contradict or vary the meaning of the agreement. To the contrary, it is being offered to explain what the parties may have intended.

The "context" rule is based on the premise that the uncertainties of language in clearly expressing intent make ambiguity an unreliable test for determining what the parties actually intended. The Arizona Supreme Court in commenting on the "context" rule said:

> Under the view embraced by Professor Corbin and the Second Restatement, there is no need to make a preliminary finding of ambiguity before the judge considers extrinsic evidence. Instead, the court considers all the proffered evidence to determine its relevance to the parties' intent and then applies the parol evidence rule to exclude from the fact finder's consideration only the evidence that contradicts or varies the meaning of the agreement.…[177]

The "context" rule should not apply where one of the parties did not participate in the drafting of the con-

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[164] Earth Movers v. State, Dep't of Transp., 824 P.2d 715 (Alaska 1992) (dispute over whether the contract gave the contractor the right to erect temporary road closure signs or whether the State could erect them); Western States Constr. v. United States, 26 Cl. Ct. 818 (1992).

[165] DiGioia Bros. Excavating v. City of Cleveland, 135 Ohio App. 3d 436, 734 N.E.2d 438 (1999) (dispute over whether the contract was ambiguous in designating responsibility for coping with underground utilities); Central Ohio Vocational Bd. of Educ. v. Peterson Constr. Co., 129 Ohio App. 3d 58, 716 N.E.2d 1210, 1213 (1998) (dispute over the meaning of the term, "Full Depth," in the contract, as it related to the depth of removal of unsuitable material).

[166] In some states, the determination as to what the contract requires may be made by a board of claims or by an arbitrator depending on what the law provides as the contractor's "final remedy." *See* Subsection A.3.b of this Section listing by state the final remedy available to contractors.

[167] Metric Constructors, Inc. v. United States, 44 Fed. Cl. 513, 520 (1999).

[168] RESTATEMENT OF CONTRACTS § 201 (2d); 11 WILLISTON ON CONTRACTS, § 32:2 (4th ed. 1999) Kass v. Kass, 91 N.Y.2d, 554, 696 N.E.2d 174, 673 N.Y.S.2d 350 (N.Y. 1998); 5 CORBIN ON CONTRACTS, § 24 (rev. ed. 1993); Leo F. Piazza Paving Co. v. Foundation Contractors, Inc., 128 Cal. App. 3d 583, 591, 177 Cal. Rptr. 268 (1981).

[169] Hotchkiss v. National City Bank of N.Y., 200 Fed. 287, 293 (S.D. N.Y. 1911), *aff'd*, 231 U.S. 50 (1913).

[170] Gould, Inc. v. United States, 935 F.2d 1271, 1274 (Fed. Cir. 1991).

[171] Patterson, The Interpretation and Construction of Contracts, 64 COLUM. L. REV. 833 (listing the maxims of contract interpretation); RESTATEMENT OF CONTRACTS § 203 (2d 1981). Dick Enterprises v. Department of Transp., *supra* note 103.

[172] Hol-Gar Mfg. Corp. v. United States, 169 Ct. Cl. 384, 51 F.2d 972, 974 (Ct. Cl. 1965); RESTATEMENT OF CONTRACTS § 212(2) (2d 1979).

[173] Sylvania Elec. Products, Inc. v. United States, 198 Ct. Cl. 1061, 458 F.2d 994, 1005 (Ct. Cl. 1972); E. Posner, *The Parol Evidence Rule, The Plain Meaning Rule and the Principles of Contractual Interpretation*, 146 U. PA. L. REV. 533 (1998).

[174] R. B. Wright Constr. Co. v. United States, 919 F.2d 1569, 1572–73 (Fed. Cir. 1990) (specification requiring three coats of paints clear and unambiguous; trade practice of applying one coat not relevant).

[175] *See* the Table in this part of the Subsection listing the states that follow the "plain meaning" rule.

[176] *See* the Table referred to in note 116 for the states that follow the "context" rule.

[177] Taylor v. State Farm Mut. Auto Ins. Co., 175 Ariz. 148, 854 P.2d 1134, 1138–39 (1993) (citations omitted); *see also* 3 CORBIN ON CONTRACTS, § 542 (1992 supp.); RESTATEMENT OF CONTRACTS § 212 (2d 1981).

tract.[178] Likewise, the "context" rule should not apply to public works that are competitively bid based on contract documents furnished by the owner.[179]

States that follow the "plain meaning" rule and the "context" rule are shown in the following Table.

[178] Morton Inter. v. Aetna Cas. & Sur. Co., 106 Ohio App. 3d 653, 666 N.E.2d 1163, 1170 (Ohio App. 1995) (insured did not participate in drafting endorsement, hence there was no evidence of mutual intent other than the language of the contract).

[179] An exception would be technical terms that have a special meaning in the construction trade. *See* Western States Constr. Co. v. United States, 26 Ct. Cl. 818, 824 (1992).

STATE	"PLAIN MEANING" RULE	"CONTEXT" RULE	CITATION
Alabama	X		*Pacific Enterprises Oil Co. v. Howell Petroleum Corp*., 614 So. 2d 409, 414 (1993)
Alaska		X	*Stepanav v. Homer Elec. Ass'n*, 814 P.2d 731, 734 (1991)
Arizona		X	*Taylor v. State Farm Mut. Auto Ins. Co*., 854 P.2d 1134, 1140 (1993)
Arkansas	X		*City of Lamar v. City of Clarksville*, 863 S.W.2d 805, 810 (1993)
California	X		*Brookwood v. Bank of America*., 53 Cal. Rptr. 2d 515, 517 (1996)
Colorado	X		*Peters v. Smuggler-Durant Min. Corp*., 910 P.2d 34, 41–42 (1995)
Connecticut	X		*Herbert S. Newman & Partners v. CFC Constr. Ltd.,* 674 A.2d 1313, 1317–18 (1996)
Florida	X		*Emergency. Assocs. v. Sassano*, 664 So. 2d 1000, 1002 (Fla. App. 1995)
Georgia	X		*Hartley-Selvey v. Hartley*, 410 S.E.2d 118, 120 (1991)
Idaho	X		*City of Idaho Falls v. Home Indem. Co*., 888 P.2d 383, 386 (1995)
Illinois	X		*Klemp v. Hergott Group*, 641 N.E.2d 957, 962 (Ill. App. 1994)
Indiana	X		*In re. of Forum Group, Inc*., 82 F.3d 159, 163 (7th Cir. 1996) (Applying Indiana Law)
Iowa	X		*Howard v. Schildberg Constr. Co*., 528 N.W.2d 550, 554 (1995)
Kansas	X		*D.R. Lauck Oil Co. v. Breitenback*, 893 P.2d 286, 288 (Kan. App. 1995)
Louisiana	X		*Lewis v. Hamilton*, 652 So. 2d 1327, 1329 (1995)
Maryland	X		*Taylor v. Feissner*, 653 A.2d 947, 955 (Md. App. 1995)
Massachusetts	X		*J.F. White Contracting Co. v. Mass. Bay Transp. Auth*., 666 N.E.2d 518 (Mass. App. 1996)
Michigan	X		*Pierson Sand & Gravel Inc*., 851 F. Supp. 850, 858 (W.D. Mich. 1994) (Applying Michigan Law)
Minnesota	X		*Michalski v. Bank of Am.*, 66 F.3d 993, 996 (8th Cir. 1995) (Applying Minnesota Law)
Mississippi	X		*Century 21 Deep S. Properties, v. Keys,* 652 So. 2d 707, 716 (1995)
Missouri	X		*Lake Cable Inc. v. Trittler*, 914 S.W.2d 431, 435–6 (Mo. App. 1996)
Montana	X		*Carbon County v. Dain Bosworth Inc*., 874 P.2d 718, 722 (1994)
Nebraska	X		*C.S.B. Co. v. Isham*, 541 N.W.2d 392, 396 (1996)
New Jersey	X		*Sons of Thunder Inc. v. Borden Inc*., 666 A.2d 549, 559 (N.J. Super. A.D.

STATE	"PLAIN MEANING" RULE	"CONTEXT" RULE	CITATION
			1995)
New Mexico		X	*C.R. Anthony Co. v. Loretto Mall Partners*, 817 P.2d 238, 242 (1991)
New York	X		*Cook v. David Rozenholc & Associates*, 642 N.Y.S.2d 230, 232 (App. Div. 1996)
North Carolina	X		*Estate of Waters v. C.I.R.*, 48 F.3d 838, 844 (4th Cir. 1995) (Applying North Carolina Law)
North Dakota	X		*Jones v. Pringle & Herigstad*, 546 N.W.2d 837, 842 (1996)
Ohio	X		*Stone v. Nat. City Bank*, 665 N.E.2d 746, 752 (Ohio App. 1995)
Oregon	X		*Housing Auth. of Portland v. Martini*, 917 P.2d 53, 54 (Or. App. 1996)
Pennsylvania	X		*Holt v. Dept. of Pub. Welfare*, 678 A.2d 421, 423 (Pa. Commw. 1996)
Rhode Island	X		*Clark-Fitzpatrick, Inc. v. Franki Foundation Co.*, 652 A.2d 440, 443 (1994)
South Carolina	X		*Friarsgate, Inc. v. First Fed. Sav. & Loan Ass'n.*, 454 S.E.2d 901, 905 (1995)
Tennessee	X		*Cummin's v. Vaughn*, 911 S.W.2d 739, 742 (Tenn. App. 1995)
Texas	X		*Gen. Devices Inc. v. Bacon*, 888 S.W.2d 497, 502 (Tex. App. 1994)
Vermont		X	*Isbrandsen v. North Branch Corp.*, 556 A.2d 81, 84 (1988)
Virginia	X		*Capitol Commercial Properties, Inc. v. Vina Enterprises, Inc.*, 462 S.E.2d 74, 77 (1995)
Washington		X	*Berg v Hudesman*, 801 P.2d 222, 228 (Wash. 1990)
Wyoming	X		*Treemont, Inc. v. Hawley*, 886 P.2d 589, 592–3 (1994)

If the meaning of the contract is unclear, the court may employ certain general rules in interpreting what it means.[180] The rules are only aids to assist the court in determining what the parties intended when they entered into their contract.[181] When a contract is subject to two or more possible interpretations, one of which is reasonable and the other or others are not, the court will adopt the interpretation that gives a reasonable and effective meaning to all of the contract provisions.[182] An interpretation that is unreasonable will be rejected.[183]

Another standard rule is that words will be given their plain and ordinary meaning, unless the context in which they are used makes it clear that they have a special or technical meaning.[184] The court may apply its own understanding of what the words mean,[185] or it may use a dictionary to define the meaning of the words.[186] Another standard rule is that specific provi-

[180] *See* Patterson, The Interpretation and Construction of Contracts, 64 COLUM. L. REV. 833 (1964) (listing the maxims of contract interpretation); RESTATEMENT OF CONTRACTS § 202 (2d 1981).

[181] Eurick v. Pemco Ins. Co., 108 Wash. 2d 338, 738 P.2d 251, 252 (1987).

[182] Dick Enters. v. Commw., Dep't of Transp., 746 A.2d 1164, 1170 (Pa. Commw. 2000) (court accepted State's interpretation as to the appropriate payment rate for certain excavation materials).

[183] Metric Contractors, Inc. v. United States, 44 Fed. Cl. 513, 521 (1999) (court found, as a matter of law, that the contractor's interpretation that it was not required by the contract to install certain equipment was unreasonable).

[184] Western States Constr. Co. v. United States, 26 Ct. Cl. 818 (1992).

[185] A-Transport Northwest Co. v. United States, 36 F.3d 1576, 1583–84 (Fed. Cir. 1994).

[186] Akron Pest Control v. Radar Exterminating Co., 216 Ga. App. 495, 455 S.E.2d 601, 602–03 (1995).

sions will govern or qualify general provisions.[187] But this rule will not apply where other provisions of the contract clearly resolve any conflict between a specific provision and a general provision.[188] Applying these rules and other maxims of interpretation,[189] it is the court's function to ascertain and give effect to the parties' intent. It is not the court's function "to re-write the provisions of the contract when the terms of the contract, taken as a whole, are clear."[190]

b. Order of Precedence Clauses

Government construction contracts often consist of a number of documents, such as standard specifications, special provisions, amendments to the standard specifications, plans, and cross-sections.[191] Some of these documents may conflict with each other. To resolve inconsistencies between the documents, the contract may contain an Order of Precedence clause that specifies which of the conflicting documents takes precedence over the other, thus resolving the conflict.[192] For example, the clause may provide that the contract plans take precedence over the special provisions, so that if there is a conflict between the two, the plans will govern.[193] The clause is a practical way of resolving conflicting provisions that would otherwise make the contract ambiguous. The clause has been consistently recognized as a valid and effective agreement by the parties as to how such conflicts are to be resolved.[194]

c. Resolving Contractual Ambiguities

When the court is unable to determine the meaning of the disputed language using the rules of contract interpretation, the court may admit parol evidence to resolve the ambiguity.[195] The evidence may consist of a course of dealings between the parties, or trade practices that are relevant to the dispute.[196] How the parties act during contract performance "before the advent of controversy, is often more revealing than the dry language of the written agreement by itself."[197] When parol evidence is admitted to explain the parties' intent, their intent is no longer a question of law but is a question of fact for the trier of fact to determine.[198]

When a contract is susceptible to more than one reasonable interpretation, it is ambiguous.[199] If the ambiguity is not resolved, the language will be construed against the party that drafted the language.[200] This is the rule of *Contra Proferentem*. Its purpose is to protect the party who did not create the ambiguity by construing the ambiguity against the party who wrote it.[201] Ordinarily, the public agency drafts the contract documents. Thus, the ambiguity is usually construed against the agency and the contractor's interpretation is controlling. The rule of *Contra Proferentem* has its limits. A bidder cannot take advantage of a patent ambiguity. The bidder has a legal duty to inform the owner about the error. Failure to do so bars any claim for extra compensation that could have been avoided had the error been disclosed to the owner.[202] This duty exists regardless of the reasonableness of the contractor's interpretation so long as the ambiguity is obvious.[203] In *J.H. Berra Constr. v. Missouri Hwy. & Transp. Comm'n*, the court said:

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[187] Dick Enters. v. Department of Transp., *supra* note 122, at 1169.

[188] *Id*. (information on the contract plans resolved apparent conflict between the special provisions and other provisions of the contract relating the types of excavation).

[189] *See generally* E. Patterson, *The Interpretation and Construction of Contracts*, 64 COLUM. L. REV. 833 (1964) and Posner, *The Parol Evidence Rule, The Plain Meaning Rule, and the Principles of Contractual Interpretation*, 146 U. PA. L. REV. 533 (1997), relating to contract interpretation.

[190] Dick Enters. v. Dep't of Transp., *supra* note 122, at 1168. When a contract term is unambiguous, the court cannot give the language another meaning regardless of how reasonable it might be to do so. Triax. Pacific v. West, 130 F.3d 1469 (Fed. Cir. 1997).

[191] Dick Enters., *Id* at 1165, n.1.

[192] For an example of an Order of Precedence clause, *see* 48 C.F.R. § 52.214-29.

[193] Pennsylvania DOT Standard Specification § 105.04, referred to in *Dick Enters*., *supra* note 122, at 1169.

[194] John A. Volpe Constr. Co. VACAB, 638-68-1 BCA 6857, 31, 705–06 (1968); Scherrer Constr. Co. v. Burlington Memorial Hosp., 64 Wis. 2d 720, 221 N.W.2d 855 (Wis. 1974).

[195] Central Ohio Joint Vocational Sch. Dist. v. Peterson Constr., 129 Ohio App. 3d 58, 716 N.E.2d 1210, 1213 (Ohio App. 1998). RESTATEMENT OF CONTRACTS § 213 (2d 1979), 6 CORBIN ON CONTRACTS, § 583 (1993) (int. ed.); 1 WILLISTON ON CONTRACTS, § 33:1 (4th ed. 1999).

[196] Sea-Land Service, Inc. v. United States, 213 Ct. Cl. 555, 553 Fed. 651, 658 (1977); Max M. Stoeckert, d/b/a Univ. Brick & Tile Co. v. United States, 183 Ct. Cl. 152, 391 F.2d 639, 645 (Ct. Cl. 1968); RESTATEMENT OF CONTRACTS §§ 222-23 (2d 1979).

[197] Macke Co. v. United States, 199 Ct. Cl. 552, 556, 467 F.2d 1323, 1325 (1972).

[198] Hillis Motors, Inc. v. Haw. Auto. Dealers Ass'n, 997 F.2d 581, 588 (9th Cir. 1993).

[199] R.W. Dunteman Co. v. Village of Lombard, 281 Ill. App. 3d 929, 666 N.E.2d 762 (1996); Metric Contractors, Inc. v. NASA, 169 F.3d 747, 751 (Fed. Cir. 1999); Dick Enters. v. Department of Transp., 746 A.2d 1164, 1170 (Pa. Commw. 2000); Community Heating & Plumbing Co. v. Kelso, 987 F.2d 1575, 1579 (Fed. Cir. 1993); Mayer v. Pierce County Medical Bureau, 80 Wash. App. 416, 909 P.2d 1323, 1326 (1995).

[200] 5 CORBIN ON CONTRACTS, § 24.27 (rev. ed. 2001).

[201] Mastrobuono v. Shearson Lehman Hutton, 514 U.S. 52, 63, 115 S. Ct. 1212, 131 L. Ed. 2d 76 (1995); Metric Contractors, Inc. v. United States, 44 Fed. Cl. 513, 523 (1999), United States v. Seckinger, 397 U.S. 203, 216, 905 S. Ct. 880, 25 L. Ed. 2d 224 (1970).

[202] D'Annunzi Bros. v. N.J. Transit Corp., 245 N.J. Super 527, 586 A.2d 302, 304 (1991); Sipco Services & Marine, Inc., v. United States, 41 Fed. Cl. 176, 215 (1998). Blount Bros. Constr. Co. v. United States, 171 Ct. Cl. 478, 346 F.2d 962, 971–72 (Ct. Cl. 1965); *see also* Section 5, Subsection B(6), "Nondisclosure," *supra*.

[203] Fortec Constructors v. United States, 760 F.2d 1288, 1291 (Fed. Cir. 1985).

> Case law has held that this type of policy, known as the patent ambiguity doctrine, "was established to prevent contractors from taking advantage of the government, protect other bidders by assuring that all bidders bid on the same specifications, and materially aid the administration of government contracts by requiring that ambiguities be raised before the contract is bid, thus avoiding costly litigation after the fact…."[204]

The duty to seek clarification of a patent ambiguity may also be imposed by an express contract provision. The following is an example of this type of clause:

> The contractor shall take no advantage of any apparent error or omission in the plans or specifications. If the contractor discovers such an error or omission, he shall immediately notify the engineer. The engineer will then make such corrections and interpretations as may be deemed necessary for fulfilling the intent of the plans and specifications.[205]

In determining whether the ambiguity is patent, the court views the language from the position of a reasonably prudent contractor.[206] However, a contractor is entitled to rely on an Order of Precedence clause in the contract and need not seek clarification if the ambiguity is resolved by that clause.[207]

3. Breach of Contract Claims and Equitable Adjustments Under Specific Contract Clauses

As a general rule, a contractor cannot sue for breach of contract when the claim arose under a specific contract clause providing for a price adjustment.[208] Often, damages for breach of contract and an equitable adjustment under the contract are priced in the same manner. This is consistent with the purpose in awarding compensatory damages for breach of contract and compensation based on an equitable adjustment. Both are designed to put the contractor in the same economic position it would have been in if the breach,[209] or the change,[210] had not occurred. There are instances, however, where the amount of compensation will vary depending on the legal theory upon which the claim is based. For example, a claim based on breach of contract for adverse site conditions may include compensatory damages for the affect of the condition upon unchanged work. Under many DSC clauses, the equitable adjustment provisions of the clause prohibit recovery for impact costs. Thus, in defending claims, care should be taken to assure that the claim is based on the appropriate legal theory.

Aside from considerations about damages,[211] claims based on breach of contract and contact price adjustment clauses have two things in common: a contractual basis for the claim and the requirement of causation. The contractual basis for breach may be the owner's failure to perform an express or implied promise in the contract.[212] The contractual basis for an equitable adjustment is a specific contract clause that provides for price adjustment in the contract amount and/or an extension of contract time if certain events covered by the clause occur during contract performance. The DSC clause, the Changes clause, and the Suspension of Work clause are some examples.[213]

Once the contractual basis for the claim is established, the contractor must prove that there is a causal link or nexus between the contractual right asserted and the event that caused the injury. Suppose, for example, that the contract provided that the project site would be available to the contractor when the contract was signed by the owner. The contract is signed, but the site is not available, causing the contractor to stand by until the site is available. There is a causal link be-

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[204] 14 S.W.3d 276, 281 (Mo. App. 2000) (quoting Community Heating & Plumbing Co. v. Kelso, 987 F.2d 1575, 1580 (Fed. Cir. 1993)) (citations omitted).

[205] Missouri Standard Specification, § 105.4.1.

[206] Delcon Constr. Corp. v. United States, 27 Fed. Cl. 634, 637 (1993).

[207] Hensel Phelps v. United States, 888 F.3d 1296 (Fed. Cl. 1989).

[208] J.F. White v. Mass. Bay Transp. Auth., 40 Mass. App. Ct. 937, 666 N.E.2d 518, 519 (1996); Wildner Contracting v. Ohio Turnpike Comm'n, 913 F. Supp. 1031 (N.D. Ohio 1996); Hensel Phelps Constr. Co. v. King County, 57 Wash. App. 170, 787 P.2d 58, 61 (1990); Hoel-Steffen Constr. Co. v. United States, 197 Ct. Cl. 561, 456 F.2d 760 (Ct. Cl. 1972).

[209] 11 CORBIN ON CONTRACTS § 992 (1993 int. ed); 24 WILLISTON ON CONTRACTS § 64:1 (4th ed. 1999).

[210] Bruce Constr. Corp. v. United States, 163 Ct. Cl. 97, 324 F.2d 516, 518 (Ct. Cl. 1963); Pacific Architects & Engineers v. United States, 203 Ct. Cl. 499, 491 F.2d 734, 739 (Ct. Cl. 1974).

[211] Damages are discussed in Subsection C of this Section.

[212] State v. Eastwind, Inc., 851 P.2d 1348, 1350 (Alaska 1993) (requiring the contractor to perform work in a manner different than called for in the contract); Hubbard Constr. Co. v. Orlando/Orange County Expressway Auth., 633 So. 2d 1154 (App. Div. 5 Dist. 1994) (imposing a stricter standard to test the density of a highway embankment than required by the contract); APAC Georgia, Inc. v. Department of Transp., 221 Ga. App. 601, 472 S.E.2d 97, 100–01 (1996) (failure to coordinate design changes between prime contractors as required by an express provision in the contract); D.H. Blattner & Sons v. Fireman's Ins. Co., 535 N.W.2d 671, 675–77 (Minn. App. 1995) (breach of implied warranty as to the correctness of the plans and specifications—following United States v. Spearin, 248 U.S. 132 (1918)); Beltrone Constr. Co. v. State, 256 A.D. 2d 992, 682 N.Y.S.2d 299 (1998) (failure to coordinate concurrent prime contractors); Chantilly Constr. Corp. v. Department of Highways, 6 Va. App. 282, 369 S.E.2d 438, 444 (1988) (defective specifications); Zook Bros. Constr. Co. v. State, 171 Mont. 64, 556 P.2d 911, 915 (1976) (failure to provide right-of-way); Gilbert Pacific Corp.v. State Dep't of Transp., 110 Or. App. 171, 822 P.2d 729, 732 (1991) (defective plans and specifications); Procon Corp. v. Utah Dep't of Transp., 876 P.2d 890 (Utah App. 1994) (changing the angle of a cut in a highway embankment from that shown in the plans was a breach); John W. Goodwin, Inc. v. Fox, 1994 Me. 33, 725 A.2d 541 (1999) (failure to make timely progress payments).

[213] *See generally* Section 5, Subsections A (The Changes Clause) and B (Differing Site Conditions).

tween the right asserted (the contractual right to begin work when the contract was executed) and the event (site not available) that caused the contractor to incur additional expense. The additional costs are factually tied to the event—the non-availability of the site as promised in the contract. The next step in the process is for the contractor to prove damages, which is discussed in the next subsection.

4. Subcontractor Pass-Through Claims

There is no contractual privity of contract between the project owner and a subcontractor.[214] In the absence of privity, a subcontractor has no standing to sue the owner contractually, either directly or as a third beneficiary of the contract between the owner and the prime contractor.[215] But the owner may be liable to a subcontractor on a pass-through basis.

> When a public agency breaches a construction contract with a contractor, damage often ensues to a subcontractor. In such a situation, the subcontractor may not have legal standing to assert a claim directly against the public agency due to a lack of privity of contract, but may assert a claim against the general contractor. In such a case, a general contractor is permitted to present a pass-through claim on behalf of the subcontractor against the public agency….[216]

Although the subcontractor has no standing to sue the owner, it can sue the prime with whom it has privity. The prime in turn can sue the owner "passing-through" the subcontractor's claim. Usually the prime and the subcontractor will enter into an agreement in which the prime agrees to pursue the sub's claim against the owner and pay any recovery to the sub. In exchange, the sub waives its claims against the prime. The agreement will contain language that it is not a release of the subcontractor's claim. This is to avoid any argument that the claim is waived under the *Severin* doctrine.

Under the *Severin* doctrine, a prime contractor may sue an owner for damages that the owner caused the subcontractor only when the prime contractor seeks reimbursement for damages it paid the subcontractor, or when the prime contractor remains liable to the subcontractor for damages.[217] In *Severin*, both the prime contractor and the subcontractor incurred damages because of owner delay. The prime was allowed to recover its damages, but it was not allowed to recover on behalf of its subcontractor. The prime contractor was not liable to its subcontractor because the subcontract contained a clause waiving delay damages. Since the prime contractor was not liable to the subcontractor, the owner was not liable for the subcontractor's damages. The rule has been stated as follows:

> Since our decision in the Severin case, supra, this court has repeatedly delineated the only ground's upon which a prime contractor may sue the government for damages incurred by one of its subcontractors through the fault of Government. The decided cases make it abundantly clear that a suit of this nature may be maintained only when the prime contractor has reimbursed its subcontractors for the latter's damages or remains liable for such reimbursement in the future….[218]

The burden, however, is on the owner to show that the prime contractor has no legal obligation to share any recovery with the subcontractor. In *Blount Bros. Constr. Co. v. United States*, the court said: "To come under the '*Severin*' Doctrine the defendant must show, through some contractual terms or a *release*, that the plaintiff-prime is not liable to the subcontractor."[219] This is consistent with the rule that standing to sue is an affirmative defense for the owner to raise and prove.[220]

The *Severin* doctrine does not apply to a subcontractor claim for an equitable adjustment when the equitable adjustment clause in the prime contract is included in the subcontract, either directly or by incorporation through a flow-down clause unless the owner can prove that the subcontractor has released or waived its claim.[221]

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[214] Jensen Constr. Co. v. Dallas County, 920 S.W.2d 761, 772 (Tex. App. 1996).

[215] Del Guzzi Constr. Co. v. Global Northwest, Ltd. 105 Wash. 2d 878, 719 P.2d 120, 125 (1986); Tarin v. Tinley, 3 P.2d 680 (N.M. App. 1999); Linde Enters., Inc. v. Hazelton City Auth., 412 Pa. Super. 67, 602 A.2d 897, 899 (1992); Lundeen Coatings Corp. v. Department of Water & Power, 232 Cal. App. 3d 816, 833, 283 Cal. Rptr. 551 (Cal. App. 1991).

[216] Howard Contracting, Inc. v. G.A. MacDonald Constr. Co., 71 Cal. App. 4th 38, 60, 83 Cal. Rptr. 2d 590 (1998). *See also* Buckley & Co. v. State, 140 N.J. Super. 289, 356 A.2d 56, 73 (1975), for cases from other jurisdictions holding that lack of privity between the subcontractor and the owner does not bar a pass-through claim. A pass-through claim was not allowed, however, where sovereign immunity was only waived with respect to parties who had contracted directly with the state. APAC-Carolina v. Greensboro-High Point Airport Auth., 110 N.C. App. 664, 431 S.E.2d 508, 511 (1993).

[217] Severin v. United States, 99 Cl. Ct. 435, 443 (1943); *cert. denied*, 322 U.S. 733, 645 Ct. 1045 (1944); *see also* Department of Transp. v. Claussen Paving Co., 346 Ga. 807, 273 S.E.2d 161, 164 (Ga. 1980); Kensington Corp. v. Department of State Highways, 74 Mich. App. 417, 253 N.W.2d 781, 783 (1977); John B. Pike & Son, Inc. v. State, 169 Misc. 2d 1037, 647 N.Y.S.2d 654 (N.Y. Ct. Cl. 1996).

[218] J. L. Simmons v. United States, 304 F.2d 886, 888 (Ct. Cl. 1962).

[219] 171 Ct. Cl. 478, 346 F.2d 962, 965 (Ct. Cl. 1965).

[220] The majority view is that the Severin defense is an affirmative defense and as such the owner has the burden of proof, not the contractor. Frank Coluccio Constr. v. City of Springfield, 779 S.W.2d 550, 552 (Mo. 1989); Gilbert Pacific Corp. v. State Dep't of Transp., 110 Ore. App. 171, 822 P.2d 729 (1991). But in Department of Transp. v. Claussen Paving Co., 246 Ga. 807, 273 S.E.2d 161 (1980), the court held that the prime contractor has the burden of proving that it is liable to the subcontractor.

[221] Owens-Corning Fiberglass Corp. v. United States, 190 Ct. Cl. 211, 419 F.2d 439, 457 (Ct. Cl. 1969), University of Alaska v. Modern Constr., Inc., 522 P.2d 1132, 1139 (Alaska 1974); Buckley & Co. v. State, Dep't of Transp., 140 N.J. Super. 289, 356 A.2d 56, 73 (1975).

A typical flow-down clause provides that the subcontractor is obligated to the prime contractor to the same extent as the prime contractor is obligated to the owner and that the subcontractor is entitled to the same rights granted the prime contractor by the owner under the main contract.[222] For example, the DSC clause in the prime contract may be incorporated into the subcontract by the flow-down clause and a DSC claim may be asserted by a prime contractor against the owner on behalf of the subcontractor.[223] Where, however, the DSC clause is not incorporated into the subcontract, there is no contractual basis for a DSC claim.[224]

The prime contractor's pass-through claim against the owner cannot exceed the amount of the prime contractor's liability to the subcontractor.[225] The prime contractor, however, is entitled to a markup on the amount it recovers on behalf of its subcontractors.[226]

5. Other Theories of Recovery

a. Unjust Enrichment

Unjust enrichment is a theory imposed by operation of law. The theory is based on the principle that a person unjustly enriched should be legally required to make restitution for the benefits received, if doing so does not violate any law, or conflict with an express provision in the parties' contract.[227] The theory usually arises in situations where there is no express contractual basis for recovery.[228] Recovery based on unjust enrichment is not permitted where it is barred by sovereign immunity,[229] violates a statute,[230] or conflicts with an express contract provision that covers the subject matter of the claim.[231]

To recover for unjust enrichment, a contractor must prove: (1) that a benefit was conferred; (2) that the owner knew that it was being conferred; and (3) that it would be inequitable for the owner to retain the benefit without paying for its value.[232] There cannot be any recovery where the contractor had no reasonable expectation of being paid for its services.[233]

The value of the benefit is determined on a *quantum meruit* basis.[234] The value of the benefit is measured by the actual costs the contractor incurred in performing the work.[235] But those costs will be disallowed to the extent they are shown to be excessive or unreasonable.[236]

b. Mutual Mistake of Fact

Another possible theory of recovery is mutual mistake. A mutual mistake occurs when contracting parties erroneously believe that some basic fact that affects contract performance is true. One party may seek to reform the contract so that it reflects what the parties actually intended.[237] The common law doctrine of mutual mistake has been applied by the Court of Claims to allow a contractor to recover additional performance costs caused by a mutual mistake about the necessity

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[222] Form No. 5, Associated General Contractors of America (AGC).

[223] Umpqua River Nav. Co. v. Cresent City Harbor Dist., 618 F.2d 588, 594 (9th Cir. 1980).

[224] Keith A. Nelson Co. v. R.L. Jones, Inc., 604 S.W.2d 351, 354 (Texas 1980) (no changed conditions clause in subcontract; subcontractor could not recover for changed conditions).

[225] John B. Pike & Son, Inc. v. State, 169 Misc. 2d 1034, 647 N.Y.S.2d 654, 656 (1996).

[226] Pa. Dep't of Transp. v. James D. Morrissey, Inc., 682 A.2d 9, 16 (Pa. 1996) (8 percent markup allowed).

[227] Aloe Coal Co. v. Department of Transp., 164 Pa. Commw. 453, 643 A.2d 757 (1994); 230 Park Ave. Assocs. v. State, 165 Misc. 2d 920, 630 N.Y.S.2d 855 (1995); J.A. Sullivan Corp. v. Commw., 397 Mass. 789, 494 N.E.2d 374, 377 (1986); 5 WILLISTON CONTRACTS, § 805 (1970).

[228] Leroy Callender, P.C. v. Fieldman, 252 A.D. 2d 468, 676 N.Y.S.2d 152, 153 (1998). Subcontractors may try to assert this type of claim when they have not been paid by the prime contractor for their work, but there is no unjust enrichment when the owner has paid the prime contractor, since equity will not require the owner to pay twice. International Paper Co. v. Futhey, 788 S.W.2d 303, 306 (Mo. App. 1990).

[229] Gregory v. Hunt, 24 Fed. 3d 781(6th Cir. 1994) (court applied Tennessee law holding that sovereign immunity was waived only with respect to breach of an express, written contract and that sovereign immunity barred a claim based on an implied contractual obligation); Cleansoils Wisconsin, Inc. v. State Dep't of Transp., 229 N.W.2d 903, 910 (Wis. App. 1999) (State did not consent to be sued for unjust enrichment); *But see* J. A. Sullivan Corp. v. Commonwealth, 397 Mass. 789, 494 N.E.2d 374, 377 (1986) (State could not avoid claim for unjust enrichment based on sovereign immunity).

[230] Parsa v. State, 64 N.Y.2d 143, 474 N.E.2d 235, 237, 485 N.Y.S.2d 27 (1984) (New York statute required contracts in excess of $15,000 to be in writing and approved by the comptroller); Seneca Nursing Home v. Kan. State Bd. of Social Welfare, 490 F.2d 1324, 1332 (10th Cir. 1974) (statute made state immune from liability for implied contracts although a unilateral contract was found to exist).

[231] P.J. Wildner Contracting Co. v. Ohio Turnpike Comm'n, 913 F. Supp. 1031, 1043 (N.D. Ohio 1996); Jensen Constr. Co. v. Dallas County, 920 S.W.2d 761, 774 (Tex. App. 1996); Mountain Pacific Chapter A.G.C. of America v. State of Wash., 10 Wash. App. 406, 518 P.2d 212, 214 (1974).

[232] Concrete Products Co. v. Salt Lake County, 734 P.2d 910, 911 (Utah 1987); Black Lake Pipe Line Co. v. Union Constr. Co., 538 S.W.2d 80, 86 (Tex. 1976); McDonald v. Hayner, 43 Wash. App. 81, 715 P.2d 519, 522 (1986).

[233] Aloe Coal Co. v. Department of Transp., *supra* note 168, at 767–68.

[234] J.A. Sullivan Corp. v. Commonwealth, *supra* note 168, at 378–79; 1 CORBIN ON CONTRACTS § 1.20 (rev. ed. 2001); 26 WILLISTON ON CONTRACTS § 68:1 (4th ed. 2003).

[235] United States ex rel. Susi Contracting Co. v. Zara Contracting Co., 146 F.2d 606, 611 (2nd Cir. 1944); RESTATEMENT OF CONTRACTS § 347-48 (2d).

[236] Acme Process Equip. Co. v. United States, 171 Ct. Cl. 324, 347 F.2d 509, 530 (Ct. Cl. 1965), *rev'd. on other grounds*, 385 U.S. 138, 87 S. Ct. 350.

[237] RESTATEMENT OF CONTRACTS § 155 (2d 1979).

for an additional step in a manufacturing process. The court held that neither party bore the burden caused by the mistake, and reasoned that the equitable resolution to the dispute was to reform the contract and split the additional costs equally between the parties.[238]

The doctrine applies only to mutual mistakes about existing facts at the time of contracting. The doctrine does not apply to mistakes about future events,"[239] or to risks that the contractor has assumed.[240]

c. Failure to Require a Statutorily Mandated Payment Bond

Public property is not subject to mechanics' liens. Subcontractors[241] on public work projects who are not paid for their work have no lien rights against the public improvement.[242] The rule is based on public policy. "It requires very little imagination to realize how disruptive the attachment and attempted foreclosure of such liens might be to the orderly operation of state and local government."[243] Subcontractors who are not paid for their work may not have any recourse against the prime contractor because of the latter's insolvency. The subcontractor's only recourse may be the payment bond and the retainage withheld by the public owner from progress payments.[244]

A public agency may be liable to unpaid subcontractors if it fails to require the prime contractor to obtain a payment bond from a surety. Some public bond statutes impose liability on the agency when it fails to require a bond.[245] Other bond statutes do not expressly impose liability on the agency for its failure to obtain a bond.[246] Courts have reached mixed results where a bond statute does not expressly impose liability. Some courts have held that a subcontractor had a direct right of action against the agency for its failure to require a bond.[247] Other courts have found no right of action, declining to create a cause of action where none had been created by statute.[248]

d. Inapplicability of Tort Law

The remedy for breach of contract is designed to put the nonbreaching party in the same position it would have been in had the breach not occurred. It is designed to protect the intentions of the parties, but it has been held that tort law was designed to protect social policies.[249] Claims for nonperformance of contractual obligations are based on breach of contract, not tort.[250]

Tort damages are not permitted in a breach of contract action unless the event constituting the breach was accompanied by conduct that amounts to a traditional common law tort.[251] In the absence of such conduct, courts will generally enforce the breach of a contractual obligation through contract law.[252] The policies underlying tort and contract remedies were stated by the Virginia Supreme Court.[253]

The controlling policy consideration underlying tort law is the safety of persons and property—the protection of persons and property from losses resulting from injury. The controlling policy consideration underlying the law of contracts is the protection of expectations bargained for. If that distinction is kept in mind, the damages claimed in a particular case may more readily be classified between claims for injuries to persons or property on the one hand and economic losses on the other.

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[238] National Presto Indus. v. United States, 167 Ct. Cl. 749 338 F.2d 99, 111–12 (Ct. Cl. 1964); *see also* Atlas Corp. v. United States, 895 F.2d 745, 750 (Fed. Cir. 1990) (court denied contractor's claim based on mutual mistake).

[239] Westinghouse Elec. Corp. v. United States, 41 Fed. Cl. 229, 238 (1998); RESTATEMENT OF CONTRACTS § 151 (2d).

[240] Knieper v. United States, 38 Fed. Cl. 128, 139–40 (1997); RESTATEMENT OF CONTRACTS § 152 (2d).

[241] The term subcontractors as used in this Subsection *also* refers to materialmen.

[242] Wells-Stewart Constr. Co. v. Martin Marrietta Corp., 103 Ariz. 375, 442 P.2d 119, 124 (Ariz. 1968); J.S. Sweet Co. v. White County Bridge, 714 N.E.2d 219, 222 (Ind. App. 1999).

[243] City of Evansville v. Verplank Concrete & Supply, 400 N.E.2d 812, 816 (Ind. Ct. App. 1980).

[244] Payment bond provides protection to those who furnish materials and services for public improvements. Davidson Pipe Supply v. Wyoming County Inds. Dev. Agency, 85 N.Y.2d 281, 648 N.E.2d 468, 469–70, 624 N.Y.S.2d 92 (1995); Retainage: city not liable to unpaid subcontractor for failure to withhold retainage from prime contractor's progress payments. Murname Assocs. v. Harrison Garage Parking Corp., 239 A.D. 2d 882, 659 N.Y.S.2d 665, 667 (N.Y. A.D. 1997).

[245] OR. REV. STAT. § 279.542.

[246] WASH. REV. CODE § 39.08.010 does not impose liability on state agencies, but rather only on counties, cities, and towns.

[247] Northwest Steel Co. v. School Dist. No. 16, 76 Or. 321, 148 Pac. 1134, 1135 (1915); City of Atlanta v. United Elec. Co., 202 Ga. App. 239, 414 S.E.2d 251, 253 (1991); Dekalb County v. J.A. Pipeline, 437 S.E.2d 327 (Ga. 1993).

[248] Accent Store Designs, Inc. v. Marathon House, Inc., 647 A.2d 1223 (R.I. 1996); *See also* Ihr v. City of Duluth, 56 Minn. 182, 59 N.W. 960 (Minn. 1894); Freeman v. City of Chanute, 63 Kan. 573, 66 Pac. 647, 649 (Kan. 1901); ABC Supply Co. v. City of River Rouge, 216 Mich. App. 396, 549 N.W.2d 73, 76 (1996).

[249] Sensebrenner v. Rust et al., 236 Va. 419, 374 S.E.2d 55, 58 (1988); Erlich v. Menezes, 21 Cal. 4th 543, 981 P.2d 978, 982, 87 Cal. Rptr. 2d 886 (Cal. 1999).

[250] State v. Transamerica Premier Ins. Co., 856 P.2d 766, 772 (Alaska 1993).

[251] Erlich v. Menezes, 981 P.2d at 983 (tortious conduct would include fraud, deceit, or an intent to cause severe harm to the non-breaching party). In addition, sovereign immunity, unless waived, would bar tort claims against state agencies.

[252] State v. Trans America Premier Ins. Co., *supra* note 191; *see also*, Foreman & Mills, Inc. v. Belcher Oil Co., 11 Cal. 4th 85, 900 P.2d 669, 682, 44 Cal. Rptr. 420 (Cal. 1995) (Mosk, J., concurring and dissenting).

[253] Sensenbrenner v. Rust et al., 374 S.E.2d at 58.

6. Claims Against the Owner's Design Professional and the Economic Loss Limitation on Liability

At common law, design professionals (typically architects and engineers) were not liable for the contractor's economic losses caused by defective plans and specifications. Design professionals could be legally responsible for personal injury and physical property damage caused by defective design, but not for economic damage suffered by third parties.[254] Traditionally, design professionals were retained by project owners. They owed their allegiance to the owners with whom they had contracted, not to the contractors with whom they had no contractual relationship.[255] The lack of contractual privity as a bar to suits by contractors against design professionals for economic damages begin to erode with the advent of products liability law.

> The law imposes upon every person who enters upon an active course of conduct the positive duty to use ordinary care so as to protect others from harm. A violation of that duty is negligence. It is immaterial whether the person acts in his own behalf or under contract with another. *** We cannot ignore the half century of development in negligence law originating in MacPherson [MacPherson v. Buick Motor Co., 217 N.Y. 382, 111 N.E. 1050 (1916)] and are impelled to conclude that the position and authority of a supervising architect are such that he ought to labor under a duty to the prime contractor to supervise the project with due care under the circumstances, even though his sole contractual relationship is with the owner….[256]

The rule has evolved in some jurisdictions that a contractor can sue a design professional in negligence for economic loss despite lack of privity between them.[257] The standard of care owed by the design professional and the failure to meet that standard requires expert testimony, unless the error is so obvious that expert testimony is not necessary.[258] The same rules apply to construction managers, who, as the name implies, are employed by owners to manage their construction projects.[259]

Under the economic loss rule, design professionals are not liable, either in tort or contract law, for economic losses suffered by contractors with whom they have no contractual privity.[260] The economic loss rule is based on the policy that a contractor's remedy for economic losses lies in the area of contract law, not tort law.[261] Courts that follow the economic loss rule often note that the rule provides predictability in allocating risk in the construction industry.[262] The fee for design services, for example, does not have to include premiums for errors and omissions coverage for economic loss due to construction delays caused by defective plans and specifications. "The fees charged by architects, …are founded on their expected liability exposure as bargained and provided in the contracts."[263]

A number of jurisdictions have concluded that lack of contractual privity will not bar a tort action by a contractor against a design professional for economic damages.[264] Other jurisdictions have reached an opposite conclusion, holding that a party cannot sue for economic loss in the absence of privity. The following Table lists many of the states that follow the economic loss rule and many that do not follow that rule.

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[254] The term "economic loss" includes increased costs of contract performance and consequent loss of profits. See, Barrett, Jr., *Recovery of Economic Loss in Tort for Construction Defects: A Critical Analysis*, 40 S.C. L. REV. 891, 892 (1989).

[255] Annotation, *Tort Liability of Project Architect for Economic Damages Suffered by Contractor*, 65 A.L. R. 3d 249, 252 (1975).

[256] Shoffner Indus. v. W.B. Lloyd Constr. Co., 42 N.C. App. 259, 257 S.E.2d 50, 55 (1979).

[257] *See* states listed in Table later in this subpart; *see also* RESTATEMENT OF TORTS § 552 (2d).

[258] Garaman, Inc. v. Williams, 912 P.2d 1121, 1123 (Wyo. 1996).

[259] James McKinney & Son, Inc. v. Lake Placid 1980 Olympic Games, Inc., 92 A.D. 2d 991, 461 N.Y.S.2d 483, 486 (A.D. 1983); John E. Green Plumb. & Heating Co. v. Turner Constr. Co., 500 F. Supp. 910, 912–13 (E.D. Mich. 1980).

[260] Floor Craft Floor Covering, Inc. v. Parma Community Gen. Hosp., 54 Ohio St. 3d 1, 560 N.E.2d 206, 208 (Ohio 1990); Berschauer/Phillips Constr. Co. v. Seattle Sch. Dist., 124 Wash. 2d 816, 881 P.2d 986, 989–90 (1994).

[261] Sensenbrenner v. Rust/Orling & Neale, 374 S.E.2d at 58; Berschauer/Phillips Constr. Co., *id*.

[262] *Id.*

[263] Berschauer-Phillips Constr. Co., 881 P.2d at 992.

[264] Insurance Co. of North America v. Town of Manchester, 17 F. Supp. 2d 81, 86 (D. Conn. 1998).

State	Economic Loss Rule Followed	Economic Loss Rule Not Followed	Citation
Alabama		X	*E.C. Ernest Inc. v. Manhattan Const. Co.*, 531 F.2d 1026 (5th Cir. 1979) (applying Alabama law).
Alaska		X	*Mattingly v. Sheldon Jackson College*, 743 P.2d 356, 360 (Ak. 1987).
Arizona		X	*Donnelly Constr. Co. v. Osberg/Hunt/Gilleland*, 677 P.2d 1292, 1294 (Ariz. 1984).
California		X	*J'Aire Corp. v. Gregory*, 24 Cal. 3d 799, 598 P.2d 60, 64 (1979). *See also Dept. of Water and Power v. City of Los Angeles v. ABB Power T&D Co.*, 902 F. Supp. 1178, 1188 (1995).
Connecticut		X	*Insurance Co. of N.A. v. Town of Manchester*, 17 F. Supp. 2d 81, 85 (D. Conn. 1998) (applying Connecticut Law).
Delaware	X		*Danforth v. Acorn Structures, Inc.*, 608 A.2d 1194, 1196 (1992).
Florida		X	*Morgansais v. Heathman*, 744 So. 2d 973, 978 (Fla. 1999).
Hawaii	X		*City Express Inc. v. Express Partners*, 959 P.2d 836, 840 (1998).
Illinois	X		*Anderson Elec. Inc. v. Ledbetter Erection Corp.*, 503 N.E.2d 246, 247 (Ill. 1986).
Louisiana		X	*Gurtler, Hebert & Co. v. Weyland Mach. Shop Inc.*, 405 So. 2d 660, 662 (La. App. 1981).
Massachusetts	X		*Priority Finishing Corp. v. LAL Constr. Co.*, 667 N.E.2d 290 (Mass. App. 1996).
Michigan		X	*Bacco Constr. Co. v. American Colloid Co.*, 384 N.W.2d 427, 434 (Mich. App. 1986).
Minnesota		X	*Prichard Bros., Inc. v. Grady Co.*, 428 N.W.2d 391 (Minn. 1988).

State	Economic Loss Rule Followed	Economic Loss Rule Not Followed	Citation
Mississippi		X	*City Council of Columbus v. Clark-Dietz & Associates-Engineers, Inc.*, 550 F. Supp. 610, 624 (N.D. Miss. 1980) (applying a Mississippi law).
Montana		X	*Jim's Excavating Services v. HKM Assocs*., 878 P.2d 248, 254 (Mont. 1994).
Nebraska		X	*John Day Co. v Alvine & Associates, Inc.*, 510 N.W.2d 462, 466 (Neb. App. 1993).
New Jersey		X	*New MEA Constr. Corp. v. Harper*, 497 A.2d 534, 540 (N.J. Super. 1985).
New York		Suit allowed if functional privity is established.	*Port Auth. of N.Y. v. Rachel Bridge Corp*., 597 N.Y.S.2d 35 (A.D. 1993) (functioning privity established); *Pile Foundation Constr. Co. v. Berger-Lehman Assocs.*, 676 N.Y.S.2d 664 (A.D. 1998).
North Carolina		X	*APAC-Carolina v. Greensboro High Point*, 431 S.E.2d 508, 517 (N.C. App. 1993).
Ohio	X		*Floor Craft v. Parma Com. Gen. Hosp*., 560 N.E.2d 206, 208 (Ohio 1990).
Rhode Island	X		*Forte Bros Inc. v. Nat. Amusements Inc*., 525 A.2d, 1301, 1303 (1987).
South Carolina	X		*Cullom Mech. Constr. Inc. v. S.C. Baptist Hospital*, 520 S.E.2d 809, 813 (S.C. App. 1999).
Tennessee		X	*John Martin Co. v. Morse/Diesel, Inc.*, 819 S.W.2d 428, 431 (Tenn. 1991) (adopting Section 552, Restatement (2d)).
Utah	X		*Anderson Towers Owners Ass'n v. CCI Mech., Inc*., 930 P.2d 1182, 1189 (Utah 1996).
Virginia	X		*Blake Constr. Co. v. Alley*, 353 S.E.2d 724, 726 (Va. 1987).
Washington	X		*Berschauer/Phillips*

State	Economic Loss Rule Followed	Economic Loss Rule Not Followed	Citation
			Constr. v. Seattle Sch. Dist., 881 P.2d 986, 990 (Wash. 1994).
Wisconsin		X	*A.E. Inv. Corp. v. Link Builders*, 214 N.W.2d 764, 768 (1974).
Wyoming	X		*Rissler & McMurray Co. v. Sheridan Area Water Supply Dist*., 929 P.2d 1228, 1234–35 (Wyo. 1996).

While the economic loss doctrine appears to have developed first at the state level, the U.S. Supreme Court recognized the doctrine in a 1986 decision, *East River Steamship Corp. v. Transamerica Delaval, Inc.*[265] In states whose courts have adopted it, the economic loss doctrine prohibits unintentional tort actions against professional or commercial defendants in which the plaintiff seeks to recover purely economic losses for the consequences of a negligent act in order to protect such defendants from unlimited liability and thereby keep the risk of liability reasonably calculable. The doctrine typically comes to bear in complex situations involving multiple contracting parties, not necessarily all in contractual privity with each other, and seeks to resolve responsibility for the consequences of negligent design through the principles of contract law rather than tort law, under which the calculation of damages might be much greater. Some analysts have suggested that contract law may, in effect, be preempting tort law in certain fields. Some have also suggested that this is explained by a rising preference for private ordering over public regulation. In determining whether to apply this doctrine, a court determines first whether the damages sought are purely economic in nature and then whether the economic loss doctrine applies to the type of claim involved. Even in some states that apply the doctrine, there may be certain exceptions, including claims for negligent misrepresentation.

In a 2010 case, *Hunt Constr. Group, Inc. v. Brennan Beer Gorman Architects, P.C. et al.*, the U.S. Court of Appeals for the Second Circuit referred to the Vermont Supreme Court the questions of whether, under Vermont law, the economic loss doctrine barred contractors from seeking purely economic damages from design professionals for breach of contract and if so whether that doctrine applied to the specific claim involved in the case.[266] The District Court had dismissed a contractor's case against a design professional retained by a property owner, involving late delivery of plans for a hotel construction project, on the grounds that Vermont had adopted the economic loss doctrine. The contractor appealed, asserting that its claims fell under exceptions for special relationships and for negligent misrepresentation. Reviewing Vermont case law, the Second Circuit found that the issues raised on appeal had not yet been resolved by Vermont courts and that these involved purely state law issues, would control the outcome of the case, lacked controlling precedent, and involved important issues. Accordingly, the Second Circuit referred the issues involving the economic loss doctrine to the Vermont Supreme Court for determination.

In a 2011 decision, *R&O Construction Co. v. Rox Pro et al.*, the U.S. District Court for the District of Nevada dismissed a contractor's actions against a design professional arising from a construction defect case.[267] While not a highway case, this was nonetheless of interest for its treatment of the economic loss doctrine. In that case, an architectural firm had been retained by the owner of a store chain to design stores, and a contractor had been hired by the owner to build a particular store. After a stone veneer installation failed during construction, requiring expensive repairs, the contractor sued both subcontractors and the design professionals, alleging negligent misrepresentation and breach of contract by the design professionals. The court granted the design firm's motion for summary judgment, ruling that the alleged negligent misrepresentation on the grounds was really a claim for professional negligence and as such was barred by the economic loss doctrine, which Nevada courts considered to bar malpractice claims against design professionals involved in commercial property development or improvement. The court also denied the contractor's breach of contract claim against the design professional, rejecting an argument that the contractor was an intended third party beneficiary to the design contract between the owner and the design professional.

In a 2010 decision, *Ohio County Devel. Auth. et ano. v. Pederson & Pederson, Inc.*, the U.S. District Court for the Northern District of West Virginia addressed the

[265] 476 U.S. 858, 868–69, 106 S. Ct. 2295, 90 L. Ed. 2d 865 (1986), cited in Maeda Pacific. Corp. v. GMP Hawaii, Inc., 2011 Guam 20; 2011 Guam LEXIS 20 (Nov. 17, 2011).

[266] 2008 U.S. Dist. LEXIS 93754 (D. Vt., Nov. 3, 2008).

[267] 2011 U.S. Dist. LEXIS 131633 (U.S. Dist. Ct. D. Nev., Nov. 14, 2011).

impact of the economic loss doctrine on the liability of design professionals in the context of an economic development project severely damaged by inadequate geotechnical and foundation design work.[268] The case involved a commercial distribution center built for a municipal development authority and leased to a commercial firm. The facility was built in a mountainous area on a dirt pad. The concrete began cracking after completion of construction due to inadequate construction of the dirt pad. After litigation commenced, a geotechnical subcontractor moved to dismiss a negligent design claim based on the economic loss doctrine. The court denied the defendant's motion to dismiss due to a lack of sufficient evidence on whether any special relationship existed that would establish an exception to the economic loss doctrine under West Virginia law. The court indicated that the existence of such a relationship would be determined largely by the extent to which the particular plaintiff was affected differently from society in general. The court also denied a motion to dismiss a breach of contract count denied, because there was insufficient evidence regarding whether the contract between the contractor and the geotechnical subcontractor was intended to benefit the owner of the facility. The court further denied a motion to dismiss an implied warranty claim on the basis that West Virginia courts rejected a lack of privity as a defense to such claims. The court granted a motion to dismiss a cross-claim for express indemnification without prejudice to refile an adequately drafted cross-claim. Finally, the court denied a motion to dismiss a cross-claim for implied indemnification and contribution.

In a 2009 case, *Federal Insurance Co. v. General Electric Co.*, the U.S. District Court for the Southern District of Mississippi addressed the economic loss doctrine but in a case arising from Hurricane Katrina and straddling the line between facility design liability issues and products liability cases.[269] **A** hospital had leased an MRI machine from General Electric (GE). A GE subsidiary had maintenance responsibilities and entered into a renovation contract with the hospital. Proper installation of the MRI machine required a special cryogenic vent system, which needed to operate continually on a on 24/7 basis. This system involved the use of liquid helium to cool a superconducting magnet and required a vent to relieve pressure in case the power failed and liquid helium vaporized and increased pressure in the system. The hospital was in the area affected by Hurricane Katrina, lost power, and had limited generators but no dedicated backup power source to keep the vent system operating and the MRI cooled. The helium in the cooling system vaporized, damaging the MRI's superconducting magnet, and efforts to refill the cooling system were thwarted by a leak somewhere in the ventilation system. The hospital ultimately replaced the damaged MRI machine with a new one at a cost of more than $1.3 million. The hospital's insurance company claimed that this was because the vent system had been inadequately designed and that GE should have known that. The insurance company brought various tort and contract claims, including negligent design of the MRI vent system, negligent failure to warn of the known risk of damage to the MRI's magnet if the vent system was obstructed, negligent failure to properly service and maintain the MRI by failing to take action when electric power was lost, breach of the service and support agreement, and breach of implied warranties provided by Mississippi law. Among multiple legal arguments for dismissal of the insurance company's claims, GE argued that the tort claims were barred under the economic loss doctrine. The court noted that the economic loss doctrine applied in product liability cases but had not been extended beyond product liability cases to apply to this case involving a duty shaped by a contract.

C. CONTRACTORS' CLAIMS—DAMAGES

1. Introduction

After entitlement is established, the contractor must prove damages.[270] Generally speaking, damages for breach and an equitable adjustment under the contract are measured in the same way. The general measure of damages for breach of contract is to put the nondefaulting party in as good a position, pecuniarily, as it would have been if the breach had not occurred.[271] Similarly, an equitable adjustment is designed to keep a contractor whole when the government modifies the contract.[272] The operative word is "equitable." The adjustment in the contract price should not give either party an advantage that it would not have had had there been no change. The measure of an equitable adjustment is "the difference between what it would have reasonably cost to perform the work as originally required and what it would reasonably cost to perform the work as changed.'"[273] A contractor who has underestimated his bid or incurred unanticipated costs may not use a

[268] 2010 U.S. Dist. LEXIS 6077 (U.S. Dist. Ct. ND W. Va. 2010).

[269] 2009 U.S. Dist. LEXIS 112931 (U.S. Dist. Ct. SD Miss. 2009).

[270] Entitlement may be based upon breach of contract or upon some remedy granting provision of the contract. *See generally*, subsection B, *supra*.

[271] Al and Zack Brown, Inc. v. Bullock, 238 Ga. App. 246, 518 S.E.2d 458, 461 (1999); 11 CORBIN ON CONTRACTS, § 992 (1993 int. ed.). 24 WILLISTON ON CONTRACTS § 64:1 (4th ed. 1999).

[272] Bruce Constr. Corp. v. United States, 163 Ct. Cl. 97, 324 F.2d 516, 518 (Ct. Cl. 1963); Morrison Knudsen Corp. v. Fireman's Fund Ins. Co., 175 F.3d 1221, 1234 n.8 (10th Cir. 1999).

[273] D.C. v. Organization for Envtl. Growth, 700 A.2d 185, 203 (D.C. App. 1997) (quoting Modern Foods, Inc., ASBCA No. 2090, 57-1 BCA ¶ 1229, 1957 WL 4960).

change order as an excuse or opportunity to shift its own losses or risks to the owner.[274]

The kinds of damages sought by a contractor may vary. They may include the cost of added labor, additional equipment costs, unabsorbed home office overhead expense, and delay and impact costs. These costs may be presented in different ways. They may be based on actual costs or estimates. They may be priced as discrete claim items, or they may be based on an approximation, using a jury verdict approach. [275] This subsection discusses the types of damages and costs that a contractor may seek, and the traditional methods that may be used to prove damages.

2. Contract Clauses Limiting Recovery

The amount of an equitable adjustment may be limited by the specific provisions of the contract. The DSC clause used by most states is one example. That clause does not allow additional compensation for any effects of the condition on unchanged work.[276] Another example is the suspension of work clause, which does not allow profit on delay costs.[277] Generally, clauses imposing limits on the amount that can be recovered under the contract are enforceable.[278]

A contractor may attempt to avoid the effect of those kinds of limiting clauses by claiming damages based on breach of contract. Whether such efforts are successful depends upon whether the contractor can prove that the changes were so substantial that they were beyond the general scope of the work specified in the contract. Changes of that magnitude may be a breach of contract.[279] If the change is within the general scope of the contract, the limitations on recovery apply.[280] The question of whether the change is within the general scope of the contract may be a question of fact,[281] of law,[282] or a mixed question of fact and law.[283]

Most construction contracts contain clauses that limit an owner's exposure for damages for breach of contract. No-damage-for-delay clauses are a common example of this type of clause.[284] Another example is clauses excluding liability for consequential damages.[285] A contracting party may validly waive its remedies for breach of contract by assenting to a clause limiting damages for breach of contract. Such clauses are enforceable unless they violate some specific public policy defined in a statute or legal precedent.[286]

In addition, some state transportation agencies do not permit contract ltitigation until after the contract work is completed. Florida standard contract provisions provide that no circuit court or arbitration proceeding on any claim or part thereof may be filed until after acceptance of all contract work or denial, whichever occurs last. New York State administrative practice moves to dismiss all filed claims until the contract work is completed and closed out. Permitting litigation can create significant obstacles to project completion. Engineers should not be forced to devote their time to attending depositions or preparing claim defenses to complex construction litigation while the project is still under construction, but should be directing their engineering efforts to completing the project. On the other hand, permitting construction litigation before project completion enhances real-time issue analysis and real-time dispute resolution, as compared with delaying litigation until after project completion, which may serve to dim memories and recollection as to what happened during the time of contract performance. Ohio DOT does permit contract claim litigation before project completion, and it has at times focused attention away from project-completion efforts, which may cause problems, especially in times of reduced state manpower.

3. Damage Principles

Certain principles apply in determining damages. The most basic principle is the purpose for awarding damages. Damages are awarded by courts, boards, and arbitrators in an attempt to put the nonbreaching party in the same position that it would have occupied had the breach not occurred.[287] Another principle is that damages will not be awarded based on speculation or conjecture.[288] But damages need not be proven with exact certainty, if the claimant clearly proves that it

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[274] Pacific Architects and Eng'rs Inc. v. United States, 203 Ct. Cl. 499, 491 F.2d 734, 739 (Ct. Cl. 1974); Nager Elec. Co. v. United States, 194 Ct. Cl. 835, 442 F.2d 936, 946 (Ct. Cl. 1971).

[275] *See* Joseph Pickark's Sons Co. v. United States, 209 Ct. Cl. 643, 532 F.2d 739, 742–44 (1976).

[276] The DSC clause mandated by FHWA for use on federally-aided state highway projects contains the same limitation. 23 C.F.R. § 635.109(a)(1)(iv).

[277] 23 C.F.R. § 635.109(a)(2)(ii).

[278] J.F. White v. Mass. Bay Transp. Auth., 40 Mass. App. Ct. 937, 666 N.E.2d 518 (1996); Hensel Phelps Constr. Co. v. King County, 57 Wash. App. 170, 787 P.2d 58, 65 (1990).

[279] V.C. Edwards Contracting Co. v. Port of Tacoma, 83 Wash. 2d 7, 514 P.2d 1381, 1383 (1973); Triple Cities Constr. Co. v. State, 194 A.D. 2d 1037, 599 N.Y.S.2d 874, 876 (1993). *See also* § 5.A.5, "Cardinal Changes," *supra*.

[280] *See* cases cited in note 278 *supra*.

[281] V.C. Edwards, *supra* note 215, 514 P.2d at 1383–84.

[282] Foster Constr. C.A. Co. and Williams Bros. v. United States, 193 Ct. Cl. 587, 435 F.2d 873, 880 (Ct. Cl. 1970).

[283] Hensel Phelps Constr. Co., *supra* note 214, 787 P.2d at 61–62.

[284] *See* § 5.C.4., *supra*.

[285] *See, e.g*., Washington Standard Specification 1-09.4 (no claim for consequential damages of any kind will be allowed).

[286] Canal Elec. Co. v. Westinghouse Elec. Co., 406 Mass. 369, 548 N.E.2d 182, 187 (Mass. 1990); Solar Turbines, Inc. v. United States, 23 Ct. Cl. 142, 157 (1991). *See also* the limitations on the use of no-pay-for-delay clauses discussed in Section 5.C, *supra*.

[287] 11 CORBIN ON CONTRACTS, § 992; 24 WILLISTON ON CONTRACTS, § 64:1 (4th ed. 1999), 1353 (3d ed. 1968).

[288] Berley Indus. v. City of N.Y., 45 N.Y.2d 683, 688, 385 N.E.2d 281, 283, 412 N.Y.S.2d 589 (1978).

has suffered damages caused by the defaulting party.[289] It is sufficient if the evidence allows a judge or jury to make a reasonable approximation of the amount of damages without resorting to conjecture or speculation.[290] However, leniency in allowing an approximation of the amount of damages does not relieve the contractor of its burden of proving liability, causation, and resultant injury.[291]

A party seeking damages for breach of contract has a duty to take reasonable steps to avoid or mitigate losses resulting from the breach.[292] The burden of proving that the claimant failed to mitigate damages rests with the nondefaulting party.[293] The party seeking damages must also show that the costs claimed are reasonable and were caused by the event or default on which the claim is based.[294] Under federal construction law, prior to 1987, a contractor's actual costs were presumed reasonable. The Government had the burden of proving that the contractor's actual costs were unreasonable.[295] In 1987, there was an amendment to the FAR eliminating that presumption and shifting the burden from the Government to the contractor to show that its actual costs were reasonable.[296] The presumption that a contractor's actual costs are reasonable may also be negated by evidentiary rules.[297] This is consistent with the general rule that the burden is on the contractor to prove that its claimed costs are reasonable.[298]

Quantum meruit is a term that relates to how damages are measured; it is not a theory of recovery although it may be used to avoid unjust enrichment.[299] Literally, it means, "As much as he has deserved."[300] It is used to measure damages where extra work was performed that was not covered by the contract,[301] or where work was performed and accepted without the presence of an authorized contract.[302] The value of the benefit conformed is usually measured by the actual reasonable costs incurred by the contractor in performing the work, plus markup for overhead and profit.[303]

Quantum meruit recovery is not allowed where the work is covered by a specific contractual remedy,[304] or where the circumstances are such that the contractor could not reasonably expect to be paid for the work.[305]

4. Methods of Calculating Damages

There is no single method for calculating damages. If the contract does not establish a method for calculating damages, the contractor may try to prove damages using various methods. This subpart discusses the traditional methods that may be used to prove damages resulting from changes or delays caused by the owner.

a. Discrete Cost Method

The discrete cost method calculates the increased costs of changes or delays to the work on an item-by-item basis. The actual costs incurred because of changes or delays are segregated, assigned to each item, and documented in the contractor's cost accounting records.[306] This method is preferred by the courts because it is considered to be the best evidence of actual damages.[307]

Estimated costs may be permitted if actual costs are unavailable, and the contractor has a valid reason for not having actual cost information. But the claim may be denied if the contractor could easily have kept records of its actual costs caused by owner action or fault,

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[289] Wunderlich Contracting Co. v. United States, 173 Ct. Cl. 180, 351 F.2d 956, 968–69 (Ct. Cl. 1965).

[290] Daly Constr. v. Garrett, 5 F.3d 520, 522 (Fed. Cir. 1993).

[291] Wunderlich Contracting Co., *supra*, note 225, 351 F.2d at 968–69.

[292] P.T. & L. Constr. Co. v. State Dep't of Transp., 108 N.J. 539, 531 A.2d 1330, 1335 (1987) (contractor must absorb expenses that would have been avoided if it had been conscientious in its investigation).

[293] Hardwick v. Dravo Equip. Co., 279 Or. 619, 569 P.2d 588, 591 (1977).

[294] Wunderlich Contracting Co., *supra* note 225, at 969; Berley Indus., 385 N.E.2d at 282–83.

[295] Bruce Constr. Corp. v. United States, 163 Ct. Cl. 97, 324 F.2d 516, 519 (Ct. Cl. 1963).

[296] 48 C.F.R. § 31.201.3 (1987). *See* Morrison Knudsen Corp. v. Fireman's Fund Ins. Co., 175 F.3d 1221, 1244, n. 30 (10th Cir. 1999).

[297] Pa. Dep't of Transp. v. United States, 226 Ct. Cl. 444, 643 F.2d 758, 763 (1981).

[298] 13 AM. JUR. *Building and Construction Contracts* § 122 (2d ed. 2000).

[299] *See* Subsection B.5.a, *supra*.

[300] BLACK'S LAW DICTIONARY (7th ed. 1999).

[301] V.C. Edwards Contracting Co. v. Port of Tacoma, 7 Wash. App. 883, 503 P.2d 1133, 1136 (1972).

[302] Ridley v. Pipe Maintenance Services, 83 Pa. Commw. 425, 477 A.2d 610, 612 (1984) (invalid contract).

[303] Cities Serv. Gas Co. v. United States, 205 Ct. Cl. 16, 500 F.2d 448, 457 (Ct. Cl. 1974); Port Chester Elec. Constr. Corp. v. HBE Corp., 782 F. Supp. 837, 845 (S.D. N.Y. 1991).

[304] Hensel Phelps Constr. Co. v. King County, 57 Wash. App. 170, 787 P.2d 58, 61 (1990).

[305] *Id.*

[306] American Line Builders v. United States, 26 Cl. Ct. 1155, 1193 (1992) ("Plaintiff's calculation of the additional work required by reference to time and labor records from the project is far more helpful to this court than the defendant's unsupported assertions, because plaintiff's calculations reflect work actually performed, not hypothetical labor time projects.").

[307] Dawco Constr. Co. v. United States, 930 F.2d 872, 882 (Fed. Cir. 1991); American Line Builders Inc., *id.*; Con-Vi-Rio of Texas v. United States, 538 F.2d 348 (Cl. Ct. 1976); D.C. v. Organization for Envtl. Growth, 700 A.2d 185, 203 (D.C. App. 1997); New Pueblo Constructors, Inc. v. State, 144 Ariz. 95, 696 P.2d 185, 194 (1985).

but did not, and has no valid excuse for not keeping records.[308]

The discrete method of calculating damages for breach of contract or an equitable adjustment under a remedy granting clause provides the owner with documented, actual costs tied directly to items of work that have been changed or delayed.

b. Total Cost Method

Under the total cost method, the contractor recovers the difference between the total cost of performing the work and the bid price, plus a reasonable profit.[309] This method is disfavored by the courts and can only be used where there is no other means of determining damages.[310] It is disfavored because it suffers from the following defects. First, it presumes that the bid was reasonable. If the bid is unreasonably low, the difference between the contractor's total costs to perform the contract and its bid is increased, thereby increasing the contractor's damages solely by underbidding the project and not by incurring additional costs caused by the owner.[311] Second, this method assumes that the owner, not the contractor, is responsible for all of the increased costs. This defect further assumes that the contractor was not responsible for any increase in the cost of the work, passing along to the owner increased costs that may have resulted from the contractor's inefficiency, or from events for which the owner was not responsible.[312]

While courts disfavor the total cost method, they do not prohibit its use. Its use is based on the principle that, "Where a contractor is entitled to an adjustment, the contracting entity should not be relieved of its liability for the same merely because the contractor is unable to prove its increased costs within a mathematical certainty."[313] Essentially, the courts will allow this method to be used if there is no better method for proving damages, and the following safeguards can be established:

- The bid was reasonable and properly prepared. This may be determined by comparing the bids submitted by the other bidders with the contractor's bid.[314]
- The total costs expended were reasonable.[315]
- The contractor is not responsible for the additional costs.[316]

These safeguards or prerequisites to the use of this method must be proved by a preponderance of the evidence.[317] Failure to prove them requires that the total cost claim be dismissed.[318] If a jury is allowed to hear evidence of damages calculated on a total cost method, the jury must be instructed by the court not to allow damages based on total costs unless these safeguards are established.[319] The owner should consider presenting evidence challenging the contractor's total cost figures rather than counting on the jury, or a judge in a bench trial, to deny the claim in its entirety because the contractor failed to establish the foundational prerequisites for use of the total cost method.[320]

The total cost method is a simple way of calculating damages. Essentially, it converts a fixed-price contract into a cost-plus contract. This method assumes that the bid for performing the work was reasonable and accurately computed. It assumes the contractor's increased costs were reasonable and that the owner, not the contractor, or factors for which the owner was not reasonable, caused the costs to increase. It is disfavored as a matter of law because it piles assumption upon assumption, and as such becomes speculative. The assertion that it is too difficult to segregate impact and delay costs and allocate them to specific work items is not enough to justify the total cost method. The contractor

[308] Dawco Constr. Co. v. United States, 930 F.2d at 882.

[309] New Pueblo Constructors, Inc. v. Department of Transp., 696 P.2d at 194; Neal & Co. v. United States, 36 Fed. Cl. 600, 638 (Ct. Cl. 1996); Servidone Constr. Corp. v. United States, 931 F.2d 860, 861–62 (Fed. Cir. 1991).

[310] New Pueblo Constructors, *id*.; Green Constr. Co. v. Department of Transp., 164 Pa. Commw. 566, 643 A.2d 1129, 1136 (1994); Servidone Constr. Corp., *id*.; Modern Builders, Inc. v. Manke, 29 Wash. App. 86, 615 P.2d 1332, 1337–38 (1980), Huber, Hunt Nichols v. Moore, 67 Cal. App. 278, 136 Cal. Rptr. 603, 621–22 (1977).

[311] Youngdale & Sons Constr. Co. v. United States, 27 Fed. Cl. 516, 541 (1993); Servidone Constr. Corp., 931 F.2d at 861.

[312] *See* cases cited in note 245, supra. *See also* MCBRIDE & TOUHEY, GOVERNMENT CONTRACTS, § 23.40[2].

[313] AMP-Rite Elec. Co. v. Wheaton Sanitary Dist., 220 Ill. App. 3d 130, 580 N.E.2d 622, 640, 162 Ill. Dec. 659 (1991).

[314] Youngdale & Sons Constr. Co. v. United States, 27 Fed. Cl. 542-43.

[315] Servidone Constr. Corp., 931 F.2d at 861–62.

[316] AMP-Rite Elec. Co., 580 N.E.2d at 641 (citing J.D. Hedin Constr. Co. v. United States, 347 F.2d 235, 346–47 (Ct. Cl. 1965); Neal & Co. v. United States, 36 Fed. Cl. at 638. The contractor does not have the burden, however, to show that it mitigated its damages; the burden of proving that the contractor failed to mitigate its damages rests with the owner. Hardwick v. Dravo, 279 Or. 619, 569 P.2d 588, 591 (1977).

[317] John F. Harkins Co. v. School Dist. of Phila., 313 Pa., *supra* 425, 460 A.2d 260, 265 (1983).

[318] Neal & Co. v. United States, 36 Fed. Cl. at 638.

[319] Geolar, Inc. v. Gilbert/Commwealth, Inc., 874 P.2d 937, 945 (Alaska 1994); Anchorage v. Frank Coluccio Constr. Corp., 826 P.2d 316, 328 (Alaska 1992).

[320] *See* Pa. Dep't of Transp. v. James D. Morrissey, 682 A.2d 9, 14 (Pa. 1996). (The court noted that the agency did not present any evidence to contradict the contractor's testimony concerning liability for damages). The total cost method may be used to calculate damages for a major contract item. *See* S.J. Groves & Sons & Co. v. State, 50 N.C. App. 1, 77-79, 273 S.E.2d 465 (1980) (contractor used total cost method to calculate damages for unclassified excavation work after encountering a changed condition. Court applied same foundational prerequisites for repricing the entire contract on a total cost basis in repricing major contract item).

should be required to prove that its accounting system and its use of cost codes do not permit allocation of specific costs to discrete events, where the effects of impacts and disruptions on unchanged work are so intertwined that allocation of those costs are highly impracticable.[321]

New York allows the use of total cost basis for calculation of damges. The total cost basis is allowed even though the contractor may be responsible for some of the damages incurred. The courts in determing liability often allocate a percentage of the total cost damages to the State.[322] The court in *Felhaber Corp. & Horm Construction Co. v. State*, held that where the contractor asserted its actual costs, together with its allowances for overhead and profit without regard to its bid, the total cost theory of damages was sanctioned.[323] Total cost calculations based on the total cost less the amount paid for specific bid items are also an acceptable damage theory in New York.

c. Modified Total Cost Method

The modified total cost method is simply the total method adjusted to satisfy two of the prerequisites for the use of the total cost method.[324] Under the modified total cost approach, deductions are actually made for costs attributable to the contractor,[325] and for underbidding where the evidence indicates that the contractor's bid was too low.[326] This approach is designed to eliminate two of the deficiencies inherent in the total cost method: the assumption that the bid was realistic and the assumption that all of the excess costs were the responsibility of the owner.[327]

The problem with this approach is that it shifts the burden of proof. It is a fundamental rule of law that a claimant has the burden of proving its damages.[328] In contrast with the discrete method of proving damages, a contractor using the modified total method can, if it chooses, allocate some of its increased costs to obvious self-inflicted wounds, leaving it to the owner to prove that there are other costs that should also be the contractor's responsibility.[329] The following factors should be considered in defending claims based on a total or modified total cost method.[330]

- The contractor's bid work-up sheets should be examined to determine how the contractor put the bid together. The examination should be made to determine whether the contractor bid too low on some aspects of the work or made assumptions in bidding that were unrealistic or unfounded. The analysis may also consider whether the bid was unbalanced with respect to items that seriously overran or underran.
- Nonimpacted items of work should be compared with similar impacted items of work. This is referred to as the "measured mile" analysis.
- Financial records obtained through an audit should be analyzed by experts.
- An engineering and schedule analysis should be performed to identify concurrent delays.[331]

This type of analysis allows the owner to determine when the contractor is attempting to obtain additional compensation for mistakes that the contractor made in its bid and during contract performance. Considerable lay and expert testimony may be required to prove these factors and may likewise be rebutted by similar evidence presented by the contractor. This type of analysis is also of major import, because the total or modified total cost methods will not be permitted if the prerequisites to their use are not established by the contractor,[332] or at least one of the prerequisites to their use are disproved by the owner.[333]

d. Jury Verdict

The "jury verdict" method is used by courts to determine (much like a jury would) a fair and reasonable amount that should be awarded as an equitable adjustment, or as damages for breach of contract. It is used by courts to reconcile conflicting testimony, and not as a method of proving damages.[334] The prerequisites for using this method are: (1) clear proof that the contractor is entitled to damages for breach of contract or an equitable adjustment; (2) sufficient evidence to

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[321] Neal & Co. v. United States, 36 Fed. Cl. 600, 641 (Fed. Cl. 1996).

[322] Columbia Asphalt Corp v. State, 70 A.D. 2d 133, 420 N.Y.S.2d 36 (1979).

[323] 69 A.D. 2d. 362, 419 N.Y.S.2d 773 (1979).

[324] Servidone Constr. Co. v. United States, 931 F.2d at 862; Youngdale Constr. Co. v. United States, 27 Fed. Cl. at 541; Seattle Western Indus. v. David Mowat Co., 750 P.2d 245 (Wash. 1988); Nebr. Pub. Power Dist. v. Austin Power, Inc., 773 F.2d 960, 968 (8th Cir. 1985).

[325] For example, in State Highway Comm'n v. Brasel & Sims Constr. Co., 688 P.2d 871 (Wyo. 1984), damages were reduced by a deduction for increased labor costs due to "overmanning."

[326] Servidone Constr. Co. v. United States, 931 F.2d at 862.

[327] Youngdale & Sons Constr. Co. v. United States, 27 Fed. Cl. at 541.

[328] *See* Subpart C.3, "Damage Principles," this Section, *supra*.

[329] D. HARP, *Preventing and Defending Against Highway Construction Contract Claims: The Use of Changes or Differing Site Conditions Clauses and New York State's Use of Exculpatory Contract Provisions and Contract Clauses, in* SELECTED STUDIES IN HIGHWAY LAW (National Cooperative Highway Research Program, Legal Research Digest No. 28, 1993).

[330] *Id.* at 29.

[331] *See* § 5.C.4.b, *supra*.

[332] Neal & Co. v. United States, 36 Fed. Cl. at 638.

[333] Youngdale & Sons Constr. Co. v. United States, 27 Fed. Cl. at 541.

[334] District of Columbia v. OFERGO, 700 A.2d at 204; Delco Elec. Corp. v. United States, 17 Ct. Cl. 302, 323–24 (1989), *aff'd*, 909 F.2d 1495 (Fed. Cir. 1990).

allow the court to make a reasonable estimation as to the amount of damages; and (3) proof that there was no more reliable method of computing damages.[335] The jury verdict method may not be used, and the claim may be dismissed, where the contractor could have kept records of its actual increased costs, but did not, and has no justifiable excuse for not doing so.[336]

e. Force Account

Specifications used by state transportation agencies in their construction contracts usually contain force account provisions.[337] Force account provisions allow the agency to pay for contract changes on a time and material basis when the contractor and the agency cannot agree on a price for the change.[338] Occasionally, force account has been used by contractors to price equipment for large claims. This occurs when the specifications provide that the price adjustment for a change, a DSC, or a contract termination for convenience will be determined by agreement of the parties, or if they cannot agree, by force account. This type of pricing can result in a real advantage to a contractor by using rates from a manual to price its equipment rather than its actual equipment costs.[339] Generally, force account should not be used to price large claims. To prevent this, the contract should provide that no claim for force account shall be allowed unless ordered in writing by the engineer prior to the performance of the work.

5. Cost Categories

Aside from miscellaneous and subcontractor expenses, a contractor's cost in performing work may be grouped into four general categories: labor, materials, equipment, and overhead. These costs can be further classified as either direct or indirect. Direct costs are those tied to a specific construction activity, while indirect costs that cannot be tied to specific work items are treated as part of overhead.

Most contractors keep detailed cost records for their projects. This allows them to account for the cost of labor, materials, and equipment used for a particular construction activity. When new or extra work is undertaken, a cost code can be established for that activity. However, the determination of extra labor hours resulting from labor inefficiency may be impossible to identify and segregate from the man-hours expended to perform the original contract work.[340]

a. Increased Labor Costs and Loss of Productivity

Direct labor costs consist of the base wages and fringe benefits that are paid to personnel who perform a specific segment of construction. The wages of an ironworker, for example, can be determined from payroll records and allocated to steel erection work. Accounting for added labor costs caused by extra work is easy if those costs are clearly allocated to a new cost code established for that purpose. Where the difficulty occurs is when the original contract work is impacted by the contract change, reducing the efficiency or productivity of the contractor's labor force. This may be due to delay causing work to be performed during adverse weather, or causing work to be performed out of sequence, or from trade stacking and over-manning to meet an accelerated completion schedule.

Loss of productivity

Loss of productivity claims are frequently part of today's contractor claim submission. Contractors assert that their labor has sustained loss of productivity occasioned by the owner's actions or inactions. Although some state transportation contracts list loss of efficiency claims as not compensable,[341] this has not stopped contractors from seeking to pursue them anyway. Some causes of inefficient operation include excessive number of mobilizations or demobilizations, restricted access, excessive inspections, large number of change orders, delays in shop-drawing approvals, working around utilities, winter work, working overtime or extended hours, or acceleration, all of which can affect labor productivity. Loss of productivity claims are also asscociated with cumulative impact claims or "ripple effect" caused by excessive number of change orders that can affect labor productivity. In *Luria Brothers & Company Inc. v. United States*,[342] the Court of Claims recognized the loss of productivity theory of damages in an airport project, caused by uprooting foundations for further subsoil investigation and specification changes made by the owner.

Because contractors rarely maintain cost records that precisely segregate inefficiency costs, such inefficiency may require expert analysis.

The most widely accepted and credible method of measurement is known as the "measured mile" method. The measured mile method compares the productivity on identical activities during the impacted and unimpacted periods of time of the project to determine the loss of productivity resulting from the impact; however, it is often difficult, if not impossible, to find areas where

[335] WRB Corp. v. United States, 183 Ct. Cl. 409, 425.

[336] Dawco Constr., Inc. v. United States, 930 F.2d 872, 881 (Fed. Cir. 1991); *see* D.C. v. OFERGO, 700 A.2d at 204 (for additional citations).

[337] Colorado DOT Standard Specification 109.4 (1999) and Washington DOT Standard Specification 1-09.6 (2000) are examples.

[338] I.A. Constr. Corp. v. Department of Transp., 139 Pa. Commw. 509, 591 A.2d 1146, 1149–50 (1991); Department of Transp. v. Anjo Constr. Co., 666 A.2d 753, 760 (Pa. Commw. 1995).

[339] Pricing equipment is discussed in the next subpart C.

[340] "Construction Claims and Damages, Entitlement Analysis," J. Hainline, AASHTO Annual Meeting (Oct. 1991); TRB Legal Workshop (July 1992).

[341] NYSDOT Standard Specifications § 109-05.3.

[342] 177 Ct. Cl. 676, 369 F.2d 701 (1966).

the work is identical and is being performed under identical conditions except for the impact factors. Quantities of work, weather, work area, and other factors may affect the validity of the measured mile calculation, resulting in an analysis of substantially similar, rather than identical, activities.[343]

The measured mile analysis has been successfully used in *Natkin & Co. v. George A. Fuller Co*. In *Natkin*, the delay in performance was caused by the owner's delay in furnishing equipment, drawings, and engineering information for the project. Natkin provided a measured mile analysis comparing installation of the pipe during the unimpacted period at the start of the job with the man hours expended during the impacted period. Natkin's claim for loss of productivity was based on the difference in man hours in the two periods. The court found that comparing the unit costs during the impacted and unimpacted period was reasonable and awarded loss of productivity damages.[344]

In *Appeals of W.G. Yates & Sons Construction*,[345] the board approved the use of measured mile analysis comparing the cost of performing work during periods both affected and unaffected by disputed events. The board accepted the contractors' use of this methodology as an acceptable vehicle for determining labor inefficiencies costs due to the government's defective specification.

The measured mile analysis has been accepted by courts and boards. It also requires a causal connection to actions or inactions of the party against whom the claim is being asserted. [346] Cost or production data or productivity data can also be used in the measured mile analysis. In *State ex rel Department of Transportation v. Guy F. Atkinson Co.*,[347] the court affimed an arbitration award of $1,130,000 for 65 percent of the claimed cumulative impact damages caused by piecemeal changes ordered by the state engineer that impacted the entire project. Essential elements of cumulative impact claims include extensive changes that fundamentally alter the contract; the contractor's ability to demonstrate a causal link between the changes and the inefficiency, and the contractor's ability to substantiate a reasonable estimate using project records or industry studies.[348]

Other theories, based on manuals, which include the *Mechanical Contractors Estimating Manual* and the *National Electrical Association Job Factors*, have also been used, but are not as uniformly accepted as the measured mile analysis.

Another method is to estimate an inefficiency percentage and apply that percentage to labor costs. For instance, in one case, the court allowed a 10 percent increase for labor inefficiency caused by work being performed out-of-sequence.[349] An analysis of this kind requires expert testimony,[350] and may rely on industry studies.[351] However, a comparison of actual labor costs to the amount estimated in the original bid has been rejected. The court said that this approach has the same shortcomings inherent in the total cost method: the labor estimate may be too low and the cost overrun may be due, at least in part, to problems that are not the owner's fault.[352] Inefficient labor claims are frequently found in acceleration claims.[353] Excessive overtime can affect work output and lower efficiency through physical fatigue. Stacking of trades within limited work areas causes congestion, affecting efficiency. There are also indirect labor costs. Field supervision costs may be increased when a delay or a change extends the project. Field supervisions costs for extended project durations should be documented as to the additional time spent on the project, rather than using an inefficiency factor as a markup on the total supervisory costs. A contractor may also recover premium pay for overtime work and for second and third shift work, where work is accelerated due to owner-caused delay. There is no recovery, however, where premium time was not due to an owner-caused breach.[354] But wage

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[343] WILLIAM SCHWARTZKOPF, CALCULATING LOSS OF LABOR PRODUCTIVITY IN CONSTRUCTION CLAIMS 194 (Aspen Pub., 2004). *See also* Gen. Ins. Co. v. Hercules Constr. Co., 385 F.2d 13, 20–21 (8th Cir. 1967); *and see* Clark Concrete Contractors v. Gen. Services Admin., GSBCA No. 14340 99-1 BCA § 30280 (1999) (Board allowed contractor to use the "measured mile" approach to several different categories of work affected by design changes made during construction).

[344] 347 F. Supp. 17 (W.D. Mo. 1972).

[345] ASBCA Nos. 49,399 and 40,300, 01-2 BCA (CCH) 31,428 (2001).

[346] SCHWARTZKOPF, *supra* note 342, at 200.

[347] 187 Cal App. 3d 25, 231 Cal. Rptr. 382 (1986).

[348] *Cases and Board Decisions on Cumulative Impact Claims,* CONSTRUCTION LAWYER 32 (Fall 2011).

[349] Youngdale & Sons Constr. Co. v. United States, 27 Fed. Ct. at 558.

[350] Luria Bros. & Co. v. United States, 177 Ct. Cl. 676, 369 F.2d 701, 712 (Ct. Cl. 1967).

[351] J.A. HANERS & R.M. MORGAN, COLD REGIONS RESEARCH AND ENGINEERING LABORATORY SPECIAL REPORT 172 (May 1972) discusses the effect of cold weather on human performance and capabilities; *Work Efficiency Decreases at Abnormal Temperatures*, CONSTRUCTOR MAGAZINE, Associated General Contractors of America (May 1972). This issue also lists a number of conditions that affect productivity and characterize the percent of loss if the condition is minor, average, or severe. Some examples: very hot or very cold weather, minor (10 percent), average (20 percent), severe (30 percent). Learning curve, minor (5 percent), average (15 percent), severe (25 percent). The publication notes that these factors are for reference only and may vary from contractor to contractor, crew to crew, and job to job.

[352] Manshul Constr. Corp. v. Domitory Auth. of N.Y., 79 A.D. 2d 383 436 N.Y.S.2d 724, 729 (N.Y. App. 1981); Joseph Pickard's Sons & Co. v. United States, 209 Ct. Cl. 643, 532 F.2d 739, 449 (Ct. Cl. 1976).

[353] Hensel Phelps Constr. Co. v. King County, 57 Wash. App. 170, 787 P.2d 58, 60 (1990).

[354] Public Constructors v. State, 55 A.D. 2d 368, 390 N.Y.S.2d 481, 487 (1977).

increases for work performed in a later time period than planned, due to owner delay, may be recovered.[355]

b. Increased Cost of Materials

An increase in the cost of materials due to owner-caused delay is compensable. The claim should not include shipping charges, since the contractor would bear those costs irrespective of when the materials were delivered, unless the shipping costs also increased.

Some contracts include an escalation clause allowing a price adjustment for certain products that increase in price during contract performance. Petroleum products are an example of materials where the price may rise suddenly.[356]

Many state transportation construction contract provisions contain price escalation or price adjustment provisions. Historically, price adjustment provisions were developed in reponse to the Organization of Petroleum Exporting Countries (OPEC) oil embargo of 1973. The provisions establish a method for unit contract price adjustment resulting from certain economic conditons. Previous examples include adjustment provisions when asphalt, fuel, and cement were in nationally short supply. These provisions reduce the contractor's risk by allocating the risk to the public owner so as to reduce inflated bid prices and overall project costs. Federal guidance suggests that adjustment standards should be based on and contain a base index, which is not susceptible to manipulation by contractors or suppliers. The state transportation agency may develop its own price index or adopt published and commonly available data such as the Consumer Price Index.[357] Federal requirements note that they have no legal authority to participate in retroactive modifications related to material price increases, so state DOTs may have to absorb such cost increases exclusively from state funding. Today's state provisions include adjustment provisions for steel, cement, asphalt, and fuel.

c. Increased Equipment Costs

Most contracts establish how equipment should be priced and refer to equipment costing guide manuals.[358] These manuals are published by a number of organizations.[359] In general, equipment costs are broken down into two categories: rented and owned. Payment for rented equipment is based on paid invoices. When equipment is rented from rental companies or other contractors, the amount paid will be allowed, if it is reasonable and the rental was an arms-length transaction. However, in federal procurement where the equipment is rented from a division, subsidiary, or organization under the common control of the contractor, the allowability of the rental charges is determined by regulation.[360] In addition, under federal regulations, certain costs, such as maintenance and minor repairs necessary to keep the equipment operational, may be allowed.[361]

The contract specifications may control the costs allowed for owned equipment. For example, recovery for owned equipment may be limited to rates established by an equipment rental agreement with the AGC, or the contractor's actual ownership and operating costs, whichever is less.[362] Some contractors who own equipment do not keep sufficient records to establish their actual equipment costs.[363] In the absence of a regulation or directive that allows or requires the use of published rates, contractors must prove that their records are inadequate to establish their actual ownership rates before they can use published rates.[364] When the actual cost of equipment ownership can be determined, those costs must be used.[365]

Contractors are generally entitled to compensation to cover their equipment costs during a period where work is suspended or delayed.[366] Recovery for idle equipment is denied, however, where the contractor could have used the equipment elsewhere.[367] This is consistent with the contractor's common law duty to mitigate its damages.[368] Standby rates for idle equipment are usually priced at actual ownership rates or 50

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[355] Gardner Displays Co. v. United States, 346 F.2d 585, 589 (Ct. Cl. 1965).

[356] *Id*.

[357] *See* FHWA, CONTRACT ADMINISTRATION CORE CURRICULUM MANUAL 18 (hereinafter CACC Manual), 2001, available at http://www.fhwa.dot.gov/programadmin/contracts/cacc.pdf, last accessed on June 27, 2012.

[358] Quality Asphalt Paring, Inc. v. State of Alaska, Dep't of Transp. & Public Facilities, 71 P.3d 865, 873–74 (Alaska 2003).

[359] Rental Rate Blue Book for Construction Equipment. Rates can be weekly or monthly. The latter has lower rates than the former. Rental Rates Compilation, Associated Equipment Distributors; Construction Equipment Ownership and Operating Expense Schedule, U.S. Army Corps of Engineers; Contractor's Equipment Cost Guide, The Associated General Contractors; Labor Surcharge and Equipment Rental Rates, The California Dep't of Transportation; Tool and Equipment Rental Schedule, National Electrical Contractor's Association.

[360] 48 C.F.R. ch. 1 §§ 31.105(d)(2)(c); 31.205.36(b)(3).

[361] 48 C.F.R. § 31.105(d)(2)(c)(ii)(A).

[362] For example, Colorado specifies the Dataquest Blue Book for establishing equipment rental. The hourly rental rate is based on the Blue Book Monthly Rate published by Dataquest times a rate adjustment factor times the regional adjustment average divided by 176 (working hours in a month). Colorado Standard Specifications § 109.04(c) (1999).

[363] These costs include: equipment depreciation, taxes and insurance, capital investment, *i.e.,* return on money spent on equipment.

[364] Meva Corp. v. United States, 206 Ct. Cl. 203, 511 F.2d 548, 559 (Ct. Cl. 1975), Nolan Bros. v. United States, 194 Ct. Cl. 1, 437 F.2d 1371, 1379–80 (Ct. Cl. 1971) (regulations allowed use of published notes).

[365] Meva Corp., *id*.

[366] Zook Bros. Constr. Co. v. State, 171 Mont. 64, 556 P.2d 911, 917 (1976); Peter Salucci & Sons, Inc. v. State, 110 N.H. 136, 268 A.2d 899, 910 (1970).

[367] Excavation-Constr., Inc., ENG BCA No. 3858, 82-1 BCA ¶ 15,770, at 78, 058 (1982).

[368] *See* Subpart 3, *supra*.

percent of equipment manual rates.[369] The standby reduction reflects the cost of owning the equipment, but not the wear and tear on the equipment and "FOG" (fuel, oil, and grease costs), since the equipment is not operating during the suspension or delay period.

d. Home Office Overhead

Home office overhead represents those costs necessary to conduct business. It includes salaries, rent, depreciation, taxes, insurance, utilities, office equipment, data processing costs, legal and accounting expenses, office supplies, and other miscellaneous general and administrative expenses.[370] Because of their nature, these expenses are indirect and cannot be directly traced to any particular contract.[371]

When a contract is delayed, home office expenses may accrue beyond the amount allocated by the contractor in its bid. Since there is little or no work, there is little or no income from contract progress payments to absorb those costs.[372] Those costs become "unabsorbed."[373] Thus, contractors who have incurred unabsorbed or extended home office expenses during a period of owner-caused delay have been permitted to recover those costs as part of their damages for compensable delay.[374] The costs are compensable because they were incurred due to owner- caused delay, but not reimbursed as part of the contract price.[375]

Some state transportation contract provisions, ranging from NYSDOT's use of a fixed overhead percentage to cover main office overhead,[376] to Caltrans requirements that mandate contractors on certain projects to provide in their bid daily overhead amounts, which are later used for contract adjustments.

i. The Eichleay Formula.—The Eichleay formula is a method of approximating home office overhead expenses caused by delay. It computes home office overhead expenses on the basis of a pro rata amount per day and then multiplies that amount times the number of days that the project was delayed. The result is the amount of home office overhead damages.[377] Its use as a method of calculating home office overhead damages for federal construction contracts spans over 40 years.[378] The basic formula consists of the following steps:

[369] L. L. Hall Contr. Co. v. United States, 177 Ct. Cl. 870, 379 F.2d 559, 568 (1967); Zook Bros. Constr. Co. v. State, 556 F.2d at 917 (standby rate was 50 percent of hourly rate established by the Montana State Highway Dep't).

[370] Contractors include some amount in their bids to cover home office expenses incurred during the duration of the contract. Aetna Casualty & Sur. v. Chapel Hill Indep. Sch. Dist., 860 S.W.2d 67,672 (Tex. 1993).

[371] Wickham Contracting Co. v. Fischer, 12 F.3d 1574, 1578 (Fed. Cir. 1994).

[372] West v. All State Boiler, Inc., 146 F.3d 1368, 1372 (Fed. Cir. 1998).

[373] In Eichleay Corp., ASBCA No. 5183, 60-2 BCA ¶ 2688 (1960).

[374] *Id.*

[375] Wickham Contracting Co. v. Fischer, 12 F.3d at 1577.

[376] NYSDOT Standard Specifications § 109-05(d)(1)(e) and (g).

[377] Eichleay Corp., *supra* note 298; Melka Marine, Inc. v. United States, 187 F.3d 1370, 1374–75 (Fed. Cir. 1999). It is the accepted method for calculating home office overhead damages in federal construction contracts. Wickham Contracting Co. v. Fischer, 12 F.3d at 1577.

[378] From 1960 to the present. *Id.*

STEP 1	**Delayed contract billings** Total billings during contract period.	X	Total home office overhead incurred during contract period.	=	Overhead allocable to the contract.
STEP 2	Allocable overhead Total number of days of contract performance	=	Overhead per day allocable to delayed contract.		
STEP 3	Daily overhead rate	X	Number of days of delay.	=	Unabsorbed overhead damages.

The formula has undergone certain modifications. For example, it is important that the actual period of contract performance be used, not the number of days planned or scheduled for contract performance. Because the formula attempts to determine the amount of overhead attributable to the *actual period of performance* of the delayed contract, the per diem rate is necessarily obtained by dividing this figure by the number of days of *actual performance*. Dividing by the number of days of the original contract period distorts the formula.[379]

Another modification is that the actual delay beyond the scheduled completion date must be used, not the suspension period. The Federal Circuit has stated, "We clarify that it is the delay at the end of performance resulting from the suspension that results in unabsorbed overhead expenses which a contractor may recover under *Eichleay*."[380]

To use *Eichleay,* the contractor must also show that it was on standby and that it was unable to take on replacement work during the suspension: work that provides the "same amount of money for the same period toward overhead costs as the government contract."[381] The standby test requires that the contractor remain ready to perform and that it was impractical for the contractor to obtain other work to which it could reallocate its home office overhead expenses.[382] In addition, *Eichleay* should not apply where the original contract duration is extended by change order work, when the added work provides sufficient income to absorb the contractor's proportionate share of home office expenses.[383]

One state has rejected the *Eichleay* formula as too speculative,[384] while other states have permitted its use in calculating delay damages.[385] *Eichleay* has been criticized for allowing damages without first determining whether additional overhead costs were actually incurred. It may also include damages for construction shut-down periods, such as weather or other non-owner-caused events, when the contractor would normally be idle. The formula also assumes that the daily overhead cost is a fixed cost, when in fact the costs are an approximation based on costs that are variable.[386]

[379] Golf Landscaping, Inc. v. Century Constr. Co., 39 Wash. App. 895, 696 P.2d 590, 593–94 (1984) (emphasis in original, citation omitted) (using the actual period of performance instead of the original contract period changed the *per diem* rate from $209.88 to $109.98).

[380] West v. All State Boiler, 146 F.3 at 1368, 1381 (Fed. Cir. 1998) (changed the period for computing damages from 58 days—the suspension period—to 22 days, the extension period beyond the scheduled completion date).

[381] Mecka Marine, Inc. v. United States, 187 F.3d at 1379.

[382] *See* West v. All State Boiler, 146 F.3d at 1373. However, a contractor's inability to take on replacement work because of bonding limitations would not be an excuse for not obtaining replacement work. *See* Satellite Elec. Co. v. Dalton, 105 F.3d 1418, 1420 (Fed. Cir. 1997).

[383] Community Heating & Plumbing Co. v. Kelso, 987 F.2d 1575, 1580–81 (Fed. Cir. 1993); Almayer v. Johnson, 79 F.3d 1129, 1133 (Fed. Cir. 1996).

[384] Berley Indus. v. City of N.Y., 45 N.Y.2d 683, 385 N.E.2d 281, 283, 412 N.Y.S.2d 589 (1978).

[385] California: Howard Contracting, Inc. v. McDonald Constr. Co., 71 Cal. App. 4th 38, 54–55, 83 Cal. Rptr. 2d 590 (1998) (City of Los Angeles conceded that Eichleay was the proper industry standard for analyzing construction delay claims); Connecticut: Southern New England Contracting Co. v. State, 165 Con. 644, 345 A.2d 550, 559–60 (Conn. 1974); Florida: Broward County v. Russell, Inc., 589 So. 2d 983 (Fla. App. 1991); Massachusetts: PDM Plumbing & Heating, Inc. v. Findlen, 13 Mass. App. Ct. 950, 431 N.E.2d 594, 595 (1982); Ohio: Conti Corp. v. Ohio Dep't of Adm. Servs., 629 N.E.2d 1073, 1077 (1993); Washington: Golf Landscaping v. Century Constr. Co., 39 Wash. App. 395, 696 P.2d 590, 592–93 (1984). Virginia: Fairfax County Redevelopment and Housing Auth. v. Worchester Bros. Co., 257 Va. 382, 514 S.E.2d 147, 150–51 (1999).

[386] Berley Indus. v. City of N.Y., 385 N.E. at 284; D. Harp, *Preventing and Defending Against Highway Construction Claims* (National Cooperative Highway Research Program Legal Research Digest No. 28, 1993); R.A. Maus, *Assessing Damages on Construction Claims*, paper presented at AASHTO annual meeting (1991); M.K. Love, *Theoretical Delay and Overhead Damages*, 30 PUB. CONT. L.J. 33 (Fall 2000); Watson,

Another criticism is that the daily rate of overhead expense may be disproportionate when there is a small amount of work remaining. In *Berley Industries v. City of New York*, the court said; "The damages computed under the *Eichleay* formula would be the same in this case whether the plaintiff had completed only 1% or 99% of the job on the scheduled completion date of May 7, 1971."[387] But despite criticism, acceptance of the *Eichleay* formula seems to be growing.[388]

ii. Other Methods of Determining Home Office Overhead Expenses.—Methods other than the Eichleay formula may be used to calculate home office overhead expenses. Using a contractor's usual markup rate in preparing bids is one such method for determining home office costs during an extended contract period. Under this method, the direct cost incurred during the extended period is multiplied by the percentage markup. The result is the home office overhead damages for the extended contract.[389] A similar method is the use of a fixed markup rate specified in the contract. For example, the FDOT has a standard clause that contains the following formula:[390]

$$D = \frac{A \times C}{B}$$

Where: A = original contract amount
B = original contract time
C = 8%
D = Average overhead per day.[391]

The courts of New York, which have rejected the *Eichleay* formula, developed an additional overhead theory based on total payment requisitions and bid amounts of overhead and profit. The court in *Manshul Construction Corp. v. Dormitory Authority*[392] developed a overhead formula by ascertaining the total requisitions in the delay period, then subtracting the portion allocable to overhead and profit, which culminated in the cost of the work after the completion date. The court than applied the bid percentage for overhead to arrive at the unabsorbed overhead amount.

Since overhead is incurred by labor costs, other more accepatable accounting theories include calculating overhead based on labor dollars or allocating the total overhead based on a percentage of labor of the project involved in the claim divided by labor cost for the entire company.

The Colorado Department of Transportation has a standard clause that determines home office overhead for the extended contract period by adding 10 percent of the total cost of additional wages for nonsalaried labor as a result of the delay and the cost of additional bond, insurance, tax, equipment costs, and extended job site overhead. No additional home office overhead expenses are allowed.[393] Instead of a fixed percentage rate, the overhead clause may contain a declining scale. As the value of the direct costs increase, the allowance markup percentages on direct costs decrease.[394]

Home office overhead claims usually arise because work is suspended or delayed, not because the duration of the contract is extended by added work. Contractually-fixed markups do not address home office expenses where work is suspended because no work is performed during the suspension period, and the only direct costs that are being incurred are idle equipment on standby, field facilities, and perhaps field supervision. Those costs may form an inadequate base for determining home office overhead costs during the suspension period. In this situation, some other method must be used to calculate unabsorbed overhead, if the *Eichleay* formula is not used. Most methods require assistance from accountants or other financial experts in analyzing the contractor's books and records.[395]

Judicial tuning of the *Eichleay* formula may make it more palatable to owners. Limiting use of the formula to situations where the contractor cannot take on replacement work,[396] but must "standby" still gives the owner some options. If the delay could be extensive, the

Unabsorbed Overhead Costs and the Eichleay Formula, 147 MIL. L. REV. 262 (1995); P.A. McGeehan and C.O. Strouss, *Learning from Eichleay: Unabsorbed Overhead Claims in State and Local Jurisdictions*, 25 PUB. CONT. L.J. (Winter 1996).

[387] Berley, 385 N.E.2d at 284. Under federal construction law, the amount of work remaining when work is suspended is only relevant to show whether the contractor could have taken on replacement work during the delay period. Satellite Elec. Co. v. Dalton, 105 F.3d at 1420 (96.7 percent of the work had been completed when the contract was suspended; the value of the remaining work was less than $30,000).

[388] *See supra* note 316, for states where Eichleay has been used to compute delay damages. *See also* note, *Home Office Overhead as Damages for Construction Delays*, 7 GA. L. REV. (1983).

[389] A.T. Kelmens & Sons v. Reber Plumbing & Heating Co., 139 Mont. 115, 360 P.2d 1005, 1011 (1961).

[390] Standard Specification 5.12.6.2 (2000).

[391] The amount calculated by this formula includes job site overhead as well as extended home office overhead. Standard Specification 5.12.6.2 (2000).

[392] Manshul Construction Corp. v. Dormitory Auth., 79 A.D. 2d 383, 436 N.Y.S.2D 724 (1981).

[393] Standard Specification 109.10 (1999).

[394] *See* Reliance Ins. Co. v. United States, 931 F.2d 863, 865 (Fed. Cir. 1991) (10 percent overhead on first $20,000, 7 ½ percent overhead on next $30,000, and 5 percent overhead on balance over $50,000).

[395] *See e.g.*, Manshul Constr. Corp. v. Dormitory Auth. of New York, 79 A.D. 2d 383, 436 N.Y.S. 724, 730 (1981). Based on proof, the following formula was used: (1) total home office overhead, (2) minus the amount of home office overhead allocated to other contracts, and (3) multiplied by the percentage of the owner's liability as determined by the jury (hence 75 percent) for delaying completion beyond the contract completion date.

[396] Melka Marine, Inc. v. United States, 187 F.3d 1370, 1376–77 (Fed. Cir. 1999).

owner can tell the contractor to seek other work until the problem causing the delay can be resolved. The owner may also have the option of terminating the contract for convenience, where the contract contains a termination for convenience clause. This option allows the owner to avoid further delay damages, which may be cheaper than allowing the damages to continue.

6. Delay and Disruption Damages

Delay and disruption are events occurring during contract performance that affect the work.[397] Although not synonymous, a delay may disrupt work and a disruption may delay contract performance. But the damages that flow from delay and disruption are different. Delay damages typically include extended overhead, both in the home office and field; idle equipment during standby; and escalated labor and material costs due to inflation. The damages that flow from disruption are loss of productivity and usually increased labor costs due to inefficiency. To recover delay damages, the contractor must show that the delay extended the project beyond the scheduled completion date or an earlier completion date, if the contractor can prove that it intended to finish early and was prevented from doing so.[398] It is not necessary to show that project completion was delayed to establish damages for disruption. The "ripple" effect refers to the impact that one contract has on other contracts and is considered as consequential damages and not recoverable in a suit for breach of contract.[399]

The nexus between entitlement and damages is causation. It ties entitlement to damages and establishes the effect that the event had upon contract performance. For example, assume that a highway construction contract provided that a bridge, to be constructed under another contract, would be available to the contractor on September 1. The bridge provides access for grading equipment to the western portion of the project site. The bridge is not available until October 1. The project completion date is extended 1 month. The contractor is on standby during September and has a claim for idle equipment and extended overhead. The three elements of a claim have been established: breach or entitlement (bridge not available on September 1 as promised); damages (extended overhead and idle equipment); and causation (unavailability of the bridge caused the damages. If the bridge had been available, the equipment would have been working, not idle, and the project would not have been delayed).

Now assume that the contractor was tied up on another, separate project and even if the bridge had been available, the project would still be delayed. In short, a concurrent delay[400] has occurred. The owner delayed the contractor and the contractor delayed itself. Neither party can recover damages from the other for the delay. Assume now that the equipment is on-site on September 1 and goes on standby, but because of heavy rain, part of September is too wet to perform earthwork. Thus, there are some days in September when the equipment would have been idle. Also, the project completion date would have been extended by those days in September that were unworkable. Under this scenario, the owner would only be partially responsible for the delay. A simple case. The only thing that might be in dispute, other than equipment standby rates and overhead damages, is whether certain days were or were not workable. No scheduling analysis is needed to identify concurrent delays and other events that could affect causation.

Now assume that a project involves over 3000 construction activities performed by the general contractor and nine subcontractors. Assume further that the project was scheduled for completion in 2 years but took 3. Assume that the contractor claims: 1) that the project was mismanaged by the owner's construction manager, 2) that the plans contained numerous errors, 3) that DSCs were encountered, 4) that numerous unilateral change orders were issued that remain in dispute, 5) that the owner's representatives were unreasonably slow or missed turn-around dates in reviewing shop drawings and other submittals, 6) that the owner's representatives were unreasonably slow in responding to the contractor's requests for information about plan clarifications, and 7) that there was over-inspection and other owner interferences with the work. Assume the owner's construction manager denies the contractor's allegations and claims that the contractor's wounds and problems were self-inflicted, 8) assume the owner's architect/engineer (designer) denies that the plans are defective and claims that the requests for information were submitted only to further a claim that the contractor intended to make from the outset of the project, and 9) assume the subcontractors, several of whom have filed bankruptcy, have submitted claims to the general contractor, who has passed them on to the owner.

The claim is for breach of contract, delay, disruption and other impacts on the work, extra work caused by defective plans, DSCs, and remission of liquidated damages. There are also claims for lost opportunities, business destruction, and consultant and attorneys' fees. The contract and the law recognize concurrent delay as a defense to delay claims. The DSCs clause in the contract does not allow impact damages for the effects of the condition upon unchanged work, but changes clauses may allow such damages unless the

[397] A changes clause may entitle a contractor to an equitable adjustment for the effect that a change has upon unchanged work. However, under most DSC clauses—an exception is the standard federal construction clause—impact costs are not allowed. *See* Subsections A and B of § 5, *supra*.

[398] *See* Subsection 5.C.3, *supra*.

[399] Smith v. United States, 34 Fed. Cl. 313, 326 (1995). The only federal construction case where "ripple" damages were allowed is Ingalls Shipbuilding Div., ASBCA No.17579, 78-1 BCA ¶ 13,038 (1978). Recovery was permitted only because of the specific language contained in the Suspension of Work clause. Smith v. United States, 34 Fed. Cl. at 326.

[400] *See* Subsection 5.C.2.C, *supra*.

contract contains a "no-pay-for-delay" clause. This is a large, complex claim and will require a detailed causation analysis using a CPM to assign responsibility for delay, and determine which clause will be enforceable.

7. CPM Schedules

a. CPM Scheduling

A CPM schedule graphically depicts the sequence and duration in which certain work activities must be performed to complete the project within the time specified in the contract. The contractor estimates the order and duration of each important work activity. This estimate is then programed by a computer, which produces a schedule showing each critical work item. The line on the schedule depicting those activities, their durations, and their interdependencies is the critical path.[401] The critical path is not rigid. It may change as conditions change during contract performance. For example, noncritical items of work may become critical if they are unduly delayed, affecting the critical path.

Originally, CPM scheduling was developed as a management tool to assist both owners and contractors. CPM scheduling allowed contractors to plan and control their work with more precision and reliability than they could using a bar chart.[402] CPM scheduling allowed an owner to determine whether the contractor's plan for performing the work would allow the project to be completed within the time specified in the contract. It also allowed both the contractor and the owner to monitor the work as construction progressed to determine if the work was on schedule and identify potential problems that could delay completion of the project.[403]

b. The Use of Scheduling Analysis for Delay and Disruption Claims

CPM scheduling has been used to analyze delay and disruption claims. For delay claims, the contractor has to show that the event causing the delay actually delayed work on the critical path.[404] The schedule analysis focuses on comparing two project schedules: The "as-planned" schedule (the schedule the contractor intended to follow in constructing the project), and the "as-built" schedule, which shows how the project was actually constructed. The comparison identifies project delays. Once delays are identified, the cause of the delay can be analyzed and responsibility for the delay determined. This is the "but-for" schedule, which shows how the project would have progressed had the events causing the delay not occurred.[405] In preparing this schedule, it is necessary to determine what activities have been delayed and the extent of the delays. The analysis should address any concurrent delay.[406] This can be done by identifying delays that are not the owner's fault. The "but-for" schedule must be accurate.[407] Disruption may be proved by a similar analysis. The "as-planned" and "as-built" schedules can be compared to show the difference between how the work should have been performed and how it was actually performed. This allows the analyst to focus on the events that caused the disruption and the extent or duration of the disruption. Scheduling analysis requires the use of experts.

Some states' schedule provisions require all delays to be measured by using the latest approved schedule so as to assess the true impact of the delays.

The contract should require the contractor to furnish the owner a complete scheduling and plotting software package used by the contractor in preparing the claim. The contract should provide that the software package is licensable by the owner to avoid copyright disputes. The contract should also require a copy of a floppy disk containing the contractor's progress schedule data files as part of its original schedule submittal. The data files contained in the floppy disk should be sufficiently complete to allow an independent analysis of the schedule using the scheduling software package. A contractor who claims delay damages should be required to show how and the extent to which the critical path was delayed. The owner should be in the position of reviewing whether the claim is supported, and not in the position of trying to determine how the various claim events impacted the critical path. Justifying the claim is the

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[401] Haney v. United States, 230 Ct. Cl. 148, 676 F.2d 584, 595 (Ct. Cl. 1982) (describing the critical path method). The durations shown in the schedule to perform critical activities shows early and late starts and early and late finishes for those activities. Any additional or spare time between the time necessary to complete the activity on schedule is usually referred to as float time, but using up the float will not delay the scheduled completion of that activity. One view is that neither the contractor nor the owner own float; it exists for the benefit of the project and is available to either party. The owner can issue a change order, but does not need to grant a time extension if the duration of the float is adequate to cover the change. The contractor can use the float as needed to reallocate resources.

[402] Bar charts do not depict the interdependencies between critical activities, a feature necessary in scheduling work in large, complex projects involving numerous activities.

[403] Harp, *supra* note 263, at 35–36.

[404] Neal & Co. v. United States, 36 Fed. Cl. 600, 643–44 (1996).

[405] The as-built schedule is a historical fact. It shows how the project was actually constructed and is prepared from project records and interviews with project personnel. The as-planned schedule is a projection of what the contractor thought would occur with respect to construction of the project, and not a historical fact like the as-built schedule. The but-for schedule depicts how the project would have been constructed but for the owner's delays. *See* Youngdale & Sons Constr. Co. v. United States, 27 Fed. Cl. 516, 550–51 (1993).

[406] Concurrent delay is discussed in § 5.C.2.d.

[407] Edwin J. Dobson, Jr. v. Rutgers, State Univ., 157 N.J. Super, 357, 384 A.2d 1121 (1978).

contractor's responsibility, not the owner's. Failure to provide this information should be reason for rejecting the delay claim.

> In light of the massive effort of appellant's delay expert (findings 147), appellant clearly could have reconstructed and inputted the change order information at the proper times into the CPM schedule had appellant prepared and maintained proper records as to when the change order and constructive change work had been performed, (finding 167). Appellant's failure to prepare and maintain these records is clearly inexcusable in light of the clear contract requirements that this type of information be provided to maintain the accuracy of the CPM schedule (finding 16 ¶ 1.4 & ¶ 15). Accordingly, appellant's delay claims cannot be granted.[408]

c. Practice: New Scheduling Innovations

NYSDOT is in the forefront of new developments in CPM systems. New York has adopted the Enterprise Web-based solutions, which enable all interested parties to share project information on a real-time basis. The Enterprise system is used in the design phase and is a valuable tool in the construction phase of the project. New York has secured site licenses for contractor and department personnel. By utilizing Primavera 6 and Enterprise data warehouse, all users, which include contractor and department personnel, are able to review CPM schedules to analyze schedule issues, claims, and issues as they occur. The project schedule is available to all online and is used as a management tool by all parties to mitigate and analyze delays and project issues. The format of the schedule is given to the contractor, who builds the schedule on the DOT server by inputting the basic required schedule information, including production rates.

This process eliminates paper and disc submissions and allows all parties to have access to the same information at the same time, making it possible to resolve issues quickly and efficiently. The system facilitates collaboration between the contractor and the department. It enables all parties to share in the plan information and measure job progress during construction. The system, along with "Contract Manager," is being implemented in the $407 million Alexander Hamilton Bridge Rehabilitation, which requires weekly schedule submissions and meetings to review and update the project schedule. In addition, New York has adopted an automated contract management system to maintain and share field documents, including inspection reports, engineers' diaries, contract documents, and submittals. The schedule tracks all submittal shop drawing and requests for information. Delays are analyzed, milestones adjusted and documented if appropriate, and mitigation strategies are developed to keep the project moving. In addition, the system permits the project teams to review look-ahead activities, analyze low-float activities, and review upcoming change orders.[409]

8. Consequential Damages, Other Costs, and Profit

a. Consequential Damages

When a project is delayed by the owner, the contractor may make a claim for lost profits on other projects that the contractor was unable to bid because of the delay. The contractor may assert that the delayed project tied up its bonding capacity, preventing it from bidding other projects where bonding was required. To support its claim, the contractor may submit a list of projects that it intended to bid, its success rate in submitting winning bids, and its profit history. Generally, such claims are denied as too speculative because they are based on assumptions or possibilities, not probabilities.[410]

Recovery for lost profits due to lost business opportunities, however, has been allowed when such damages were reasonably foreseen and contemplated by the parties when the contract was made, are a probable consequence of a breach, and can be proven with reasonable certainty.[411] An owner seeking an order from a court summarily dismissing a lost profits or lost opportunities claim should focus on the remote and speculative nature of such damages, forcing the contractor to show that they were contemplated by the parties when the contract was let, that they are a probable consequence of the breach, and that they can be proven with reasonable certainty. If the contractor cannot make that showing, the claim should be dismissed as a matter of law.[412]

Contracts may contain clauses barring consequential

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[408] Santa Fe Eng'rs, ASBCA Nos. 24578, 25838, and 28687, 94-2 BCA ¶ 26,872, at 133, 753 (1994).

[409] Address of Mark White, NYSDOT, and Manual Silva, AGC/DOT Annual Technical Conference, Saratoga Springs, N.Y., Dec. 8, 2011.

[410] Manshul Constr. Corp. v. Dormitory Auth., 111 Misc. 2d 209, 444 N.Y.S.2d 792, 803 (1981) (a case of first impression in New York). *See also* Golf Landscaping, Inc. v. Century Constr. Co., 39 Wash. App. 895, 696 P.2d 590 (1984); United States v. Merritt Meridian Constr. Corp., 95 F.3d 153, 161 (2d Cir. 1996). In Manshul Constructions, the court characterized the contractor's assumptions that it would obtain other contracts and make a profit as wishful and too speculative to stand as a matter of law, 444 N.Y.S.2d at 803–04. *See also* Land Movers, Inc. and O.S. Johnson-Dirt Contractors (JV), ENGBCA No. 5656, 91-1BCA ¶ 23,317, at 14–15 (1990), (Board said that it was unaware of any Board or federal court decision where consequential damages were allowed); Zook Bros. Constr. Co. v. State, 171 Mont. 64, 556 P.2d 911, 918 (Mont. 1976) (loss due to contractor having to sell its equipment not allowed).

[411] Hadley v. Baxendale, 9 Ex. 341, 156 Eng. Rep. 151 (1854); Lass v. Mont. State Highway Comm'n, 483 P.2d 699, 704 (Mont. 1971); Larsen v. Walton Plywood Co., 65 Wash. 2d l, 390 P.2d 677, 687 (1964); Gouger & Veno, Inc. v. Diamondhead Corp., 29 N.C. App. 366, 224 S.E.2d 278, 279 (1976).

[412] Manshul Constr. Corp. v. Dormitory Auth*;* 444 N.Y.S.2d at 802–04; Golf Landscaping, Inc. v. Century Constr. Co., 696 P.2d at 594–95.

damages.[413] Inclusion of this type of clause serves two purposes: First, it bars lost profit claims and other consequential damage.[414] Second, inclusion of the clause clearly establishes that consequential damages were eliminated by the parties as a probable consequence of a breach when the contract was signed. As noted earlier, this is an element (among others) that the contractor must prove to recover lost profits. A classic example of such clauses is provided by FDOT Section 5-12.10, which provides no recovery for consequential damages including, but not limited to, loss of bonding capacity, loss of bidding opportunities, loss of credit standing, cost of financing, interest paid, loss of other work, or insolvency. The AASHTO Guide Specifications also list loss of profit more than what is provided in the contract, loss of profit, attorneys' fees, claim preparation expenses, and litigation costs.[415]

b. Financing Costs

In the absence of a clause in the contract or a statute barring recovery, interest paid on money borrowed to finance the work may be recovered, if the contractor can prove that the money was borrowed solely because of owner-caused delays and extra work.[416] To recover, the contractor must show that interest was paid to an independent entity, such as a bank. In other words, the contractor cannot recover interest on funds that it furnished to itself to finance the extra work or delay costs.[417] The contractor must be able to trace the interest paid for the borrowings,[418] and prove that the borrowed funds were actually used to finance the extra work or delay costs caused by the owner.[419] Recovery will be denied if the contractor cannot segregate the interest paid on the borrowings from the interest paid on its general line of credit.[420]

c. Prejudgment Interest

Recovery of prejudgment interest may be allowed when the claim is liquidated[421] or sovereign immunity does not apply.[422] Damages are not liquidated where the amount owed requires determination by a jury.[423]

Prejudgment interest, when owed, runs from the date on which payment is due until it is paid.[424] Under the Contract Disputes Act,[425] federal agencies are required to pay interest on contract claim settlements or awards from the date the contracting officer receives a properly certified claim until the claim is paid.[426] Some states have adopted "prompt payment" acts. Under these acts, a state agency is liable for interest, at a specified rate, if it fails to make a payment due the contractor within 30 days after receiving the contractor's invoice.[427]

d. Bond and Insurance Costs

Increased bond and insurance costs caused by owner delay are compensable[428] unless recovery is precluded by a "no-pay-for-delay" clause in the contract.[429] Increased bond and insurance costs may be included as part of an equitable adjustment under a changes clause where added work or compensable delay extends the contract's duration.[430]

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[413] The Standard Specifications used by Colorado (Spec. 109.10 (1999)), Florida (Spec. 5-12.10 (2000)) and Washington (Spec. 1-09.4.4 (2000)) are examples of this type of clause.

[414] The clause may enumerate the kinds of consequential damages that are barred. For example, the Florida Standard Specification (5-12.9) provides that there is no liability for consequential damages including, but not limited to: loss of bonding capacity, loss of bidding opportunities, loss of credit standing, loss of financing, insolvency, loss of other work, cost of financing, and interest paid on money borrowed to finance the job.

[415] AASHTO § 109.09 B.

[416] Gevyn Constr. Corp. v. United States, 827 F.2d 752, 754 (Fed. Cir. 1987); Bell v. United States, 186 Ct. Cl. 189, 404 F.2d 975, 984 (Ct. Cl. 1968); Drano Corp. v. United States, 594 F.2d 842, 847 (Ct. Cl. 1979); Westland Constr. Co v. Chris Berg, Inc., 35 Wash. 2d 284, 215 P.2d 683, 690 (1950). *But see* 48 C.F.R. § 102.

[417] Gevyn Constr. Corp. v. United States, 827 F.2d at 753–54.

[418] Neb. Public Power Dist. v. Austin Power, Inc., 773 F.2d 960, 973 (8th Cir. 1985).

[419] Neb. Public Power, *id.*; Cal-Val Constr. Co. v. Mazur, 636 S.W.2d 391, 392 (Mo. App. 1982).

[420] State Highway Comm'n v. Brasel & Sims Constr. Co., 688 P.2d 871 (Wyo. 1984).

[421] A claim is liquidated when the amount of the claim can be determined without reliance on opinion or discretion, Simes Constr. Co. v. Wash. Public Power Supply System, 28 Wash. App. 10, 621 P.2d 1299, 1304 (1980), or by reference to a fixed standard in the contract such as Force Account provisions, Fiorito Bros. v. Department of Transp., 53 Wash. App. 876, 771 P.2d 1166, 1167 (1989).

[422] Architectural Woods, Inc. v. State, 92 Wash. 2d 521, 598 P.2d 1372, 1375 (1979). (Sovereign immunity waived by entering into the construction contract). But a state may expressly preclude liability for prejudgment interest. P.T. & L. Constr. v. State Dep't of Transp., 108 N.J. 539, 531 A.2d 1330, 1344 (1987).

[423] Green Constr. Co. v. Kan. Power & Light Co., 1 F.3d 1005, 1010 (10th Cir. 1993).

[424] Paliotta v. Department of Transp., 750 A.2d 388, 394 (Pa. Commw. 1999); Department of Transp. v. Anjo Constr. Co., 666 A.2d 753, 760 (Pa. Commw. 1995).

[425] 41 U.S.C. § 611.

[426] Youngdale & Sons Constr. Co. v. United States, 27 Fed. Cl. 516, 562 (1993).

[427] For example, *see* Alaska Statute § 36.90.200.

[428] Luria Bros. & Co. v. United States, 177 Ct. Cl. 646, 369 F.2d 701 (Ct. Cl. 1966).

[429] *See* § 5.C.

[430] Harp, *supra* note 262, at 32.

e. Attorney Fees

Under the "American Rule," each litigant bears its own attorneys' fees.[431] However, there are exceptions to the rule. One exception is where the contract allows fees to the prevailing party.[432] Another exception is where fees are allowed by statute.[433] In addition to contractual provisions and statutes as grounds for awarding fees, courts have awarded fees based on equity,[434] or for federal construction where legal fees are incurred by the contractor as costs of performing the contract, as opposed to costs associated with prosecuting a claim.[435] This rule has been applied in state public works disputes.[436]

f. Claim Preparation Costs

The rule that attorneys' fees are not allowed in claims against the Government applies to claim preparation costs.[437] Legal, accounting, or consulting costs incurred in connection with the prosecuting of a Contract Disputes Act claim are unallowable because they were not incurred to benefit contract performance. However, like attorneys' fees, consulting costs incurred during contract performance that result from changes ordered by the Government may be recoverable.[438] Alaska follows this view.[439]

g. Profit and Markup

A contractor is entitled to a reasonable profit on the cost of performing extra work,[440] even if the original contract price (bid) did not contain any profit.[441] The rate of profit allowed may consider the risks and difficulties involved in performing changed or extra work.[442] The contract may specify the profit rate or specifically preclude profit on certain costs, such as delay costs incurred under a Suspension of Work clause.[443]

A contractor may also recover overhead allocable to direct costs incurred due to owner-caused delays or extra work. Overhead is usually calculated as a percentage of the direct costs, but does not include any recovery for unabsorbed or extended home office overhead. Those costs are calculated separately as discussed earlier.[444] A contractor may also be entitled to a markup on the award of extra costs to its subcontractor on a pass-through claim.[445]

D. CONSTRUCTION CONTRACT LITIGATION: TRIAL PREPARATION AND STRATEGIES

1. Introduction

Construction claims seem inevitable.[446] Virtually every construction project has disputes over money, time extensions, or both. The disputes are usually resolved by the parties through negotiations. When they are not settled, the next step may be litigation or arbitration.[371]

While the rules for trying cases may vary from jurisdiction to jurisdiction, the litigation process is generally the same in most jurisdictions. The contractor, who is typically the plaintiff, files a complaint in court against the owner for damages.[448] The owner files a response in the form of an answer denying the claim.[449] The answer

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[431] Urban Masonary Corp. v. N&N Contractors, 676 A.2d 26, 33 (D.C. App. 1996). Alaska follows the "English Rule," which allows the prevailing party to recover attorneys' fees from the losing party. Ryan v. Sea Air, Inc., 902 F. Supp. 1064, 1070 (D.C. Alaska 1995) (applying Alaska law).

[432] Urban Masonary Corp. v. N&N Contractors, *id.*

[433] Equal Access to Justice Act, 28 U.S.C. § 2412; *see* Mega Constr. Co. v. United States, 29 Fed. Cl. 396, 479 (1993); *See also* WASH. REV. CODE § 39.04.240 (allows the prevailing party (either the contractor or the agency) to recover reasonable attorneys' fees in a public works construction contract dispute).

[434] Public Utility Dist. No. 1 v. Kottsick, 86 Wash. 2d 388, 545 P.2d 1, 3 (1976) (bad faith or wantonness).

[435] Appeal of S & E Contractors, AEC BCA No. 97-12-72, 74-2 BCA ¶ 10, 676 (1974) at 50,695 (fees allowed when they are a necessary expense in carrying out changes to the contract ordered by the Government). But if the fees are not performance related, they are not recoverable. Singer Co. v. United States, 568 F.2d 695, 720–21 (Ct. Cl. 1977).

[436] Anchorage v. Frank Coluccio Constr. Co., 826 P.2d 316 (Alaska 1992).

[437] Singer Co. v. United States, 568 F.2d 695, 720–21 (Ct. Cl. 1977).

[438] Bill Strong Enters. v. Shannon, 49 F.3d 1541, 1549 (Fed. Cir. 1995). This case traces the history of decisions and regulations addressing the allowability of legal and consulting costs related to federal construction contracts.

[439] *See* Anchorage v. Frank Coluccio Constr. Co., 826 P.2d at 330 (applying the rule in Singer that fees incurred in prosecuting a claim that is not associated with contract performance are not recoverable; citing and quoting from a federal Board of Contract Appeals decision); Fiorito v. Goerig, 27 Wash. 2d 615, 179 P.2d 316, 319 (1947) (consultant fees not recoverable in the absence of express contractual or statutory provisions permitting recovery).

[440] United States v. Callahan Walker Constr. Co., 317 U.S. 56, 61, 63 S. Ct. 113, 87 L. Ed. 49 (1942).

[441] Keco Indus., ASBCA 15184, 72-2 BCA ¶ 9576, at 44, 733-4 (1972) (5 percent profit allowed).

[442] American Pipe & Steel Corp., ASBCA 7899, 64 BCA ¶ 4058, at 19,904 (1964).

[443] *See* 48 C.F.R. § 52.242-14(b).

[444] *See* § 6.C.5.d., *supra*.

[445] Pa. Dep't of Transp. v. James D. Morrison, Inc., 682 A.2d 9, 16 (Pa. Commw. 1996). Subcontractor pass-through claims are discussed in § 6 B.4., *supra*.

[446] This chapter incorporates *Trial Strategy and Techniques in Contract Litigation*, by K.T. Hoegestedt and Orrin F. Finch, published in SELECTED STUDIES IN HIGHWAY LAW (Transportation Research Board 1979).

[371] *See* Subsection 6.A, listing the "Final Remedy" established for state transportation agencies.

[448] A similar process is used to initiate arbitration. For example, if the contract specifies arbitration by the American Arbitration Association (AAA), arbitration is initiated by filing a demand for arbitration with the AAA.

[449] A party may file an answer in response to a demand for arbitration. *See* Construction Industry Arbitration Rules and

may assert affirmative defenses,[450] which if proven would bar or limit the claim. The answer may also include a counterclaim.[451]

Once the case is at issue and the parties have formally stated their positions, pretrial discovery takes place, usually through interrogatories, document production requests, and depositions.[452] Consideration should be given for the public owner to obtain priority to conduct depositions, and to obtain discovery of records, without awaiting completion of claimants' discovery efforts. In addition, either party may try to narrow the case and define the issues that will be tried through requests for admissions and pretrial orders.[453] Pretrial motions may be made to dismiss claims or even to dismiss the lawsuit in its entirety.[454] Motions in limine may be made to exclude evidence and prevent witnesses from testifying about matters that are not admissible.[455]

Consideration should be given to requesting the court to preassign a large, complex construction case to one judge for all pretrial motions and the trial. In some jurisdictions this may be automatic, but in others it may require a motion by the party to have the case preassigned. Consideration should also be given to bifurcating the case into a liability phase and then a damage phase, if liability is found.[456] Counsel should consider the use of summaries where the documents are too voluminous to be conveniently examined in court.[457] In complex or extended cases, a trial judge may permit the jurors to take notes. If the jurors are permitted to take notes, the jurors should be instructed by the court to be guided by their own individual recollections of the evidence and not be swayed by one juror who took copious notes. Finally, care should be taken in drafting jury instructions. Jury instructions must do more that just accurately state the law; they must also be understandable. "A charge ought not only be correct, but it should also be adapted to the case and so explicit as not to be misunderstood or misconstrued by the jury."[458]

When discovery is completed, the case is ready for trial and a trial date is set.[459] The keys to success in litigation are often expressed in two words: preparation and credibility. These keys are interrelated. A solid strategy is also important in trying the case. Construction litigation often involves a mass of details and acts that may impact numerous construction activities. It is therefore essential that the case be simplified and presented in a way that will persuade a judge, jury, or an arbitrator that the agency's position is fair and legally correct.

Careful preparation is also important to avoid overpreparing the case, which can waste time and money, and under-preparation, which can be disastrous. The construction trial lawyer should develop a plan at the outset of the case to guide case preparation between these two extremes. The purpose of this subsection is to suggest ways that will assist the trial lawyer in preparing and trying the case. While the focus of this subsection is on defending claims against public owners, much that is said here may also be used by owners in prosecuting claims against contractors.

2. Trial Preparation—Organizing the Case

There are several preliminary steps in organizing the case. The first step is understanding the claim. A good place to start is with the claim that the contractor filed with the agency as part of the administrative claim process.[460] This is especially true when the contract requires that the claim contain sufficient information to ascertain the basis and the amount of the claim.[461] If the claim lacks the required detail, it may be subject to dismissal where compliance with the claims specification is a contractual condition precedent to judicial relief.[462] Another source of information is the complaint,

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Mediation Procedures, Rule R-4(b) (American Arbitration Association 2003) [AAA Constr. Rules]. The Rules may be obtained from the AAA Customer Service Department, 140 W. 51st Street, New York, N.Y. 10020-1203, telephone: (212) 484-4000, fax no: (212) 765-4874. AAA rules are also available on AAA's Web site at www.adr.org.

[450] Subpart 6.D.6.b *infra* discusses affirmative defenses. The appendix to this Subsection lists affirmative defenses that may apply.

[451] *See, e.g.,* FED. R. CIV. P. 13; AAA Constr. Rule R-4(b).

[452] Discovery methods are discussed in Sub.A.4.a.

[453] Requests for admission and pretrial motions are discussed in Subsections 6.D.4.a and 6.D.6.c respectively *infra*.

[454] *See* FED. R. CIV. P. 56.

[455] *See* G.O. Kornblum, *The Voir Dire, Opening Statement, and Closing Argument*, 23 PRAC. LAW. No. 7 at 1, 21 (1977).

[456] FED. R. CIV. P. 42 and advisory committee note to 1966 amendment.

[457] *See* FED. R. EVID. 1006.

[458] DiGioia Bros. Excavating Co. v. Cleveland Dep't of Pub. Util., 135 Ohio App. 3d 436, 734 N.E.2d 438, 453 (1999) (citing Aetna Ins. Co. v. Reed, 33 Ohio St. 283, 395 (1878)).

[459] In some jurisdictions, a trial date is not set until the parties certify that the case is ready for trial. If the case has been preassigned, a trial date is usually set before discovery is completed. Usually, the court will set a discovery cut-off date some time in advance of the trial date. All discovery must be completed by that date, and extension of the discovery period requires court approval.

[460] *See* § 6.A.3., Administrative Claims Procedures and Remedies, *supra*.

[461] *See* generally the discussion of the Florida claims specifications in Subpart 6.A.3.a *supra*.

[462] Metropolitan Dade County v. Recchi Amer., Inc., 734 So. 2d 1123 (Fla. App. 1999) (contractor must follow contract claim procedures prior to commencement of suit). The contract should also preclude the contractor from increasing the amount of the claim or the basis for entitlement after the claim has been filed. *See* Florida Standard Specification 5-12.3 (contractor claim is limited to amount and basis for entitlement that is

although most complaints contain broad allegations and few specifics. The attorney should also review the final acceptance papers, where the contract requires the contractor to reserve its claims and to release those claims that are not reserved.[463]

After reviewing the claim documents, the next step is usually a meeting with agency personnel to discuss the claim.[464] The meeting has several purposes. The primary purposes are to obtain more information about the claim, help develop the agency's position in the lawsuit, answer questions, explain legal procedures, and explain what will be expected of those involved. A secondary purpose is to refresh and reinforce the knowledge and memories of others through a group discussion. The meeting is also an opportunity for the attorney to make preliminary judgments about whom he or she could call as witnesses in the case.

The meeting should be orderly, but also uninhibited. Project personnel should be encouraged to speak freely, or even refute what others have said when they disagree. This too serves several purposes. First, it provides an opportunity to resolve differing recollections or interpretations of events that occurred during construction. Second, it is also an opportunity to assess the relative merits of the agency's position with respect to the claim. It is far better to learn about problems with the agency's position in a meeting like this than in a deposition or, even worse, at trial.

Normally, conversations between agency personnel and the agency's attorney, in preparation for litigation, should be privileged under both the attorney-client privilege and the attorney work-product privilege. But as a practical matter, the attorney should not automatically assume that such conversations are privileged and therefore immune from discovery. Instead, the attorney should carefully review the precedents of his or her jurisdiction before deciding whether to memorialize conversations in recordings.[465]

Either prior to the meeting or after, the attorney should conduct a detailed review of the administrative records maintained by the agency to get a complete understanding of the history, personnel, and issues of the claim. While not always feasible given the attorney's work schedule, reviewing the records prior to the meeting will provide the attorney with a greater opportunity to make a more effective use of the meeting by posing informed questions to project personnel.

a. The Claims Summary

Following the meeting, the attorney should have enough information to develop a "claim summary" for the attorney's trial notebook. The summary should contain the following information and be inserted loose-leaf in the notebook to allow pages to be added or replaced as the attorney becomes more familiar with the facts. The summary may contain:

- A brief description of the project, together with a simple drawing or sketch illustrating the construction features involved in the claim.
- A chronology of the project showing: 1) when the contract was executed, 2) when the contractor was given notice to proceed, 3) when the contractor began work, 4) when substantial completion occurred, and 5) when final acceptance occurred.
- The number of days that the contract overran, if applicable.
- The bid price.
- Significant change orders.
- Time extensions.
- Edition of the Standard Specifications that applies to the contract.
- Significant plan sheets from the contract plans and why they are significant.
- Any amendments to the Standard Specifications.
- Any permits issued by governmental agencies that affect construction.
- Pertinent special provisions.
- A reference to pertinent photos and videos, what they show, and who has custody.
- Significant diary entries, inspector's daily reports, memoranda, and letters identified during the meeting with project personnel.
- List of significant subcontractors and material suppliers who may have information pertinent to the claim, but do not have pass-through claims.
- Job site arrangements, such as material storage areas, haul roads, and access restrictions that may affect construction.
- List of contractor personnel whom agency personnel believe may have information pertinent to the claim and a brief description of what that information entails.
- Significant weather days by date that affected construction.
- Consultants who participated in the preparation or review of the contract plans and specifications, soils reports, and shop drawings, as they pertain to the claim.
- Brief statement of the contractor's position regarding each claim.
- Brief statement of the owner's position regarding each claim.
- Pertinent case law and statutes (citations).
- Affirmative defenses that may be asserted.
- Project personnel and their connection with the claim, general observations about them from the meeting, and their phone numbers and fax numbers.

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stated in written claim, and may not be amended in court proceeding or arbitration).

[463] California Department of Transportation Standard Specification 9-1.07B (2002) and New York Standard Specification 109-14 (2002) are examples.

[464] The meeting often includes a visit to the project site, which is usually helpful in understanding the claim.

[465] The subject of attorney-client and work-product privileges is discussed in Sub.D.2.e. *infra*.

Typically, the next step in the process is to file an answer to the complaint. This pleading is the principal vehicle for stating the owner's position in the case. Under most court rules, it must be a section by section response admitting or denying each numbered paragraph of the complaint. The answer may also contain affirmative defenses and counterclaims. Affirmative defenses may include any factual or legal defense that is appropriate.[466] Prior to filing the answer, the attorney should meet with the agency to review the claim, contract provisons, and proposed affirmative defenses. Failure to assert a mandatory counterclaim (one involving the same contract that gives rise to the claim) in the answer may waive the counterclaim.[467]

b. The Litigation Team

There are some initial considerations in organizing the litigation team and developing a litigation plan. Construction litigation can be very expensive. Because it can be so expensive, an owner should consider whether the case can be resolved short of trial through further negotiations or mediation.[468] If so, the initial preparation of the case should be limited to those steps necessary for effective mediation. Experts should be retained early, but given limited assignments necessary for the mediation process. Discovery should be limited to a few key depositions, or there even should be a moratorium on depositions, except perhaps for record depositions for subcontractors, suppliers, or other nonparties.[469] These steps are important in achieving a cost-effective resolution of the case. If mediation is not successful, then the more expensive and laborious discovery and case preparation can begin. Typically, in a large construction case, the litigation team will be composed of a lead trial counsel, other attorneys as necessary, paralegals, support staff, and experts who can either be in-house experts, retained experts, or both. Many state transportation agencies utilize claims engineers or auditors, who assist the trial attorney with claims defense and preparation and coordinate the agency claims defense with witness and record production.

c. Locating and Retaining Experts

Most complex construction cases will require the use of expert testimony. Claims consultants are usually retained at an early stage to assist the litigation team in developing an overall trial strategy, as well as assist in more discrete tasks such as developing issues for document coding and assisting in the preparation of discovery requests. In the absence of an agency claims engineer, the claims consultant can also assist in the selection of other experts needed to cover gaps in the case.

In selecting an expert witness, it is important, even critical, to keep in mind that the expert will probably testify if the case goes to trial. Therefore, the person selected must not only be an expert and qualified to testify, but the expert must be a good witness, someone who will impress the judge or jury. In addition to being credible, the expert should be experienced in litigation and be able to think and handle himself or herself under cross-examination. The expert should be able to present ideas clearly and persuasively in plain language. Ideally, the expert should be able to make the complex simple and readily understandable by a judge or jury. Above all, the expert should be able to present opinions in a comprehensible, convincing, and understandable manner on direct examination and defend them in the same way under hostile cross-examination.

Where do you find a claims consultant to help defend the claim? One source is to ask other lawyers whom they have retained in similar cases. Another source is a national list of construction experts published by the American Bar Association. The list will usually include several attorneys as references. In checking with the references, you should ask each attorney whether the expert testified for that attorney. If not, obtain from the expert the names of attorneys for whom the expert has testified.[470]

Some considerations in retaining an expert include the following. First, always retain the individual who will testify, not a firm that will select the witness. The agreement for consultant services can be with the firm, but the agreement should specify the person that will testify, if requested by the attorney.[471] For example, the standard agreement used by the Washington State DOT provides that, "the Consultant shall designate (*name of expert*) to provide factual and expert consultation to owner and testify as an expert witness, if so designated by owner's counsel." Second, the agreement should also provide that work and work product produced by the consultant shall be deemed confidential until the owner desires to designate the consultant as

[466] The Appendix to this Subsection contains a list of affirmative defenses.

[467] *See* FED. R. CIV. P. 13.

[468] Mediation is discussed in § 7.

[469] Records can be obtained from nonparties voluntarily or by subpoena duces tecum at a records deposition. Federal Rule of Civil Procedure 45 protects nonparties by requiring them to attend a deposition not more than 100 miles from where they reside, are employed, or transact business in person.

[470] M. Beisman, *How To Choose a Construction Expert*, 37 PRACT. LAW. No. 7, at 19 (1991).

[471] The agreement for the consultant's services should not state that the consultant will testify as an expert witness, but only that the consultant may be asked to testify if requested by the defendant. To designate the expert as a witness in the agreement, instead of as a possible witness, raises several problems. First, it exposes the expert to being deposed because the expert is not a consulting expert who cannot be deposed until designated as a testifying expert. Second, it provides ammunition for cross-examination: Why did the unbiased expert agree to testify to his or her opinions before the expert even investigated the claim?

an expert witness: All information developed by the consultant should be confidential and should not be revealed by the consultant to any other person or organization without the express consent of the owner or by court order.

d. The Litigation Plan

The litigation plan is an outline identifying the key issues in the case. The issues in the outline are given numbers for use in coding and indexing documents, and form the basis for establishing a method of retrieval. The better and more complete the outline, the more efficient retrieval will be. This portion of the outline should be done by someone who has a good understanding of the case and is thoroughly familiar with a computerized litigation support system. Usually, that person is the claims consultant. At this point in the litigation, a decision should be made whether to retain an outside litigation support firm or use an in-house computer and in-house staff for coding documents with issue numbers. This presupposes that a decision has been made to use a computerized system instead of a manual index and retrieval system. An outside support firm should be used if the agency does not have experience using an in-house computer for litigation support.

The plan should also designate the attorneys and paralegals who will have primary responsibility for certain issues and for gathering and controlling documents. The plan should provide for the development of a standard form for coding and indexing the categories of information that will be stored in the computer. The form should contain a line for a Bates number[472] that has been stamped on each page of each document. The coder reviews a document and fills out the form for entry in the computer. An alternative is use of an imaging system in which documents are electronically scanned and stored on disks for later retrieval.

The plan should also provide for a chart showing various tasks that have to be performed, who is responsible for performing them, and the time allotted for performing each task. The chart can be a simple bar chart, or for the more technically inclined, a CPM chart. But whatever its form, its purpose is to provide direction for the overall team effort in preparing the case. The plan should also contain a budget estimating the cost of case preparation up to the time of trial.

e. Attorney-Client and Work-Product Privileges

The attorney-client privilege is recognized in every state.[473] Generally, the privilege applies to conversations between a government entity to the same extent that privilege would apply between a private entity and its attorney.[474] The cases recognize "the need of the government client for assurance of confidentiality equivalent to a corporation's need for confidential advice."[475] However, scholarly opinion is divided with respect to whether government entities should have the privilege.[476]

The work-product privilege protects an attorney's efforts in preparing a case for litigation.[477] The privilege extends to confidential communications between the employees of a corporation and the corporation's attorneys, where such communications are necessary in enabling the corporation to obtain legal advice and prepare for litigation.[478] The work-product privilege, like the attorney-client privilege, has been extended to government entities.[479] The privilege protects communications between an attorney and a consulting expert who will not be called to testify at trial.[480] But the privilege is waived when the expert is identified as a witness who will be called to testify,[481] or when the consulting expert's report is provided to a testifying expert.[482]

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[472] Each category in the database is represented by an eight digit number that is consecutively numbered. These numbers, which identify all documents in the computer by category, are commonly known as Bates numbers. The numbers can be coded to identify the type of document, the source from which it was obtained, the importance of the document, and whether the document is privileged. For example, all documents in the 10000000 series may be coded as contractor's documents, all documents in the 20000000 series as owner's documents, and all documents in the 30000000 series as designer (A/E) documents.

[473] Ford Motor Co. v. Leggat, 904 S.W.2d 643, 647 (Tex. 1995).

[474] California: People ex rel. Dep't of Public Works v. Glen Arms Estate, Inc., 230 Cal. App. 2d 841, 854, 41 Cal. Rptr. 303 (1964); New Jersey: Matter of Grand Jury Subpoenas Duces Tecum, 241 N.J. Super. 18, 574 A.2d 449, 454 (1989); New York: Mahoney v. Staffa, 184 A.D.2d 886, 585 N.Y.S.2d 543, 544 (1992); Ohio: State ex. rel. Thomas v. Ohio State Univ., 71 Ohio St. 2d 245, 643 N.E.2d 126, 131 (1994); Washington: Amoss v. University of Wash., 40 Wash. App. 666, 700 P.2d 350, 362 (1985); *see also* Coastal States Gas Corp. v. Department of Energy, 617 F.2d 854, 863 (D.C. Cir. 1980); Roberts v. City of Palmdale, 5 Cal. 4th 363, 20 Cal. Rptr. 330, 853 P.2d 496 (1993) (privilege extended by statute to public entity).

[475] Matter of Grand Jury Subpoenas, *id*. at 455.

[476] *See* L.A. Barsdate, *Attorney-Client Privilege for the Government Entity*, 97 YALE L. J. 1725 (1988); Note, *The Applicability and Scope of the Attorney-Client Privilege in the Executive Branch of the Federal Government*, 63 B.U.L. REV. 1003 (1982).

[477] Hickman v. Taylor, 329 U.S. 495 (1947); FED. R. CIV. P. 26(b).

[478] Upjohn Co. v. United States, 449 U.S. 383 (1981); STRONG, MCCORMICK ON EVIDENCE, 87-1, at 320 (4th ed. 1992).

[479] L.M. Cohen, *Expert Witness Discovery Versus the Work Product Doctrine: Choosing a Winner in Government Contracts Litigation*, 27 PUB. CONT. L.J. 719 (1998); *see also* State ex rel. State Bd. of Pharmacy v. Otto, 866 S.W.2d 480 (Mo. App. W.D. 1993).

[480] Crenna v. Ford Motor Co., 12 Wash. App. 824, 532 P.2d 290 (1975) (non-testifying expert's opinion not discoverable based on superior court rule that mirrors FED. R. CIV. P. 26(b)(4)(A)); Morrow v. Stivers, 836 S.W.2d 424 (Ky. App. 1992).

[481] Karn v. Ingersoll-Rand, 168 F.R.D. 633, 635 (N.D. Ind. 1996) (information given by an attorney to an expert witness

3. Gathering and Managing Documents

There are several keys to the successful preparation of a large construction case. You must understand the claim, you must have a theory as to why the claim is not valid, you must have the facts to support your theory, and you must have the resources to prove those facts. This subsection focuses on obtaining documents and then organizing them so that they can be retrieved from storage, as needed, in an orderly and efficient manner for use in defending the claim.

Generally, the facts about what occurred during a construction project are found in two places: the recollections of personnel associated with the project and the project documents. Organizing and managing documents is often the most time consuming and laborious task in case preparation. This subsection offers some suggestions about where to obtain project documents and what to do with them once they are obtained.

a. Gathering Documents

Where do we get documents? The answer seems obvious: from the contractor, first, and lower tier subcontractors and materialmen that have pass-through claims or whom we suspect may have useful information. Other obvious sources are the agency's own records and those of its design consultant, if the claim is based on defective plans and specifications. Obtaining records from this latter source may require a decision by the agency as to whether it intends to make a claim against the designer for indemnification. Designers are usually reluctant to open their records to inspection by someone who intends to sue them. Often, the designer will want to know, early in the case, what the agency's position is on that issue.

Consideration should also be given to utilizing contract audit provisions, which provide the agency access to a myriad of the contractor's financial records. Contactor records worthy of examination include foreman's daily reports, job diaries, superintendent's reports, correspondence with subcontractors and suppliers, subcontracts, and all payment records, invoices, job-cost ledgers, financial statements, bid estimates, and workup sheets.

Another obvious source is the records of the contractor's claim consultant, especially the software used by the consultant to generate "as-built," "as-planned," and "but-for" schedules to support delay and impact claims. The contract should require the submission of this type of information as part of the administrative claims process. If not, then this information probably cannot be obtained until the consultant is designated as an expert witness. When that designation is made, the consultant's work product is discoverable.

There are, however, some less obvious sources of information. For example, ask the project office if the contractor obtained any documents from the agency before the lawsuit or even the claim was filed. The agency should have a policy of making a copy of or keeping a record of every document furnished to the contractor after a claim has been made or a dispute has arisen. If the agency did not keep a record or copies, the information will have to be obtained through discovery, usually through an interrogatory. Counsel for the agency should contact FHWA to see if the contractor has obtained any documents from that agency through FOIA.[483] Counsel should also contact other federal regulatory agencies such as the Coast Guard, the Army Corps of Engineers, or the Department of Labor about documents obtained from them under FOIA requests, when the claim involves actions by these agencies or involves matters within their jurisdiction.

Another source of information is the performance bond surety. The surety may require a contractor to make a report to the surety about the project and the contractor's basis and evaluation for claims that it has against the owner. Counsel should request the surety to furnish the information without having to resort to a subpoena duces tecum. Counsel should also check with local regulatory agencies about any documents that the contractor may have obtained from them. Counsel should also contact other bidders to see how they bid the work and if they are willing to help.

Usually other bidders or contractors on the project are reluctant to get involved, but not always. For example, in one case the second bidder testified for the State of Washington that in making its bid it included the cost of reinforcing steel bars in certain precast concrete members, even though steel bars were not shown in the plans. The contractor, who was the low bidder, claimed that it did not include the cost of steel bars in its bid because they were not shown on the plans, and that bars had to be used to prevent the concrete members from cracking when they were removed from the concrete forms. The contractor claimed additional compensation for the steel and other damages. The representative of the second low bidder was a powerful witness. His testimony helped persuade the judge that the cost of steel was incidental and should have been included in the bid price because the members could not be made without steel, and that the contractor, as an experienced concrete fabricator, should have known this.

b. Organizing the Documents

Once the documents are gathered, they can be photocopied, microfilmed, or imaged. Under this latter process, each document page is placed on a scanner,

had to be disclosed; disclosure could not be avoided by claiming that the information was work product).

[482] Heitmann v. Concrete Pumping Machinery, 98 F.R.D. 740,742 (E.D. Mo. 1983).

[483] 5 U.S.C. § 552; *see also* O.F. FINCH & G. A. GREEN, FREEDOM OF INFORMATION ACTS, FEDERAL DATA COLLECTIONS AND DISCLOSURE STATUTES APPLICABLE TO HIGHWAY PROJECTS AND THE DISCOVERY PROCESS (National Cooperative Highway Research Program, Legal Research Digest No. 33, 1995).

which takes an image of the document, similar to a photocopier, and stores the image on a disk. Documents that have been microfilmed can be reproduced as hard copies.

There are, however, certain steps that should be taken before the documents are stored and organized for later use. The first step is to stamp an identifying eight-digit number on the lower right hand corner of each page of each document.[484] After the documents have been stamped, they should be put in chronological order. Once documents are arranged in chronological order, the next step is to develop a working set that can be used for coding the documents. This involves two more steps. The first task is to cull duplicate copies. Care must be taken in performing this task. Only duplicate copies that are identical are removed. If one copy of a memorandum is clean and the other copy has marginalia, they are not duplicates, they are separate documents. Once duplicate material is culled from the working set, the next step is to eliminate documents that clearly have nothing to do with the lawsuit. Irrelevant documents, however, should not be discarded. They should be kept in separate, chronological files in case they become relevant.

The next step in the development of a database is the method used to store and retrieve the documents in the working set. The traditional way is to store hardcopies in notebooks in numerical order and put the notebooks on shelves in the document repository. The latest method of storing and retrieving documents is imaging, or scanning the documents onto disks. The image produced by the computer on a screen or by a printer is an exact reproduction of the original document, including all notations or other marginalia. Imaging eliminates storage problems. Its disadvantage is that it is more expensive than photocopying. Its advantage is decreased storage space and greater efficiency. As technology improves, the cost of imaging should become cheaper.

The final step is to index the documents for later retrieval. Indexing can be done either by computer or manually.[485] The index should contain fields that identify the issues, the individuals, and the events and transactions that are important to the case. Indexing involves objective and subjective coding. The coding sheet used by the coder for objective coding typically contains the following fields of information.[486]

- Document Number. These are the Bates numbers stamped on the first and last page of the document. If the document is one page, only one number is used.
- Date of the document.
- Author.
- Recipient.
- Persons mentioned in the document text.
- Carbon copy recipients.
- Document type (letter, memo, diary, etc.).
- Coder.

The coding sheet may also contain fields that relate to the interpretation of a document and its relevance to the case. This involves subjective coding and may include the following fields:

- Issue(s).
- Priority (routine; hot, i.e., extremely important to the case).
- Privileged. This should identify the type of privilege involved, attorney-client, and work-product. This is useful in responding to an interrogatory asking about documents that have been withheld from production to opposing counsel and the basis for the privilege.
- Summary. This section allows the reviewer to make an abstract or summary of the document. Generally, use of this field is discouraged since the attorney will read the document. Thus, a summary in view of the time and expense to make it is usually not worthwhile.

Caution should be taken not to use too many codes, particularly issue codes. If the database becomes too complicated, it will be difficult to work with and may even fail. Access to the computer should be limited to only those who have been given passwords. Subjective coding should be done by personnel who are knowledgeable about the case and the issues.

Optical Character Recognition (OCR) is another technological feature that can be used for document control. This process can be used with documents that contain a substantial number of pages. Although each page is imaged, OCR reviews only those pages that relate to a certain subject or a particular item. OCR allows the computer to locate the specific information within the document and make it readily available for review. Once the information is coded and stored in a computer database, the system will search, sort, and provide specific information. The system can search large volumes of information in a very short period of time. It can list all documents a particular person authorized or received regarding a certain topic during a particular time frame. This is very helpful in preparing a person for his or her deposition. The computer has a perfect memory. It can access any information stored in the system. If used properly, the computer can be a great tool; if used improperly, it can be a disaster. Thus, certain things should be carefully considered before creating a litigation support system. They include:

- What information will you want from the computer system? The information the computer provides is only as good as the information given it.

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[484] *See supra* note 472 describing the Bates numbering system.

[485] If a manual system is used, issue books can be prepared that contain all documents that pertain to each issue or to a particular witness. Documents pertaining to more than one issue or witness can be cross-referenced in the issue book.

[486] The information is objective because it can be gleaned from the document by the coder without interpretation or analysis.

• How much will the system cost? Is the cost justified in light of what is involved in the case?
• Should the claims consultant manage the documents? If not, is the agency's system compatible with any system that the consultant may be using?

Control and management of the opponent's documents involves the same process used to manage your own documents. However, there are some things that should be kept in mind. If your opponent will be numbering its documents, try to agree on a numbering sequence that does not conflict with your numbering system. If your opponent does not intend to number its documents, request permission to number them when they are reviewed. Numbering the documents is a good way of keeping track of whether all documents are produced. Review the production of the opponent's documents carefully to determine whether any documents are withheld. If you are not permitted to number the documents, make an inventory of what was reviewed. This can be done with a dictating machine. If the agency and the contractor have the same document in their files, do not treat them as duplicates. Both should be put in the database. The Bates number will identify the source of the document.[487] Fields can be added to the database that relate specifically to the opponent's documents, such as the date it was produced, and whether it was part of an original production or identified in an interrogatory answer and then later produced.

The time, effort, and money spent in developing the database is wasted if the information contained in the database cannot be retrieved quickly. It is important to design the system correctly. Redesigning the system or trying to patch it up later with bandaids can be expensive and delay trial preparation.

When the records of the contractor or any adverse party are made available for inspection, they should be copied rather than simply inspected. It is often difficult to determine, in a quick inspection, the significance of a particular document. Documents that may have appeared insignificant earlier may become significant as more information is developed about the case. Technical assistance may be obtained from consultants about the types of documents that should be inspected. This information should be included in the litigation plan. This plan should list each claim, the information needed from the contractor to analyze the claim, the methodology that will be used to analyze the claim, the estimated number of hours that are needed to perform the analysis, the priority given to the task, and whether the documents have been produced. The information can be shown in a spread sheet format as follows:

[487] *See supra* note 472.

Claim	Analysis	Estimate of Hours	Priority	Documents Required	Documents Produced
Home Office Overhead	1. Analyze General Ledger Cost Data	100	High	1. General Ledger	1. Yes
	2. Analyze Home Office Overhead Costs and Make Adjustments for Costs That are Not Time Related or Do Not Correspond to the Claimed Delay Period			2. Contractor's Explanation of Corporate Overhead Allocations in Claimed Overhead Pool	2. No
	3. Prepare a Revised Home Office Overhead Rate Per Calendar Day to be Applied to Allowable Delay Days			3. Inquiries to Contractor about Certain Costs.	3. No

Counsel should try to obtain documents from the opposing party and from third parties by agreement. Counsel should seek advice from the retained consultants in identifying documents that should be sought. The experts will use the right nomenclature in identifying documents, avoiding disputes over what is being requested. Counsel should insist that all documents withheld under a claim of privilege be identified together with the basis for the privilege. If opposing counsel refuses, this information can be obtained by interrogatories. Whether the privilege is valid or not can be tested by a motion to compel production of the document and, if necessary, by an in camera inspection of the document by the court.[488] Counsel for the owner should also arrange, if possible, for the financial experts to review the contractor's cost records. Similar arrangements should be made with subcontractors who have pass-through claims. Once informal discovery is exhausted, formal discovery should begin.

c. Photographic and Video Evidence

Photographs and videos can be highly persuasive evidence in construction claims litigation if the circumstances under which they are created are documented carefully and if care is taken to obtain and provide authenticating evidence when seeking their introduction as evidence.

Comparison among photographs taken during various stages of a construction project, including aerial photos taken on a regular basis, may be useful in demonstrating progress or lack of same on the project. Photos showing equipment breakdowns can also be significant in explaining lack of progress. Videos should be taken when the video will document particular problems. Photos and videos should always be dated.

If a state DOT has reason to suspect possible fraud in the performance of construction work, surveillance videos and photographs taken from concealed locations with telephoto lenses may play an important role in evaluating any confidential allegations of fraud, and in revealing and documenting the fraud if it is in fact occurring, and may prove to be essential evidence at the center of any subsequent criminal prosecutions and contract claims litigation.[489]

When state DOTs or the offices of state AGs prepare claims summaries in preparing to litigate a contract claims case, such summaries should include reference to any available and relevant photos and videos, what they show, and who has custody. Information about the photographs and videos will be needed to authenticate them for purposes of introduction into evidence. Such information, if obtainable, should include who took them, what equipment was used to take them, what they portray, when and under what conditions they were taken, where and from what vantage point they were taken, why they were taken, and the background and qualifications of the people who took them, particularly if they were not taken on a routine basis in the

[488] 8 WIGMORE, EVIDENCE § 2322 (rev. ed. 1961).

[489] One of the authors of the 2011 update to this volume was involved as an attorney in the investigation of suspected fraud involving the intentional driving of short and defective piles for overpass foundations on NYSDOT's $100 million Suffern Interchange project during the early 1990s. That investigation included the collection of extensive photographic and video evidence by investigators from concealed locations, and the comparison of such evidence with construction records and contractor requests for progress payments to identify fraudulent requests for payment. FBI agents and an Assistant U.S. Attorney used video evidence furnished by NYSDOT in questioning one of the defendants in the case, who agreed on the advice of his defense attorney to enter into a plea bargain shortly after they were both confronted with the video evidence and fraudulent payment requests immediately after they denied that any of the construction work had been defective. Both of the authors of the 2011 update of this volume later assisted the Office of the State Attorney General in representation of the State in the multi-year, multi-party, multi-million dollar contract claims litigation that followed the criminal case.

ongoing performance of ordinary construction oversight functions.

If claims litigation is conducted in federal court, photographs, like other types of documents, may be obtained from an adverse party to the lawsuit through a request for production of documents[490] and from nonparties by a subpoena duces tecum.[491] Information concerning the contents of photographs, needed to authenticate them for purposes of admission into evidence, may also be sought through interrogatories or requests for written admissions.[492] Conventional photographic prints have been subject to pretrial discovery for many years. Photographs and videos in electronic form are now also expressly included among electronic documents that are subject to electronic discovery, or "e-discovery," in federal litigation, under the 2006 amendments to FRCP Rules 26(b) and 34. Similar rules may apply at the state level. The topic of e-discovery is discussed further in subsection 6(D)(4), below.

To the extent that information in photographs or videos appears to have potential importance, it may be useful to question witnesses during pretrial depositions regarding the origin and contents of such photos or videos. If the witness being deposed is a potential expert witness, it may be appropriate to inquire what documents and records he or she considered in preparing to testify, and in forming any expert opinion regarding issues in the case; whether such documents and records included photographs and videos (including any specific photographs or videos considered to be potential trial evidence); if so, what significance the expert considered them to have; and if not, why the expert failed to obtain and consider them before forming any expert opinion regarding issues in the case.

In preparing engineering witnesses to testify at trial, it may be useful to show them photographs or videos likely to be offered as evidence, ask what meaning or significance (if any) the engineer attaches to them, and ask what things the engineer sees in them that a person who is not a professional engineer might fail to notice or understand. In addition to possibly eliciting information of which the attorney may previously have been unaware, this may also help the attorney plan which witnesses to use in authenticaticating the photographs and videos as evidence and in explaining their significance to the court.

Attorneys may find it helpful to use photographs and videos, along with other visual aids, during opening statements in litigation to explain and illustrate what the evidence will show. It may be advisable to pre-mark them as exhibits and obtain permission from the court in advance to use them in the opening statement, if opposing counsel refuses to stipulate to their use, in order to avoid any objections that might undercut the effectiveness of the opening statement.

[490] FED. R. CIV. P. 34.

[491] FED. R. CIV. P. 45(a).

[492] FED. R. EVID. 1007.

It is difficult to find any recent reported highway or bridge construction claims cases in which the use of photographic or video evidence was contested successfully, suggesting that state DOTs and the offices of state AGs may have sufficient experience in the collection and use of photographic and video evidence in construction contract claims litigation to use them effectively. There have been some recent decisions in the building construction industry involving such issues, however.

In a 2006 decision by a court in Connecticut, for example, photographs of cracking in concrete, coupled with expert testimony that associated the cracks with a contractor's allowing the concrete to dry too quickly, were among the evidence that led to imposition of damages against the contractor in a construction defect case.[493]

In a comparable 2007 decision by an appellate court in Texas, the court found sufficient evidence in the record to support a jury verdict in favor of a purchaser who had sued a contractor over a construction defect that caused water penetration. The court's decision noted, among other things, that, "As additional evidence of the damage, the Cantus [ed.: one of the parties in the case] introduced photos showing mold growing on sheet rock, doors, ceilings, and trusses. All of these photos were admitted into evidence."[494]

The use of photographic and video evidence is not without some potential problems, however. Counsel must comply in a timely manner to requests by opposing counsel for copies of photographs or videos used in testimony during a deposition in a construction defect case. As shown by a 2006 appellate decision in Mississippi, failure to do so, along with other failures to comply with discovery requests, may result in dismissal of the case with prejudice.[495]

The significance of the photographs or videos must be established by additional evidence connecting them to the issues in the case. As indicated by a 2009 decision by the Court of Appeals of the State of Washington, merely getting photographs of a condition at a construction site into evidence, without obtaining the admission of expert testimony or other testimony establishing a connection between the photographed condition and the conduct of one of the parties or its subcontractors, does not suffice to establish liability. In that case, the trial court had admitted photographs into evidence but had not admitted proffered statements by certain expert witnesses. The appellate court pointed out that "photographs of loose Tyvek on the exterior of the structure, with no expert testimony to explain them, do not estab-

[493] Feldgiose v. A.L. Star Constr. Co., 2006 Conn. Super. LEXIS 2852 (Conn. Superior Ct., Ansonia-Milford Jud. Dist., 2006).

[494] Vanounou v. Cantu, 2007 Tex. App. LEXIS 7168 (Texas Ct. App., 13th Dist., Corpus Christi-Edinburg, 2007).

[495] Beck v. Sapet, 937 So. 2d 945; 2006 Miss. LEXIS 484 (Sup. Ct. of Mississippi, 2006).

lish that any of the subcontractors breached their contracts with respect to Tyvek installation."[496]

To be persuasive as evidence, photographs must portray conditions as they were at or shortly after the time of the alleged conditions or incident at issue in the litigation, rather than at some other time when different conditions prevailed. As an Ohio appellate court noted in 2008, in a case involving a vehicular accident allegedly resulting from roadway conditions adjacent to a construction site, "…although plaintiffs presented Henry with photographs of the site entrances, taken sometime after the accident, that showed the construction site to be muddy and filled with tire ruts, Henry noted the ruts depicted in the photos were not present when he worked at the site. Litton likewise testified to the absence of ruts on December 23, stating the photos showed wet ground, not the dry, frozen conditions he encountered at the site."[497]

Merely photographing defects in construction, especially doing so in a nonsystematic or incomplete manner, will not be considered to excuse performing remedial work without first allowing the contractor allegedly responsible for such defects to inspect them thoroughly before the remedial work is performed. Proceeding with remedial work without first allowing a physical inspection may be considered to constitute spoliation of evidence, a situation in which photographs will not be sufficient to avoid. This is especially true if the complaining party fails to take photographs of all of the allegedly defective work, fails to do so in a systematic or consistent manner, or fails to take photographs of sufficient detail or quality to support the forming of opinions by expert witnesses.

This is the situation that transpired in a New Jersey case decided in 2010.[498] A commercial building owner sued a construction contractor and a glass installer, alleging that the installation of new windows had been defective and that the windows had leaked. The building owner photographed the allegedly defective window installations but did not do so in a complete or systematic manner, and did not offer the contractor a chance to inspect them before proceeding to carry out repairs on its own. The trial court found that the photographs were insufficient to protect the building owner against a finding of spoliation of evidence and precluded the owner's expert witness from testifying. An intermediate appellate court reversed and remanded, finding that the installer had greater knowledge than the building owner of how the windows had been installed, had many opportunities to inspect them, and merely limited the testimony of the owner's expert to matters established by evidence obtained prior to the removal and replacement of the windows. On further appeal, however, while affirming that decision with regard to the installer, the Supreme Court of New Jersey reversed and remanded with regard to the contractor, finding that the spoliation of evidence had caused such prejudice by depriving the contractor of the opportunity to inspect as to require the complete dismissal of all claims against the contractor. The photographs taken by the building owner before and during the performance of the repairs were not sufficient to save him from this determination.

In accordance with Rule 103(a)(1) of the Federal Rules of Evidence (FRE), any objection to photographic or video evidence, or to its interpretation, must be made on a timely basis at trial. It is too late to do so for the first time when a party is pursuing an appeal. This is illustrated by a federal appellate decision from 2005, involving a dispute between two firms, Crossley Construction and NCI Building Systems.[499] During trial, counsel for NCI offered in evidence a videotaped deposition of a former NCI employee who represented NCI in early negotiations with Crossley. Counsel for Crossley did not object to its introduction and in fact used excerpts from that videotaped deposition in presenting its own case. The trial court found the videotaped deposition testimony more persuasive than that of witnesses who appeared and testified in person, and found against Crossley. Appealing to the Sixth Circuit from that decision, counsel for Crossley objected for the first time both to the trial court's use of the videotaped testimony and to the conclusions the trial court reached about the credibility of the videotaped testimony as compared with the testimony of witnesses who appeared in person. Counsel requested that, if the Sixth Circuit did not exclude the videotaped testimony from evidence, it conduct a *de novo* review of the credibility of the videotaped testimony, without granting any deference to the trial court's findings. Citing FRE Rule 103(a)(1), noting that counsel for Crossley had failed to file a timely objection to the videotape and had in fact used excerpts from it, and finding that Crossley's rights were not adversely affected by the trial court's evaluation of the videotaped testimony, the Sixth Circuit precluded Crossley's counsel from raising the objection on appeal.

While parties may on occasion seek to block the disclosure of their own photographs on grounds of privilege as work product created by or for attorneys in preparation for trial, at least one Federal District Court indicated in a 2009 decision that photographs, along with measurements, diagrams, or other factual summaries or reports merely transmitting factual information, are not likely to be treated as privileged by the courts.[500]

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[496] Ballard Residential, LLC v. Pac. Rim Framing Co., 2009 Wash. App. LEXIS 948 (Wash. Ct. App. 2009); subsequent history 2009 Wash. App. LEXIS 1103 (Wash. Ct. App. 2009).

[497] Farley v. Duke Constr., 2008 Ohio 6419; 2008 Ohio App. LEXIS 5363 (Ohio Ct. App., 10th App. Dist., Franklin Co., 2008).

[498] Robertet Flavors, Inc. v. Tri-Form Const., Inc., 203 N.J. 252; 1 A.3d 658; 2010 N.J. LEXIS 747 (Sup. Ct. of N.J., 2010).

[499] Crossley Constr. Corp. v. NCI Bldg. Sys., L.P., 123 Fed. Appx. 687; 2005 U.S. App. LEXIS 2702 (6th Cir. 2005).

[500] Metzler Contr. Co. LLC v. Stephens, 642 F. Supp. 2d 1192; 2009 U.S. Dist. LEXIS 61198 (D. Haw. 2009).

Under FRE Rule 403, while photographs and videotapes made of conditions in the field that are relevant to issues in litigation, or videotapes of witnesses testifying under oath in a pretrial deposition, may well be admitted, videotapes of counsel presenting their own discussions, opinions of, or conclusions about evidence are likely to be rejected by courts as duplicative and cumulative. This is illustrated by a 2005 decision by the U.S. Court of Federal Claims. In that case, which involved a contractor's contractual duty to provide the U.S. Army Corps of Engineers with design services without negligence and whether a contract calling generally for use of a preengineered metal building absolved the contractor of any responsibility for the design of the building, the evidence offered by the contractor's counsel included a 4-minute video on a disc of counsel explaining how another exhibit, a model of a building frame, had been used to address certain engineering issues at trial. Government counsel opposed its introduction on the ground that counsel's arguments did not constitute evidence, that the videotape was slanted toward the contractor's version of the case, and that government counsel had been denied the right to cross-examine. Noting that all of the matters described in the video had previously been addressed by testimony given in person by witnesses who appeared at the trial of the case, the court denied the contractor's motion for admission of the video on the grounds that under FRE Rule 403, even relevant evidence may be excluded on the grounds of needless presentation of cumulative evidence.[501]

4. Electronic Discovery: Federal and State Provisions, E-Discovery Software, and Practice

Pretrial discovery has been a significant part of transportation construction contract claims litigation for many years. Claims litigation, like other litigation, can be won or lost during the discovery phase. The party who can locate, analyze, store, and retrieve communications, documents, and records relevant and material to contested issues the most quickly, fully, and efficiently has a decided edge in being able to organize and present its case clearly and persuasively, and in preparing to defend itself against any evidence adverse to its interests.

Since 2006, pretrial discovery in contract claims litigation, as in other forms of litigation, has been revolutionized by the advent of electronic discovery, or "e-discovery," which has outstripped (though not totally supplanted) traditional discovery of paper documents. This is due to major and accelerating changes in the way that government transportation agencies and construction contractors communicate, generate, and maintain records; to changes in the rules governing litigation; and to changes in the professional practices, skills, and equipment of attorneys engaged in such litigation. To some extent, e-discovery has become a specialized area of legal practice, as attorneys equipped with the necessary tools and skills have, all other things being equal, a strong advantage over adversaries who have failed to acquire them. State DOTs, state AG offices, and private sector law firms cannot have any reasonable expectation of being effective in litigating construction claims cases without equipping themselves with the necessary computer hardware, software, and staff training to handle e-discovery in a timely and efficient manner.

Since developments at the federal level have led the way in this field and have been highly influential, the discussion that follows will focus on federal law. While offering some examples from selected state law, this discussion does not attempt to provide a systematic or thorough survey of state law in this area. Practitioners will have to research such matters further for the jurisdictions they regularly litigate in. In doing so, they may find participation in the Sedona Conference to be helpful.[502]

a. Revolutionary Impact of 2006 Amendments to Federal Rules of Civil Procedure

In certain regards, the fundamental rules of discovery have not changed greatly, and e-discovery may be seen as the proverbial old wine in new bottles. Subject to claims of legal privilege, parties have always had an obligation to instruct their personnel to preserve records of matters involved or foreseeably about to become involved in litigation and to produce relevant and nonprivileged records to opposing counsel on demand under statutes, regulations, and case law governing pretrial discovery in litigation. For almost 300 years now, Anglo-American courts have also recognized that, if a party fails to preserve or produce documentary evidence that is relevant and material to the determination of contested issues in litigation, and if it is that party's fault that such evidence is missing, the court may draw an adverse inference from the missing evidence and presume that it would have been favorable to the other party.[503]

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[501] C. H. Guernsey & Co. v. United States, 65 Fed. Cl. 582; 2005 U.S. Claims LEXIS 125 (U.S. Ct. Fed. Clms. 2005).

[502] The Sedona Conference describes itsef as an organization that

> exists to allow leading jurists, lawyers, experts, academics and others, at the cutting edge of issues in the area of antitrust law, complex litigation, and intellectual property rights, to come together—in conferences and mini-think tanks (Working Groups)—and engage in true dialogue, not debate, all in an effort to move the law forward in a reasoned and just way.

One of its working groups describes its mission as "to develop principles and best practice recommendations for electronic document retention and production in civil litigation." For additional information, see the organization's Web site at http://www.thesedonaconference.org/, last accessed on Jan. 4, 2012.

[503] Armory v. Delamirie (Smith's L. Cas.) 1 Strange 505, 93 Eng. Rep. 664 (K.B. 1722); cited in numerous federal appellate cases, *see, e.g.*, Bigelow v. RKO Radio Pictures, Inc., 327 U.S. 251, 66 S. Ct. 574, 90 L. Ed. 652 (1946), McKee v. Gratz, 260

During the past 20 or 30 years, however, the increasingly widespread availability of computers, software, the Internet, email, and other aspects of electronic communications and information storage and retrieval systems have thoroughly transformed the ways in which state DOTs, consultant engineers, and construction contractors communicate, design projects, and let, award, and administer construction contracts. Where communications used to involve letters, memoranda, and telephone calls, they are now increasingly handled through email and through electronic preparation and transmission of maps, engineering plans, specifications, bids, contracts, construction inspection reports, payment vouchers, and other records typically generated and maintained during the performance and after the completion of construction projects.

While initially slow to recognize or deal with this, federal and state legal systems and courts have definitely caught up. The rules for litigating civil cases in federal civilian courts are set by the FRCP. In 2006, significant amendments updated the FRCP rules to recognize and make express provision for e-discovery. Many states have since adopted comparable revisions to state laws governing civil procedure in state courts. For the past several years, these new rules have been mandatory and binding on parties, attorneys, and courts, including those involved in construction contract litigation. They are compulsory, rather than advisory, and parties and attorneys who fail to comply with them can be severely penalized by the courts.

Key provisions are found in Rules 26, 34, and 37 of the FRCP. Amended extensively in 2006, these now make express provision for the discovery of electronically stored information (ESI), as well as paper communications, documents, and records. Sufficient time has passed since the amendments went into effect for a body of case law interpreting them to have begun emerging.

The assembly, disclosure, and production of ESI as well as paper records in federal civil litigation is governed by FRCP Rule 34, *Producing Documents, Electronically Stored Information, and Tangible Things, or Entering onto Land, for Inspection and Other Purposes*. Broader requirements to preserve, disclose, and produce ESI and paper records in discovery are set forth in FRCP Rule 26, *Duty to Disclose; General Provisions Governing Discovery*, specifically including but not limited to Rule 26(b), *Discovery Scope and Limits*, and Rule 26(b)(2)(B), *Electronically Stored Information*. Penalties and consequences for failure to comply with Rules 34 and 26 are set forth in FRCP Rule 37, *Failure to Make Disclosures or to Cooperate in Discovery; Sanctions*. These amended rules, and the case law interpreting them, represent a marked departure in significant respects from prior law governing paper records.

U.S. 127, 43 S. Ct. 16, 67 L. Ed. 167 (1922), Confederated Tribes v. United States, 248 F.3d 1365 (Fed. Cir. 2001), Kronisch v. United States, 150 F.3d 112 (1998).

b. Discovery of Electronically Stored Information

The basic requirement for discovery of ESI is set forth in FRCP Rule 34.[504] In addition to seeking the production of printed or written records, tangible things, or entry and inspection of land or other property, a party in federal litigation may, under Rule 26(b), request any other party to produce and allow the requesting party to inspect, copy, test, or sample items within the responding party's possession, custody, or control, specifically including "any designated…electronically stored information—including writings, drawings, graphs, charts, photographs, sound recordings, images, and other data or data compilations—stored in any medium from which information can be obtained either directly or, if necessary, after translation by the responding party into a reasonably usable form."[505]

The request must describe each item or category of items to be inspected with reasonable particularity; must specify a reasonable time, place, and manner for production; and "may specify the form or forms in which electronically stored information is to be produced."[506]

The party to whom the request is directed has 30 days after being served to respond in writing, unless a shorter or longer time is stipulated to or ordered by the court.[507] The response must, for each item or category, indicate that inspection will be allowed or set forth an objection, including the reasons for the objection.[508] If an objection is directed to only part of a request, it must specify the part which is objected to, and allow discovery of the rest.[509]

Where the request is for production of ESI, the response may object to the requested form for producing the ESI, and if such an objection is made or if the request failed to specify any particular form, the response must state the form or forms it intends to use.[510] The following requirements all apply to responses to requests for ESI, unless otherwise stipulated by the parties or ordered by the court.[511] The responding party must either produce ESI documents as they are kept in the usual course of business or must organize and label them to correspond to the categories set forth in the request.[512] If the request fails to specify a form in which to produce ESI, the responding party must either produce it in a form in which it is ordinarily maintained or

[504] FRCP Rule 34, Producing Documents, Electronically Stored Information, and Tangible Things, or Entering onto Land, for Inspection and Other Purposes.

[505] FRCP Rule 34(a)(1)(A).

[506] FRCP Rule 34(b)(1)(C).

[507] FRCP Rule 34(b)(2)(A); and see FRCP Rule 29 regarding stipulations.

[508] FRCP Rule 34(b)(2)(B).

[509] FRCP Rule 34(b)(2)(C).

[510] FRCP Rule 34(b)(2)(D).

[511] FRCP Rule 34(b)(2)(E).

[512] FRCP Rule 34(b)(2)(E)(i).

in a reasonably usable form or forms.[513] The responding party need not, however, produce the ESI in more than one form.[514] Nonparties may also be compelled to produce documents and tangible things or to permit inspections under FRCP Rule 45.[515]

As a matter of practice, it is crucial for state counsel, a state DOT, or another party framing or responding to a pretrial discovery request for ESI to determine in advance what computer hardware, what e-discovery software program or programs, and/or what e-discovery external services they will be using to access and analyze the ESI they are requesting another party to produce; to determine in advance what electronic media and file format or formats such hardware and software can access and analyze effectively; and what the consequences of a choice between formats may be, both in terms of feasibility and effectiveness of access and analysis and in terms of financial costs.

As discussed below, there are a variety of competing commercial products in the market for e-discovery software and services, with a considerable variety of tradeoffs in terms of costs, ease of use, and effectiveness. A choice between different e-discovery software or services may result in a difference in the hundreds of thousands of dollars in the costs of conducting e-discovery. While the connection between cost and effectiveness is not always direct or uniform, in many cases it is true that although inexpensive e-discovery software is available, it is not easy or flexible to use and does not deliver very useful results. Some other software programs or services are far more intuitive, easier, and more flexible to use, and produce far more effective results, but are considerably more expensive. Far too often, the choice appears to be made based on a budget-driven evaluation of the initial acquisition costs of the hardware, software, and/or services involved, rather than on a realistic evaluation of its usability and effectiveness and the financial consequences of losing a major contract claims case due to inadequate e-discovery capability.

The differences among different e-discovery software, and the weaknesses of some lower-cost software, may not become fully apparent until counsel attempt to perform privilege reviews of large quantities of electronically stored information, to prepare privilege logs identifying privileged electronic documents and setting forth the legal reasons for withholding them, and to prepare redacted copies of electronic documents where privileged portions may be withheld and the remaining portions of the documents may be produced. Glaring deficiencies in some software may not become evident until counsel is in the midst of such efforts, but by then it may be too late to switch to (and learn how to use) more effective software in time to comply with court-imposed discovery deadlines in the litigation.

As a practical matter, such issues may be of particular concern because of differences in the way clients deal with paper and electronic records. A written memorandum to or from an attorney, with a header marked "privileged and confidential attorney-client communication," may, if transmitted in printed rather than electronic form, receive sufficiently careful handling to sustain the attorney–client privilege. Such a memorandum emailed as an attachment, however, or (worse) as an email message to or from counsel regarding privileged matters, may without much thought be electronically forwarded to persons outside the scope of the privilege, thus destroying the attorney–client privilege for highly sensitive communications and forcing the subsequent disclosure of such communications during e-discovery.

It should also be noted that people who tend to be professional, cautious, and careful in the preparation of written documents, such as letters or memoranda, may be much more casual, informal, and careless in composing and sending electronic messages. Email messages containing candid acknowledgments of problems, frank discussions of conflicts between personnel, language dominated by slang or profanity, or communications of a personal nature with individuals other than a spouse, can prove to be particularly embarrassing in e-discovery, but there is no rule protecting embarrassing as opposed to legally privileged electronic information from mandatory disclosure during e-discovery.

c. Timing, Scope, and Form of Electronic Discovery: Issues of Undue Burden, Cost, and Privilege; Protective Orders

Like other forms of pretrial discovery, the discovery of ESI in federal litigation is, in addition to FRCP Rule 34, subject to the general provisions of FRCP Rule 26. This rule has evolved and grown over time and is now highly complex and many pages long. It would go beyond the scope of the current volume to discuss all the provisions of Rule 26, and the current discussion must of necessity be a selective one focusing on provisions likely to affect discovery of ESI in claims litigation.

FRCP Rule 26 requires the attorneys of record for the parties to convene a pretrial discovery conference as soon as practical after commencement of the case and no less than 21 days before a scheduling conference is held or a scheduling order is due under FRCP Rule 16.[516] They must make certain mandatory disclosures (discussed below), attempt in good faith to agree on a proposed discovery plan, and submit it to the court in writing within 14 days after the conference.[517] The discovery plan must state the parties' views and proposals on a variety of discovery issues, including whether there should be any changes in requirements for mandatory disclosures; the subjects on which discovery may

[513] FRCP Rule 34(b)(2)(E)(ii).

[514] FRCP Rule 34(b)(2)(E)(iii).

[515] FRCP Rule 34(c).

[516] FRCP Rule 26(f)(1).

[517] FRCP Rule 26(f)(2).

be needed, when it should be completed, and whether it should be conducted in phases or focused on particular issues; any issues about claims of privilege, including whether the parties are willing to agree to a "claw-back" arrangement providing procedures for asserting claims of privilege after documents are produced; and whether the parties consider it necessary to ask the court for issuance of a protective order on such issues.[518] The discovery plan is expressly required to address "any issues about disclosure or discovery of electronically stored information, including the form or forms in which it should be produced."[519]

Within 14 days after the pretrial discovery conference, unless otherwise stipulated or ordered, the parties must make certain mandatory disclosures to each other, even in the absence of specific discovery requests or demands. Such mandatory disclosures include the names of individuals likely to have discoverable information that the parties may use to support their claims or defenses, computations of each category of damages claimed by the parties, and any insurance policies that might cover any liabilities in the case. They also include providing either copies, or descriptions by category and location, of the evidence that the parties have and may use to support their claims or defenses, specifically including but not limited to ESI.[520]

Mandatory disclosures must be in writing, signed, and served.[521] Pretrial discovery must be completed at least 30 days before trial.[522] Parties that have made mandatory disclosures or responded to discovery requests are under an ongoing responsibility to supplement their prior disclosures if they learn that such disclosures have been materially inaccurate or incomplete.[523] By signing mandatory disclosures, discovery requests, and responses to discovery requests, the attorneys of record for the parties certify that, to the best of their knowledge, information, and belief formed after reasonable inquiry, their discovery requests are legitimate under the rules and not intended for purposes of harassment, delay, or increasing the costs of opposing parties; their requests are neither unreasonable nor unduly burdensome or expensive to comply with; and their disclosures and responses are complete and correct as of the time when made.[524]

The scope of discovery in federal litigation is generally quite broad, extending to "any nonprivileged matter that is relevant to any party's claim or defense." For cause, the court may order discovery not only of admissible evidence, but also of any relevant information "reasonably calculated to lead to the discovery of admissible evidence."[525] The court may, however, limit the frequency or extent of discovery if the discovery sought is unreasonably cumulative or duplicative; can be obtained from another source with greater convenience and less burden and cost; or the burden or cost of discovery outweighs its likely benefit considering certain enumerated factors.[526]

Rule 26 includes provisions placing limitations on the discovery of ESI. In particular, a party "need not provide discovery of electronically stored information from sources that the party identifies as not reasonably accessible because of undue burden or cost." Upon a motion by the requesting party to compel discovery, or by the responding party for a protective order, the responding party bears the burden of proving that such sources are not reasonably accessible based on undue burden or cost. Even if such a showing is made, however, the court may order discovery to be made, although the court may specify conditions for such discovery.[527]

A party responding to a discovery request, including a request for ESI, may withhold otherwise discoverable information from disclosure based on a claim of privilege or protection as trial-preparation material. If and when doing so, the party claiming privilege must expressly assert the claim of privilege; describe the nature of the documents, communications, or tangible things not produced or disclosed; and do so in a manner that, without revealing privileged information, will allow the other parties to assess the claim of privilege.[528] If a responding party notifies a requesting party that ESI or other records already produced are privileged, the requesting party must promptly return, sequester, or destroy the privileged material and any copies it has, may not use or disclose the information until the claim of privilege is resolved, and may promptly present the information to the court under seal for a determination of the claim of privilege.[529]

A responding party that has been unable to resolve a discovery dispute with a requesting party may move for a protective order in the court where the action is pending. The moving party must certify that the movant has attempted in good faith to confer with the other parties and resolve the dispute without court action. For good cause shown, the court may issue an order protecting a party or person from "annoyance, embarrassment, oppression, or undue burden or expense." The court may, in such an order, forbid the disclosure or discovery, impose terms on the disclosure or discovery; prescribe a discovery method other than the one sought, forbid inquiry into certain matters or limit the scope of disclosure or discovery to certain matters, protect trade secrets or comparable commercial information, or require that the parties simultaneously file specified documents

[518] FRCP Rule 26(f)(3).

[519] FRCP Rule 26(f)(3)(C).

[520] FRCP Rule 26(a)(1); *see* Rule 26(a)(1)(A)(ii) in particular with regard to electronically stored information.

[521] FRCP Rule 26(a)(4).

[522] FRCP Rule 26(a)(3)(B).

[523] FRCP Rule 26(e)(1).

[524] FRCP Rule 26(g).

[525] FRCP Rule 26(b)(1).

[526] FRCP Rule 26(b)(2)(C).

[527] FRCP Rule 26(b)(2)(B).

[528] FRCP Rule 26(b)(5)(A).

[529] FRCP Rule 26(b)(5)(B).

or information in sealed envelopes, to be opened as the court directs.[530] The party seeking the protective order may also request attorneys' fees and other expenses.[531]

d. Sanctions for Failure to Disclose or Cooperate[532]

State DOTs maintain a wide variety of ESI that may be the subject of pretrial discovery demands in highway or bridge construction contract information. Such records may include, but not be limited to, CADD or other electronic records concerning the engineering design of the project; electronically stored engineers' estimates of project costs; electronic records related to the letting and award of the contract; electronic records concerning construction administration, including subcontractor approvals, DBE utilization, engineers' diaries, inspectors' daily reports, the review and approval of progress payments, and orders on contract (change orders); fiscal records on the funding of the project; accounting records concerning payments made to contractors and funds remaining available in state accounts for the project; and general correspondence.

State DOT information technology (IT) systems have typically not been designed, however, with implementation of litigation hold (records preservation) orders and retrieval and production of large quantities of ESI in mind. Candor also requires acknowledging that, due to fiscal constraints, the IT hardware, operating systems, and software of state DOTs are in many cases badly outdated. Many components of state DOT IT systems have been developed for different purposes by different units at different times, are not fully integrated, and are not readily accessible to people other than IT staff or personnel of the units that developed them.

One of the most challenging aspects of electronic discovery for state DOTs involved in claims litigation may be the retrieval, assembly, copying, and production of email communications sent and received during the relevant time periods by the various engineers, managers, and staff members who have been involved with the design, estimating, funding, letting, award, construction, payment processing, and miscellaneous administration of the project. While email systems were originally envisioned as a method of quickly transmitting brief, temporary messages, they have evolved in actual use into systems that have largely, if not completely, replaced communications that used to be handled by paper memoranda and correspondence. Most email systems were never designed, however, to retain, store, manage, and retrieve large volumes of communications on a long-term basis. Some email systems limit the duration of time for which emails may be kept or the quantity of emails that individual users may keep. Few email systems have been designed with built-in capabilities to retrieve simultaneously the email communications of multiple users, sort and screen such emails for communications on specific projects or topics, and download electronic copies of such communications onto electronic media that can readily be provided to the Assistant State AGs representing state DOTs in construction claims litigation or to opposing counsel representing contractors suing for damages.

In many state DOTs, IT personnel are ignorant of the legal requirements for pretrial discovery of ESI in construction claims litigation. Within the internal chains of command of state DOTs, IT personnel typically report to fiscal or business managers, rather than to attorneys or engineers, and they are often less than fully responsive to requests for assistance with responding to pretrial discovery demands for ESI, especially once they become aware of the scope, magnitude, and volume of the discovery demands the agency has been confronted with.

For these reasons, e-discovery, the pretrial discovery of ESI, can be a considerable headache for Assistant State AGs and state DOT attorneys or personnel confronted with pretrial discovery demands. Simply ignoring or disregarding such demands can be a serious mistake, however.

In federal litigation, failure to make disclosures or to cooperate in discovery is subject to sanctions under FRCP Rule 37. This rule includes an important provision relating to ESI. FRCP Rule 37(e) provides expressly that, "Absent exceptional circumstances, a court may not impose sanctions under these rules on a party for failing to provide electronically stored information lost as a result of the routine, good-faith operation of an electronic information system."

Should circumstances indicate, however, that failure to produce ESI has resulted from a cause other than a loss occurring in the routine, good-faith operation of an electronic information system, the penalties under Rule 37 can be substantial. If a responding party fails to make disclosure, the party will be precluded from using the nondisclosed material as evidence in support of any motions or during the trial.[533] The requesting party may file a motion for an order to compel disclosure or discovery and seek to recover attorneys' fees and other costs for having to do so.[534] If the responding party fails to comply with a court order requiring disclosure, the court has authority and discretion to issue a further order, which may include the following: directing that the matters involved in the order be taken as established for purposes of the litigation; prohibiting the disobedient party from supporting or opposing designated claims or defenses, or from introducing designated matters in evidence; striking pleadings in whole or in part; staying further proceedings until the order is obeyed; dismissing the action or proceeding in whole or in part; rendering a default judgment against the disobedient

[530] FRCP Rule 26(c)(1).

[531] FRCP Rule 26(c)(3), making FRCP Rule 37(a)(5) applicable to the award of such expenses.

[532] FRCP Rule 37, Failure to Make Disclosures or to Cooperate in Discovery; Sanctions.

[533] FRCP Rule 37(c)(1).

[534] FRCP Rule 37(a).

party; or treating the failure to comply as a contempt of court.[535] The court may also order the disobedient party to pay the requesting party's attorneys' fees and expenses.[536]

Federal district and circuit courts have taken somewhat varying approaches to the application of these provisions but have made it clear that significant sanctions will be imposed in appropriate cases.

In one noted case with a complex procedural history, the U.S. District Court for the Southern District of New York and the U.S. Court of Appeals for the Second Circuit indicated that parties are under a duty to issue litigation holds preventing the destruction or loss of evidence including ESI; that a plaintiff's failure to issue such an order constitutes gross negligence per se and that late issuance constitutes negligence per se; that gross negligence is sanctionable through permissive adverse inference, and mere negligence is also sanctionable through monetary sanctions; and that an offending party may be ordered by a court to search through its backup tapes at its own cost.[537] The ruling in that case makes it clear that taking affirmative preventive measures is highly advisable to avoid risk of sanctions under Rule 37.

Taking a somewhat different approach, in another case with a complex procedural history, the U.S. District Court for the Southern District of Mississippi and the U.S. Court of Appeals for the Fifth Circuit indicated that they consider the intentional destruction of ESI to give rise to permissive adverse inferences and the imposition of attorneys' fees and costs.[538]

e. Proposals to Amend the FRCP, and Local Supplemental Rules

The 2006 FRCP amendments on e-discovery have been criticized for, among other things, establishing a current protocol for the preservation of electronic records, which is allegedly inconsistent from jurisdiction to jurisdiction, and being imprecise in terms of triggering events, scope, duration, and manner of preservation; radical in its approach; unjustified by evidence of need; unbalanced as between plaintiffs and defendants; expensive to comply with; and a source of ancillary litigation.[539] Critics point to cases such as a 2011 decision by a federal magistrate judge to deny a motion by an accounting firm for a protective order to reduce the scope and/or shift some of the cost of preserving 2,500 individual computer hard drives at a cost of more than $1.5 million.[540] This has led some groups, including the Judicial Conference Advisory Committee on Rules, Practice and Procedure, to consider proposing an amendment to the FRCP e-discovery rules to address perceived problems with the existing records preservation requirements.[541]

Some individual federal courts have issued their own local rules to address e-discovery issues to address proportionality and reasonableness standards with regard to preservation, identification, and production of ESI under the 2006 FRCP amendments.[542]

f. The Roles and Responsibilities of State DOT Counsel, IT Staff, and State Attorneys General

State DOT counsel and IT staff members, and more broadly state DOT officials responsible for the creation, retention, and disposition of agency records, have three broad areas of responsibility for which they and the state DOTs they work for can be held legally accountable.

They have a baseline responsibility to develop, adopt, and implement legally defensible document retention and disposition policies that make express and specific written provision for the generation, length of retention, and disposition of state DOT written and electronic records in the normal course of business. Unless they have such policies in place, any discarding or destruction of written or electronic records relating to construction projects, even if done in the normal course of business prior to the commencement of any litigation, may later be considered by a court to have been intentional destruction of records to prevent their discovery, leading to the drawing of adverse inferences and the imposition of significant financial or other penalties during subsequent contract claims litigation.

Such document retention and disposition policies must include express, specific, and detailed provisions

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[535] FRCP Rule 37(b)(2).

[536] FRCP Rule 37(b)(2)(C), (c)(1)(A), and (d)(3).

[537] Pension Comm. of the Univ. of Montreal Pension Plan v. Banc of Am. Sec. LLC et al., 2009 U.S. Dist. LEXIS 82301 (S.D.N.Y. 2009), subsequent proceedings 685 F. Supp. 456 (S.D.N.Y. 2010), amended by 2010 U.S. Dist. LEXIS 4546 (S.D.N.Y. 2010), partial summary judgment denied, 750 F. Supp. 2d 450 (S.D.N.Y. 2010), motions re expert testimony, 691 F. Supp. 2d 448 (S.D.N.Y. 2010); prior proceedings in same case, 592 F. Supp 2d 606 (S.D.N.Y. 2009), on motions for reconsideration, 617 F. Supp. 2d 216 (S.D.N.Y. 2009), vacated and remanded, 568 F.3d 374 (2d Cir. 2009), summary judgment denied, 652 F. Supp. 2d 495 (S.D.N.Y. 2009).

[538] Aiken v. Rimkus Consulting Group, Inc., 2007 U.S. Dist. LEXIS 2327 (S.D. Miss. 2007), 2007 U.S. Dist. LEXIS 96185 (S.D. Miss. 2007), 2007 U.S. Dist. LEXIS 85489 (S.D. Miss. 2007), 333 Fed. Appx. 806; 2009 U.S. App. LEXIS 11243 (5th Cir. 2009).

[539] Robert Owen, *Reset to Neutral: Rethinking EDD Preservation Protocol*, LAW TECHNOLOGY NEWS, Dec. 1, 2011.

[540] Pippins et al. v. KPMG, No. 1:11-CV-0037, 2011 U.S. LEXIS 116427 (2011), cited in Mark Michels, *More on Pippins Decision—Preservation Proportionality*, Electronic Datas Discovery Update, Nov. 14, 2011; available at http://www.eddupdate.com/2011/11/more-on-judge-cotts-pippins-decisionpreservation-proportionality.html.

[541] Mark Michels, *More on Pippins Decision—Preservation Proportionality*, Electronic Datas Discovery Update, Nov. 14, 2011.

[542] *See, e.g.*, the Default Standard for Discovery, Including Discovery of Electronically Stored Information (ESI), issued by the U.S. District Court for the District of Delaware on Dec. 8, 2011; *and see* discussion in Mark Michels, *Delaware's Default E-Discovery Developments*, LAW TECHNOLOGY NEWS, Dec. 20, 2011.

governing the retention and disposition of email in the normal course of business. The term "electronically stored information," as used by the FRCP and by courts interpreting pretrial discovery rules, very clearly includes email communications, the scheduling of meetings via electronic calendars, and the like, just as much as engineering plans and bidding documents in electronic form or business records in the form of spreadsheet or word processing data files. Being unable to retrieve or produce emails relevant to a construction project during contract claims litigation, and having no standard records retention and disposition policy to document how long emails are retained and how soon they are disposed of in the normal course of business, would place a state DOT and its officials at serious risk of incurring significant penalties for violating discovery rules in contract claims litigation.

Such document retention and disposition policies must take into consideration any planned changes to the agency's IT infrastructure, including server upgrades, changes in major applications software, and the like. In particular, even if a new IT system is to be implemented, the agency must retain the ability to comply with any pretrial discovery orders requiring the location, assembly and production of records generated and maintained by the old system being replaced.

Any policy calling for the routine disposition or destruction of business records, and particular any policy establishing a short timeframe for the preservation of such records prior to routine disposition, must have an express, clearly stated, written business purpose that will be defensible in court if challenged. In the context of pretrial discovery, assertions by state DOT personnel that "We didn't have enough storage capacity to retain any emails beyond 30 days," or "We didn't have enough money to buy more than a few backup tapes, so we regularly erased and reused them," tend to be viewed in the same category as "The dog ate my homework."

State DOT counsel, IT staff, and officials responsible for agency records also have a responsibility for developing, adopting, and implementing legally defensible procedures for issuing written orders to key personnel once they receive a notice of claim or notice that construction contract litigation has commenced through the filing of a claim or once they even have reasonable grounds to expect that such litigation may occur. At minimum, such a litigation hold procedure must provide for the immediate issuance, transmittal, and confirmed delivery of a written hold order on receipt of a notice of claim, notification of the commencement of litigation, or recognition that circumstances make the occurrence of future construction claims litigation likely. The written hold order must identify (and be delivered to) key officials, agency personnel, and consultants involved in the project or having custody of categories of records concerning the project and related contracts. It must expressly direct them immediately to take affirmative steps to preserve all paper records and ESI concerning the project and any related contracts, and to protect such records against either accidental or intentional disposition or destruction. It must direct IT managers and staff, other agency records custodians, and consultants involved in the project immediately to cease the routine deletion in the normal course of business of any emails or other paper records or ESI created, sent, or received by such key officials, personnel, and consultants. It must also direct IT managers and staff immediately to preserve, and not to re-use, re-record, or otherwise dispose of or destroy any and all email or other backup tapes that could be used to retrieve such information in the event of accidental or intentional disposition by individual employees.

State DOT counsel, IT staff, and officials responsible for agency records have a further responsibility to put such litigation hold procedures into immediate effect as soon as a claims case is reasonably anticipated or a notice of claim or perfected claim is received and to cooperate actively with attorneys and investigators from their office or insurance claims counsel in the assembly and transmission of paper and electronic records in connection with pretrial discovery.

State counsel involved in the defense of contract claims litigation have a related but different set of responsibilities. They are responsible for providing general legal advice and guidance to agency lawyers and managers to encourage and to support the development, adoption, and implementation of appropriate, legally defensible records preservation and disposition policies and litigation hold procedures. It must be emphasized, however, that actual compliance with the applicable legal requirements for the preservation, assembly, and production of records in claims litigation remains the obligation of state DOT personnel and that they will not be able to avoid the imposition of sanctions by attempting to shift blame to state counsel if they ignore or intentionally disobey such legal requirements.

g. Specialized Software for E-Discovery

The need to assembly large quantities of ESI in pretrial discovery, search through such ESI to locate relevant records, identify and redact any records subject to privilege, and the like has given rise to the development of a number of competing private sector e-discovery software programs and services for lawyers. Such programs vary considerably in cost, capability, and performance. Without making or implying any commercial endorsement, such programs include, for example, Clearwell, Kroll Ontrack (Verve SaaS), D4 eDiscovery (Relativity), Concordance, ZyLAB, eDiscovery Tools, Digital Reef, Iron Mountain (NearPoint), CaseCentral, Discovery Assistant, FTI Technology (Acuity and Ringtail), Breeze Legal Solutions (Breeze eDiscovery Suite), Guidance Software (EnCase eDiscovery), Trial Solutions (OnDemand), Blackstone Discovery, Cataphora, Autonomy (Protect), Access Data (Access Data eDiscovery, Early Case Assessment, Summation, and Discovery Cracker), Equivalent DATA (Needle Finder), Commvault (Simpana), and Recommind (End-to-End

eDiscovery). It would not be appropriate for this volume to offer any opinion on the individual merits of these particular programs or any others, and the software field appears to be subject to rapid ongoing developments and changes. Any state counsel or state DOT seeking to acquire such software should choose very carefully and consider usability, power, and flexibility as well as cost, because the phrases "you get what you pay for" and "caveat emptor" definitely apply to such products. The least expensive products should not be expected to be as easy to use, as functional, or as effective as more expensive products, and the differences among such software may have a significant impact on which party is likely to prevail in litigation.

h. Development of E-Discovery as a Specialized Area of Litigation Practice

As in other areas of litigation practice, e-discovery requires not only investment in computer hardware, computer software, and related services, but also the use of trained and experienced lawyers to assemble, search through, and evaluate ESI as potential evidence. While lawyers may speak slightingly of "document review" as a function, construction cases can be won and lost during e-discovery and document review. It is thus not surprising that e-discovery is gradually evolving into a specialized area of litigation practice, one with which even many experienced litigators are not fully familiar. It is also not surprising that large private sector law firms representing clients with deep pockets may be able to afford more expensive e-discovery hardware, software, and services than are state counsel and State DOTs able to afford, and may thus have an advantage when it comes to e-discovery. This is all the more reason why government officials involved in the defense of construction claims litigation should devote focused attention to e-discovery in the pretrial phases of litigating such cases.

5. Formal Discovery

Aside from depositions, discussed later, the principal discovery methods are interrogatories (written questions to your opponent) and requests for production of documents. Also, requests for admission may be used to narrow issues, eliminate having to offer evidence to prove certain facts, authenticate documents, and establish a foundation for dispositive motions.

a. Interrogatories

Interrogatories should be carefully drafted. Routine use of form or boilerplate interrogatories should be discouraged. Form interrogatories should be used mainly as a guide in organizing and drafting interrogatories that are tailored to the case. The interrogatories or questions should be simple, easily understood, and in plain English. Technical terms used in the questions should be defined in the definitional section of the preface or introduction to the interrogatories. Compound questions and questions with qualifying subordinate clauses should be avoided. Simple, declaratory sentences should be used. This avoids objections and makes the use of the interrogatories at trial more effective. Each question should be followed by an appropriate space for the answer.

Using numerous subparts for the answers can be confusing. The better practice is to have individual questions and individual spaces for each answer.

The interrogatory set should contain a preface. The preface should provide definitions and instructions that are to be used in answering the questions. Careful preparation of the preface helps reduce objections and may be useful at trial in excluding documents that were not identified in the answers. Thus, a broad, all encompassing definition of the terms “documents” and “identify” will help eliminate an argument about whether an interrogatory called for identification of a particular document or a particular person.[543]

Interrogatories can be used to obtain information about the allegations in a complaint. Each allegation in the complaint can be broken down into a series of questions asking about the facts upon which the allegation is based, the events relating to the allegation, the identity of persons who have knowledge of those facts, the identity of documents containing information about those facts, and the identity of persons who have custody of those documents.[544]

Interrogatories can be used to explore a party’s opinions or contentions that relate to facts or the application of law to fact.[545] Contention interrogatories can be written in different ways. These include: (1) asking the opposing party to state all facts upon which it bases some contention; (2) asking the opposing party to explain how the law applies to the facts; or (3) even asking the opposing party to state the legal basis for its contentions.[546] A party, however, may be able to defer answering contention interrogatories if the party can show that such interrogatories are more properly answered at or near the end of the pretrial phase of the litigation.[547] Thus, under some liberal discovery rules, an opponent may be compelled to disclose the legal as well as factual basis for its claims.[548]

Interrogatories can be used to require the opposing party to identify expert witnesses whom it intends to call at trial and the subject matter on which the expert

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[543] R.M. Gelb, *Standard Paragraphs in Interrogatories*, 28 PRAC. LAW. No. 4, at 51 (1982). This article contains suggestions on how to draft interrogatories, regardless of the subject matter of the litigation. It also offers examples of introductory language and definitional sections that can be used in drafting interrogatories.

[544] FED. R. CIV. P. 26(b)(1).

[545] FED. R. CIV. P. 33 advisory committee note.

[546] McCormick-Morgan, Inc. v. Teledyne Indus., 134 F.R.D. 275, 286, *rev’d in part on other grounds*, 765 F. Supp. 611 (N.D. Cal. 1991).

[547] *Id*.

[548] FED. R. CIV. P. 33(b) advisory committee note; McCaugherty v. Sifferman, 132 F.R.D. 234, 249 (N.D. Cal. 1990).

is expected to testify.[549] This information, provided in the answer to the expert witness interrogatory, can be explored in detail when the expert is deposed.

The basic function of interrogatories is to provide facts, identify persons who have knowledge concerning those facts, and identify documents containing information about those facts. They can be used for specific purposes, such as inquiring about whether certain documents have been lost or destroyed and how damages were calculated. But beyond these uses, the effectiveness of interrogatories is limited. This is so for one basic reason: lawyers write the answers to interrogatories, not witnesses. Keeping this limitation in mind, the number of interrogatories that a party can serve is limited by the federal rules and may be similarly limited by state or local court rules as well.[550] Ordinarily, the limitation on the number of interrogatories that is permitted by rule cannot be avoided through the use of numerous subparts.[551]

When interrogatories are received, they should be promptly reviewed to determine if any are objectionable. In most jurisdictions, failure to serve objections within a specified time period waives the objection.[552] In addition to specific objections to specific interrogatories, counsel should consider making general objections, as appropriate. The following are some examples of general objections.

- Defendant objects to these Discovery Requests to the extent that they may be construed as calling for information or documents subject to a claim of privilege or otherwise immune from discovery, including, without limitation, information protected by the attorney-client or work-product doctrine.
- Defendant objects to these Discovery Requests to the extent that they seek facts, documents, and/or information already known to plaintiff.
- Defendant objects to providing confidential or proprietary information or producing documents that contain such information until a properly framed protection order is entered.
- Defendant objects to the "Definitions and Instructions" to the extent that they call for information from individuals or entities over whom the defendant has no control. Defendant further objects to the discovery requests as oppressive, unduly burdensome, and not reasonably calculated to the discovery of admissible evidence.

A common practice for answering questions that are marginally objectionable is to couple the answer with an objection. This does two things: First, it preserves the objection for trial. If the objection is sustained, the answer cannot be used in the trial.[553] Second, it avoids raising the ire of the court in having to rule before trial on an objection that is marginal.

FRCP 33(d) allows a party to produce its business records in response to an interrogatory when the answer to the interrogatory may be found in the records and "the burden of deriving or ascertaining the answer is substantially the same for the party serving the interrogatory as for the party served." To avoid Rule 33(d) and obtain complete answers, the party serving the interrogatory must show that the burden of deriving the information from the records is heavier on it than on the other party.[554]

b. Request for Production of Documents

When documents cannot be obtained on a voluntary basis, they may be obtained from a party to the lawsuit through a request for production of documents,[555] and from nonparties by a subpoena duces tecum.[556] In requesting documents, a party should try to specify particular categories of documents, rather than a broad request for all documents. Usually, this type of request will be met with a response that documents not privileged will be available for inspection and copying on a certain date and at a certain place during normal business hours.

The request should specify that the documents are to be produced in their original files in the manner in which they are kept. The request should require identification of all documents that are not produced. The request can be accompanied by an interrogatory requiring that for each document not produced, the party must identify: (1) the type of document withheld; (2) the

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[549] FED. R. CIV. P. 33(c); *see also* FED. R. CIV. P. 26(b)(4)(A).

[550] FED. R. CIV. P. 33(a) (limiting number of interrogatories to 25); Clark v. Burlington Northern R.R., 112 F.R.D. 117, 119 (N.D. Miss. 1986) (rule is designed to eliminate the previously common practice of serving sets of interrogatories consisting of hundreds of unrelated and mostly irrelevant boiler plate or form interrogatories).

[551] Some local rules specify that "subparts" are to be counted. *See, e.g.,* Armstrong v. Snyder, 103 F.R.D. 96, 103 (E.D. Wis. 1984). *But see* Clark, *id*. at 118 (court considered subparts to be so integrally related as to make up single question); Myers v. U.S. Paint Co., 116 F.R.D. 165 (D. Mass. 1987) (court declined to mechanically count each subparagraph as a separate interrogatory). Whether the subparts count as individual interrogatories will generally depend on whether the subparts bear any relationship to the primary question or to each other. Myers, 116 F.R.D. at 165. Also, local rules may provide for counsel to stipulate to a greater number of allowable interrogatories. Armstrong, 103 F.R.D., at 104 (citing E.D. Wis. L.R. 7.03).

[552] FED. R. CIV. P. 33(b)(4).

[553] Interrogatories may be used as evidence at trial. FED. R. CIV. P. 33(c). They can be read to the jury or read by the judge in a bench trial.

[554] P.R. Aqueduct & Sewer Auth. v. Clow Corp., 108 F.R.D. 304, 307 (D.P.R. 1985) (citing former FED. R. CIV. P. 33(c)); *see also* Daiflon, Inc. v. Allied Chemical Corp., 534 F.2d 221 (10th Cir. 1976).

[555] FED. R. CIV. P. 34.

[556] FED. R. CIV. P. 45(a).

date, author, and addressee of the document; (3) the general subject matter of the document; (4) the identity of any persons copied;[557] and (5) the type of privilege asserted. The privilege can be tested by a motion to compel production of the document.

Information about what to ask for can be obtained from the consultants. In addition, the litigation plan should list the documents that should be obtained. The plan can be updated as documents are obtained, allowing counsel to keep a running record of what has been produced and what still has to be obtained.

c. Requests for Admissions

Requests for admission require an opponent to admit or deny a particular fact or contention.[558] Like interrogatories, requests for admission should be simple, straightforward, and clear. Each request should deal with a single fact or contention and be worded so that the response must either admit or deny the fact or contention.[559] Requests for admission can be used to establish a foundation for a dispositive motion[560] or a partial summary judgment.[561] Requests for admission can be used to authenticate documents attached to the request and to establish documents as business records. The contents of writings and photographs may also be proved by written admissions.[562]

Under the FRCP, requests for admission can be used as a discovery device concerning the opposing party's theories. Requests for admission concerning contentions that relate to fact or the application of law to fact are permitted.[563] Requests that are denied should be followed up with interrogatories asking for the basis of the denial.[564]

d. Depositions

Depositions are important in case preparation and trial strategy. Counsel can learn from the witness (lay or expert) what the witness's testimony will be at trial. If the witness changes the testimony at trial from what was said in the deposition, the inconsistent statements can be used to impeach the witness. Depositions are also an opportunity to try and elicit admissions from the opposing party or its managing agents, which can be used at trial as substantive evidence. Preparing for and defending the deposition are equally important. Inadequate witness preparation or failure to protect the witness from unfair or abusive questioning can have serious consequences. Depositions, like most things, have two sides: one side is taking the deposition, the other is defending it.

i. Taking the Deposition.—Depositions can be expensive. The party taking the deposition (the interrogator) usually pays an hourly attendance fee for the court reporter, and if the deposition is ordered, pays in addition a set amount per page for the original and for a copy.[565] Any party may order the deposition or a copy.[566] If an expert is being deposed, the party taking the deposition customarily pays for the expert's time at the deposition and the time spent that was reasonably necessary in preparing for the deposition. Travel expenses may be involved if the expert has to travel to the place where the deposition is taken.[567] Because depositions can be expensive, the first considerations should be: "Why am I taking this deposition?" and "What do I hope to accomplish?" The usual answer is knowledge about what the witness will say at trial and the ability to pin down the witness to a particular story, so that if the testimony at trial varies from that story, the deposition can be used to impeach the witness. But depositions can also be used to learn about potential witnesses, about documents that have not been produced, and about events that may bear on liability or damages. Depositions may be used to perpetuate testimony for use at trial for a witness who will not be able to testify in person. Depositions, under rules similar to FRCP 30(b)(6), also allow a party to obtain information from a representative of an organization concerning particular matters.[568] Depo-

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[557] Disseminating the document to someone outside the scope of the privilege may waive the privilege. Ulibarri v. Superior Court, 184 Ariz. 382, 909 P.2d 449, 452 (1995).

[558] FED. R. CIV. P. 36.

[559] *Id.* A party may recover its costs in proving a fact or contention that was denied. FED. R. CIV. P. 37(c)(2).

[560] For example, a request for admission could be used to establish as a fact that the contractor failed to provide written notice of its intention to file a claim before proceeding with what it claims was extra work. That failure can then be the basis for dismissal of the claim. A.H.A. Gen. Constr., Inc. v. N.Y. City Housing Auth., 92 N.Y.2d 20, 677 N.Y.S.2d 9, 699 N.E.2d 368 (1998); Absher Constr. Co. v. Kent Sch. Dist., 77 Wash. App. 137, 890 P.2d 1071 (1995) (summary judgment granted dismissing claim).

[561] Kiewit-Grice v. Wash. State Dep't of Transp., Thurston County Superior Court No. 89-2-02756-6 (1989) (partial summary judgment granted limiting damages claimed in the lawsuit to the amount reserved in the final contract estimate, even after contractor denied in its response to a request for admission that its claim was so limited).

[562] FED. R. EVID. 1007.

[563] FED. R. CIV. P. 36(a).

[564] *Id*. At one time, a common practice was to combine requests for admission with interrogatories. The interrogatory following each request asked why the request was denied. Some jurisdictions prohibit combining requests for admission and interrogatories in a single pleading, because if admissions are not denied within the 30 days allowed for response, they are deemed admitted. *See, e.g.*, FED. R. CIV. P. 36(a). Where the practice of combining them is prohibited, denials can be followed up in a separate set of interrogatories.

[565] Some reporters may waive the appearance fee if the deposition transcript is ordered.

[566] Usually, the party defending the deposition does not order the deposition, but will order a copy of the deposition if it is ordered by the opposing party.

[567] Where both sides have the same number of experts, the parties may agree to pay for their own expert's time and travel costs.

[568] FED. R. CIV. P. 30(b)(6) requires the entity to designate one or more persons to testify about the matters listed in the subpoena.

sitions are the only method of obtaining information from a nonparty who is unwilling to cooperate.

Once the decision to take the deposition is made, the next step is to develop a deposition outline. The outline should focus on the objectives in taking the deposition and be divided into topics, in order of importance. Each topic should identify the points that the interrogator wishes to establish with the witness. Evidentiary gaps that need to be filled in should be highlighted in the outline. Avoid an outline that always proceeds in chronological fashion or that always begins with the witness's educational background and work experience. Consider varying the approach to catch the witness off guard. Avoid questions about facts that have been clearly established in interrogatory answers, unless there is something to be gained by asking about them. Interrogatory sets verified by the deponent should be used to develop facts further, as appropriate. This is especially true in depositions of expert witnesses. The standard interrogatories dealing with the expert's opinions and the facts upon which those opinions are based provide a good segue for detailed questioning about the expert's opinions.

Few depositions in construction cases are conducted without the use of documents. The documents that will be used in a deposition should be arranged to avoid having to shuffle through them during the deposition. One method is to keep each exhibit in a separate labeled folder. The documents can be premarked as exhibits by the court reporter in advance of the deposition,[569] and each folder can be numbered with the exhibit number and arranged in chronological order. Each folder should contain the exhibit that will be handed to the witness and retained by the court reporter, a courtesy copy for opposing counsel, and a working copy for the interrogator. The exhibit number can be keyed into the deposition outline under the appropriate topic. The interrogator's working copy can contain notes and questions about the document. This allows counsel to focus entirely on the working copy in asking questions, avoiding having to skip back and forth between the outline and the document. This makes the examination smoother and more effective and helps reduce mistakes and confusion.

Another cost saving device, for out-of-state witnesses or witnesses in other cities, is the use of telephone depositions. Telephone depositions are cost-effective when it is not important to observe the witness's demeanor or to confront the witness face-to-face. Videotaped depositions should be considered when the witness will not be available to testify at trial, and the witness's appearance and demeanor will be impressive.[570]

Usually, the depositions of persons who will be called to testify at trial as experts are deferred until all other discovery has been completed. Scheduling depositions can be done either informally by agreement of counsel, or by an order establishing a discovery schedule. If an order is entered, it should require that the depositions of expert witnesses will be completed by a specific date, and further provide that all experts must formulate the opinions, to which they will testify, prior to the date of their depositions.

The order should also address the situation where the expert changes his or her opinion after having been deposed. The order can provide that if that occurs, the opposing party must be notified of the change, and be allowed to take a supplemental deposition with respect to the changes. The order should also prohibit any further changes in the opinion after a specified date, unless the party can show good cause as to why the change should be allowed.

The attorney should prepare for the expert's deposition by educating himself or herself about the subject matter. Consult your own expert who can educate you in the "basics" of the subject and provide you with questions to ask and why they should be asked. This will prepare you to ask follow-up questions. Talk to other lawyers about their experiences with the witness. Review any articles or other written materials authored by the expert. Review any depositions and trial testimony transcripts that other attorneys have and are willing to share.

Consider the place where the deposition should be held. Usually, the best place to take the expert's deposition is at the expert's office. This allows greater access to the expert's work file and eliminates any excuse by the expert for inadvertently leaving part of the expert's work file back at the office. If the deposition is not held at the expert's office, consider serving a subpoena duces tecum upon the expert to bring the case file to the deposition, including all written instructions, information, and requests that he or she was given relating to the case.[571] The subpoena duces tecum should also require

[569] Numbering of deposition exhibits should be consecutive throughout all depositions by all parties. Counsel should stipulate to this procedure at the first deposition. For example, the exhibits used in the deposition of Ms. X taken by the contractor should be marked No. 1 through No. 20. The exhibits taken in the next deposition taken by the owner would be marked beginning as No. 21 through 40. The first exhibit in the third deposition would be marked No. 41 and so on. Consider using one court reporter or court reporter service for all depositions. This allows the court reporter to have a master deposition list that can be brought to every deposition allowing the witness to be shown a document marked as an exhibit in an earlier deposition. By agreeing on one reporter for all depositions, the parties can obtain competitive bids from court reporters and save money.

[570] See generally D.R. SUPLEE & D.S. DONALDSON, THE DEPOSITION HANDBOOK (3d ed. 1999).

[571] This may raise questions about work product and protection of an attorney's mental impressions and theories. *See* Karn v. Ingersoll Rand, 168 F.R.D. 633 (N.D. Ind. 1996) (generally, whatever the expert has considered in formulating the opinion is discoverable); *see also* L.M. Cohen, *Expert Witness Discovery Versus the Work Product Doctrine: Choosing a Win-*

the expert to bring materials of any kind used by the expert, or by anyone who assisted the expert.

The primary purpose in taking the expert's deposition is discovery. A secondary purpose is to impeach the witness when his or her testimony during the trial differs from what was said in the deposition. The statements in the deposition that the expert later contradicts are usually in response to questions furnished by the interrogator's expert. Therefore, it is important to write down questions given to you by your expert and ask them exactly as they are written. Aside from potential impeachment questions, and other questions given to you by your expert, you should ask broad, open-ended questions that are designed to obtain information. The attorney should not worry that the answers may hurt.[572] It is better to know what the expert will say and address it at trial than to be ambushed. Ask the expert to explain his or her answers as appropriate. Make sure that you have obtained everything that the expert has to say about a particular topic. Leave nothing undiscovered. Keep asking questions until you have exhausted everything connected with the expert's opinion and there is nothing further to discover. Insist on answers. If the expert refuses to answer, call the judge for a ruling by telephone, if possible, or make a record for a motion to compel an answer and for sanctions.[573] Above all, listen to the answer. Some attorneys, in thinking about the next question, fail to listen carefully to what the expert has said. Failure to listen prevents follow-up questions. Before concluding the deposition, check your outline again to make sure that you covered everything. Bring your expert to the deposition. Check with your expert to see if anything else should be asked.

The deposition of the opposing expert typically includes certain topics. They are:

- Qualifications and resume.
- Prior testimony in other cases and details.
- When was the expert retained and by whom.
- What was the expert asked to do.
- What facts did the expert rely upon.
- Who or what was the source(s) for those facts.
- What documents did the expert review and why.
- Who furnished those documents to the expert.
- What information did the expert obtain from those documents and how did the expert use that information in formulating opinions.
- Did the expert verify information provided by others and if so, how.
- What is the expert being paid for the work and what has the expert been paid to date (ask to see the expert's invoices for work performed).
- Whether compensation is contingent upon the outcome of the case (the answer is almost always no, but the question should be asked).
- If there is no discovery cutoff order, whether the opinions are final, or what further work the expert plans on doing and why. There should be a follow-up deposition if the opinions are revised.
- Whether assumptions were made in forming opinions and what those assumptions were, why they were made, and how the opinion would be affected if the assumptions were incorrect.[574]
- Whether the expert knows your expert and the opposing expert's opinion of your expert.
- When appropriate, try to narrow the differences between your expert and the opposing expert.
- Ask what the witness did to prepare for the deposition, what materials he or she reviewed, and whom he or she consulted.[575]

The deposition of an opposing expert is an opportunity to learn what the expert will testify to at trial. If the attorney properly takes advantage of the opportunity, the attorney should be prepared for cross-examination and should not be surprised by the testimony.

All depositions should be indexed so that essential points for cross-examination are not overlooked. Usually, indexing is done by a paralegal. However, the attorney who will conduct the cross-examination should review the deposition transcript rather than simply rely on the index.

ii. Defending the Deposition: Preparing Witnesses.— The first phase in defending a deposition is to prepare the witness to testify. The level of detail that is necessary depends upon the witness. Expert witnesses who are old hands at testifying need little preparation other than to discuss potential problem areas in their analysis and conclusions and to review any documents that they may be questioned about and any conflicting testimony from other witnesses.

Witnesses who have little or no experience should be thoroughly prepared. Begin by finding out if they have ever had their deposition taken. If they have not been deposed before, explain to them what a deposition is, why it is important, and how it can be used at trial. Also review the mechanics of a deposition, including the

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ner in Government Contracts Litigation, 27 PUB. CONT. L.J. 719 (1998); L. Mickus, *Discovery of Work Product Disclosed to a Testifying Expert Under the 1993 Amendments to the Federal Rules of Civil Procedure*, 27 CREIGHTON L. REV. 773 (1994); Comment, *Discoverability of Attorney Work Product Reviewed by Expert Witnesses: Have the 1993 Revisions to the Federal Rules of Civil Procedure Changed Anything?* 69 TEMP. L. REV. 451 (1996).

[572] An exception is where the deposition can be used by the opponent because the witness is not available for trial, and the court allows the deposition to be read to the jury or read by the judge in a bench trial.

[573] *See* FED. R. CIV. P. 37(a).

[574] A good expert's logic in formulating opinions is often unassailable, assuming that the premises are correct. Where the expert may be vulnerable is in the assumptions that the expert makes, or the facts upon which the expert relies.

[575] Material used in preparation for a deposition may be discoverable. Al-Rowaishan Establishment Universal Trading & Agencies, Ltd. v. Beatrice Foods Co., 92 F.R.D. 779, 780 (S.D. N.Y. 1982); FED. R. EVID. 612 (writings used to refresh recollection while testifying or before testifying discoverable).

seating arrangements, the oath taken by the witness, and the role of the court reporter.[576] An attorney preparing a witness to testify, especially one who has never had the experience of testifying before, should also advise the witness of the standard guidelines for testifying effectively. These include the following:

• Always tell the truth. The witness's most important asset is credibility, the ability to testify and be believed by the court, the attorneys, and any jurors. The witness should plan to leave the witness stand the same way he or she came to it, with his or her credibility intact. Witnesses also testify under oath, and there are potential civil and ciminal penalties for testifying falsely under oath, which is referred to as "perjury." You can never be tripped up by truthful answers. Stick to your answers. An examiner may try to shake your testimony by creating doubt in your own mind about the accuracy or completeness of your answers. Tell your story truthfully and stick to it. Do not concede that you could be wrong or equivocate about your answer.

• Listen carefully to the question. Make sure you understand the question before you answer.

• If you do not know the answer, say so. Never guess, and do not allow opposing counsel to entice you into offering an estimate or approximation. If you guess, or agree to a suggested estimate or approximation, opposing counsel might then be able to undermine your credibility by confronting you with evidence showing that your guess, estimate, or approximation is incorrect, and that you do not know what you are talking about.

• If the question is unclear, say so and ask that it be rephrased. Never interpret the question. It is the examiner's job to ask clear and understandable questions. It is not the witness's responsibility to try to figure out what is being asked.

• Answer only the question that is asked. Do not volunteer information not called for by the question. For example, if you are asked how long have you lived at your current address, say "10 years" and stop. The answer "10 years" is responsive to the question. Adding, "and before that I lived in New York for 5 years," is not responsive; it volunteers information not called for by the question.

• Provide a factual answer. Do not offer opinions unless you have been called as an expert witness. Do not use descriptive but judgmental or emotional adjectives or adverbs—stick to the facts, and keep it brief.

• Answer as briefly as possible, consistent with providing a truthful and responsive answer to the question that has been asked. If a witness continues talking for a long time, trying to explain the answer, he or she is almost certainly volunteering more information than what the question asked for and perhaps revealing things that help the other side's case. It is not the witness's job to provide the attorney with a free ride or a free education. Make the lawyer earn his or her living by having to ask more questions.

• Pay attention to the lawyer's questions, even if they seem to be routine or boring. Sometimes a lawyer may try to catch the witness unaware by asking a series of routine and seemingly unimportant questions to lull the witness into complacency and then asking with the same low-key demeanor a deceptively simple but carefully phrased question honing in on key facts or issues in the case. Sometimes a lawyer may be trying to set the witness up for a question that will distort the facts or issues in the case. If so, the witness should still answer the lawyer's questions honestly, factually, and briefly, and should not give an answer that anticipates the next question or argues with the lawyer. Instead, the witness should simply remain alert and be prepared to respond appropriately if the lawyer asks a misleading or distorted question.

• Maintain a calm and professional demeanor. Never get angry or argue. Take your time and think before you answer. Refer to documents as appropriate, but remember that any document referred to could then be part of the deposition. Do not let opposing counsel get under your skin and make you angry, even if the lawyer is arrogant, condescending, patronizing, insulting, sarcastic, belittling, or obnoxious in questioning you. When lawyers do such things, they are often using an intentional professional tactic designed to make witnesses angry and lose their temper, because when witnesses lose their temper, it undermines their credibility, which is what lawyers intend to achieve when they are deliberately insulting.

• Stop when you have finished your answer and wait for the next question. Some examiners will stare at the witness, creating a pregnant pause that suggests to the witness that the answer is incomplete, as if to say, "Well go on, there must be more." This is nothing more than a tactic; do not fall for it. Even if the silence becomes uncomfortably long, do not blurt out additional information that the question did not ask for. Just sit and wait for the next question.

• Do not make facetious, ironic, sarcastic, or flippant remarks. In particular, never ever say the opposite of what you really believe, with a tone of voice, facial expression, or body language that indicates that you mean something else. The transcript records only your words as printed symbols on a page; it does not record your tone of voice, facial expressions, or body language, and will not reflect the irony. If the case later goes up on appeal, an appellate judge reading the transcript will probably take the words you spoke at face value and think that you meant exactly what you said.

• Do not try to sell your story to the interrogator, no matter how fair or charming he or she may appear.

• Do not talk to your lawyer during depositions unless it is critical, except to ask for a break.

• If you genuinely do not know the answer to a question, say so, but do not pretend lack of memory in an effort to evade a question when you do know the an-

[576] SUPLEE & DONALDSON, *supra* note 570 § 10.13.

swer. Witnesses are expected to be able to respond to questions in their areas of responsibility. If a witness being questioned about significant matters within the witness's area of direct responsibility repeatedly says, "I do not know," or "I do not recall," it will quickly become obvious to everyone, including the judge, that the witness is being intentionally evasive, and this will severely undermine the witness's credibility.

- The witness may be asked whether his or her testimony was discussed with the attorney defending the deposition. The question is legitimate; however, any inquiry about what was discussed is not, if the witness is the client and discussions are privileged. If the discussions are privileged, the attorney should instruct the witness not to answer. If the interrogator persists, the attorney should stop the deposition and seek a protective order and sanctions.
- Advise the witness that you will tell him or her not to answer only when the question invades a privilege, is harassing, or is clearly not relevant.

An attorney defending a deposition should not be a "potted plant," nor should he or she be an active participant. The attorney defending the deposition should protect the witness from harassment and abuse by the interrogator and protect the record by objecting to improper questions. The defending attorney should not coach the witness or inject himself or herself into the proceedings by making comments to the witness such as, "If you recall," after a question is asked. Someone once said that when a defending attorney speaks, the words should start with, "I object." While this is too restrictive, it does suggest limits to the role of the attorney in defending a deposition.

The following are excerpts from a general federal court order governing depositions in the Western District of Washington. The order exemplifies how depositions should be conducted.

> (a) Examination. If there are multiple parties, each side should ordinarily designate one attorney to conduct the main examination of the deponent, and any questioning by other counsel on that side should be limited to matters not previously covered.
>
> (b) Objections. The only objections that should be raised at the deposition are those involving a privilege against disclosure, or some matter that may be remedied if presented at the time (such as the form of the question or the responsiveness of the answer), or that the question seeks information beyond the scope of discovery. Objections on other grounds are unnecessary and should generally be avoided. All objections should be concise and must not suggest answers to, or otherwise coach, the deponent. Argumentative interruptions will not be permitted.
>
> (c) Directions Not to Answer. Directions to the deponent not to answer are improper, except on the ground of privilege or to enable a party or deponent to present a motion to the court or special master for termination of the deposition on the ground that it is being conducted in bad faith or in such a manner as unreasonably to annoy, embarrass or oppress the party or the deponent, or for appropriate limitations upon the scope of the deposition (e.g., on the ground that the line of inquiry is not relevant nor reasonably calculated to lead to the discovery of admissible evidence). When a privilege is claimed, the witness should nevertheless answer questions relevant to the existence, extent or waiver of the privilege, such as the date of the communication, who made the statement in question, to whom and in whose presence the statement was made, other persons to whom the statement was made, other persons to whom the contents of the statement have been disclosed, and the general subject matter of the statement.
>
> (d) Responsiveness. Witnesses will be expected to answer all questions directly and without evasion, to the extent of their testimonial knowledge, unless directed by counsel not to answer.
>
> (e) Private Consultation. Private conferences between deponents and their attorneys during the actual taking of the deposition are improper, except for the purpose of determining whether a privilege should be asserted. Unless prohibited by the court for good cause shown, such conferences may, however, be held during normal recesses and adjournments.
>
> (f) Conduct of Examining Counsel. Examining counsel will refrain from asking questions he or she knows to be beyond the legitimate scope of discovery, and from undue repetition.
>
> (g) Courtroom Standard. All counsel and parties should conduct themselves in depositions with the same courtesy and respect for the rules that are required in the courtroom during trial.

e. Discovery Problems

Discovery is the most abused phase of the litigation process. Responses to discovery requests are, on occasion, used as tactical weapons to delay and even to mislead the opponent. Stonewalling document productions is not unusual. Some say that this type of conduct is endemic to an adversary system that requires lawyers to zealously represent their clients. Others say that such conduct violates the Rules of Professional Conduct and is unethical. It is not the purpose of this section to debate either side. The topic is raised merely to suggest some techniques that may be used to deal with such conduct. If your opponent makes frivolous objections to interrogatories or refuses to produce documents, file a motion to compel answers to the interrogatories and compel production of documents. Ask the court to impose appropriate sanctions, including attorneys' fees caused by your opponent's action or foot dragging.[577] Judges have no patience for responses that are misleading and contrary to the purposes of discovery. Such conduct "is most damaging to the fairness of the litigation process."[578]

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[577] FED. R. CIV. P. 11 and 37.

[578] Wash. State Physicians Insurance Exchange & Ass'n v. Fisons Corp., 122 Wash. 2d 299, 858 P.2d 1054, 1080 (1993); *see also* Dondi Prop. Corp. v. Commerce Savings and Loan Ass'n, 121 F.R.D. 284 (N.D. Tex. 1988); Comment, *Sanctions*

Another abuse is the tactics of the "Rambo" type lawyer. Counsel should conduct themselves in depositions with the same courtesy and respect for the rules required in the courtroom during trial.[579] In this sense, the deposition room is an extension of the courtroom. If the rules are not followed and the attorney becomes abusive, adjourn the deposition and seek a protective order and attorney fees. Ask the court to make the attorney personally responsible to pay the fee, not the attorney's client. For significant depositions that could be troublesome, ask the court to appoint a discovery master to preside over the deposition. Schedule a discovery motion before the court for entry of a discovery order like the one discussed earlier. During the motion, ask the court for permission to send to the judge a copy of any deposition in which there is improper conduct by your opponent. Tell the judge that such conduct will be highlighted in the deposition and will be sent to the judge to allow the court to monitor discovery. This only works if the case is preassigned to one judge. The potential for sanctions that this poses will usually prevent or discourage improper or abusive deposition tactics.

There is a natural reluctance to run to the court for help in discovery disputes. Instead, trial lawyers, who are naturally aggressive, have a tendency to slug it out, to fight fire with fire. Unfortunately for the client, this type of response does not work well. It does not produce the information or documents needed to prepare the case. The tendency to respond in kind should be resisted. Help should be sought from the court to resolve serious discovery problems. That is the court's job, and involving the court is the best way to protect your client's interests.

6. Preparing the Engineering Witness to Testify

When preparing witnesses to testify at trial, attorneys should provide all of the same standard advice to the witnesses as the advice indicated previously in the discussion about preparing witnesses for depositions. There are some additional factors to take into account, however, when the witness is an engineer.

Generally, witnesses in a construction case consist of project personnel and experts. For the owner, the principal employee witness is usually the project engineer or chief inspector. Occasionally, in cases involving technical engineering issues, the owner may call staff engineers who are experts in a particular field of engineering or call outside technical experts as witnesses.

Although engineers and lawyers may think that they speak the same language, the professional educations that they receive are quite different, and the professional environments in which they operate and gain their professional experience are based on significantly different assumptions. For these reasons, attorneys and engineers may sometimes have difficulty communicating clearly and effectively with each other. They may also fail to recognize that they are having such difficulty.

Engineers are trained and expected to use precise mathematical techniques to determine answers to questions for which there can only be one correct answer and for which there are no shadings or gradations of meaning. The strength of a bridge beam of a certain dimension, fabricated from a certain specific type of material, can be calculated with precision (assuming that it has been properly fabricated and is a new beam that has not undergone years of corrosion and material fatigue). If placed under a load within its maximum strength, it will bear the load; if it is placed under a load greater than its maximum strength, it will break. Determining the strength of the beam may be quite important, and in complex structures there may be a great many different forces acting upon the beam, which must be accounted for in the calculations, but the question is ultimately capable of a single clear-cut answer. Either the beam is strong enough for its intended use, or it is not, period.

Conditioned by dealing with questions that have clear-cut, precise answers, engineers tend to be confident of their ability to understand things. They recognize that lawyers are uninformed when it comes to engineering matters. They tend to think, however, that because they themselves are intelligent and can read and write English, they can understand legal issues and proceedings clearly and that underneath all the formal procedures, things are really simple and clear-cut, with only one right answer.

Lawyers, by contrast, operate primarily with words rather than numbers. Words can have many different shades of meaning or be understood differently by different people. Trials involve situations in which people with conflicting legal, financial, and reputational interests swear under oath to tell the truth, and then give testimony asserting such completely different versions of "the truth" that it appears somebody must be lying. The rules governing trial procedures and the admissibility of evidence are of Byzantine complexity, and frequently susceptible to multiple interpretations. Lawyers are trained to operate in an environment where there are two sides to every story, where many if not all witnesses have some personal interest in the outcome of the case, and where a great deal of money, the survival of a business, or a personal or corporate reputation may be at stake. Witnesses who have an interest in the outcome of a case tend not to answer questions in a straightforward way. Witnesses may tell the truth, but only part of the truth, leaving out the part that might place their financial interests or reputation at risk. Witnesses may pretend to be more forgetful than they

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Imposed by Courts on Attorneys Who Abuse the Judicial Process, 44 U. CHI. L. REV. 619 (1977); Note, *The Emerging Deterrence Orientation in the Imposition of Discovery Sanctions*, 91 HARV. L. REV. 1033 (1978).

[579] M. Frankel, *The Search for Truth: An Umpireal View*, 123 U. PA. L. REV. 1031 (1975) (attorney's ethical duty to seek the truth even when it does not advance his or her client's interests).

really are, give evasive answers, or intentionally shade the truth somewhat. Witnesses may even intentionally give answers that they know to be flat-out false in order to protect their jobs, financial interests, or reputations.

In legal cases, there are often few clear-cut, black-and-white answers. Instead, the testimony of the witnesses and the other evidence may sometimes involve many different shades of grey, often blending almost imperceptibly into each other, with no clear or readily determinable demarcation between truth and falsehood. A trial puts lawyers in the position of diving into a pool of muddy water, where conflicting testimony and evidence obscures visibility so much that the truth can sometimes be glimpsed through the silt only dimly, if at all. [580] It is nonetheless a trial lawyer's responsibility and duty to try to persuade the judge to believe that his or her clients are telling the truth, that the opposing party's witnesses are not credible, and that his or her clients deserve to win the case. Lawyers are trained to be skeptical of the accuracy of everything they are told by anybody unless they can verify it independently through other reliable evidence; to recognize that it may never be possible for them to determine with precise certainty exactly what happened in the situation that the parties are suing each other over; and to approach trials by advocating for their client's interests and leaving it up to the court to figure out what the truth is.

A trial is not a process designed to be easy, pleasant, or entertaining for witnesses. It is instead intended to test witnesses and evidence to determine who is telling the truth, and failing that, whose version of the truth is more believable. To draw an admittedly imprecise analogy to the engineering world, courts may be compared to materials laboratories, lawyers to materials engineers, and witnesses to concrete core samples. It is the job of lawyers to test the truthfulness and accuracy of testimony given during a trial by using cross-examination and other methods to place the witnesses under pressure. Lawyers subject engineering witnesses and their testimony to the legal equivalent of tension, compression, torque, high and low temperatures, and other stresses, to determine whether the witnesses are credible. It is the job of engineering witnesses to emerge intact by telling the truth, surviving all of the different testing pressures, and being believed by the court.

Often, engineers who are called to testify have little or no experience as witnesses in a trial. Engineers and lawyers work in professions that are based on different assumptions and have different cultures. This means that lawyers and engineers often have difficulty communicating effectively with each other. If an engineer has never testified in court before, an attorney has only a short time to prepare the engineer to function effectively in an environment that the engineer's professional education, training, and experience has not equipped him or her to understand very well, and about which he or she may be overconfident, apprehensive, or both. This does not make the process of preparing an engineering witness for trial especially easy for either the lawyer or the engineer, so patience and good will are indispensable to succeeding.

In preparing the engineer to testify, it is important for the attorney to emphasize that a trial is an adversary proceeding. The engineer must realize that the basic principles and facts that the engineer has regarded as true may be questioned. Engineers inexperienced in the courtroom arena often assume that their role is to dispense the facts to the court, that the court will consider them to be as honest as they themselves do and will believe them, and that the facts will automatically result in a favorable decision. This somewhat naive assumption misperceives the nature of the adversary system of justice. Some engineers may also be apprehensive about the prospect of having to deal with the legal system. If appropriate, it may be helpful for the lawyer to arrange for a visit to the courtroom with the engineer in efforts to ease any discomfort.

The attorney should tell the engineer that the outcome of the case may depend upon the credibility of the engineer’s testimony. The attorney must convince the engineer of the importance of his or her role as a credible witness. The attorney should emphasize that the engineer knows more about engineering than the attorney does, or more about what happened on the project than the attorney, since the engineer was there and the attorney was not. The witness must understand that the credibility of his or her testimony may depend more on the witness’s demeanor than what the witness says. In answering questions, the witness should talk to the jury and make eye contact with them. Although the answer is important, it is not always the answer itself that determines the outcome of the case. Other factors may influence a jury more, including factors such as the engineer’s experience, courtroom demeanor, and overall credibility.

An attorney who has an articulate and perceptive witness has an advantageous position. While these qualities are to some degree individual characteristics, an attorney can help cultivate those qualities in a witness through effective trial preparation. One technique is to have another attorney cross-examine the witness to sharpen those qualities. Another technique is to put the witness through a mock direct and cross-examination that is videotaped. The witness can later view the videotape as part of further trial preparation. Also, a witness will occasionally ask the attorney to furnish the witness with a written list of the questions that will be asked. Whether either of these practices is followed depends upon whether there is an attorney-client privilege prohibiting the cross-examiner from exploring what was said and done by the attorney and the witness during trial preparation. The better prac-

[580] Lawyers engaged in construction contract claims litigation consider it amusing that one state DOT's formal publication establishing standards for maintaining records on construction contracts is entitled the Manual of Uniform Record-Keeping, and that its acronym is "MURK," a moniker they consider completely appropriate given the issues in most claims cases.

tice is to put the questions to the witness orally, and not have the witness answer from a written list. Written answers to the questions should never be furnished by the attorney to the witness for obvious practical and ethical reasons. Most of us have heard the horror story of the witness who, while on the witness stand, pulls out a list of questions and answers that were given to the witness by the attorney.

The task of the engineering witness is to persuade the court and jury that the witness's opinions are reasonable and result in the correct solution to the problem, and to do so in plain, nontechnical terms. The engineering expert witness should not rest his or her testimony on harsh technical specifications or strict contract provisions. The witness should understand the underlying policies that the contract provisions serve. Judges and juries will consider and be influenced by those policies in enforcing those provisions, without feeling that the result is harsh or unfair. If the engineer understands the policy behind the technical provision, the witness will be less likely to rely on a mere recital of the provision itself, and will be able to explain it in more understandable terms. Moreover, in most instances there is a valid and salutary purpose to be served by each contract provision, harsh as it may seem. This is particularly true in the case of contracts subject to competitive bidding requirements.[581] The attorney should ensure that in answering questions, the engineer should consider, as appropriate, the purpose of a particular contract provision and not merely rely on the literal wording of the provision itself.

7. Pretrial Strategies and Considerations

a. Judge or Jury

If the contractor did not file a jury demand, should the agency demand a jury? Often, this may be a difficult question. The decision of whether to try the case to a judge or to a jury may depend upon a variety of considerations. How will the parties be perceived by the jury? Will the owner be regarded as fair and evenhanded in the way it managed the project? Will the contractor appear to be fair in its demands, or opportunistic and overreaching? Who has the equities—Or as one lawyer once put it: who will be perceived as the "bad guy"? Who will the judge be? Is judicial bias a concern? If so, can the agency seek recusal? Is the case more legal than factual? Is the case too complex for a jury?[582]

These considerations (among others) lead to the ultimate question: From the public owner's standpoint, is it better to try the case to a judge or to a jury?

b. The Answer and Affirmative Defenses

Traditionally, the answer to the complaint in a construction case will deny the essential allegations in the complaint, placing the dispute at issue. In addition, most answers will contain affirmative defenses. An exhaustive list of potential affirmative defenses is included in the Appendix to this subsection. Failure to plead an affirmative defense may result in a waiver of the defense.[583] However, wholesale inclusion of affirmative defenses without any factual or legal basis is unwise and may, in some jurisdictions, result in sanctions.[584] Counsel should thoroughly review and investigate the case to be certain that all appropriate affirmative defenses are included in the answer. If new affirmative defenses are discovered after the answer has been filed, counsel should promptly file a motion to amend the answer to include the new defense or defenses.[585] Several affirmative defenses often available to the owner in a construction case are failure to file timely notice of the contractor's claim,[586] finality of the engineer's decision on some aspect of the claim,[587] and

[581] For example, the New York Court of Appeals has articulated the public policy considerations that underlie notice requirements in public works contracts. A.H.A. General Constr., Inc. v. N.Y. City Housing Auth., 92 N.Y.2d 20, 677 N.Y.S.2d 9, 699 N.E.2d 368, 376 (1998) (timely notice of claim or extra work allows a public agency to make necessary adjustments in the work, mitigate damages, document costs, and maintain the integrity of the public bidding process).

[582] Green Constr. Co. v. Kan. Power & Light Co., 1 F.3d 1005, 1011 (10th Cir. 1993) (motion to strike the jury, on the ground that the case was too complex to be generally comprehensible, was denied); R.O. Lempert, *Civil Juries and Complex Cases: Let's Not Rush to Judgment*, 80 MICH. L. REV. 68 (1981); Note, *The Right to a Jury Trial in Complex Civil Litigation*, 92 HARV. L. REV. 898 (1979).

[583] 71 C.J.S. *Pleading* § 199-200; FED. R. CIV. P. 12.

[584] FED. R. CIV. P. 11.

[585] Another device is a "Notice of Trial Amendment." The notice tells opposing counsel that the attorney for the defendant will move at trial to amend the answer to include the defenses set forth in the notice in the same detail as they would be in the answer. This puts opposing counsel on notice and gives counsel an opportunity to conduct discovery about the defenses before the trial.

[586] A.H.A. Gen. Constr., Inc. v. N.Y. City Housing Auth., *supra* note 581; *see supra* § 5.A.7 and 5.B.4.

[587] Where the engineer has authority to render final decisions regarding contract interpretations, courts will uphold the decision unless it was: (1) arbitrary or capricious; (2) based on clear mistake; (3) unsupported by substantial evidence; or (4) based on an error of law. J. J. Finn Elec. Service, Inc. v. P&H Gen. Contractors, Inc., 13 Mass. App. Ct. 973, 432 N.E.2d 116, 117 (1982); R.W. Dunteman Co. v. Village of Lombard, 281 Ill. App. 3d 929, 666 N.E.2d 762, 765 (Ill. App. 1996); Main v. Dep't of Highways, 206 Va. 143, 142 S.E.2d 524, 529 (1965); State Highway Dep't v. W. L. Cobb Constr. Co., 111 Ga. App. 822, 143 S.E.2d 500, 504–05 (1965); Ardsley Constr. Co. v. Port Auth. of N.Y. & N.J., 75 A.D. 2d 760, 427 N.Y.S.2d 814, 815 (1980). The rule is based on the principle that the parties anticipate that differences may arise, and to avoid further disputes agree to make the engineer the arbitrator of such differences. State_Highway Dep't v. MacDougald Constr. Co., 189 Ga. 490, 6 S.E.2d 570, 575 (1939); State v. Martin Bros., 138 Tex. 505, 160 S.W.2d 58, 60 (Tex. 1942). The finality of the engineer's decision has been held to be final and binding only

failure to reserve claims in the acceptance document as required by the contract.[588]

Construction contracts customarily contain provisions that require contractors to provide formal written notice of claims whenever the contractor believes that it is being required to perform extra work beyond the requirements of the contract. The purpose of the notice provision is to alert the agency, at an early date, that the contractor has a claim. Early notice allows the agency to take appropriate action to protect itself.

Where the only issue is the legal effect of the contract language, summary judgment dismissing the claim is appropriate.[589] Where the claim is limited to the amount reserved in the final contract estimate, an order in limine limiting the claim to the amount reserved is also appropriate.[590]

c. Pretrial Motions

Pretrial motions may be classified generally as dispositive, partially dispositive, and procedural. A dispositive motion, if granted, disposes of the case. Dispositive motions usually take the form of a motion for summary judgment and are granted only when disposition of the case is not dependent upon any factual determination, and the moving party (the party filing the motion) is entitled to judgment in its favor as a matter of law.[591] An example is dismissal of a case barred by a statute of limitations. Partial disposition of the case may be made by a partial summary judgment using the same criteria—the facts of a particular issue are not in dispute and the law is in the favor of the moving party. If material facts are in dispute, the court will not grant summary judgment. Judges are reluctant to dispose summarily of a case where the facts are not clear. When the facts are not clear, the nonmoving party is entitled to a presumption that the facts are in its favor, although it cannot rely on this presumption alone, but must present evidence demonstrating that there is a factual dispute. Moreover, judges are often reluctant to summarily dismiss claims that arise from a contractual relationship, preferring to give the party its day in court where it can develop its contentions further and tell the judge or jury the entire story.

Because of a court's general reluctance to grant summary dismissal of the case, some see a tactical disadvantage in moving for summary judgment, unless there is a good chance that it will be granted. An unsuccessful motion for summary judgment alerts the nonmoving party to what it can expect at trial, giving it an opportunity to prepare its defense. However, the motion, even though unsuccessful, can also operate as a discovery tool since it can force the nonmoving party to present its evidence in affidavits in order to establish a factual dispute, thus alerting the moving party to what it can expect at trial. It may also help convince the opposition to adopt a more conciliatory attitude toward settlement.

Procedural motions may involve numerous procedural and housekeeping items. Motions may be made: (1) to allocate time between the parties at trial for the presentation of their respective cases; (2) to publish depositions, interrogatories, and requests for admission; (3) to exclude or obtain an advance ruling on the admissibility of evidence; (4) to determine whether the jury should be able to take notes during the testimony of witnesses; and (5) to determine whether to realign codefendants and change their order of proof.[592]

Another type of procedural motion that may be used, before and during trial, is a motion in limine to exclude evidence and witnesses.[593] This type of motion may be used to exclude evidence that is legally inadmissible or overly prejudicial.[594] The motion may also be used to prevent experts, who were never identified in answers to interrogatories, from testifying. This type of motion can be a powerful tool and should be used whenever improper evidence is anticipated.

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where the contract expressly conferred authority upon the engineer to make the decision. C.B.I. Na-Con, Inc. v. Macon-Bibb County Water & Sewerage Auth., 205 Ga. App. 82, 421 S.E.2d 111, 112 (1992) (contract did not give engineer express authority to decide claims for time extensions and extra compensation).

[588] Failure to reserve claim on contract acceptance document as required by the contract waived claim. DiGioia Bros. Excavating v. Cleveland Dep't of Pub. Utils., 135 Ohio App. 3d 436, 734 N.E.2d 438, 453 (1999); United States v. William Cramp & Sons, 206 U.S. 118 (1907) (contractor who executes a general release cannot later sue for damages or additional compensation in excess of the amount reserved or raise new claims that were not specifically exempted from the releases). The rule extends to subcontractor pass-through claims. Once the subcontractor releases its claim against the prime contractor, the prime contractor cannot revive the claim by attempting to pass it on to the owner. George Hyman Constr. Co. v. United States, 30 Fed. Cl. 170, 177–78 (1993); Miss. State Highway Comm'n v. Patterson Enters. Ltd., 627 So. 2d 261, 263 (Miss. 1993). Also, contract standard specifications may specify that failure to reserve the claim in accordance with the contract claim procedures waives the claim. California Standard Specifications 9-1.07B (2002); New York Standard Specifications 109-14 (2002); Washington State Standard Specifications 1-09.9 (2004).

[589] Absher Constr. Co. v. Kent School Dist., 77 Wash. App. 137, 890 P.2d 1071 (1995).

[590] A motion in limine precludes counsel and witnesses from mentioning or referring to matters that the court has excluded. *See* G.O. Kornblum, *The Voir Dire, Opening Statement, and Closing Argument*, 23 PRAC. LAW. No. 7 at 1, 21 (1977).

[591] FED. R. CIV. P. 56.

[592] Traditionally, the order of proof is determined by how the defendants are named in the caption of the complaint filed by the plaintiff. They are named in that order simply because the plaintiff chose to list them that way. The issue may arise, for example, in a case where the agency is named as a codefendant with its consulting engineer. Arguably, it may be more logical for the party who prepared the plans to present its defense first when the adequacy of those plans is in dispute. *See* Green Constr. Co. v. Kansas Power & Light Co., 1 F.3d 1005 (10th Cir. Kan. 1993); *see also* FED. R. EVID. 611(a).

[593] *See supra* note 590.

[594] FED. R. EVID. 403.

d. Trial Briefs and Premarked Exhibits

i. Trial Briefs.—It is usually advisable to file a trial brief in a construction case.[595] The length and details of the brief should be governed by common sense, and to the extent known, the personal preferences of the trial judge.[596] In addition to suiting the judge's preferences, the length and details of the brief will also depend upon whether the case is jury or nonjury and the extent of the judge's familiarity with the case from pretrial proceedings.

In general, a trial brief serves several purposes. First, it allows counsel to argue the case in advance of trial.[597] A popular method of brief writing is to divide the brief into sections: introduction, statement of the case, argument, and conclusion. The argument section is further divided into subsections that argue each point that counsel wishes to make. Each subsection should have a heading summarizing the argument. The headings should be indented and italicized or underscored for emphasis.[598] The trial brief is also an outline of a party's case. In addition to educating and persuading the court, the brief allows the judge to follow the testimony. If the judge is unfamiliar with construction jargon and clauses unique to construction contracts, the brief should contain a glossary explaining technical terms and a section quoting pertinent contract clauses, a brief description of how they work, and their significance to the case. If the brief is extensive, there should be a detailed table of contents to make it easier for the judge to locate issues and statements of law.

The benefits of an extensive brief, where one is warranted, are not as valuable if a jury is involved. With a jury, the education process is limited to testimony, exhibits, instructions, and oral argument. However, the advantage of a knowledgeable judge presiding over the trial should not be overlooked. The judge has the power to veto the verdict, if the judge believes that the jury decided the case incorrectly. Also, the brief may help convince the court that, as a matter of law, the issues must be determined by the plain language of the contract, thus avoiding issues of fact for the jury. In jury cases, the brief should also contain a section that supports the jury instructions requested by the party.

ii. Pre-marked Exhibits.—Trials should be efficient. Efficient trials save money and improve the quality of justice. One way to improve efficiency is to pre-mark exhibits in advance of trial. Each side meets and presents the exhibits that they intend to use at trial. Attorneys should not be overly concerned that disclosing proposed exhibits will reveal trial strategy. By the time of trial, the attorneys will usually be aware of the documents that will be offered as exhibits. After documents are pre-marked, counsel should stipulate to the admissibility of as many documents as possible. Premarked exhibits that have been stipulated to may be put in notebooks in numerical order. The exhibits are removed from the book(s) and used with the witnesses, without having to take the time to mark them and lay a foundation. This makes the trial go smoother and faster. Exhibits that are pre-marked but not admitted by stipulation can be handled in the normal manner and their admissibility determined by the court when they are offered.

e. Visual Aids

As trial preparation proceeds, the attorney should consider the use of visual aids to illustrate graphically the party's contentions. Most attorneys are familiar with the value of a chart or diagram of an accident scene in a tort case, or a map indicating the location of comparables in an eminent domain case. Often, just the mention of the type of case suggests the form of the visual aid needed to assist in the presentation of the case. This is not necessarily true in a construction case. The kinds of visual aids that will be helpful will depend upon the complexity of the issues presented and whether they can be better explained by the use of a diagram, chart, model, or computer animation.

i. Charts.—Many of the claims in construction litigation involve delay in completing work. The owner may seek to assess liquidated damages because the work is not completed within the contract time. The contractor may seek damages for owner-caused delays. Charts showing the planned work schedule and the events that transpired affecting the schedule are necessary aids in explaining to the court why the delay occurred and assigning responsibility for the delay.

These charts may take various forms. The most common and accepted method of proving delay, and showing the causal relationship between culpable acts and actual work progress, is CPM scheduling. Another is a chart plotting the contractor's progress against the time it took to complete the project. For example, in a typical highway construction project, this chart will show when the contractor began grading and the amount of grading performed each day. Witnesses can use this chart to show delay and then explain why the delay occurred. Other major construction activities that are in controversy can be depicted in the same manner. The use of a simple bar chart presentation is easily understood.[599] A bar chart, however, does not illustrate the

[595] Some local court rules require all parties to file trial briefs.

[596] For example, string-citing cases from other jurisdictions is usually not helpful, unless the issue before the court is one of first impression. Some judges are impressed by policy arguments and how the position urged by counsel comports with that policy.

[597] State or local court rules may require a working copy of the brief to be provided to the judge before trial, and it should be provided even in the absence of a requirement.

[598] *See generally* F.T. Vom Baur, *The Art of Brief Writing*, 22 PRAC. LAW. No. 1, at 81 (1976).

[599] Charts can be reduced to notebook size, annotated, and included in the trial notebook for use in cross-examination. For example, if the contractor has claimed that it was unable to

interrelationships between various work items or demonstrate how a delay of one work item affects other items of work. The CPM chart, if properly used, shows those interrelationships.[600] This type of schedule analysis is necessary to show the overall effect of concurrent delay on separate items of work. Computer-generated CPM demonstrations also may prove useful in demonstrating delays and impacts.

Some claims or defenses can be better presented by a model or tridimensional chart. For example, in a DSC case, a model or tridimensional chart can illustrate, through color coding in cross-sections, the type of material encountered in the highway prism or borrow site. This allows the viewer to see the type of material that was encountered at various locations throughout the cross-sections.

ii. Photographs.—Photographs taken during various stages of a construction project can be very helpful. Aerial photos taken on a regular basis can be important evidence in showing lack of progress on a project. Photos showing equipment breakdowns can also be significant in explaining lack of progress. Videos should be taken when the video will document particular problems. Photos and videos should always be dated.

iii. Models.—One of the most dramatic visual aids that an attorney can use in presenting the case is a model. A model can provide a view of the site, depict terrain, or show relationships and concepts that can be illustrated in no other way. Because a model is dramatic, its use requires special consideration.

The first consideration is how will the model be used: Will it be offered in evidence as a reproduction of what it purports to copy, or will it be used as demonstrative evidence to illustrate testimony? If it is offered in evidence as a reproduction, it must be to scale and its accuracy established by testimony, usually by an engineer and the model maker. If it is used for illustrative purposes, it need not be to scale, but it cannot be misleading and must assist the witness in explaining the testimony.[601]

Another consideration is cost. Models are expensive to construct, particularly when they are built to scale. The attorney should weigh the cost of the model against its prospective benefits. The attorney should anticipate how the judge will react to an elaborate and obviously costly model.[602] If the model does not illustrate an important point in the case, the court may feel that its use is not justified and exclude the model on the ground that its introduction was calculated to impress rather than enlighten.[603] This is especially relevant where the model is presented by a public agency. Care should be taken so that it does not appear that the agency, with its vast resources, is trying to overwhelm the contractor.

Highway construction cases lend themselves particularly well to the use of models to explain or illustrate testimony. A three-dimensional visual aid, like a picture, can be worth a thousand words. Models make it easier to understand testimony about cuts and fills, super-elevations, embankment compaction, bridges, and other three-dimensional features that are more easily shown by a visual presentation than by oral testimony.

iv. Overhead Projectors.—Because construction cases rely heavily on documentary evidence, it may be hard for a jury to understand the significance of a document unless they can see the document along with the witness. The use of an overhead projector can solve this problem.[604] Through its use, the jurors can see the document during the examination of the witness. Projectors can also be used during final argument or even opening statement with respect to documents that have been previously admitted by stipulation. Care should be taken in the type of projector used. Projectors that can be used without having to dim the courtroom lights and that are not noisy should be used. The presentation, to be effective, should be smooth. The attorney should consider having a legal assistant or paralegal operate the projector and handle the transparencies or the original documents if they are placed on the projector.

v. Other Considerations.—Effective demonstrative exhibits illustrate a point clearly and quickly. Juries pay attention to what they understand and reject or ignore what they do not understand. Thus, exhibits should not attempt to convey too much information. They should be limited to one key message that is readily understood.[605] Once the attorney has made the point with the exhibit, the attorney should stop and not be redundant. Juries and judges quickly become tired of hearing the same point over and over.

There are companies that specialize in creating visual aids for use in litigation. They are experts in how to present graphic information. There are also companies that specialize in building scale models. Both types of companies should be consulted in appropriate cases,

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place concrete because there were no inspectors on hand, the use of the chart can show that even if there were no inspectors on hand, concrete could not have been placed because of a breakdown in the batch plant. This may establish concurrent delay, preventing delay damages.

[600] CPM charts simplify complex problems. However, they should not be accepted by courts simply because they have been prepared using a computer. "As-planned" and "but for" schedules contain assumptions, not facts. The court should require the party introducing a CPM schedule to prove that it is accurate and that its assumptions have a factual basis.

[601] 29A AM. JUR. 2D *Evidence* § 993 (1994); *Propriety, in Trial of Civil Action, of Use of Model of Object or Instrumentality, or of Site or Premises, Involved in the Accident or Incident*, 69 A.L.R. 2d 424 (1960; supp. 2003); 7 AM. JUR. *Proof of Facts* § 601, "Maps, Diagrams, and Models" (1960).

[602] If the model maker testifies, he or she will probably be asked how much the model cost. The cost can run into thousands of dollars.

[603] *See generally* 3 AM. JUR. 2D *Trials* at 377 (1965).

[604] The use of Microsoft PowerPoint® is another option for presenting documentary evidence.

[605] Billboard advertising and roadside signs are an example. Television commercials are another. They are designed to convey a message.

where the use of a model or innovative graphics will be helpful or necessary. Companies that offer these kinds of services usually advertise in the yellow pages and bar journals. Claims consultants, particularly financial consultants, have computer programs that will produce graphic information in a variety of formats. Consultants are usually the best source of ideas on how to create visual aids for effective presentation of their testimony.

f. Settlement Negotiations Practice

Serious consideration should be given to possible settlement of the litigation. In a typical construction dispute, the contractor should be placed in the situation where he should consider sound business considerations as opposed to moral principles and just causes. There are many reasons favoring the settlement of litigation, which include avoiding the cost and time of litigation. It is not unusual for a case to take 3 to 5 years to reach a trial, even without considering the time for appeals. Early negotiated settlement relieves all parties of the cost of attorney fees and other expenses. Indirect costs, such as the cost of preparing demonstrative evidence and the costs of retaining experts, can be avoided. Avoiding lengthy litigation also allows key employees to focus their attention on business or governmental matters, which are their primary responsibilities, instead of being tied up with interviews, document production, depositions, trial testimony, and the other demands of litigating a case to conclusion.

Another good reason for considering settlement, often overlooked, is the risk of ultimate failure or loss in the litigation. Serious attention should be focused on an exposure analysis prepared by the litigation team that evaluates the potential outcome of the litigation. The potential evidence and testimony, contract provisions, damages, accounting, defenses, and applicable case law should be reviewed and assessed to arrive at a potential exposure analysis. This should be discussed by counsel with agency management prior to trial, permitting the agency to make a sound business decision on whether to go ahead with the litigation or pursue a negotiated settlement. If a negotiated settlement is desired, a negotiation team should be assembled and a strategy developed to arrive at a successful negotiation.

The team should have only one spokesman, whose rank and authority is recognized by team members, who serves as the battlefield commander. The team should also be supported by various experts and engineering staff who have knowledge of the claim.

Successful negotiation demands that agency negotiators should establish and maintain a sound cooperative relationship of mutual respect with contractors.

Basic personal guidelines for negotiation include the following principles:

- Do not dictate. You do not represent the government but you are reasonable.
- Do not ridicule or insult.
- Do not try to make anyone look bad or prove anyone wrong.
- Do not discriminate; accept a good offer.
- Do fight hard on important points, but do not fight battles that you have no chance of winning—focus on winning the war, not the battle.
- Be courteous and considerate, and do what you say you will; have integrity.
- Do know when to talk and when to sit and listen.[606]
- Bargain in good faith. Negotiations carried out in an atmosphere of hostility and distrust are rarely successful, because neither side is willing to listen with an open mind to what the other side is saying.[607]

8. The Trial

The presentation, argument, and examination techniques of a construction contract trial are not dissimilar to other types of trials.[608] There are, however, certain unique aspects that should be considered in the presentation of the case.

a. The Opening Statement

No single guideline governs how opening statements should be made. Their use is governed by a variety of considerations that depend upon the nature and complexity of the case and whether the case is tried to a judge or jury. There are, however, some guidelines that usually apply.

As a general rule, an opening statement should be presented at the commencement of the trial and not deferred until defense counsel commences his or her case-in-chief. If the opening statement is reserved, there should be a good reason for doing so.[609] The opening statement should be a road map of what your case will be and have an overall theme or theory that pieces the case together.[610] Outline the segments of the trial and their function to allow the jury to have a better understanding of how the trial will proceed. Do not read an opening statement. Counsel should talk directly to the judge or jury and maintain eye contact with them. The use of notes should be minimized. Visual aids, such as photographs, maps, aerials, and models, should be used to explain and illustrate what the evidence will

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[606] ARMED SERVICE PROCUREMENT REGULATION MANUAL (ASPM No. 21, Feb. 24, 1969).

[607] CONTRACT CONSTRUCTION LITIGATION COURSE MANUAL 88 (Federal Publications).

[608] *See* D. Schwartz, *Going to Trial in The United States Claims Court*, 32 PRAC. LAW. No. 1, at 35 (1986). Although the article discusses trying cases in the United States Claims Court, it offers suggestions that the reader may find useful in any bench trial regardless of the forum.

[609] An exception may be a bench trial where the trial judge is familiar with the case from pretrial proceedings or where counsel can gain a clear tactical advantage by deferring the opening statement. *See also* Schwartz, *id*.

[610] M. Mitchell, *A Method for Evolving a Trial Strategy*, 27 PRAC. LAW. No. 4, at 82 (1981). The article offers suggestions for developing a theme.

show. Pre-mark the exhibit and obtain permission from the court to use it in the opening statement, if opposing counsel refuses to stipulate to its use. This practice avoids an objection that could harm the effectiveness of the opening statement.

The opening statement should not be argumentative. Opening statements that are argumentative will usually draw an objection, which is likely to be sustained. Although argument must be avoided, counsel should make a strong statement of what he or she intends to prove, remembering that your opponent is entitled to comment in final argument on what you failed to prove. The opening statement should be phrased in simple terms with an explanation of the technical terms that may be used during the trial. However, counsel should never talk down to the jury or appear condescending. Witnesses should be introduced by occupation, not by name. For example, refer to the project engineer as the project engineer, not Mr. James.[611] The jury should be told how the witnesses fit into the case, and what they will say when they testify.

An opening statement should be comprehensive. As a general rule, an attorney will gain more in educating and conditioning the trier of fact than the attorney will lose in exposing his or her case in advance.[612] While the opening statement should be comprehensive, it should not be redundant. Counsel should avoid covering the same ground over and over. The trier of fact should be favorably impressed by an opening statement that is logical and comprehensive, yet succinct. This type of presentation will enhance the attorney's credibility and the credibility of his or her client's case. In the final analysis, the most important attribute that a trial attorney has is credibility.

b. Direct Examination

Typically, the most important part of any trial is direct examination. More cases are won by direct testimony than by cross-examination or final argument. Because of its importance, counsel should ensure that direct testimony is presented in a way that is easily understood by a judge or jury.

Direct examination should be business-like, not spectacular or dramatic. It should be brief and to the point. Once a point is made, stop. Go on to the next point. Covering the same ground again may do more harm than good. It may weaken the impact of what has been established and irritate the judge and the jury. It may even draw an objection from the court on its own volition, if not from opposing counsel.

The focus should be on the witness, not on the attorney, during the direct examination. A case is won by what the witnesses say. Counsel should not draw attention to himself or herself by pacing back and forth or by engaging in other distracting mannerisms. Questions should be short, clear, and whenever possible phrased in plain, simple English. Construction jargon and technical terms should be used only when necessary, and the witness should be asked to explain them and give examples to illustrate their meaning. Visual aids should be used to explain and illustrate the witness's testimony.[613]

Leading questions should be avoided, not only because they are objectionable, but more importantly because the witness should be testifying, not the lawyer.[614] A witness who is nothing more than a sounding board for the attorney has little credibility. Some lawyers write out their questions, others do not. Attorneys write down their questions in case they have problems formulating them and as a safeguard when direct examination is interrupted by an objection. Whatever one's preference, it is a good practice to have an outline listing point by point each topic that will be covered with the witness. An outline of this kind should be part of every trial notebook.[615] The outline should be reviewed with the witness before trial. Psychologically, this is helpful to the witness since the witness knows, when taking the stand, what the questions will be. Ideally, the direct examination should be like a friendly chat about some aspect of the case. Transitional questions such as "turning now to…" should be used to make the direct smoother and easier to follow. Avoid leading questions by using the "who," "how," "where," and "why" approach in formulating questions.

In preparing witnesses to testify, counsel should discuss certain guidelines with the witness. The witness should be told to listen to the question and answer the question as asked. The witness should be told not to volunteer or elaborate and that you will develop the witness's testimony.[616]

The order in which witnesses are called should be logical, and should allow you to lay out the case the way you want it presented. The conventional trial wisdom that you should begin and end with strong, substantive testimony is not always true. While you should end with a strong witness,[617] you may wish to begin with a minor witness, when that witness's testimony is the starting point for your case. For example, calling the office engineer from a project office to show in a DSC claim that the agency provided the boring logs to the

[611] Consider personalizing the case by having the project engineer sit with you at counsel table throughout the trial.

[612] *See* possible exceptions to this view noted *supra* note 609.

[613] Witnesses should be asked if the use of a picture or model, or some other visual aid, will assist them in explaining their testimony. This makes it difficult for opposing counsel to object to its use.

[614] *See* J. Weinstein, *Examination of Witnesses*, 23 PRAC. LAW. No. 2, at 39 (1977).

[615] *See generally* L. Packel and D. Spina, *A Systematic Approach to Pretrial Preparation*, 30 PRAC. LAW. No. 3, at 23, 33 (1984).

[616] A witness who volunteers information may appear to be biased.

[617] Expert witnesses on liability and damages ordinarily should be called last because they can summarize the case and handle any loose ends.

contractor during the bidding phase. This testimony is necessary to establish a foundation that the contractor actually knew or should have known about the soil conditions.[618] Contractor personnel who are managing agents (superintendents, foremen, project managers) should be subpoenaed and called as adverse witnesses. This permits counsel to ask leading questions and in effect cross-examine them.[619] The trial notebook should contain a list of questions that must be asked to lay a foundation for the admission of a document, photograph, or chart. Use of the outline allows counsel to lay a foundation crisply and smoothly, thus enhancing counsel's credibility with the court and the jury.

Sometimes owners feel so strongly about their lack of liability for a construction claim that they ignore damages. Owners should keep in mind that when liability and damages are tried together, large losses by the contractor may influence the trier of fact in making a determination about liability. Moreover, plaintiff's damages may be so poorly presented that doubt is cast on the overall merits of the claim. The dilemma for the defense is whether to offer testimony on damages, or stand on the contractor's failure to meet its burden of proof on damages. There are no rules concerning this dilemma. The strategy in dealing with this problem must be carefully considered and will vary depending upon the case. However, conventional wisdom tells us that it is probably better to put on some evidence refuting damages as part of the owner's case-in-chief, unless the defense has successfully refuted the damage calculations.

c. Cross-Examination

More books and articles have probably been written about cross-examination than any other phase of a trial. The most dramatic part of any movie or television show featuring a trial is the cross-examination of a key witness. Invariably, writings about cross-examination point out what the cross-examiner should not do—the so-called "don'ts" of cross-examination.[620] For example, avoid asking open-ended questions such as "why" or "how" of an articulate and knowledgeable hostile witness. Instead ask leading questions that call for a "yes" or "no" answer, or questions to which the witness will give only the answer you anticipate. If you gamble—because you do not know for sure what the witness will say—do so only when the answer cannot hurt your case. Be fair to the witness, do not embarrass the witness, and do not get angry at the witness. The cross-examination should be business-like and have a purpose. Generally, cross-examination can be designed to discredit the witness, or to solicit facts or admissions that can support your case. It should not be used to discover information about the case unless the witness is friendly and cannot possibly say anything that will hurt your case, but even then be cautious. Be thorough, but be brief and do not cover the same points over and over. Make your point and stop.

Should you always cross-examine every witness simply because the witness testified? Conventional trial wisdom says no, if the testimony has not hurt your case.[621] But if the testimony is damaging, it should not stand unchallenged. Find something you can attack, particularly if the witness is a retained expert. For example, if the witness is a retained expert, explore bias. Through discovery, you should have obtained what the witness's fee arrangement is, how much the witness has been paid, when, by whom he or she was retained, and any other cases in which the opposing attorney or party has engaged the witness.

Counsel should be thoroughly familiar with the deposition testimony of the witness he or she is interrogating. Statements in the deposition transcript that are inconsistent with the witness's testimony at the trial can be used for impeachment, but counsel should avoid the appearance of nitpicking by using a minor or trivial inconsistency to impeach.[622] Also, counsel should consult his own expert for areas of cross-examination. This is particularly important in preparing for cross-examination of the opposing party's expert. Your expert can review the deposition transcript of the opposing expert and can suggest questions that should be asked on cross-examination.[623] But counsel should be careful about asking questions on cross-examination suggested by others (including your own experts) when you do not understand the question. The opposing expert will usually have an answer, and if you do not understand the question you asked you probably will not understand the answer, leaving counsel with the choice of letting the answer stand or asking another question and maybe getting into even more trouble.

One of the problems of cross-examination in a construction case is keeping track of what occurred on the project and how those facts bear on the witness's testimony. This is often true in cross-examining a claims expert or project superintendent or manager who has overall knowledge of the project. One technique is a

[618] The contractor may be charged with knowledge of what the borings show even if the contractor did not examine them. *See* § 5.B, Differing Site Conditions, *supra*.

[619] FED. R. EVID. 611(c).

[620] A.S. CUTLER, SUCCESSFUL TRIAL TACTICS 123–30 (4th ed. 1950), "Some Don'ts in Cross Examination." Irving Younger referred to them as the "Ten Commandments of Cross-Examination" in his evidence seminars (reprinted at www.nebarfnd.org/10commandments.pdf, Nebraska State Bar Foundation Web site).

[621] *See, e.g.*, CUTLER, *id*.

[622] A number of inconsistencies, even though minor, may help convince the trier of fact that the witness is mistaken or lying.

[623] Usually, an expert's opinion is a logical extension of the premises upon which the opinion is based. Where the expert may be vulnerable is in the premises used to form that opinion, particularly if a premise is an assumption that is not supported by the evidence.

chart that diagrams the various construction phases of the project, including significant construction activities. This chart allows counsel to keep track of all aspects of the project as they occurred. The chart should be keyed to counsel's trial notebook.[624] The notebook can contain a section on each phase of the project, including areas to inquire about on cross-examination and documents by exhibit number (if pre-marked), that can be used during the cross-examination.

There are other ways, of course, of preparing for cross-examination. Often, how one prepares is a matter of personal choice. However, prepare for cross-examination before the trial begins. Counsel should know from pretrial discovery what the witness will say and be prepared to deal with it.

d. Presentation of Multiple Claims

Rarely will a construction contract case be limited to a single claim. Once a contractor decides to file suit on one claim, all disputes that have been preserved can be expected to be litigated. Where the lawsuit consists of several claims, the contractor has several methods it can use in presenting its claim. One method is to present each claim separately. The difficulty with this method is that some aspects of the project will be repeated as the facts are developed for each of the claims. The contractor will usually begin with the dominant claim and then proceed to the more minor claims. Another method is to present each claim as it arose in chronological order during the course of the project. This method avoids redundancy by allowing the project facts to be presented in an orderly and sequential manner from the commencement of the project to its completion.

Rather than anticipate which method the contractor will use in presenting its case, the owner may ask the court to rule in advance of trial as to which method must be used.[625] Knowing in advance how the contractor's case-in-chief will be presented helps the owner organize its cross-examination. Establishing the order in which the claims will be presented makes the trial more efficient and saves the court time.[626]

e. Closing Argument

Some lawyers have a section in their trial notebook to jot down ideas for final argument. Some attorneys review their trial notes and from them develop an outline of their final argument. Others prepare an outline of their final argument before the trial even starts on the assumption that the case is sufficiently well prepared to prevent any surprises.

Whatever technique is used, the final argument should be just that—an argument. Someone once observed that more cases are lost by a poor argument than won by a good one. That is a good admonition for lawyers to follow even if it is not precisely true. The final argument should be carefully prepared. Many who write about trial practice say that the closing argument must tell a story. The lawyer should paint a picture that is so compelling that the judge or jury must find in his or her client's favor. This, of course, is the ideal presentation. Attaining this ideal is even more difficult when the case is complex and involves a multitude of issues.

The closing argument, like other phases of a trial, has certain recognized guidelines that counsel should consider. These guidelines are often referred to as "do's" and "don'ts." For instance, it is improper to refer to matters that are not in evidence.[627] Another "don't" is never read a closing argument to a jury. To be effective and creditable, counsel must talk to the jury. Reading a speech to the jury is not talking to them. If permitted by the court rules, relate and argue how the jury instructions apply to the issues and the conclusions that the jury should reach in deciding the case. Relate the evidence in a way that shows that you proved what you said you would prove in your opening statement. This ties the opening statement to the closing argument, giving your case continuity and credibility.

Organize documentary evidence in a way that is keyed into your argument. Use enlargements of important documents that the jury can easily read as you argue their significance.[628]

Some lawyers make very little, if any, preparation for closing argument. They jot down a few notes on a yellow tablet sheet and then speak extemporaneously. Unless you have a natural talent for arguing cases, you should avoid this practice. Take the time to organize the argument in outline form. In concluding your argument, tell the jury that your opponent now has the opportunity to rebut what you have said. Point out that your opponent has this opportunity because plaintiff has the burden of proof. Tell the jury that you will not have an opportunity to respond to your opponent's remarks, but that you do not need that opportunity. Why? Because the evidence itself serves as rebuttal to what he or she may say.

The closing argument is an important part of the trial. Your argument may not win the case, but you should avoid a hastily prepared argument that could lose it.

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[624] The trial notebook is usually a three-ring notebook that allows issues and facts to be organized alphabetically or chronologically. *See* Packel and Spina, *supra* note 615.

[625] FED. R. EVID. 611(a).

[626] *Id*. Under this rule, the court has the power to "exercise reasonable control over the mode and order of interrogating witnesses and presenting evidence so as to (1) make the interrogation and presentation effective for the ascertainment of the truth, (2) avoid needless consumption of time…."

[627] It is proper to draw reasonable inferences from the evidence. But counsel should avoid overstating what the evidence actually proves.

[628] A common practice is to enlarge the document on a poster board that is light and easy to handle.

f. Other Trial Considerations

i. Taking Notes During Trial.—Conventional trial wisdom suggests that the attorney divide each page of a legal tablet down the middle with a vertical line. Notes are placed on one side of the line and comments, questions, or reminders on the other. One problem with this method is that it is an invitation to try to write down everything the witness says. If you accept this invitation, you may miss the jury's reaction to the witness, any nuances in the testimony, objections that should be made, and more important, what the witness is really saying.

In the first place, the attorney does not need to take notes during the direct examination of his or her witness. Second, note taking should be selective. It should be limited to the points that will be covered in cross-examination, and not a re-hash of the direct examination. Points developed through pre-trial discovery, and questions suggested by your experts can be prepared in advance for cross-examination and added to the notes on separate sheets of paper.

Good, complete note taking should not be performed by the trial lawyer. That task should be done by someone else sitting at counsel table.

ii. Housekeeping.—Good housekeeping techniques are important. A chart should be kept of each document that is marked as an exhibit. The chart should identify the document, show whether it was admitted, and show whether it was admitted only for illustrative purposes.[629] The chart should list the exhibits in numerical order. Pre-marked exhibits can be listed in advance. The task of keeping track of exhibits should be assigned to the paralegal sitting at counsel table with the trial lawyer.

iii. Jury Instructions.—In preparing jury instructions, considerations should be given to the verdict form. A special verdict form submitting questions to the jury may help in focusing the case. For example, the verdict form in a case involving the assessment of liquidated damages could provide as follows:

We, the jury, make the following answers to the questions submitted by the court:

Question No. 1: Should liquidated damages be assessed against the plaintiff?
Answer: (Yes or No) _____.

Question No. 2: If your answer to Question No. 1 is "yes," then answer the following question: The number of days that should be charged for liquidated damages are _____.

The questions may also ask the jury to focus on the State's liability. For example:

Question No. 1: Did the State breach its contract with plaintiff by withholding information about the pit site, which was vital for the preparation of plaintiff's bid?
Answer: (Yes or No) _____.

Question No. 2: Did a differing site condition occur in the pit site as alleged by plaintiff?
Answer: (Yes or No) _____.

If your answer is "no" to all of the above, do not answer any further questions. If your answer is "yes" to any of the above, then answer the following questions:

Question No. 3: Did the breach cause damage to plaintiff's subcontractor?
Answer: (Yes or No) _____.

Question No. 4: If the answer to Question No. 3 is "yes," what is the amount of those damages?
Answer: _____.

Question No. 5: If you award damages to plaintiff's subcontractor, what percentage is plaintiff entitled to as markup for overhead and profit on the amount of those damages?
Answer: _____percentage.

[629] Ordinarily, exhibits admitted for illustrative purposes are not substantive evidence and do not go to the jury room. *See* Arnold v. Riddell, Inc., 882 F. Supp. 979, 995 (D. Kan. 1995).

iv. Excluding Evidence.—Counsel should consider whether evidence proffered by opposing counsel may be excluded by the court as a matter of law. For example, there is some authority, although slight, that expert testimony as to the cause and effect of construction delays is not admissible, because the subject matter is not beyond the common knowledge of the jury.[630] Defense counsel should also consider excluding the contractor's employees as experts on delay claims.[631] Reports prepared for settlement discussions should not be admissible.[632] Efforts to exclude testimony should be raised by motions in limine.[633]

v. Summaries.—Counsel should consider using summaries of records where the underlying records are so voluminous that it would be impractical to admit them in evidence. To be admissible in summary form, the underlying records themselves must be admissible, and they must be made available to the opposing party for inspection.[634] Trial courts have wide discretion in determining whether summaries are necessary to expedite the trial, and whether the opposing party had a reasonable opportunity to examine the records.[635]

vi. Trial Preparation for Witnesses.—Witnesses should be provided with general instructions that serve as a guide when they testify.[636] Witnesses must be warned that they must fully understand each question before they answer. The witnesses should be told that they can have a question repeated or rephrased if they do not understand it.

Witnesses should be reminded that they do not have to answer a question "yes" or "no" during cross-examination if they cannot do so. Even if the witness does answer "yes" or "no," he or she may explain the answer. If the examining attorney prevents the witness from explaining the answer, the defending attorney can have the witness explain the answer during the redirect examination.

Witnesses should be advised not to take notes or documents to the witness stand when they testify, or review them in the courtroom before they testify, because the questioning attorney will be entitled to review those materials.[637] Any documents they need should be supplied by their attorney. Finally, the witnesses must be aware that they are expected to be knowledgeable in the areas of the construction project in which they were directly concerned. They do not have to be experts in those areas of responsibility where they rely on the expertise of others, such as a project engineer relying on the expertise of a soils engineer or geologist. But the witness must be able to respond to questions in his or her area of responsibility. Witnesses who have been deposed should carefully review their deposition transcripts before testifying.

vii. Present the Case in Plain English.—Counsel and their witnesses must keep in mind that judges and juries base decisions on their understanding of the relevant facts. Because construction cases are often complex, it is essential that the trier of fact does not become lost in technological details. Present the case in plain English and have the witnesses explain technical terms, using examples as appropriate to illustrate their meaning. But never talk down to the trier of fact. The attorney or witness who speaks in a condescending or oversimplified fashion may alienate the judge or jury and harm his or her case.

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[630] Jurgens Real Estate Co. v. R.E.D. Constr. Corp., 103 Ohio App. 3d 292, 659 N.E.2d 353, 356–57 (1995).

[631] FED. R. EVID. 701.

[632] FED. R. EVID. 408; *but see* Scott Co. of Calif. v. MK-Ferguson, 832 P.2d 1000 (Colo. App. 1991) (employee's analysis of claim's worth entitled "Settlement Detail" was not an offer of settlement within scope of Rule 408 but was a report prepared in ordinary course of business, and was admissible).

[633] *See* "Pre-Trial Motions," sub.D.6.c, *supra*.

[634] FED. R. EVID. 1006.

[635] C.L. Maddox, Inc. v. The Benham Group, Inc., 88 F.3d 592, 601 (8th Cir. 1996) (admission of summaries of business records was within trial court's discretion; all underlying information was available to opposing party as required by rule).

[636] *See generally* 5 AM. JUR. *Trials* § 888-906 (1965).

[637] FED. R. EVID. 612.

APPENDIX[638]

List of Affirmative Defenses

Denial of liability on the merits
Engineer's determination of claims final
Waiver or release of claim rights
No notice of potential claim
Failure to give proper, detailed, and timely notice required by contract
Extra work not ordered in writing
Work performed was beyond the scope or requirements of the contract
Failure to protest written change order
Subject matter of claim covered by an executed change order
Failure to comply with or fulfill condition precedent provisions of the contract
Failure to submit contemporaneous records
Claim compromised and released
An election to perform work knowing it was misrepresented by the contract
Negotiation of final pay warrant releasing any and all claims without reservation
Payment
Bid submitted without seeking clarification or interpretation of contract provisions
Estimated quantities approximate only
Failure to cooperate with other forces
Assumption of the risk of unforeseen difficulties
Superior knowledge and expertise
Duty to examine plans, specifications, and work site and satisfy himself as to conditions
Voluntary selection of the method of performance
Statute of limitations
Statute of frauds
Failure to mitigate damages
Failure to comply with claims statute
Failure to exhaust contractual remedies
Unjust enrichment
No damage
No damages for delay clause (time extension only)
Subcontractor's damage without liability (*Severin* Doctrine)
Collateral source rule
Damages consequential in nature
Damages as a result of inefficiencies and matter of the contractor's control and responsibility
Failure to mitigate damages
Damage or delay caused by the contractor
Acts of the engineer beyond scope of authority
Oral modifications of the contract
Oral promises or representations
Acts beyond delegated responsibilities
Violations of law or contract
No contractor's license
Subcontracting in violation of the contract or law
Violation of prequalification statutes or regulations
Claim sounds in tort
Failure to comply with public tort claims statutes
Sovereign immunity
Failure to state a cause of action or claims

[638] Affirmative defenses reproduced from *Trial Strategy and Techniques in Highway Contract Litigation, NCHRP Research Results Digest No. 108*, by Orwin F. Finch and Kingsley T. Hoegstedt (1979).

SECTION 7

OWNERS' RIGHTS AND REMEDIES AND ALTERNATIVES TO LITIGATION

A. OWNERS' RIGHTS AND REMEDIES

1. Introduction

Owners are entitled to have their construction contracts fully performed. A contractor's failure to perform is a breach of contract, entitling the owner to damages.[1] Generally, an owner's damages for breach are of two types: damages for delayed performance and damages for defective performance.Damages for delayed performance are usually addressed by a liquidated damage clause in the construction contract as discussed earlier.[2] The second type of damages, defective performance, and other related issues are discussed in this subsection.

2. Contract Performance

As a general rule, contractors must strictly comply with contract specifications.[3] The owner is entitled to receive full performance with the contract specifications, even if that exceeds what is necessary for a satisfactory result.[4] In addition, the strict compliance rule enhances the integrity of the competitive bidding system by requiring contractors to bid on the basis of meeting contract requirements.[5]

The strict compliance rule, however, is not absolute. Once the work is complete, the rule is tempered by the doctrine of substantial completion. Under this doctrine, the owner is legally required to accept nonconforming work in exchange for a reduction in the contract price.[6]

Substantial completion of a construction contract occurs where the work is substantially complete and the structure or facility can be used for its intended purpose.[7] The contract may define when substantial completion occurs. For example, the WSDOT defines substantial completion as work that, "has progressed to the extent that the Contracting Agency has full and unrestricted use and benefit of the facilities both from the operational and safety standpoint and only minor incidental work…remains to physically complete the total contract."[8]

Substantial completion has other legal consequences in addition to allowing the contractor to recover for the value of its work. Liquidated damages are not assessed after substantial performance has occurred.[9] Once substantial completion is achieved, liquidated damages may be reduced, and further overruns in contract time are assessed based on direct engineering and other related costs until all of the contract work has been physically completed.[10] Another consequence is that once substantial completion is achieved, the contract cannot be terminated for default.[11]

The doctrine of substantial completion is an equitable doctrine, designed to avoid forfeiture[12] and economic waste.[13] The doctrine only applies where the contractor acted in good faith, and its failure to perform fully was not intentional.[14]

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[1] Failure to perform any term of the contract, no matter how minor, is a breach, entitling the owner to at least nominal damages. 4 ARTHUR CORBIN, CORBIN ON CONTRACTS § 946 (1951); Delta Envir. v. Wysong & Miles Co., 510 S.E.2d 690, 698 (N.C. App. 1999) (nominal damages can be $1).

[2] *See* "Owner's Remedies for Delay," § 5.C.7, *supra*.

[3] United States v. Wunderlich, 342 U.S. 98 (1951); United States ex rel. Compton v. Midwest Specialties, Inc., 142 F.3d 296 (6th Cir. 1998); DiGioia Bros. Excav. v. Cleveland Dep't of Pub. Util., 734 N.E.2d 438 (Ohio App. 1999); R.B. Wright Constr. Co. v. United States, 919 F.2d 1569 (Fed. Cir. 1990); Metric Constructors, Inc. v. United States, 44 Fed. Cl. 513, 523 (1999).

[4] R.B. Wright Constr. Co. v. United States, *Id*.; Am. Elec. Contracting Corp. v. United States, 579 F.2d 602 (Ct. Cl. 1978); J.L. Malone & Assocs. v. United States, 879 F.2d 841 (Fed. Cir. 1989); CORBIN, *supra* note 1, § 946. Owner entitled to reject shop drawings that do not strictly comply with contract specifications. McMullan & Son, Inc., ASBCA 21159, 77-1 BCA ¶ 12, 453 (1977).

[5] Troup Bros. v. United States, 643 F.2d 719, 723 (Ct. Cl. 1980). Bids that do not comply with the invitation for bids are nonresponsive. George Harms Constr. Co. v. Ocean County Sewerage Auth., 394 A.2d 360 (N.J. Super. Ct. App. 1978).

[6] Ujdar v. Thompson, 878 P.2d 180 (Idaho App. 1994); Ahlers Bldg. Supply v. Larsen, 535 N.W.2d 431 (S.D. 1995); 3A ARTHUR CORBIN, CORBIN ON CONTRACTS § 701 (1951); 13 AM. JUR. 2D *Building and Construction Contracts* § 46 (2000); 5 WILISTON ON CONTRACTS § 805 (3d ed. 1962); Granite Constr. Co. v. United States, 962 F.2d 998 (Fed. Cir. 1992), *cert. denied*, 506 United States 1048 (1993); Hannon Elec. Co. v. United States, 31 Fed. Cl. 135 (1994); Kirk Reid Co. v. Fine, 139 S.E.2d 829 (Va. 1965).

[7] Granite Constr. Co. v. United States, *Id*.; Restatement, Contracts (Second) § 348; Annotation, 41 A.L.R. 4th 131 (1985); 13 AM. JUR. 2D *Building and Construction Contracts* § 48 (2000).

[8] Washington DOT Standard Specification 1-08.9.

[9] Phillips v. Hogan Co., 594 S.W.2d 39 (Ark. App. 1980); Great Lakes Dredge & Dock Co. v. United States, 96 F. Supp. 923 (Ct. Cl. 1952); Lindwall Constr. Co., ASBCA No. 23,148, 79-1 BCA ¶ 13,822 (1979); Paul H. Gantt & Ruth Brelaver, *Liquidated Damages in Federal Government Contracts*, 47 B.U.L. REV. 71 81–82 (1967); Robert S. Peekar, *Liquidated Damages in Federal Constructions Contracts*, 5 PUB. CONT. L. J. 129, 146 (1972).

[10] For example, *see* Kansas DOT Standard Specification 1.08.08 (1996); North Dakota DOT Standard Specification 1.08.04 (1997); Washington State DOT Standard Specification 1.08.09 (2000).

[11] Olson Plumbing & Heating Co. v. United States, 602 F.2d 950 (Ct. Cl. 1979). However, if a contractor refuses to complete punch list work, or the corrections are unduly prolonged, the contractor may be deemed to have abandoned the contract. *Appeal of* F&D Constr. Co., ASBCA No. 41,441 91-2 BCA, ¶ 23, 983 (1991).

[12] Stevens Constr. Corp. v. Carolina Corp., 217 N.W.2d 291 (Wis. 1974).

[13] Granite Constr. Co. v. United States, 962 F.2d 998 (Fed Cir. 1992), *cert. den.*, 506 U.S. 1048 (1993). Economic waste is discussed in subpart 3A *infra*.

[14] 13 AM. JUR. 2D *Building and Construction Contracts* § 47; 41 A.L.R. 4th 131, 189.

3. Common Contract Disputes

Transportation projects are complex undertakings that often create conflicts and misunderstandings. Claims and disputes cannot always be avoided. Today's contract disputes may involve right-of-way, environmental issues, different site conditions, delays caused by change orders, interferences, extra work, stop orders, utility relocation, ambiguous contract provisions, changes in design and specifications, extra work, conflicts with other contractors, shop drawing and approval delays, permit conditions, and liquidated damages. Research by the construction industry has found that construction disputes arise from three major sources: project uncertainty, process problems, and people issues.[15]

4. Remedies for Defective Performance

a. Repair or Replacement of Defective Work

The general measure of damages for defective performance is the lesser amount of either: 1) the reasonable cost of remedying the defects or omissions, or 2) the difference between the market value of the performance actually rendered and the market value of what the owner would have received, if the contract had been fully performed.[16]

But what if the structure or facility has no market value? This is usually the case with respect to most public improvements such as bridges and highways, because they are not bought and sold and therefore have no market value.[17] In such cases, the market value rule does not apply, and the public owner is entitled to recover damages based on the reasonable cost of remedying the defects or omissions.[18] The application of the "cost to remedy" rule will not apply where the cost would be so clearly unreasonable as to constitute "economic waste."[19] However, the doctrine of economic waste does not apply where the defects or omissions affect the integrity of the structure.[20] Also, there can be no substantial performance where the defect is structural, because the defect affects the soundness of the building and its use for its intended purpose.[21] In the absence of substantial performance, the owner may only be liable in *quantum meruit* to the extent that the work performed has some actual value to the owner.[22] But some courts have denied the contractor any recovery.[23]

The owner is obligated to specify the items of work that have to be corrected and provide the contractor with a reasonable opportunity to correct them.[24] A refusal by the owner to allow the contractor a reasonable opportunity to correct the defects is a breach and may waive the defects.[25]

The determination of damage of lost value of the work has often been difficult.

An important analysis of damages in the construction context is provided by *Commercial General Contractors, Inc. v. United States*.[26] In that case, the U.S. Army Corps of Engineers had contracted with Commercial General (CCI) to build portions of a flood control channel, which involved excavation, pouring of concrete, and backfill. After completion of the work, CCI filed several claims for extra compensation, and the government counterclaimed, asserting violation of the False Claims Act. Although this particular case involves false claim issues, it also provides an excellent discussion of the issues surrounding damage determinations.

The Federal Circuit court found that CCI had built the channel shorter than specified in the contract to avoid difficult work, and had knowingly submitted false

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[15] Former FHWA Federal-Aid Highway Program Manual of 1991, at 38. For additional background on this publication and its current equivalent, *see* Section 1 of this volume, at note 12 and accompanying text. *See also* FHWA Federal Policy Guide available at http://www.fhwa.dot.gov/legsregs/directives/fapgtoc.htm, last accessed July 22, 2012.

[16] Spring Indus. v. Ohio Dep't of Transp., 575 N.E.2d 226 (Ohio App. 1990) (reduction in contract price based on market value of nonconforming asphalt); State Property and Bldg. Com. v. H.W. Miller Constr. Co., 385 S.W.2d 211 (Ky. 1964) (damages for defective construction of state office building based on reduction in market value); 13 AM. JUR. 2D *Building and Construction Contracts* § 80; Annotation, 41 A.L.R. 4th 131; Restatement (Second) Contracts § 348 (1981); Commercial Contractors v. United States, 154 F.3d 1357 (Fed. Cir. 1998).

[17] Annotation, 31 A.L.R. 5th 171 (1995); Tuscaloosa County v. Jim Thomas Forestry Consultants, 613 So. 2d 322 (Ala. 1992); Department of Transp. v. Estate of Crea, 483 A.2d 996 (Pa. Commw. 1977); Shippen Township v. Portage Township, 575 A.2d 157 (Pa. Commw. 1990).

[18] Granite Constr. Co. v. United States, 962 F.2d 98 (Fed. Cir. 1992), *cert. den.*, 506 U.S. 1048 (1993). Commercial Contractors v. United States, 154 F.3d 1357 (Fed. Cir. 1998); Restatement (Second) Contracts § 348 (1981); Rhode Island Turnpike and Bridge Auth. v. Bethlehem Steel Corp., 379 A.2d 344 (R.I. 1977) (cost to correct defective painting on bridge did not constitute "economic waste," even though cost was approximately 25 percent of $19 million contract price).

[19] Economic waste occurs when the cost of remedying defects is clearly disproportionate to the probable loss in value caused by the defects. Commercial Contractors v. United States, 154 F.3d 1357 (Fed Cir. 1998); Restatement (Second) Contracts § 348 (1981).

[20] *Id*.

[21] O.W. Grun Roofing & Constr. Co. v. Cope, 529 S.W.2d 258 (Tex. Civ. App. 1975); Spence v. Ham, 57 N.E. 412 (N.Y. 1900). Commercial Contractors v. United States, *id*. at 1372 ("structural defects are deemed to cause such a great loss in value that the cost of remedying such defects is almost never considered to be out of proportion to that loss").

[22] 13 AM. JUR. 2D *Building and Construction Contracts* § 84; Annotation, 41 A.L.R. 4th 131.

[23] *See* cases collected in Annotation, 41 A.L.R. 4th at 139–42.

[24] Hartford Elec. Applicators of Thermalux, Inc. v. Alden, 363 A.2d 135 (Conn. 1975).

[25] Carter v. Kruger, 916 S.W.2d 932 (Tenn. Ct. App. 1995).

[26] 154 F.3d 1357 (Fed. Cir. 1998); cited and discussed in FALSE CLAIMS IN CONSTRUCTION CONTRACTS, FEDERAL, STATE AND LOCAL 74–75 (Charles M. Sink & Krista L. Pages eds., American Bar Association, 2007).

claims for the noncompliant work. The court further found that CCI had knowingly backfilled the channel with construction debris, contrary to the prohibition in the contract, and had improperly heated concrete test cylinders and knowingly submitted claims for work violating contract quality requirements.

The trial court indicated that if it was not possible for the injured party to prove the loss of value caused by the contractor's deficient performance, damages could be computed on an alternative basis. The CCI court indicated it was difficult to determine the loss of value because no competitive private-sector market exists for flood control channels that would establish commercial prices or values for such channels. The court focused instead on the cost to remedy the construction defects, determined that the damages for the improperly shortened channel should be measured by the full cost to repair the channel, and determined that damages for the improper use of debris backfill would be the full cost of removing the construction debris and rebuilding the affected sections of the channel.[27]

The Federal Circuit affirmed the trial court's findings on the majority of damages, but reversed the trial court's decision on damages for defective concrete testing, stating that

> an injured party is not entitled to recover the full replacement costs for any deviation from the exact terms of the contract, however minor. In the unusual case in which actual cost cannot be ascertained, the injured party may recover the replacement cost, but only, if that cost is not clearly disproportionate to the probable loss in value caused by the defects in question.[28]

The appellate court reversed the trial court's damage award on damages for defective concrete testing because the government was unable to show that the quality control violations affected the structural integrity of the channel, and the cost of tearing down and rebuilding the affected portions was clearly disproportionate to the probable loss in value caused by CCI's deficient work.

b. Reduction in the Functional Life of the Improvement

Public owners should be entitled to recover for the reduction in the functional life of an improvement when repairs are not feasible. One example is a paved road. Under normal wear and tear, the road should be useable for a certain number of years before it has to be repaved.

Assume for example that a road that is properly constructed has a functional life of 20 years. Assume further that defects in the surface of the road have reduced the road's functional life to 15 years. In this sense, the road's value has been reduced by 25 percent (functional life: 15 years instead of 20 years, or 25 percent of what it should have been). To make the owner whole, it should be entitled to a 25 percent reduction in the contract price.[29]

An alternative to a reduction in the contract price is an agreement by the contractor to repave the road at its own expense if the road wears out sooner than it should. An agreement of this type should be guaranteed by a commercial surety bond in case the contractor is no longer in business when the road wears out.

c. Disincentive Specifications as Liquidated Damages for Defective Work

Another variation in quantifying damages for substandard work is the use of disincentive clauses. Disincentive clauses establish the outer limits of performance: work that is superior and work that is unacceptable. The specification establishes a graduated payment schedule for work between those two levels. Payment for work that is substandard but acceptable will be reduced in accordance with the graduated payment schedule. Those downward adjustments are applied to the unit bid price, reducing the amount paid for the work.[30]

The legal question that the use of disincentive clauses raises is whether such clauses are a penalty and thus unenforceable, or liquidated damages and thus enforceable. For example, in *Complete General Construction v. Ohio Department of Transportation*, the specifications for the construction of concrete pavement provided that the contractor was to be paid in proportion to the degree that the work complied with the standard specifications in the contract.[31] Under this provision, the contractor was paid less than the contract price when the work failed to meet minimum acceptable standards. The contractor sued, claiming that the disincentive clause was a penalty, and thus unenforceable. The court disagreed, holding that the clause was a valid liquidated damage clause.

A disincentive clause, to be enforceable, must be a reasonable means of estimating damages that cannot otherwise be easily computed. A disincentive clause that is found to be a penalty is void, and the owner must prove actual damages.[32] In this regard, care should be taken in justifying and quantifying the liquidated damage provisions.[33]

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[27] *Id*. at 1372.

[28] *Id*. at 1373-75.

[29] Black Top Paving Co. v. Department of Transp., 466 A.2d 774 (Pa. Commw. 1983) (credit assessed for nonconforming work).

[30] 3 ORRIN F. FINCH, *Legal Implications in The Use of Penalty and Bonus Provisions in Highway Construction Contracts: The Use of Incentive and Disincentive Clauses as Liquidated Damages for Quality Control and for Early Completion, in* SELECTED STUDIES IN HIGHWAY LAW 1582, n.80 (hereinafter FINCH); *see also* Transportation Research Record 1056 for a collection of technical papers on statistical quality control.

[31] 593 N.E.2d 487 (Ohio Ct. Cl. 1990).

[32] State of Ala. Hwy. Dep't v. Milton Constr. Co., 586 So. 2d 872 (Ala. 1991).

[33] FINCH, *supra* note 30, at 1582, n.83.

d. Administrative Setoffs

The cost of remedying defective work may be withheld by the owner from money owed to the contractor, usually from contract payments or retainage. This is a form of "self-help" recognized by the common law as an administrative setoff. The Government has the same right as any creditor to setoff debts owed the Government by the contractor against an indebtedness that the Government owes the contractor.[34]

Standard contract provisions in all New York State contracts provide for an administrative set off. The N.Y. provision provides:

> The State shall have all of its common law, equitable and statutory rights of set–off. These rights shall include, but not limited to, the State's option to withhold for the purposes of set-off, any monies due or that may become due to the Contractor under this Contract up to any amounts due and owing to the State under this Contract, any other Contract with any State department or agency, including any contract for a term commencing prior to the term of this Contract, plus any amount due and owing to the State for any other reason including, without limitation, tax delinquencies, or monetary penalties relative thereto. The State shall exercise its set-off rights in accordance with normal State practices, including, in case of set-off to an audit, the finalization of such audit to the appropriate State agency, its representatives, or the New York State Comptroller.[35]

Wisconsin DOT administratively exercises its common law rights to set off without specific contract authority. NCHRP Legal Research Digest 55, *Identification, Prevention, and Remedies for False Claims in Highway Improvement Contracting*, recommended consideration be given to modifying standard contract provisions to include express contractual authorization for recouping of costs of false claim investigative efforts through appropriate deduction from contract payments.

The right extends to setoffs between separate contracts that the owner has with the contractor.[36] The deduction may be made even though the debt owed by the contractor is unliquidated and arose from a separate transaction.[37] The contractor can challenge the setoff, and a board or court can determine whether the withholding was proper. This protects the contractor against withholdings that are unwarranted or improper.[38] Deductions should be reasonably prompt so that the contractor's position with its subcontractors is not prejudiced.[39]

The right to setoff has some limitations. The right does not extend to contract payments owed to a performance bond surety for completing the contract after the original contractor has defaulted.[40] "When the surety pays construction expenses under its performance bond obligations, it receives the contract proceeds free from setoff by the government, because the surety receives the proceeds as a subrogee of the government as well as the contractor."[41] The government, however, is entitled to setoff debts owed by the original contractor against contract proceeds claimed by the surety under its payment bond.[42]

The rule that the payment bond surety's claim to contract proceeds is subordinate to an owner's right of setoff does not apply to contract retainage withheld by an owner for the benefit of subcontractors, materialmen, and laborers. When a surety pays those claimants after the contractor has failed to pay them, the surety is subrogated to the claimant's rights to the retainage. That right of subrogation is superior to the owner's right of setoff against the contract retainage.[43] Whether a surety can enforce that right against a state agency holding retainage depends upon whether the state has waived sovereign immunity.[44]

5. Unauthorized Acceptance of Defective Work

Ordinarily, project inspectors are not authorized to alter the contract by accepting work or materials that do not conform to contract specifications. Usually, the authority to change or modify the contract is vested in the engineer for state construction contracts,[45] and in

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[34] United States v. Munsey Trust Co. of Washington, D.C., 332 U.S. 234 (U.S. Ct. Cl. 1947); Cecile Indus. v. Cheney, 995 F.2d 1052 (Fed. Cir. 1993).

[35] Office of the New York State Attorney General, Schedule A, Required Clauses [for State contracts].

[36] Mega Constr., Inc. v. United States, 29 Fed. Cl. 396 (1993); Dale Ingram, Inc. v. United States, 475 F.2d 1177 (Ct. Cl. 1973); Project Map, Inc. v. United States, 486 F.2d 1375 (Ct. Cl. 1973).

[37] Warren Little & Lund v. Max J. Kuney, 796 P.2d 1263 (Wash. 1990); *but see* H.J. McGrath Co. v. Wisner, 55 A.2d 793 (Md. 1947) and Eyer v. Richards & Conover Hardware Co., 55 P.2d 60 (Okla. 1936).

[38] Philco Constr. Co., DOTCAB 67-33, 68-2 BCA ¶ 7110 (1968).

[39] Southwest Eng. Co., NASA 87-4 BCA 2515, 68-1 BCA 6977 (1968). Public works "Prompt Pay" acts may require the agency to notify the contractor within a specified number of working days that payment is being withheld. *See, e.g.,* WASH. REV. CODE 39.76.011(2)(b).

[40] Aetna Cas. & Sur. Co. v. United States, 435 F.2d 1082 (5th Cir. 1970); Trinity Universal Ins. Co. v. United States, 382 F.2d 317 (5th Cir. 1967); Morrison Assur. Co. v. United States, 3 Ct. Cl. 626 (1983).

[41] Morrison Assur. Co., *id*. at 632.

[42] United States v. Munsey Trust Co., 332 U.S. 234 (1947).

[43] Nat. Sur. Corp. v. United States, 118 F.3d 1542 (Fed. Cir. 1997).

[44] Liberty Mutual Ins. Co. v. Sharp, 874 S.W.2d 736 (Tex. App. 1994) (suit by surety against state agency for agency setoff against retainage dismissed based on sovereign immunity); *see* § 6.21.A., *supra*, containing a table listing the states that have waived sovereign immunity.

[45] AASHTO Guide Specification 104.03 (1998); Arizona DOT Specification 104.04 (1996); California DOT Specification 104.4 (1996); California DOT Specification 4.10.3 (1995); Florida DOT Specification 4.3.2.1 (1996); Texas DOT Specification 10.3.2(B) (1996).

the contracting officer for federal construction contracts.[46]

As a general rule, the Federal Government and state governments are not bound by the unauthorized acts of their representatives.[47] The doctrine of "apparent authority," which allows private parties to be bound by the unauthorized acts of their agents, clothed with apparent authority to act on their behalf, does not apply to federal and state governments.[48]

However, an unauthorized acceptance may bind the government, if it is ratified by a person whose actual authority is to accept nonconforming work or materials.[49] Ratification occurs when the ratifying contract official has knowledge of the unauthorized acceptance and expressly or impliedly approves the acceptance.[50] However, ratification will not be applied where the contractor does not prove that the person with authority to bind the government had knowledge of the unauthorized acceptance and either expressly or tacitly approved it.[51]

The unauthorized acceptance may be used by the contractor as proof that its interpretation of the specification, which coincided with the inspector's, was reasonable.[52] The contractor is entitled to perform in accordance with its interpretation of the contract, provided that its interpretation was reasonable.[53]

6. Latent Defects

Contract specifications usually address defects in construction discovered after final acceptance has occurred. Some specifications reflect the common law rule that final acceptance, without any reservations, waives defects in construction that the owner knew about, or could have discovered by the exercise of reasonable care.[54] Only patent defects are waived; latent defects survive acceptance because they are unknown and therefore cannot be voluntarily waived.[55]

Contract specifications, based on the common law rule, typically provide that acceptance is final and conclusive except for latent defects, fraud, gross mistake amounting to fraud, or rights under contract warranties.[56] Under this type of clause, the owner has no remedy for defects discovered after final acceptance unless the defect is latent, the result of fraud, or covered by warranty.[57]

Some states include "anti-waiver" provisions in their contracts. These specifications negate any inference that patent defects are waived because of final acceptance. For example, the specification may provide that:

> The Department shall not be precluded or estopped by any measurement, estimate, or certificate made either before or after the completion and acceptance of the work and payment therefor, from showing the true amount and character of the work performed and materials furnished by the contractor, nor from showing that any such measurement, estimate, or certificate is untrue or is incorrectly made, nor that the work or materials do not in fact conform to the contract. The Department shall not be precluded or estopped, notwithstanding any such measurement, estimate, or certificate and payment in accordance therewith, from recovering from the contractor or his sureties, or both, such damage as it may sustain by reason of his failure to comply with the terms of the contract. Neither the acceptance by the Department, or any representative of the Department, nor any payment for or acceptance of the whole or any part of the work nor any extension of time, nor any possession taken by the Department, shall operate as a waiver of any portion of the contract or of any power herein reserved, or of any right to damages. A waiver of any breach of the contract shall not be held to be a waiver of any other or subsequent breach.[58]

Under this type of specification, the owner does not waive its right to damages for patent defects discovered after final acceptance. To establish waiver, the contractor must prove that the owner intentionally waived the defect by accepting the work without reservation.[59] "Anti-waiver" clauses reveal the intent of the parties to

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[46] 48 C.F.R. 43.102(A).

[47] MCQUILLIAN, MUNICIPAL CORPORATIONS § 29.04 (3d ed.); Noel v. Cole, 655 P.2d 245 (Wash. 1982); ECC Intern. Corp. v. United States, 43 Fed. Cl. 359 (1999); Williams v. United States, 127 F. Supp. 617 (Ct. Cl. 1955).

[48] Noel v. Cole, *id*.; Williams v. United States, *id*.

[49] Dan Rice Constr. Co. v. United States, 36 Fed. Cl. 1 (1996); Dolmatch Group Ltd. v. United States, 40 Fed Cl. 431 (1998).

[50] Aero-Arbe, Inc. v. United States, 39 Fed. Cl. 654 (1997); Williams v. United States, 127 F. Supp. 617 (Ct. Cl. 1995).

[51] EWG Assocs., Ltd. v. United States, 231 Ct. Cl. 1028 (1982); United States v. Beebe, 180 343 (1901); Dolmatch Group Ltd. v. United States, 40 Fed. Cl. 421 (1998); Restatement (Second) Agency, § 91 (1957).

[52] Canupp Trucking, Inc., Comp. Gen. Dec., B-261127 (1996).

[53] Constructors Metric, Inc. v. United States, 44 Fed. Cl. 513 (1999) (court rejected contractor's interpretation of specifications as unreasonable).

[54] 13 AM. JUR. 2D *Building and Construction* § 63; Mt. View Evergreen/Improvement and Service Dist. v. Casper Concrete Co., 912 P.2d 529 (Wyo. 1996); United States v. Lembke Constr. Co., 786 P.2d 1386 (9th Cir. 1986); Stevens Constr. Corp. v. Carolina Corp., 217 N.W.2d 291 (Wis. 1974); United Technologies Corp. v. United States, 27 Fed. Cl 393 (1992).

[55] United Technologies v. United States, *Id*.; Mastor v. David Nelson Constr. Co., 600 So. 2d 555 (Fla. App. 1992); Shaw v. Bridges-Gallagher, Inc., 528 N.E.2d 1349 (Ill. App. 1988).

[56] 48 C.F.R. ch. 1, 52.246-12; Georgia DOT Standard Specification 107.20; Arkansas DOT Standard Specification 107.20.

[57] United States v. Lembke Constr. Co., 786 P.2d 1386 (9th Cir. 1986).

[58] Nebraska DOT Standard Specification 107.18; Washington DOT Standard Specification 1-07.27.

[59] V.P. Owen Constr. Co. v. Dunbar, 532 So. 2d 835 (La. App. 1988).

eliminate the binding effect of final acceptance of the work.[60]

One survey revealed that claims made by some States for defective work discovered after final acceptance were either settled administratively or shortly after litigation commenced.[61] There are probably various reasons why contractors chose to settle. First is the contractor's desire to maintain its reputation and good will with the agency. A second reason is the merits of the agency's claim. The contractor, of all the parties, should be able to recognize whether the work is defective. Third is the cost of litigation, if the claim is not settled. And finally, in most cases, it is probably cheaper for the contractor to effect repairs than to pay the owner the cost of having someone else do the work.

In the absence of an "anti-waiver" clause, the key determination in most litigation involving defects discovered after final acceptance is whether the defect was patent or latent.[62] This is largely a matter of proof. The owner, to establish liability, must prove that the defect was latent, that it existed before final acceptance, and did not occur after the project was accepted.[63]

7. Statutory Time Limitations as a Bar to Recovery for Construction Defects Discovered After Final Acceptance

a. Statutes of Limitation and Statutes of Repose—How They Differ

Statutes of limitation and statutes of repose are similar in that both prescribe time periods within which lawsuits must be commenced. They differ as to when the time periods begin to run.[64] A statute of limitations usually begins to run when the claim accrues. Generally, a claim accrues when a claimant or potential claimant knew or should have known, through reasonable diligence, that it had a claim for which relief from a court could be sought.[65]

A statute of repose begins to run from a certain event specified in the statute.[66] Statutes of repose that apply to improvements to real property usually specify substantial completion of the improvement as the event that causes the statute to run.[67] Once the statutory time period has elapsed, the claim is extinguished and cannot be revived.[68] A statute of repose reflects a legislative policy determination that, "a time should come beyond which a potential defendant will be immune from liability for his past acts and omissions."[69]

Under a statute of limitations, a contractor is subject to potential liability until the claim accrues and the time period for commencing suit has elapsed.[70] Under a statute of repose, any liability for construction defects is extinguished once the time period has run even though the owner is unaware that it has been damaged, because the defect did not manifest itself until after the statutory period had elapsed.[71] In short, time ran out before the owner had an opportunity to pursue relief for the defect.[72]

Whether a particular statute is a statute of limitations or a statute of repose is a question of statutory construction.[73] Usually, a statute is characterized as a statute of repose if the statutory period for commencing suit is triggered by the occurrence of an event, irrespective of whether the potential plaintiff knew or should have known that he or she had a cause of action.[74]

> We recognize the fundamental difference in character of [the statute of repose] provisions from the traditional concept of a statute of limitations. Rather than establishing a time limit within which action must be brought, measured from the time of accrual of the cause of action, these provisions cut off the right of action after a specified time measured from the delivery of a product or the completion of work. They do so regardless of the time of the accrual of the cause of action or of notice of the invasion of a legal right.[75]

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[60] Metropolitan Sanitary Dist. of Greater Chicago v. Anthony Pontarelli & Sons, Inc., 288 N.E.2d 905, 915 (Ill. App. 1972).

[61] D.W. HARP, LIABILITY OF CONTRACTORS TO STATE TRANSPORTATION DEPARTMENTS FOR LATENT DEFECTS IN CONSTRUCTION AFTER PROJECT ACCEPTANCE (National Cooperative Highway Research Program Legal Research Digest No. 39, 1997). The article lists 16 states that have had projects with latent defects at some time in the past. Most settled without litigation. A few settled after litigation commenced. None went to trial.

[62] Harris v. Williams, 679 So. 2d 990 (La. App. 1996).

[63] M.A. Mortenson & Co. v. United States, 29 Fed. Cl. 82 (1993).

[64] Corkill v. Knowles, 955 P.2d 438 (Wyo. 1998); Cheswold Volunteer Fire Co. v. Lambertson Constr. Co, 462 A.2d 416 (Del. Super. 1984).

[65] Gibson v. Department of Highways, 406 S.E.2d 440 (W. Va. 1991); Metropolitan Life Ins. Co. v. M. A. Mortenson Cos., 545 N.W.2d 394 (Minn. App. 1996); City of Gerling v. Patricia G. Smith Co., 337 N.W.2d 747 (Neb. 1983).

[66] Corkill v. Knowles, 955 P.2d 438 (Wyo. 1998); Russo Farms, Inc. v. Vineland Bd. of Educ., 675 A.2d 1077 (N.J. 1996); Trinity River Auth. v. URS Consultants, Incorporated-Texas, 889 S.W.2d 259 (Tex. 1994).

[67] *See* table in subpart 60, *infra*, listing events that trigger the statutes.

[68] Com. v. Owens-Corning Fiberglass Corp., 385 S.E.2d 865 (Va. 1989).

[69] *Id*. at 867. *See* Monson v. Paramount Homes, Inc., 515 S.E.2d 445 (N.C. App. 1999).

[70] *See, e.g.,* Bellevue Sch. Dist. v. Braiser Constr. Co., 691 P.2d 178 (Wash. 1984) (suit for construction defects 20 years after improvement was completed).

[71] Com. v. Owens-Corning Fiberglass Corp., 385 S.E.2d 865 (Va. 1989).

[72] Funk v. Wollin Silo & Equip., 435 N.W.2d 244 (Wis. 1989); Corkill v. Knowles, 955 P.2d 438 (Wyo. 1998).

[73] Smith v. Liberty Nursing Home, Inc., 522 S.E.2d 890 (Va. App. 2000).

[74] Corkill v. Knowles, 955 P.2d 438 (Wyo. 1988); Com. v. Owens-Corning Fiberglass, 385 S.E.2d 865 (Va. 1989).

[75] Bauld v. J.A. Jones Constr. Co., 357 So. 2d 401, 402 (Fla. 1978); *see also* Univ. of Miami v. Bogorff, 583 So. 2d 1000, 1003

In addition to the question of how a limitations statute should be classified, there may also be issues regarding the constitutionality of a statute of repose and whether a limitation statute applies to actions brought by a state in its own behalf. These issues are discussed in the following subparts of this section.

b. Constitutionality–Statutes of Repose

Statutes of repose have been declared unconstitutional in a few states on several grounds. First, the statutes have been viewed as providing special immunity from suit to architects, engineers, and contractors without specifying a rational basis for immunity.[76] Second, the statutes denied open access to the courts,[77] without expressing a strong public necessity for the provision.[78] Access was denied because the statute could extinguish a potential cause of action before a person knew that it has been injured by defective or negligent construction.[79]

Several states have reenacted their repose statutes, after the statutes were declared unconstitutional, specifically spelling out the public necessity for their creation.[80] For example, in *Craftsman Builder's Supply v. Butler Mfg*., the court said,

> In enacting that statute, the legislature specifically found that exposing providers to liability after the possibility of injury has become highly remote is a clear social and economic evil in that it creates costs and hardships to providers and citizens of the state which include (1) liability insurance costs, (2) records storage costs, (3) undue and unlimited liability risks during the life of both a provider and an improvement, and (4) difficulties in defending against claims asserted many years after completion of an improvement (citation omitted). To remedy this perceived evil, the legislature enacted Utah Code Ann. § 78—12-25.5, which eliminates an injured party's remedy for injury to person or property arising out of an improvement to real property after a set number of years when the possibility of injury and damage becomes highly remote and unexpected. [81]

The reenacted Florida and Utah statutes have been held constitutional.[82] These jurisdictions now follow the majority of state courts, which hold that statutes of repose are constitutional.[83] One study has revealed that the vast majority of claims brought for design defects were brought within 10 years after the improvement was completed.[84]

c. Nullum Tempus

Under the common law doctrine of *nullum tempus*,[85] a state and its agencies were exempt from statutes of limitations generally applicable in civil lawsuits between private parties.[86] Historically, the *nullum tempus*

(Fla. 1991); Craftsman Builder's Supply v. Butler Mfg., 974 P.2d 1194, 1202 (Utah 1999).

[76] Phillips v. ABC Builders, 611 P.2d 821 (Wyo. 1980); Loyal Order of Moose Lodge 1785 v. Cavaness, 563 P.2d 143 (Okla. 1977); Broome v. Truluck, 241 S.E.2d 739 (S.C. Super. 1978). In McFadden v. Ten-T Corp., 529 So. 2d 192, 198 (Ala. 1988), the court noted that statutes of repose were often the result of lobbying efforts by the American Institute of Architects, the National Society of Professional Engineers, and the Associated General Contractors of America.

[77] Thirty-eight states have open court provisions in their constitutions. Craftsman Builder's Supply v. Mutler Mgf., 974 P.2d 1194, 1204 (Utah 1999) (citing David Schumau, *The Right to a Remedy*, 65 TEMP. L. REV. 1197, 1202, n.25 (1992)). The Utah open courts clause provides in part that, "All courts shall be open and every person…shall have remedy by due course of law." UTAH CONST. art. I, § 11.

[78] *See* Overland Constr. Co. v. Sirmons, 369 So. 2d 572 (Fla. 1979).

[79] Jackson v. Mannesmann Demag Corp., 435 So. 2d 725 (Ala. 1983); Horton v. Goldminer's Daughter, 785 P.2d 1087 (Utah 1989); Kallas Millwork Corp. v. Square D Co., 225 N.W.2d 454 (Wis. 1975).

[80] FLA. STAT. 95.11(3)(c)(1980); WIS. STAT. ANN. 893.89 (1982); UTAH CODE ANN. § 78 – 12-25.5 (1996).

[81] 974 P.2d 1194, 1199 (Utah 1999).

[82] Sabal Chase Homeowners Ass'n v. Walt Disney World Co., 726 So. 2d 796 (Fla. App. 1999); Craftsman Builder's Supply v. Butler Mfg., 974 P.2d 1194 (Utah 1999).

[83] Klein v. Catalano, 437 N.E.2d 514, 524 (Mass. 1982) (court discusses the various public interests that are served by a statute of repose); Rosenberg v. Town of North Bergen, 293 A.2d 662 (N.J. Super. 1972); Arkansas: Carter v. Hartenstein, 455 S.W.2d 918 (1970); Delaware: Cheswold Vol. Fire v. Lambertson Constr., 462 A.2d 416 (Del. Super. 1983); California: Barnhouse v. City of Pinole, 183 Cal. App. 3d 171 (1982); Colorado: Yarbo v. Hilton Hotels Corp., 655 P.2d 811 (Colo. 1983); Georgia: Mullis v. Southern Co. Services, Inc., 296 S.E.2d 579 (1982); Idaho: Twin Falls Clinic & Hospital Bldg. Corp v. Hamill, 644 P.2d 341 (1982); Illinois: Cross v. Ainsworth Steel Co., 557 N.E.2d 906 (Ill. App. 1990); Kentucky: Carney v. Moody, 646 S.W.2d 40 (1983); Maryland: Whiting-Turner Contracting Co. v. Coupard, 499 A.2d 178 (1985); Michigan: O'Brien v. Hazelet & Erdal, 299 N.W.2d 336 (1980); Missouri: Blaska v. Smith & Entzeroth, Inc., 821 S.W.2d 822 (1991); Nevada: Wise v. Bechtel Corp., 766 P.2d 1317 (1988); North Carolina: Lamb v. Wedgewood South Corp., 286 S.E.2d 876 (N.C. App. 1982); Ohio: Gamble Deaconess Home Ass'n v. Turner Constr. Co., 470 N.E.2d 950 (Ohio App. 1984); Pennsylvania: Freezer Storage, Inc. v. Armstrong Cork Co., 382 A.2d 715 (1998); Virginia: Hess v. Snyder Hunt Corp., 392 S.E.2d 817 (1990); Washington: Yakima Fruit & Cold Storage Co. v. Central Heating & Plumbing Co., 503 P.2d 108 (1972). The following law review articles discuss the constitutional implications raised by statutes of repose: 18 CATH. U. L. REV. 361 (1969); 38 VAND. L. REV. 627 (1985); 65 TEP. L. REV. 1101 (1994). See also 25 PUB. CONT. L. J. 1101 (1996).

[84] Gibson v. Department of Highways, 406 S.E.2d 440, 447 (W. Va. 1991) (citing study showing that 99.6 percent of claims for design and defective construction are brought within 10 years).

[85] *Nullum tempus* is derived from "*nullum tempus occurri regi*," which is translated as "time does not run against the King." BLACK'S LAW DICTIONARY 1069 (6th ed. 1990); Rowan Cty. Bd. of Educ. v. U.S. Gypsum, 418 S.E.2d 648, 653 (N.C. 1992); Guaranty Trust Co. of N.Y. v. United States, 304 U.S. 126, 132 (1938).

[86] Department of Transp. v. Rockland Constr. Co., 448 A.2d 1047 (Pa. 1982); Hamilton County Bd. of Educ. v. Asbestospray Corp., 909 S.W.2d 783, 785 (Tenn. 1995); Port Auth. of N.Y. &

doctrine was based upon sovereign power and prerogative.[87] The contemporary *nullum tempus* doctrine is based on public policy: The public should not suffer because its officials failed "to promptly assert causes of action which belong to the public."[88]

Several states have codified the common law rule of *nullum tempus* by enacting statutes that exempt the states from the operation of a statute of limitations unless the statutes, by their terms, expressly include the states.[89] A number of states, however, have taken a different tack by abrogating the *nullum tempus* doctrine, either statutorily or though court decisions. The following table lists each state where the limitations apply to lawsuits brought by the state, unless a pertinent statute expressly excludes a state from the operation of a statute of limitations. Table A provides citations to the applicable statutes or court decisions that have abrogated *nullum tempus*, the applicable limitation period affecting claims for defective construction, and the event that triggers the running of the statute.

N.J. v. Bosco, 475 A.2d 676 (N.J. App. Div. 1984); Colorado Springs v. Timberlane Associates, 824 P.2d 776, 778 (Colo. 1992); "a majority of states, when filing lawsuits in the posture of plaintiffs are immune from statutes of limitations, except where their respective legislatures have decided otherwise." N.J. Educ. Facilities Auth. v. Conditioning Co., 567 A.2d 1013, 1016 (N.J. Super. A.D. 1989).

[87] People v. Asbestospray, 616 N.E.2d 652, 654 (Ill. App. 1993); United States v. Thompson, 98 U.S. 486, 489 (1878).

[88] People v. Asbestospray, *id*.; Shootman v. Department of Transp., 926 P.2d 1200, 1203 (Colo. 1996); State ex rel. Condon v. City of Columbia, 528 S.E.2d 408, 413 (S.C. 2000); Guaranty Trust Co. v. United States, 304 U.S. 126, 132 (1938).

[89] Arizona: Statute 12-510 (1987); Hawaii: Statute 657-1-5; Mississippi: Statute Ann. 51-1.51; Tennessee: Statute 28-1-113; Virginia: Statute 8.01-231; *but see* Com. v. Owens-Corning Fiberglass Corp., 385 S.E.2d 865 (Va. 1989) (state's cause of action extinguished when the time limitation of the statute of repose has run).

Table A.

STATE	*NULLUM TEMPUS* ABROGATED BY:	TIME PERIOD, TRIGGERING EVENT, AND STATUTE
Alaska	STAT. 9.10.120 (1997).	Six years from accrual of cause of action. STAT. 9.10.120 (1997).
California	Civ. Proc. Sec. 345 (1984).	Within 4 years after discovery, but no later than 10 years after substantial completion. Civ. Proc. 337.15 (1982).
Colorado	Abrogated by court decision: *Shootman v. Dept. of Trans*., 926 P.2d 1200 (Colo. 1996).	Within 2 years after claim accrues, but not more than 6 years after substantial completion. REV. STAT. 13-80-104 (2001).
Florida	STAT. ANN. 95.011 (1977).	Four years after defect is discovered or should have been discovered, but not more than 15 years after completion of the contract. STAT. 95.11(c) (1995).
Georgia	CODE ANN. 9-3-1 (1933).	Eight years after contract completion. CODE ANN. 9-3-51 (1968).
Idaho	CODE 5-225 (1881).	Six years from final completion of improvement. CODE 5-241 (1965).
Illinois	CODE 13-214. Use of the term "body politic" in the statute of repose included the state in its coverage. *People v. Asbestospray Corp*., 616 N.E.2d 652 (Ill. App. 1993).	Not more than 10 years from acceptance of the improvement. CODE 5/13-214 (1993).
Kansas	STAT. ANN. 60-521. Limitations do not apply when action arises out of governmental functions. *State ex rel Schneider v. McAfee*, 578 P.2d 281 (Kan. 1978).	Within 5 years after cause of action has accrued. STAT. ANN. 60-511 (1966).
Kentucky	REV. STAT. 413.150. *See Louisville & N.R. Co. v. Siler*, 186 F. 176 (C.C.E.D. Ky. 1911).	Within 10 years from completion. REV. STAT. 413.120.
Massachusetts	GEN. L. 260.18 (1902). *See Com. v. Owens-Corning Fiberglass Corp*., 650 N.E.2d 365 (1995).	Within 3 years after cause of action accrues, but not more than 6 years from the earlier of 1) acceptance of the project; or 2) opening the facility to public use; or 3) acceptance by the contractor of a final estimate prepared by the agency; or 4) substantial completion. GEN. L. 260 § 2.
Minnesota	STAT. 541.01 (1986). *See City of St. Paul v. Chicago M. & St. P. Ry. Co.*, 48 N.W. 17 (Minn. 1891).	Two years after discovery of defect, but not more than 10 years after substantial completion. STAT. 541.051 (1990).
Missouri	REV. STAT. 516.360 (1929).	Within 10 years from completion of improvement, but limitation does not apply if the defect was concealed or resulted in an unsafe condition. REV. STAT. ANN. 25-218 (1991).

Montana	CODE ANN. 27-2-103 (1991).	Not more than 10 years after completion of improvement. STAT. 27-2-208 (1999).
Nebraska	Rev. STAT. ANN. 25-218 (1991).	Within 4 years from discovery, but not more than 10 years beyond the time of the act giving rise to the cause of action. STAT. 25-223 (1976).
New Jersey	Abrogated by court decision: *N.J. Ed. Facilities Auth. v. Gruzen Partnership*, 592 A.2d 559 (1991). Legislature then enacted a 10-year statute of limitations applicable to state claims. STAT. 2A 14-1.1 and .2. *See State v. Cruz Constr. Co*., 652 A.2d 741 (N.J. Super. A.D.) (1995).	Within 10 years from completion of construction. REV. STAT. 2A: 14-1.1 (1998). Limitation does not apply if defect arises from fraudulent concealment or gross negligence. STAT. 2B 14-1-1 B(2).
North Carolina	GEN. STAT. 1-30. Limitation only applies when state acts in a proprietary capacity. *Rowan County Bd. of Educ. v. United States Gypsum Co*., 418 S.E.2d 648 (N.C. 1992).	Within 6 years from breach or substantial completion. STAT. 1-50-(5) A (1996). Limitation does not apply to defects caused by fraud or gross negligence, STAT. 1-50(5)(E).
North Dakota	CODE 28.01-23 (1943).	Not more than 10 years after substantial completion. The time to commence suit is extended 2 years if the injury occurs in the tenth year after substantial completion. CODE 28-01.44 (1989).
Oregon	CODE 28.01-23 (1943).	Within 10 years after substantial completion. REV. STAT. 12.135(1).
South Carolina	Abrogated by court decision: *State ex rel. Condon v. City of Columbia*, 528 S.E.2d 408 (S.C. 2000).	Within 13 years after substantial completion of improvement. STAT. 28-3-202 (1980).
Vermont	STAT. ANN. 461 (1947).	Within 6 years after cause of action accrues. STAT. ANN. 511 (1959). *Univ. of Vermont v. W.R. Grace & Co.* 565 A.2d 1354 (Vt. 1989).
Virginia	Expiration of the period in statute of repose extinguishes cause of action, preventing state from maintaining suit. *Com. v. Owens-Corning Fiberglass Corp.,* 385 S.E.2d 865 (Va. 1989).	Not more than 5 years after performance of construction. CODE ANN. 8-01-250 (1977).
Washington	REV. CODE 4.16.310 (1988). The statute added the state to its coverage, overruling *Bellevue School Dist. No. 405 v. Braizer Const. Co*., 691 P.2d 178 (Wash. 1984), which had applied *nullum tempus*.	Within 6 years after substantial completion of construction. REV. CODE 4.16.310 (1988). See *Gevaart v. Metro Constr. Inc*., 760 P.2d 348, 350 (Wash. 1988), discussing how the 6-year period can be extended.
West Virginia	CODE 55-2-19 (1923). *Gibson v. Dept. of Highways*, 406 S.E.2d 440 (W. Va. 1991).	Within 10 years after acceptance of improvement. Code 55-2-6A (1983).

Wisconsin	STAT. 893.87 (1980). Action by state must be brought within 10 years after cause of action accrues.	Within 10 years from substantial completion. Limitation does not apply to defects resulting from fraud, concealment, or misrepresentation. CODE 893.89 (1994).

The Supreme Courts of Colorado, New Jersey, and South Carolina,[90] as noted in the table, held that the common law doctrine of *nullum tempus* was abrogated when sovereign immunity was waived. Those courts also said that it would be anomalous that a state, which is not protected from suit by sovereign immunity, should be entitled to benefit from *nullum tempus*.

The view that abrogating sovereign immunity also abrogates *nullum tempus* has been rejected by other courts. For example, in *Rowan Cty. Bd. of Educ. v. U.S. Gypsum Co.,* the North Carolina Supreme Court said:

> Further, while USG correctly notes that this Court has expressed an intent to restrict rather than extend application of sovereign immunity (citation omitted), our treatment of that doctrine does not affect our view of nullum tempus, which serves a different purpose. While the two doctrines share a similar "philosophical origin and have a similar effect of creating a preference for the sovereign over the ordinary citizen," (citation omitted) retrenchment on the one does not require retrenchment on the other. While limiting sovereign immunity diminishes the government's escape of its misdeeds, the same concern for the rights of the public supports retention of nullum tempus, as that doctrine allows the government to pursue wrongdoers in vindication of public rights and the public purse.[91]

8. Damage to Structures During Contract Performance

a. Liability for Damage

Generally, destruction of the subject matter of the contract excuses further performance, but only when performance becomes objectively impossible. To excuse performance, the impossibility must be produced by an unforeseen event that could not have been prevented or guarded against by the contractor. The fact that unforeseen events, beyond the contractor's control, make performance more difficult or costly does not excuse performance. The contractor must either perform or respond in damages.[92] To protect itself against unforeseen events, the contractor could purchase builder's risk insurance. The cost of insurance would typically be passed on to the owner as part of the bid price.[93] To reduce bids and encourage competition, owners often include risk sharing clauses in their construction contracts. Such clauses allocate the risk for *force majeure* events.[94]

Typically, these clauses excuse the contractor from responsibility for damages to the work caused by any of the events listed in the clause.[95] To avoid responsibility for damage to work, the contractor must show that the damage caused by one of the enumerated events in the clause was beyond the control of the contractor and did not result from the contractor's negligence.[96]

b. Age and Condition of Structure as Factors in Determining Damages

Generally, public bridges and roads do not have a commercial market value, because ordinarily they are not bought and sold.[97] Because they do not have a market value, the usual rules for determining damages to real property improvements do not apply.[98] If the damage to the structure can be repaired without affecting its integrity and safety, the measure of damages is the cost of repair.[99] If the structure is destroyed, the proper

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[90] Shootman v. Department of Transp., 926 P.2d 1200 (Colo. 1996); N.J. Educ. Facilities Auth. v. Gruzen Partnership, 592 A.2d 559 (N.J. 1991); State ex rel. Condon v. City of Columbia, 528 S.E.2d 408 (S.C. 2000).

[91] 418 S.E.2d 648, 657 (N.C. 1992). While the North Carolina Statute (1-30) applies to actions brought by the State in the same manner as actions brought by private parties, the Statute does not apply if the function that gives rise to the claim is governmental, because when the State acts in a governmental capacity it does not act in the same manner as a private party. *See* 71 N.C. L. REV. 879 (1993).

[92] United States v. Spearin, 248 U.S. 132 (U.S. Ct. Cl. 1918); Kel Kim Corp. v. Central Market, 519 N.E.1d 295 (N.Y. 1987); Kans. Turnpike Auth. v. Abramson, 275 F.2d 711 (10th Cir. 1960); Sornsin Constr. Co. v. State, 590 P.2d 125 (Mont. 1978); 13 AM. JUR. 2D *Building and Construction Contracts* § 64. *See* § 7.B.9, *supra*.

[93] The cost to procure and maintain insurance may be high where the project is located in an area subject to severe storms or earthquakes.

[94] *Force majure* clauses allocate risk. Chase Precast Corp. v. John J. Paonessa Co., 566 N.E.2d 603 (Mass. 1991) (*force majure* clauses allocate and excuse specific risks that might affect performance). For example, "acts of God, the public enemy or governmental authorities," Kansas Standard Specification 107.16.

[95] Standard Specifications: Florida 7.14; Kansas 107.16; South Dakota 7.17; Washington 1-07.13; Donald B. Murphy Contractors v. State, 696 P.2d 1270 (Wash. App. 1985); Reece Constr. Co. v. State Highway Comm'n, 627 P.2d 361 (Kan. App. 1981).

[96] Reece Constr. Co. v. State Highway Comm'n, *id*.; Appeal of Norla Gen. Contractors Corp., ASBCA No. 5695, 59-2 BCA (CCH 2474).

[97] Shippen Township v. Portage Township, 575 A.2d 157 (Pa. Commw. 1990). Annotation: 31 A.L.R. 5th 171 (1995).

[98] Warrick County v. Waste Management of Evansville, 732 N.E.2d 1255 (Ind. App. 2000) (cost of repair or reduction in market value, whichever is lesser).

[99] United States v. State Road Dep't of Fla., 189 F.2d 591 (5th Cir. 1951).

measure of damages is the replacement cost of a similar structure, consistent with current design standards.[100]

The authorities disagree, however, as to whether the replacement cost of a structure should be adjusted to compensate for the age, condition, and utility of the structure. Under one view, the measure of damages for the loss of the structure is the reasonable cost of replacement by a similar structure, consistent with current design standards. The age, condition, and utility of the bridge are inapplicable in calculating damages.[101] Under the other rule, damages are calculated by taking into consideration the structure's age, utility, and condition.[102] These factors are considered in addition to the replacement cost of the bridge.

In addition to damages for loss of the structure, a public agency may seek damages for design costs, engineering costs, and damages to the public for increased road user costs as a result of the structure being unavailable for use.[103] Liquidated damages for the delay in project completion may also be recoverable.[104] These factors are considered in addition to the replacement cost of the bridge.

The contractor may be liable for damage to other property on, or in the vicinity of, the work site, where the damages were a foreseeable consequence of the contractor's failure to protect the work.[105]

9. Owner's Rights Against the Construction Bond Surety

a. Performance and Payment Bonds

All states have laws that require the contractor to obtain performance and payment bonds for public works construction contracts.[106]

Research has found little use of letters of credit to replace performance bonds. However, many design-build and PPP projects are now using letters of credit or 50 percent performance bonding, as discussed in Section 1 of this study.[107]

Essentially, the performance bond is a tripartite agreement composed of the principal (the contractor), the obligor (the surety), and the obligee (the owner).[108] The performance bond protects the owner when the contractor it has retained fails to perform in whole or in part.

Performance and payment bonds are distinguished by the different obligations they impose. Under a performance bond, the surety is responsible when the contractor defaults on its contractual obligations affecting contract performance. As such, a performance bond protects the owner.[109] A payment bond guarantees payment to persons who furnish labor and materials to the general contractor for the public improvement. As such, a payment bond protects subcontractors, laborers, and materialmen.[110] This type of protection is necessary because such persons have no lien rights against public works when the contractor fails to pay them for their labor and materials.[111] A performance bond and a payment bond may be separate instruments,[112] or combined into one instrument.[113]

All conditions precedent specified in a performance bond must be satisfied before the surety's obligation can mature. One of the most significant is the requirement that the owner provide clear notice of default prior to terminating the contractor's rights under the contract. A failure to provide notice would be fatal to asserting a claim under a performance bond.

The terms of the performance bond are of critical importance in the relationship between the surety, obligee (owner), and principal. Performance bond forms should be reviewed and updated by state DOTs or other owners to specify as clearly as possible the surety's options, obligations, and time periods for action. Ancient bond terminology such as "know ye all present…" should be eliminated to reflect the clear purpose of the performance bond: to secure performance and completion of the contract in event of a default. Many bonds forms currently in use omit the word "performance" from the standard form, which may prove problematic in the event of seeking to enforce substitute performance by the surety.

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[100] Department of Transp. v. Estate of Crea, 483 A.2d 996 (Pa. Commw. 1977); Annotation 31 A.L.R. 5th 171 (1995).

[101] Tuscaloosa County v. Jim Thomas Forrestry Consultants, Inc., 613 So. 2d 322 (Ala. 1992); Shippen Township v. Portage Township, 575 A.2d 157 (Pa. Commw. 1990); State Highway Comm'n v. Stadler, 148 P.2d 296 (Kan. 1944); Puget Power & Light Co. v. Strong, 816 P.2d 716 (Wash. 1991).

[102] Vlotho v. Hardin County, 509 N.W.2d 350 (Iowa 1993); Town of Fifield v. St. Farm Mut. Ins. Co., 394 N.W.2d 684 (Wis. 1984); Warrick County v. Waste Management, 732 N.E.2d 1255 (Ind. App. 2000).

[103] *See* State Highway Dep't v. Milton Constr. Co., 586 So. 2d 872 (Ala. 1991) (liquidated damages provided full compensation for delay to ongoing work and as such the State could not recover road user costs).

[104] Southeast Alaska Constr. Co. v. State, 791 P.2d 339 (Alaska 1990).

[105] DSCO, Inc. v. Warren, 829 P.2d 438 (Colo. App. 1991); Beaver Valley Power v. National Eng'g & Contracting, 883 F.2d 1210, 1221 (3d Cir. 1989) (under Pennsylvania DOT Standard Specification 107.12, liability for damages inflicted by the contractor applied only to property within or adjacent to the project site, and not to noncontiguous lands damaged by the contractor; bridge contractor not liable to upstream dam owner for damages caused by cofferdams and high waters).

[106] *See* table in § 2.C, *supra*.

[107] *See, e.g.*, *infra* § 1(d), notes 514 through 517 and accompanying text, of this volume.

[108] Federal Ins. Co. v. United States, 29 Fed. Cl. 302 (1993); Gates Constr. Inc. v. Talbot Partners, 980 P.2d 407 (Cal. 1999).

[109] Morrison Assurance Co. v. United States, 3 Ct. Cl. 626 (1983); United States for Use and Benefit of James E. Simon Co. v. Ardelt-Horn Constr. Co., 446 F.2d 820 (8th Cir. 1971).

[110] Morrison Assurance Co. v. United States, *Id*.

[111] J.S. Sweet Co. v. White County Bridge Comm'n, 714 N.E.2d 219 (Ind. App. 1999).

[112] Miller Act, 40 U.S.C. *et seq*.

[113] *See, e.g.*, WASH. REV. CODE § 39.08.010.

NYSDOT bond forms provide that the surety, if requested by the State DOT, has the option to remedy the default, or take charge and fully perform and complete the work pursuant to the terms and conditions of the contract. The bond further provides that the procedure by which the surety undertakes to discharge its obligation shall be subject to advance written approval of the State DOT. The bond requires notice of the surety's election to remedy the default or perform and complete the contract within 45 days after receipt of notice from the State DOT.

The NYSDOT bond forms further provide that in the event the surety fails to exercise its options, then the State DOT shall give 10 days' notice to the surety and have the work completed pursuant to the provisions of Section 40 of the State's Highway Law. The bond also provides that the surety has the obligation to pay all damages that may result from failure to perform, and to complete the contract, including costs necessary to protect the traveling public, liquidated damages, engineering charges, and all repair and replacement costs necessary to correct construction errors.[114]

After a claim or demand is made on the surety, it has the obligation to make an independent investigation of the situation and determine how to proceed. There is an implied obligation of "good faith and fair dealing" between the surety and obligee.[115] The owner has the obligation to make available pertinent records that will assist the surety in its investigation. The surety should be given access to basic project records, including payment requisitions, retainages, liens, adjusted contract price amounts to date, contract balances, project schedules, time extensions, and other contract documents. The obligee should permit the surety or its expert consultants to visit the project site and discuss basic project information with engineering staff. Delays and denial of record requests often can delay the surety's investigation, and thus delay ultimate project completion.

b. Surety's Options When the Contractor Defaults

A performance bond renders the surety liable up to the penal sum of the bond when the contractor defaults.[116]

Once the surety has completed its investigation, and has considered all the issues, it must decide whether or not to perform, and then communicate its decision to the owner. If the surety decides not to perform, it will prepare to defend its decision in the litigation that will inevitably result. If it decides to perform, it has numerous options.

One of the low-cost options for the surety is to finance the principal's (contractor's) completion of the project by paying its bills as they accrue, if the principal is still in operation and capable of performance. This is an attractive option to the surety if the majority of the work is already complete, if the owner has made no complaints about the quality of the principal's (contractor's) work, and if the surety believes that the default was caused by financial difficulties.[117]

Another option for the surety is a "takeover," driven by the surety's determination that the principal's completion of the contract is no longer possible or prudent. In the takeover, the surety agrees to complete the contract using a different completion contractor. Of most significance, once the surety agrees to take over the contract, its ultimately liability will not be limited to the penal sum of the bond. The surety seeks the owner's approval of a "takeover" agreement. The takeover agreement defines the surety's activities and current and future obligations. The surety will usually demand that provisions in the takeover agreement limit its liability to the penal sum, which is contrary to the general rule that once the surety undertakes to complete the work it is liable for all the cost of completion.[118] Public owners have been successful in not agreeing to this penal sum limit, or agreeing to a provision that preserves all parties' positions for future litigation.

Government attorneys, especially those in agencies which do a high volume of construction business, are in a unique and powerful position in negotiating takeover agreements with surety companies. If negotiations are unsuccessful, and litigation ensues, this could place the surety in jeopardy for existing and future relationships, by placing at risk the surety's ability to continue providing performance bonds acceptable to the agency on future projects.

In *Fidelity & Deposit Co. of Md. v. Bristol Steel & Iron Works, Inc.*,[119] for example, the state highway department defaulted the contractor for his refusal to make repairs on a bridge reconstruction project. The surety denied liability and the highway department disqualified the surety from bonding future state contracts. Subsequently the surety settled with the state and sought indemnification against the principal contractor. The court determined that the surety acted with utmost good faith in protecting the interest of the contractor.[120] In summary, government attorneys should exercise their discretion carefully and responsibly in protecting the public interest.

Terms of the takeover agreement should be closely reviewed by attorneys for the state DOT or other owner prior to execution to determine whether they alter the terms of the basic contract. Public owners are not re-

[114] NYSDOT Standard Specifications, § 103.00.

[115] DUNCAN L. CLORE, BOND DEFAULT MANUAL 31 (2d ed., American Bar Association).

[116] Normally, the surety's liability is limited to the penal sum of the bond. American Home Assurance Co. v. Larkin General Hosp., Ltd., 593 So. 2d 195 (Fla. 1992); United States v. Seaboard Sur. Co., 817 F.2d 956 (2d Cir. 1987); Bd. of Supervisors of Stafford County v. Safeco Ins. Co., 310 S.E.2d 445 (Va. 1983).

[117] CLORE, *supra* note 115, at 115.

[118] *Id.* at 179.

[119] Fidelity & Deposit Co. of Md. v. Bristol Steel & Iron Works, Inc., 722 F.2d 1160 (4th Cir. 1983).

[120] CLORE, *supra* note 115, at 237.

quired even to enter into a takeover agreement, especially if the terms of the contract and performance bond provisions are clear and unambiguous. The surety will seek waivers of liquidated damages, assurances that it will receive all future contract payments, and an amended contract completion date. These provisions should be given careful review so as not to affect the holders of previously filed liens, and other parties who may have rights to contract balances. Public owners often extend contract completion dates and reserve liquidated damage assessments to promote job progress towards the new completion date.

Another option available to the surety is to tender a sum of money to the obligee in full and final settlement of all claims. In some cases, this amount could be less than the penal sum of the bond. The tender ends the surety's obligation quickly and at a fixed cost.

An additional option for the surety is to fulfill its performance obligations by obtaining bids from other contractors to complete the work, and having the low bidder (new contractor) enter into a new contract with the obligee, with a new performance bond to complete the work, and/or paying the obligee its damages and/or the additional cost to complete with this new contractor. The surety would also obtain a full or partial release from the obligee. This would limit the surety's losses, and shift the risk of completion to a new completion contractor. This method is not in wide use by public entities, which fear the loss of federal participation in project costs because the new contractor may not have been chosen through federally mandated bidding requirements. A new completion contractor hired by the surety, however, must be licensed to perform the type of work necessary to complete the contract. Payments by the owner for the work can be made directly to the completion contractor if agreed to by the surety, or to the surety, who then pays the contractor. This procedure may also require serious negotiation over responsibility for defective work and latent defects, but has proven to be successful in non-federally funded projects.

In addition, the contractor can let the owner complete the work and litigate the owner's claim for the cost of completing the contract in excess of the balance of the contract price.

Another option is to arrange for the completion of the work by another contractor, or by the original contractor, when the contractor's cash flow problems prevented it from further contract performance.

c. Surety's Liability for Breach of the Construction Contract that Results in Latent Defects and Other Contractual Defaults

Typically, the construction contract between the owner and the contractor is incorporated by reference into the performance bond.[121] The performance bond and the construction contract are read together to determine the surety's liability for a breach of the construction contract by the contractor.[122] Generally, the surety's liability corresponds with that of its principal. Thus, if the principal (the contractor) can be held liable for breach of the construction contract, so may the surety.[123] A surety may be liable to the owner for latent defects that result from a breach of the construction contract by the contractor.[124]

The surety's liability may extend to other contractual obligations that the contractor failed to perform. For example, in *Hartford Accident and Indemnity Co. v. Arizona Dept. of Transportation*,[125] the court said that the performance bond guaranteed the full performance of the construction contract, which required the contractor to pay unemployment insurance taxes. The surety became liable for those taxes when the contractor failed to pay them. The surety may also be liable for liquidated damages for late completion of the project caused by the original contractor's default,[126] although there is authority to the contrary.[127]

d. Limitations on the Surety's Liability Under Its Performance Bond

As observed earlier, the surety's liability under its performance bond is limited to the penal sum of the bond. This is the general rule,[128] although the surety's liability may exceed the penal sum of the bond if it fails to act reasonably in dealing with the owner's claim.[129] Whether a surety's refusal to pay the owner's claim

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[121] *See* table, § 2.C, *supra*. Hunters Pointe Partners v. U.S.F. & G. Co., 486 N.W.2d 136 (Mich. App. 1992).

[122] Hunters Pointe Partners, *id*.; School Bd. of Pinellas County v. St. Paul Fire & Marine Ins. Co., 449 So. 2d 872 (Fla. App. 1984); City of Gering v. Patricia G. Smith Co., 337 N.W.2d 747 (Neb. 1983).

[123] Ackron Contracting Co. v. Oakland County, 310 N.W.2d 874 (Mich. App. 1983); AgriGeneral Co. v. Lightner, 711 N.E.2d 1037 (Ohio App. 1998).

[124] *See* Hunters Pointe Partners, *id*.; School Bd. of Pinellas County v. St. Paul Fire & Marine Ins. Co., 449 So. 2d 872 (Fla. App. 1984); City of Gering v. Patricia G. Smith Co., 337 N.W.2d 747 (Neb. 1983).

[125] 838 P.2d 1325 (Ariz. 1992); *see also* Employment Sec. Comm'n v. C.R. Davis Contracting Co., 462 P.2d 608 (N.M. 1969), where a similar result was reached.

[126] Pacific Employers Ins. Co. v. City of Berkely, 204 Cal. Rptr. 387 (1984); Grady v. Alfonso, 315 So. 832 (La. App. 1975); Ken Sobol, *Owner Delay Damages Chargeable to Performance Bond Surety*, 21 CAL. W. L. REV. 128 (1984).

[127] American Home Assurance Co. v. Larkin Gen. Hosp., 593 So. 2d 195 (Fla. 1992).

[128] American Home Assurance Co. v. Larkin Gen. Hosp., *id*.; United States v. Seaboard Sur. Co., 817 F.2d 956 (2d Cir. 1987); Dodge v. Fidelity and Deposit Co. of Md., 778 P.2d 1236 (Ariz. App. 1986); Lawrence Tractor Co. v. Carlisle Ins. Co., 249 Cal. Rptr. 150 (1988).

[129] Loyal Order of Moose, Lodge 1392 v. International Fidelity Ins., 797 P.2d 622 (Ak. 1990) (surety has duty of good faith in dealing with owner's claim); Discovery Bay Condominium v. United Pacific Ins. Co., 884 P.2d 1134 (Haw. 1994); Continental Realty Corp v. Andrew J. Crevolin Co., 380 F. Supp. 246 (D. W. Va. 1974).

amounts to bad faith is a question of fact.[130] As noted earlier, the surety's liability may extend beyond the penal sum once it undertakes to complete the project or finance its completion using the principal.[131]

An owner's right to recover against the performance bond surety for latent defects may be affected by a time limit within which the owner must assert its cause of action. A time limit for asserting a cause of action against the performance bond surety may be imposed by a statute or by a provision in the bond. While many states have enacted statutes establishing the limits for bringing actions against contractors for latent defects,[132] few have enacted similar laws dealing specifically with performance bond sureties,[133] although most states have laws establishing a limitation period for actions against the payment bond.[134]

In the absence of a special statute of limitations, a cause of action against the performance bond surety is governed by the general statute of limitations that applies to written contracts.[135] However, unless prohibited by statute,[136] the parties may agree to a time limitation (within which suit must be brought on the performance bond) that is shorter than the general statute of limitations applicable to written contracts.[137] Thus, parties are free to contract for any reasonable limitation period they choose, if it does not conflict with an express limitation in a public bond statute.

> [W]e held that parties could not contract to shorten the one-year limitation period for payment bonds required by the public bond statute. However, in contrast to the provisions governing payment bonds, our public bond statute does not specify a limitation period for performance bonds. Therefore, parties entering into a public performance bond are free to contract for any reasonable limitation period they chose.[138] (citations omitted).

Thus, most cases involving claims against the performance bond are governed by the limitation period specified in the bond.[139] An owner's claim against the contractor for defective construction may be time barred by a statute of repose. Is the claim against the surety barred where the general statute of limitations applicable to a claim against the surety has not expired? There are two views.

Under one view, the owner may sue the surety on the performance bond even though the limitation period in a statue of repose has expired, barring the owner's claim against the contractor.[140] Under the opposing view, a cause of action that is time barred against the contractor is also time barred against the surety, even though the statute of limitation applicable to the surety has not expired. This view is based on the rule that a surety's liability corresponds with that of its principal, so if the principal cannot be held liable, neither should the surety.[141]

e. Alteration of the Construction Contract

An alteration of the construction contract by the owner, without the surety's consent, discharges the surety to the extent that it is prejudiced by the alteration.[142]

After default termination, and during completion by the surety, public owners should refrain from making improvements to the existing contract work without additional compensation. If such improvements are

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[130] Loyal Order of Moose Lodge 1392, *id*.

[131] CLORE, *supra* note 115, at 116.

[132] *Latent Defects in Government Contracts Law*, 27 PUB. CONT. L.J., No. 1 (1997); *see* Table A, *supra*, this section.

[133] 16 FORUM L. REV. 1057 (1981). The following states have enacted statutes of limitation dealing with performance sureties: HAW. STAT. 657-8—within 2 years after cause of action accrues, but not more than 10 years after completion of improvement); LA. REV. STAT. 38:2189—5 years after completion of contract; *see* State v. McInnis Bros. Constr., 701 So. 2d 937 (La. 1997); WIS. STAT. 779.14—1 year after completion of contract. A Virginia Statute (11-59) established a 5-year statute of limitations for an action on a performance bond. However this statute has been repealed. *See* Acts 2001, c. 844 (Oct. 1, 2001).

[134] New York (Stat. 137, McKinney's Finance Law; A.C. Legnetto Constr., Inc. v. Hartford Fire Ins. Co., 680 N.Y.S.2d 45 (A.D. 1998)—Statute of limitations—1 year); Virginia (Stat. 11-60—1 year after completion of contract); Wyoming (Stat. 16-6-115—1 year after publication of notice of final contract payment). For other examples, see table of "Notice and Filing Requirements," appendix to NCHRP Legal Research Digest No. 37 (1999). This article appears as a supplement in VOL. 3, SELECTED STUDIES IN HIGHWAY LAW.

[135] 74 AM. JUR. 2D *Suretyship* § 119 (2001); Regents of Univ. of Cal. v. Hartford Accident & Indem. Co., 581 P.2d 197 (Cal. 1978); People v. Woodall, 271 N.W.2d 298 (Mich. 1976); Southwest Fla. Retirement Ctr., Inc. v. Fed. Ins. Co., 682 So. 2d 1130 (Fla. App. 1996); AgriGeneral Co. v. Lightner, 711 N.E.2d 1037 (Ohio App. 1998).

[136] For example, FLA. REV. STAT. 95-03 prohibits contract provisions that allow a shorter time than that provided in the applicable statute of limitations. *See also* HAW. REV. STAT. 657-8.

[137] Timberline Elec. Supply Corp. v. Ins. Co. of N. America, 421 N.Y.S.2d 987 (A.D. 1979); General Ins. Co. of America v. Interstate Service Co., 701 A.2d 1213 (Md. App. 1997); Alaska Energy Auth. v. Fairmount Inc. Co., 845 P.2d 420 (Alaska 1993); Howard & Lewis Constr. Co. v. Lee, 830 S.W.2d 60 (Tenn. App. 1991).

[138] Town of Pineville v. Atkinson/Dyer/Watson, 442 S.E.2d 73, 74 (N.C. App. 1994) (limitation period 2 years—reasonable); Hunters Pointe & Partners, Inc. v. U.S.F.G., Co., 486 N.W.2d 136 (Mich App. 1992). (Limitation 1 year—reasonable).

[139] Armand v. Territorial Constr., Inc., 282 N.W.2d 365 (Mich. App. 1979); Gen. State Auth. v. Sutter Corp., 403 A.2d 1022 (Penn. 1979).

[140] Regents v. Hartford Accident & Ind. Co., 581 P.2d 197 (Cal. 1978) (surety has a cause of action against the contractor for indemnification); President & Directors v. Madden, 505 F. Supp. 557, 591 (D. Ct. Md. 1980); *See also* Note, *Running of Statue of Limitations in Favor of Principal Does Not Exonerate a Surety*, 67 CAL. L. R. 563 (1979).

[141] Hudson County v. Terminal Constr. Corp., 381 A.2d 355 (N.J. 1977); 16 FORUM L. REV. 1057; State v. Bi-States Constr. Co., 269 N.W.2d 455 (Iowa 1978).

[142] Restatement of Security § 128B; Continental Ins. Co. v. City of Virginia Beach, 908 F. Supp. 341 (E.D. Va. 1995).

made, a separate accounting should be kept, so as to avoid increasing improperly the surety's obligations under the performance bond on the original construction contract.

This rule is obviated with respect to change orders when the bond contains a provision incorporating the construction contract by reference. By agreeing to the incorporation of the construction contract, the surety agrees in advance to changes made by the owner under the "changes" clause.[143]

f. Disputes Over the Right to Contract Payments When the Contractor Defaults

i. Disputes Between the Surety and the Bank.—Occasionally, contractors borrow money from banks to finance their operations. Banks usually require the contractor to sign an agreement assigning future contract payments earned by the contractor to the bank to secure the loan.[144] In a similar fashion, sureties usually require contractors to sign a general indemnity agreement in favor of the surety.[145] A conflict may arise between the surety and the bank over the right to the contract proceeds when the contractor defaults. The positions of the surety and the bank in this type of dispute were summarized by the court in *Alaska State Bank v. General Insurance Company* as follows:

> The bonding company argues that when a contractor defaults and a bonding company steps in to complete the job and pay laborers and materialmen, it is subrogated to the rights of the owner, the contractor, the laborers, and the materialmen. Since the owner could have used funds still in its hands to complete the job, there would have been no sums available for the contractor and, therefore, the contractor's secured creditor who stands in the contractor's shoes. Under this view the bonding company has first rights to the progress payment, although it may have been fully earned by the contractor's prior performance.
>
> The bank argues that progress payments are contract rights and that the bonding company's subrogation theory merely purports to impose on them a hidden lien. The bank urges that both it and the bonding company had the power to take advantage of Article 9 of the Uniform Commercial Code and perfect their respective security interests. Under this view, the bank had prior rights since it utilized the U.C.C. while the bonding company did not.[146]
>
> ....
>
> The bank urges the court that this "classic dispute" between bank and bonding company should be resolved under the Uniform Commercial Code.

With respect to this type of dispute, the general rule is that the surety is entitled to the contract proceeds.[147] However, there is some authority that the surety's assignment of contract proceeds is subject to the filing requirements of the Uniform Commercial Code, giving the bank priority to contract proceeds when the surety does not comply with the Code's filing requirements.[148]

But what if it's not clear as to whom the owner should pay? An owner caught in a dispute between the surety and the bank may have the option of filing an interpleader action. This type of action would allow the owner to seek a court order authorizing it to pay the contract proceeds into the registry of the court, discharging the owner from further liability as to whom it should pay and leaving it up to the surety and bank to litigate entitlement to the proceeds.[149]

ii. Disputes Over Contract Proceeds Between the Owner and the Surety.—An owner's right to a setoff[150] against unpaid progress payments for its claims against a contractor that has defaulted is superior to the surety's subrogation claim under its payment bond.[151] However, the authorities differ on whether the owner's right is superior to the surety's subrogation rights under its performance bond.[152] A surety who pays the subcontractor, materialmen, and labor claims has a right to the contract retainage that is superior to the owner's right of setoff.[153] Whether the surety can enforce that right against a state agency may depend upon whether the state has waived sovereign immunity.[154]

10. Owner's Rights Against Its Design Consultant

a. Contractual Liability

Design consultants are obligated to perform their contractual duties with the same degree of ordinary care and skill exercised by members of their profession.

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[143] Mergentime Corp. v. Washington Metro. Area Transit Auth., 775 F. Supp. 14 (D.D.C. 1991).

[144] Alaska State Bank v. Gen. Ins. Co. of America, 579 P.2d 1362 (Ak. 1978).

[145] Book Run Baptist Church v. Cumberland, 983 S.W.2d 501 (Ky. 1998); Nat. Shawmat Bank of Boston v. New Amsterdam Casualty Co., 411 F.2d 843 (1st Cir. 1969).

[146] 579 P.2d at 1364.

[147] *Id*.

[148] Transamerica Ins. Co. v. Barnett Bank of Marion County, 524 So. 2d 439 (Fla. App. 1988).

[149] City of N.Y. v. Cross Bay Contracting Corp., 709 N.E.2d 459 (N.Y. 1999) (interpleader action to resolve competing claims to contract funds held by owner); Trans America Ins. Co. v. Barnett Bank, *id*.

[150] *See* § 7.A.3.D, "Administrative Setoff," *supra*.

[151] United States v. Munson Trust Co., 332 U.S. 234 (1947).

[152] Owner's right *superior*: Standard Accident Ins. Co. v. United States, 97 F. Supp. 829 (Ct. Cl. 1951). Owner's right *not superior*: Universal Ins. Co. v. United States, 382 F.2d 317 (5th Cir. 1967).

[153] Nat. Sur. Corp. v. United States, 118 F. 3d 1542 (Fed. Cir. 1997) (by paying claimants, the surety is subrogated to the claimants' rights to the retainage).

[154] Liberty Mutual Ins. Co. v. Sharp, 874 S.W.2d 736 (Tex. App. 1994) (suit by surety against state agency challenging agency's setoff against retainage dismissed because of governmental immunity). *See* § 6.2.A. "Sovereign Immunity," *supra*.

Failure to perform those duties is a breach of contract.[155]

In addition to the evidence normally admissible in breach of contract actions, the evidence may establish the consultant's breach by showing that it was negligent in performing its contractual obligations.[156] Generally, negligence must be proved by expert testimony,[157] unless the act or omission is so obvious that lay persons can easily recognize the act or omission as negligent.[158]

b. Betterment

Should the design consultant be liable for the cost of a construction feature that had to be added during construction because it was erroneously omitted from the contract plans? Under the "betterment" rule, the answer is generally "no." Usually, liability is limited to the difference between adding the construction feature by change order and what it should have cost if the construction feature had been included in the contract bid price.[159] The "betterment" rule puts the owner in the position it would have occupied had the error not occurred, and prevents the owner from obtaining a windfall.[160]

c. Indemnification

Another theory of recovery against a design consultant is indemnity under an indemnification clause in the design agreement. The clause is triggered by the design consultant's negligence when it causes harm to third persons, resulting in damage claims against the project owner.[161] The owner's ability to recover may be limited, however, by an anti-indemnification statute, or by a limitation of liability clause in the design agreement.[162]

11. Indemnity and Insurance Requirements

a. Indemnity

Most owners employ indemnity provisions in their construction contracts.[163] Such provisions protect the owner by requiring the contractor to indemnify the owner against all claims arising from the performance of the contract.[164] An example of a general indemnity clause is the standard provision used by the Maryland State Department of Transportation in its construction contracts.[165]

> To the fullest extent permitted by law, contractor shall indemnify, defend and hold harmless the State, its officials and employees from all claims arising out of, or resulting from performance of the contract. Claim as used in this specification means any financial loss, claim, suit, action, damage, or expense, including but not limited to attorney's fees, bodily injury, death, sickness or disease or destruction of tangible property including loss of use resulting therefrom. The contractor's obligation to indemnify, defend and hold harmless includes any claim by contractor's agents, employees, representatives or any subcontractor or its employees.

An indemnity clause may require the indemnitor to indemnify the indemnitee against damages that are caused by the indemnitee's negligence. As a general rule, such clauses are enforceable where the clause clearly provides that the indemnitee is to be indemnified, notwithstanding the indemnitee's negligence.[166] Some states, however, have enacted anti-indemnification statutes, which prohibit the use of such clauses in construction contracts.[167] The following is an example of this type of statute:[168]

> A covenant, promise, agreement or understanding in, or in connection with or collateral to a contract or agreement

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[155] Brushton-Moira Cent. School Dist. v. Alliance Wall Corp., 600 N.Y.S.2d 511 (N.Y. A.D. 1993); Paxton v. Acameda County, 259 P.2d 934 (Cal. 1953).

[156] *Id*.

[157] Garaman, Inc. v. Williams, 912 P.2d 1121 (Wyo. 1996); Annotation, *Necessity of Expert Testimony to Show Malpractice of Architect*, 3 A.L.R. 4th 1023 (1981).

[158] Hull v. Engr. Constr. Co., 550 P.2d 692 (Wash. App. 1976); Town of Breckenridge v. Golforce Inc., 851 P.2d 214 (Colo. App. 1992).

[159] St. Joseph Hosp. v. Corbetta Constr. Co., 316 N.E.2d 51 (Ill. App. 1974); Lochrane Engr., Inc. v. Willingham Realgrowth Inv. Fund, Ltd., 552 So. 2d 228 (Fla. App. 1989).

[160] *Id*.

[161] Indemnification requirements are discussed in the next subpart of this section.

[162] Those limitations affecting indemnification are also discussed in the next subpart.

[163] The following are some examples of indemnity clauses used by state transportation agencies: Arkansas Standard Specifications 7.2.12A; Maine Standard Specification 1-07.15; Missouri Standard Specification 1-07.12; New Hampshire Standard Specification 1-07.14; Washington State Standard Specification 1-07.14; Wisconsin Standard Specification 1-07.12.

[164] Smith v. Cassadago Valley Cent. Sch. Dist., 578 N.Y.S.2d 747 (N.Y. A.D. 1991).

[165] General Provision 7-13. The owner may also be entitled to common-law indemnification when the owner is exposed to liability due to the contractor's negligence or breach of contract. Margolin v. N.Y. Life Ins. Co., 297 N.E.2d 80, 82 (N.Y. 1973). Inclusion of an indemnity provision in the construction contract does not alter the common law right to indemnity. Hawthorne v. South Bronx Community Corp., 582 N.E.2d 586 (N.Y. 1991). But the common law duty to indemnify may be limited by the terms of the express indemnity clause. Regional Steel Corp. v. Superior Court, 32 Cal. Rptr. 2d 417 (Cal. App. 1994).

[166] Cunningham v. Goettl Air Conditioning, Inc., 980 P.2d 489 (Ariz. 1999). *See generally* WILLIAM L. PROSSER, LAW OF TORTS § 46, at 249–54 (2d ed. 1955).

[167] For example, the following states have enacted anti-indemnification statutes: Alaska (STAT. 45.45.900); Arizona (REV. STAT. 34-226(A)); California (CIV. CODE § 1782); Georgia (CODE 20-50A); Illinois (REV. STAT. ch. 29, § 61); New York (GEN. OBLIG. LAW 5-322.1); Washington (REV. CODE § 4.24.115).

[168] N.Y. GEN. OBLIG. LAW § 5-322.1. *See* Sheehan v. Fordham Univ., 687 N.Y.S.2d 22 (N.Y. A.D. 1999) (statute precluded contractual indemnification for indemnitee's negligence).

> relative to the construction, alteration, repair or maintenance of a building, structure, …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….

Another limitation on indemnification is a liability limitation clause in the contract. This type of clause imposes a ceiling on the indemnitor's liability. Typically, the clause will limit liability to a fixed dollar amount specified in the clause.[169]

Generally, such clauses are enforceable.[170] However, their enforceability may be affected by an anti-indemnification clause. In *City of Dillingham v. CH2M Hill Northwest, Inc*.,[171] the court held that a limitation of liability clause in an engineering services agreement was invalid under the Alaska anti-indemnification statute,[172] because the statute prevented the indemnitor from limiting its liability for its negligent acts.

In *Valhal Corp. v. Sullivan Associates*,[173] the court distinguished indemnification and limitation of liability clauses. The court said that an indemnity clause immunizes a party from its own negligence and therefore is void under an anti-indemnification clause. A limitation of liability clause, however, is not invalid. The clause did not purport to immunize a party from its own negligence; it only capped the amount of the indemnitor's liability.

b. Insurance

Owners usually specify in the construction contract the types of insurance that the contractor must procure for the project.

Standard insurance provisions require that the insurance be in place continually and without lapse from beginning of work until contract final acceptance, and cover all the operations under the contract, whether performed by the contractor or any subcontractors. Transportation agencies usually obtain and rely on the certificate of insurance furnished by the insurance carrier's authorized agent, although they may obtain full copies of the insurance policy.

New York State has experienced many disputes with insurance carriers disclaiming coverage in connection with tort claims litigation arising from work site construction accidents or work zone vehicular accidents. NYSDOT requires that insurance companies be authorized to do business in the State by the New York State Department of Financial Services (the agency resulting from the merger of the former State Insurance Department and State Banking Department), and have an A.M. Best Company rating of (A-) or better approved by that Department.[174] Nonauthorized carriers may submit documentation required by the Insurance Department regulations and may be permitted at the discretion of NYSDOT.

NYSDOT's Standard Specifications require that satisfactory evidence of such policies shall be delivered to NYSDOT prior to the commencement of work, provide for certificates of insurance in a form satisfactory to the Commissioner of Transportation, and authorize immediate issuance of stop-work orders in the event of any lapse in insurance coverage. NYSDOT does not accept the use of the commonly used "Accord" certificate of insurance form, but requires the use of its own certificate form, signed by authorized representative of the insurance carrier. NYSDOT also specifies the policy form must be written on an occurrence basis, but will accept a form written on a claims-made basis if certain conditions are met. The NYSDOT insurance certificate requires disclosure of any deductible, self-insured retention, or any exclusions in the policy that materially change the contract coverage.

c. Self-Insured Retention

Contractors, in order to save on premiums, may obtain policies that have deductibles or self-insured retention provisions. Permitting contractors to have deductibles or self-insured retention has created some obstacles and difficulties for claimants seeking claim adjustments. NYSDOT has developed a system that permits contractors to adopt a self-insured retention program. NYSDOT provisions require prior approval of the program. Such programs are limited to $100,000 or the amount of the bid deposit, whichever is less. New York requires that security for such programs be deposited to assure payment of both the self-insured limit and the cost of adjusting claims. The contractor is solely responsible for all claims, expenses, and loss payments within any permitted self-insured retention or permitted deductible program. If the contractor's self-insured program exceeds the amount of the bid deposit, it is required to submit an irrevocable letter of credit or collateral to guarantee its obligation. If NYSDOT determines that the contractor is not paying the deductible or self-insured retention on any of its policies, it may withhold payments.[175]

The most commonly required type is liability insurance, protecting the insured against liability for third-party claims that result from construction activities.[176]

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[169] Valhal Corp. v. Sullivan Assocs., 44 F.3d 195 (3d Cir. 1995); C&H Eng'rs P.C. v. Klargester, Inc., 692 N.Y.S.2d 269 (N.Y. A.D. 1999).

[170] Vahal Corp v. Sullivan Assocs., *id.*

[171] 873 P.2d 1271 (Alaska 1994).

[172] ALASKA STAT. § 45.45.900.

[173] 44 F.3d 195 (3d Cir. 1995).

[174] NYSDOT Standard Specifications 107.06.

[175] *Id*.

[176] D.W. HARP, INDEMNIFICATION AND INSURANCE REQUIREMENTS FOR DESIGN CONSULTANTS AND CONTRACTORS ON HIGHWAY PROJECTS (National Cooperative Highway Research Program Legal Research Digest No. 37, 1996.) Supplement to Vol. 3, SELECTED STUDIES IN HIGHWAY LAW. While state transportation agencies require these construction con-

The contract may also require the contractor to obtain builder's risk insurance, protecting the insured against damage to the improvement during the course of construction.[177]

Additional insurance requirements include subcontractor liability insurance, workers' compensation, builders' risk of damage to structures or buildings, railroad protective liability, professional liability for errors and omissions, and commercial auto liability insurance.

d. Liability Insurance

The contract specifications typically specify the type or types of liability insurance that the contractor is required to procure and the limits of coverage. The two most common forms of such insurance are commercial general liability (CGL) insurance[178] and owners and contractors protective insurance, in which the owner is the insured.[179] Both forms of insurance are based on occurrence coverage.[180] Under occurrence coverage, a claim is covered if the event causing the damage or injury occurred during the period that the policy was in force.

> [S]tandard comprehensive or commercial general liability [CGL] insurance policies provide that the insurer has a duty to indemnify the insured for those sums that the insured becomes legally obligated to pay as damages for a covered claim. Such a policy is triggered if the specified harm is caused by an included occurrence, so long as at least some such harm results within the policy period.[181]

The specifications requiring insurance may require that the owner be named as an additional insured on the contractor's CGL policy.[182] The specification may also require that in addition to the agency, the agency's officers and employees must also be named as additional insureds. [183] The insurance limit ranges from $1 million to $5 million depending upon the size of the project. The specifications typically specify the minimum limits of coverage for each occurrence, and in the aggregate for each year that the policy is in force.[184] The limits for owners and contractors protective insurance are usually the same as the limits specified for CGL coverage.[185] The specifications may require the contractor to obtain liability insurance on standard forms published by the Insurance Services Office (ISO), a national organization that provides services to the insurance industry.[186]

NYSDOT's Standard Specifications require specific ISO forms for coverage for commercial general liability, products completed operations, and blanket Pollution Liability. In addition, the coverage must also include Explosion Collapse and Underground Hazard coverage for contracts that involve excavation, underground work, and/or the use of blasting equipment.

In addition to the basic CGL policy, N.Y. requires a separate dedicated Special Protective and Highway Liability Policy for the State of New York, using a separate ISO form with separate liability amounts to cover liability for the State of N.Y. for any damages the insured may be held liable for. Such protective liability coverage for the owner must expressly and specifically include all of its individual officers and employees as well as the owner as an organization. This can be of considerable importance if a claimant sues the owner's officers and employees individually and seeks to recover from their personal assets.

In the absence of such express and specific requirements, individual engineers, inspectors, or others employed by the owner can be sued individually in their personal rather than official capacity, placing their personal assets at risk without insurance to cover them. In New York, a construction worker suffered permanent disabling injuries in a construction work zone vehicular accident. He then discovered that the construction contractor had failed to pay its insurance premiums and did not have either liability or Workers Compensation coverage in effect. His lawyers sued to commence federal diversity jurisdiction tort litigation against individual NYSDOT officers and employees, as well as seeking to pursue state claims litigation against the

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tractors to obtain liability insurance, not all of them require their design consultants to obtain professional errors and omissions (E&O) coverage. *Id*.

[177] Annotation, *Builder's Coverage Under Builder's Risk Insurance Policy*, 97 A.L.R. 3d 1270 (1980).

[178] Arizona DOT Standard Specification 1-07.14 (2000); California DOT Standard Specification 7-1-12 B (1999); Colorado DOT Standard Specification 1-07.15 (1999); Florida DOT Standard Specification 7.13.2 (2000); Washington State DOT Standard Specification 1-07.18 (2000).

[179] Colorado (Standard Specification 1-07-15) and Washington (Standard Specification 1.07.18) are examples of states requiring OCP coverage in addition to CGL coverage.

[180] The specifications listed in note 178, *supra*, are examples of specifications requiring liability insurance based on "occurrence" coverage.

[181] Aerojet-General Corp. v. Transport Indem. Co., 948 P.2d 909 (Cal. 1997). A claim under a claims-made policy must be made before the policy expires or during an extended reporting period provided in the policy. A typical E&O policy is written on a claims-made basis rather than an occurrence basis.

[182] Colorado Standard Specification 1-07.15.

[183] California Standard Specification 7-1.12 B.

[184] California: $1 million each occurrence, $2 million aggregate, $5 million excess liability coverage for projects under $25 million, $15 million excess coverage for projects over $25 million, Standard Specification 7-1.12 B (1999). Florida: bodily injury or death: $1 million each occurrence, $5 million aggregate; property damage: $50,000 each occurrence, $100,000 aggregate for all damages occurring during the policy period, Standard Specification 7.12.2 (2000). Colorado: $600,000 each occurrence, $2 million aggregate, Standard Specification 1-07.15 (2000); Washington: $1 million each occurrence, $2 million aggregate, Standard Specification 1-07.18 (2000).

[185] Colorado (Specification 1-07.15) and Washington (Specification 1-07.18) are examples.

[186] California (Specification 7-1.12 B) and Washington (Specification 1-07.18), for example, require the use of ISO Form G0001 or a form providing the same coverage.

owner.[187]

Disputes between the insured and insurer over coverage may lead to litigation. Whether the policy covers a particular occurrence is a question of contract interpretation.[188] An insurance policy is treated in the same way as contracts are treated generally. The court's goal in interpreting the policy is to ascertain the intent of the parties. If that intent cannot be determined, and the policy is ambiguous, the policy will be construed against the insurer and in favor of coverage for the insured.[189]

e. Builder's Risk Insurance

This form of insurance provides coverage for damage to the improvements during the course of construction.[190] Coverage may be limited by specific exclusions in the policy.[191] But an exclusion will not prevent coverage when it conflicts with other provisions of the policy granting coverage. "When provisions of an insurance policy conflict, they are to be construed against the insurer and in favor of the insured."[192]

f. Use of Industry "Accord" Form or Other Forms

Many state transportation agencies rely on the standard insurance industry "Accord" form. The form states: "This certificate is issued as a matter of information only and confers no rights upon the certificate holder….This certificate of insurance does not constitute a contract between the issuing insurer(s), authorized representative or producer and the certificate holder." The form specifically states it is information only, and cannot be relied upon as proof of insurance. In the event of litigation arising from an occurrence on a project for which an Accord form certificate has been used, the insurance carrier will typically limit coverage to the specific terms and limitations set forth in its policy as opposed to the certificate. The policy typically authorizes cancellation of coverage without notice in the event of nonpayment of premiums, and provides for large deductibles. The policy is also typically limited to coverage of the contractor alone, and fails to include coverage of the owner or the owner's individual officers or employees. Even if someone has filled in the Accord form with recitations of no cancellation of coverage without prior notice to the owner, and with coverage of the owner and the owner's individual officers and employees as well as the contractor, the insurance carrier will typically disclaim being bound by such recitations even if the Accord certificate has been issued by the carrier's authorized agent, pointing to the form language that "This certificate is issued as a matter of information only and confers no rights upon the certificate holder."

NYSDOT does not permit the use of the Accord form, and requires a certificate of insurance satisfactory to NYSDOT to be filled out by the insurance carrier's authorized representative or producer, although this has met with resistance from the insurance industry and complaints to the New York State Department of Financial Services (the agency resulting from the merger of the former State Insurance Department and State Banking Department). The form is required to be submitted before the contractor will be allowed to commence any work under the contract. The form requires that it be acknowledged before a notary public, requires disclosure of additional insureds and named insureds, and expressly references the inclusion of all required

[187] The manner in which lack of express language requiring protective liability coverage of the owner's individual officers and employees can result in litigation against such officers and employees is illustrated by Mohammed v. Farney et al., one of multiple cases arising from a NYSDOT highway project.

The cases resulted from a highway work zone vehicular incident, in which an uninsured motorist inflicted permanent disabling injuries upon a construction worker and then fled. When the State notified the contractor's insurance carrier, the carrier disclaimed any responsibility, asserting that it had cancelled all insurance coverage without notifying the owner (the State) as required by the insurance certificate, because the prime contractor had failed to pay its insurance premiums.

This allowed the disabled worker to pursue civil litigation, because the insurance carrier refused to honor the contractor's Workers' Compensation coverage. Rather than merely suing the State in its Court of Claims, the attorneys for the disabled construction worker, who resided in an adjacent state, also filed roughly $20 million in federal diversity jurisdiction tort actions against the contractor, the contractor's personnel, and individual NYSDOT engineers and inspectors. The insurance carrier then additionally disclaimed any responsibility to defend or indemnify any individual state personnel, pointing to the absence of any express and detailed language in the insurance certificate requiring it to do so, as opposed to language requiring protective liability coverage for the State as an entity.

This situation was demoralizing for the state DOT engineers and inspectors who were sued as individuals. This was true even though legal defense and indemnification of the individual state personnel involved was eventually arranged, and the litigation against the State was ultimately settled (for somewhat less than $1 million), resulting in withdrawal of the federal litigation against the individual State DOT employees. This litigation also had a considerable disruptive effect upon the continued performance and completion of the project, which involved a major urban arterial expressway.

[188] Simon v. Shelter General Ins. Co., 842 P.2d 236 (Colo. 1992).

[189] California Pacific Homes, Inc. v. Scottsdale Ins. Co., 70 Cal. Rptr. 4th 1187, 83 Cal. Rptr. 2d 328 (1999); Simon v. Shelter Gen. Ins. Co., *id.*; 13 APPLEMAN, INSURANCE LAW AND PRACTICE, § 7401 (1976).

[190] Annotation, *Builder's Coverage Under Builder's Risk Insurance Policy*, 97 A.L.R. 3d 1270 (1980).

[191] Safeco Ins. Co. of America v. Hirschmann, 773 P.2d 413 (Wash. 1987); Markman v. Hoefer, 106 N.W.2d 59 (Iowa 1960).

[192] Simon v. Shelter Gen. Ins. Co, 842 P.2d 236 (Colo. 1992).

endorsements.[193]

g. Pollution Exclusions

Many insurance policies have pollution exclusion provisions that delete or restrict coverage for environmental hazards, which may include asbestos removal, oil removal and other hazardous waste, and improper disposal of contaminated construction and demolition debris. The owner's attorneys should examine the insurance certificate or policy for such exclusions. If such coverages are needed, the state DOT or other owner should request the removal of such exclusions from the policy. Many public owners are unaware that pollution exclusions may be part of the contractor-furnished insurance policies. If the owner is aware that pollution hazards are likely to exist on the project (e.g., the known presence of asbestos in a building undergoing demolition), it should specifically require the contractor to obtain the Contractor Pollution Liability policy. Relying on the standard policy, which may contain such pollution exclusions, can only lead to coverage issues. If the policies contain such pollution exclusions, they must be noted on the certificate of insurance.

h. Owner Controlled Insurance Programs

Some state transportation agencies, motivated to find ways to reduce costs and control construction budgets, have turned towards the use of Owner Controlled Insurance Programs, especially for "mega projects."

Owner Controlled Insurance Programs (OCIP) or "wrap-up" insurance can be an effective way to improve safety and reduce the costs of insurance for large projects. The essential idea is to have one party, either the owner or the contractor, procure, maintain, and control the insurance coverage and services for all the parties.[194] Basic features of an OCIP are: 1) the owner purchases the insurance coverage to cover all contractors and subcontractors; 2) there is an integrated owner-contractor managed safety program; and 3) claims are centrally processed. OCIPs are able to achieve savings through the use of lower bulk insurance rates, improved safety management, and reductions in disputes between contractors as to who is liable for the loss.[195]

The advantages of the program are derived from the economies in purchasing coverage for all parties.[196] The coverage protects all parties for claims arising under worker's compensation, general liability, and excess or umbrella liability, but does not include coverage for performance bond claims. OCIPs can provide improved insurance coverage, enhanced contract and claims management, and possibly enhanced achievement of DBE goals. Owner's contract management is simplified since the owner will not have to track many policies with differing terms, conditions, effective dates, and limits. OCIPs also may promote safety by coordinating an effective safety program for the entire project. OCIPs on projects involving complex, high-risk construction, and in excess of $100 million in construction costs, represent significant opportunities for project cost savings.

Wrap-up insurance, which includes OCIPs and Contractor Controlled Insurance Policies (CCIPs), may also provide savings and improve claim management and loss control. If an OCIP is used, the transportation agency is responsible for procurement of an insurance broker and the creation of the OCIP program. The OCIP program will include all the general and professional liability and other insurance for the project. All contractors and subcontractors would be contractually required to participate in the program, and to delete insurance costs from their overhead. If a CCIP is used for a design-build project, the design–builder is required to provide an insurance program that covers the design-builder and its subcontractors. The design-builder would be responsible for administration of the CCIP and insuring that all subcontractors do not include insurance costs in their overhead.

OCIPs have been used on the Boston Central Artery Tunnel Projects ("Big Dig"), and on many of the larger projects for Caltrans, with much success. Caltrans has adopted a Rolling Owner Controlled Insurance Program (ROCIP) and issued a ROCIP program insurance manual for all contractors and subcontractors (with certain exceptions) who provide direct labor on the project site. The ROCIP provides general liability, completed operations coverage, excess liability, and worker's compensation for enrolled contractors. The ROCIP does not cover professional liability or other types of insurance required by the contractor or contract provisions. Caltrans pays the ROCIP premiums, and the contractor is required to submit cost documentation that supports the costs for insurance from the bid for the work. Caltrans has the right to audit the contractor's records to confirm that the costs of general liability insurance, excess liability insurance, and worker's compensation are not included in the original bid. The provisions further provide that failure of the contractor to comply with the ROCIP provisions shall entitle the department to suspend performance by the contractor or terminate the contract for cause. The provisions require the contractor to develop a Site Specific Safety Program, and to allocate a full time Safety Quality Control Manager for duration of the contract. Provisions for documentation, safety conditions, fall protection, and tool box safety meetings are also included.[197]

[193] NYSDOT Standard Specifications 107.06 A 3.

[194] James Evans, Owner-Controlled Insurance Programs: A Public Sector Perspective, ASSE Proceedings, June 1, 2011.

[195] Dwight A. Horne, Action: Owner Controlled Insurance Policy, Oct. 7, 2002, FHWA memorandum setting forth FHWA policy on OCIP, http://www.fhwa.dot.gov/programadmin/contracts/100702.cfm, last accessed on July 26, 2012.

[196] Evans, *supra* note 194.

[197] CalTrans Standard Specifications 5-1.13, Rolling Owner Controlled Insurance Program (ROCIP).

i. Failure to Obtain Insurance

The contractor's failure to obtain insurance, as required by the contract, is a breach, entitling the owner to damages.[198] A contractor cannot avoid a contractual insurance requirement by arguing that a specification requiring insurance should be construed as an indemnification clause and, therefore, unenforceable under an anti-indemnification statute. The specification is an insurance requirement, not an indemnification provision.[199]

The owner's failure to obtain proof of liability insurance before notifying the contractor to proceed with the work does not waive the insurance requirement.[200]

In N.Y., if it comes to the attention of NYSDOT that the required insurance is not in place, or that adequate proof of insurance has not been provided, the department may immediately issue a stop-work order suspending the work, withhold contract payments, or treat such failure as a breach of contract or default and terminate the contract.[201]

j. Tendering the Claim

When an owner receives a claim, several questions should be asked: Is the claim covered by insurance? Is the claim covered by an indemnification provision in the contract? If the answer to the first question is "yes," the claim should be tendered promptly to the insurer. If the answer to the second question is also "yes," the claim should be tendered promptly to the contractor.

Tender of the claim to the design consultant may raise special considerations. Should the owner sue the designer in the same action brought by the contractor against the owner? Pursuing the claim in one action avoids the cost of multiple litigation and may avoid inconsistent results by a court, jury, or arbitrator, although joining the designer in the same action brought by the contractor does not guarantee a consistent result. This can occur because different standards of liability may apply. The contractor will sue the owner for breach of contract or an equitable adjustment under a specific clause in the contract. The owner will usually sue the designer for indemnification based on the designer's negligence.[202]

In addition to avoiding multiple litigation, there is also another advantage in bringing the claim against the designer in the same action brought by the contractor against the owner. By bringing the claim in the same action, it allows the owner to point the finger at the designer, as the party ultimately responsible for the damage, and to a large extent "piggyback" the contractor's case. A major disadvantage in pursuing all claims in the same action, however, is that it may force the designer to point the finger at the owner. The designer may claim that it recommended a time extension, a different design, or more soils investigation, but the owner refused. Another disadvantage is where the designer is also the construction manager, and the owner is an "absentee owner." In those situations, only the construction manager, on the owner's side, may have day-to-day knowledge about the project. The problem of whether recovery should be sought from design consultants for design errors occurred in a major rail link project in New York State.[203]

Typically, however, many states use design and/or construction inspection consultants to complement their own staff.

This may result in a blending of responsibilities, an unclear scope of responsibility, or the procurement of various engineering consulting services that do not require complete designs. Construction inspection services are similarly procured.

A problem occurred in connection with the Oak-Point Link Rail Project in New York State. A major rail link to New York City was to be placed on a viaduct in a nearby river. The government agency gave the consultant the criteria on expected loads the viaduct would carry. The project was on a quick track, but the funds allocated were insufficient. The design consultant was told that the State would provide the soil samples, borings, and evaluations and was instructed to use as-built plans for existing structures in the immediate area to gain whatever information it deemed appropriate in connection with the design. The State instructed that the limited boring information and interpolations were to be used to determine where rock formations and other obstructions might reasonably be anticipated. As it turned out, the rock formations, in many instances, deviated from the information obtained from the plans. The State subsequently ordered additional site boring and worked closely with the consultants to identify a solution.

Because of the overlapping agency staff and consultant activity and the lack of clear engineering responsibility placed solely on the consultants, the agency officials were not able to decisively determine who was responsible for the errors and failures when the project was terminated. The State paid the contractor several million dollars for extra work and delay damages after determining that no recovery should be sought from the

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[198] Mass. Bay Transp. Auth. v. United States, 129 F.3d 1226 (Fed. Cir. 1997); PPG Indus. v. Continental Heller Corp, 603 P.2d 108 (Ariz. App. 1979); Caputo v. Kimco Dev. Corp., 641 N.Y.S.2d 211 (N.Y. A.D. 1996).

[199] Homes v. Watson-Forsberg Co., 488 N.W. 473 (Minn. 1992); Jokich v. Union Oil Co. of Cal., 574 N.E.2d 214 (Ill. App. 1991).

[200] Batterman v. Consumers Illinois Water Co., 634 N.E.2d 1253 (Ill. App. 1994).

[201] NYSDOT Standard Specifications 107.06 A.

[202] An error in a plan or specification may be a breach of the construction contract, but the design consultant is not necessarily liable to the owner if the error was not caused by the designer's negligence. *See* subpart 7.9.A., *supra*.

[203] DARRELL W. HARP, INDEMNIFICATION AND INSURANCE REQUIREMENTS FOR DESIGN CONSULTANTS AND CONTRACTORS ON HIGHWAY PROJECTS (NCHRP Legal Research Digest 37, Transportation Research Board, 1997).

consultant because of the instructions from the agency staff and the fusion of engineering functions.[204]

An owner may choose to defer action against the designer until the action against the owner is resolved. One method of accomplishing this is through the use of a "stand-still" agreement.[205] A stand-still agreement typically provides that the owner will not initiate any action against the designer that is related to the claim brought by the contractor during the effective period of the agreement.[206] The agreement usually provides that the parties agree to toll any applicable statutes of limitations that might otherwise be interposed.

Another potential limitation on the power of the owner to resolve its claims in one proceeding is where one prescribed dispute resolution method is litigation and the other is arbitration. This problem also exists where the contract or the design agreement does not authorize joinder of another party. All jurisdictions view arbitration as purely consensual. Thus, an owner cannot join the designer in an arbitration between the owner and the contractor unless the designer agrees.[207]

k. Recovery Against Design Professionals

The best protection state transportation agencies can have against liability to third parties for consultant liability for design errors and omissions is to provide contract provisions that assign responsibility to the consultant and contractor. At the federal level, 48 C.F.R. § 36.608 provides:

> Architect-engineer contractor shall be responsible for the professional quality, technical accuracy, and coordination of all services required under their contract. A firm may be liable for government costs resulting from errors or deficiencies in design furnished under this contract. Therefore when a modification to a construction contract is required because of an error or deficiency in the services provided under the architect–engineer contract, the contracting officer (with the advice of technical personnel and legal counsel) shall consider the extent the architect-engineer contractor may be reasonably liable.

Many state transportation agencies and the Army Corps of Engineers have adopted provisions in their design contract that provide that the designer is responsible for the professional quality, technical accuracy, and coordination of all design drawings, specifications, and other services. The standard provisions further provide that neither approval nor acceptance of, nor payment for, the services shall operate as a waiver of any rights, and the designer shall remain liable under applicable law for all damages.[208] Adopting similar requirements, together with requiring consultants to provide professional liability coverage for their errors and omissions, and requiring indemnification provisions, can serve to limit or avoid potential liability problems.[209] In any such situation, the consultant should be put on notice pursuant to the standard contract indemnification provisions. It is critically important that the transportation agency not pay the consultant to correct its design errors and omissions.[210] Clear identification of consultants' services and responsibilities will serve to protect the public agency if it expects to hold the consultant liable for its failures, errors, and omissions. In addition, federal regulations require state transportation agencies to set up a procedure for the review of design errors, omissions, or deficiencies.

Special attention should be paid to the blending of responsibilities between state and consultant personnel. This is especially true where the state DOT supplements its staff with consultant inspectors, as exemplified by the Oak Point Link Rail Project in New York State previously discussed.

Some recent cases shed light on how precedents on the liability of design professionals are evolving. Since most such cases are resolved through settlement without litigation to a final court decision, the majority of court decisions identified by our research involved rulings on motions rather than final decisions on the merits.

In a 2005 decision, *Lyndon Prop. Ins. Co. v. Duke Levy & Assoc. LLC*, the U.S. Court of Appeals for the Fifth Circuit reversed a decision that had granted summary judgment to an engineering firm in a case filed by a surety, alleging that the company was negligent in carrying out its inspection duties on a public construction project, and remanded the suit for further proceedings on the surety's negligence claim.[211] The surety had issued a performance bond for a contractor agreement to build a sewage treatment system for a water and sewer district. The engineering firm was hired to inspect the contractor's work, and to make recommendations on whether payments should be made to the contractor. The contract was terminated, and some of the work had to be redone. The surety paid for the project's completion. On appeal, the Fifth Circuit held that the surety could pursue an equitable subrogation claim, and that the fact that the sewer district did not ultimately suffer a loss, due to the surety's payment for completion of the project, was inconsequential. The

[204] *Id*. at 7.

[205] The agreement reserves, until a later time, the owner's rights against the designer and the designer's defenses against the owner.

[206] The effective period of the agreement commences upon its execution and ends upon a final resolution of the contractor's claim against the owner. This may occur upon a final judgment, arbitration award, or final settlement of all of the contractor's claims for which the owner may seek indemnification from the designer.

[207] The consensual nature of arbitration is discussed in the next subsection.

[208] Article 25 of NYSDOT Standard Design Agreement.

[209] HARP, *supra* note 203, at 7.

[210] Address of Eric Kerness, NYSDOT, Maintaining Control of Design Liability in Government Contracting, TRB 39th Annual Workshop on Transportation Law, July 2000.

[211] 475 F.3d 268; 2007 U.S. App. LEXIS 93 (5th Cir. 2007).

Fifth Circuit also held that an exculpatory clause in the company's contract was not sufficiently clear to act as a limitation of liability under Mississippi law, and that the sewer district could not bargain away the engineering firm's potential duty to the surety. Further, the Fifth Circuit ruled that the language of the engineering firm's contract showed that the firm had a duty to inspect the contractor's work before recommending payment, and noted that the surety had presented an expert's report articulating how the engineering firm had failed to use ordinary professional skills and diligence in doing so.

In a 2009 ruling, *Sewell et al. v. Barge, Waggoner, Sumner & Cannon, Inc., et al.*, a magistrate judge of the U.S. District Court for the Northern District of Alabama grappled with design liability issues arising from a highway accident.[212] The case involved catastrophic and permanent personal injuries incurred in a vehicular collision, which resulted from allegedly unsafe design of a highway intersection and traffic control devices. On cross motions for summary judgment, the magistrate judge recommended denial of plaintiff's motion for partial summary judgment because there were unresolved issues of material fact regarding liability that required determination by a jury; the judge also recommended that a motion for summary judgment by an engineering design firm be denied on the same basis, and recommended dismissal of a derivative claim filed by a relative, on statute of limitation grounds. Evidence in the case indicated that two vehicles could legally be in the intersection at the same time, creating a risk of collisions. The magistrate judge noted that the Manual of Uniform Traffic Control Devices (MUTCD) established standards for the design of intersections. The highway interchange involved in the case was not constructed exactly as designed, without the knowledge of the design firm. There was a factual dispute as to whether the design met MUTCD standards. Plaintiff's expert witness testified that the design did not meet applicable standards, was unsafe as designed, and was even more unsafe as built. The magistrate noted that the designer was not responsible for the timing of the traffic control devices once they were installed, and that timing of the four-way red light was insufficient to clear the intersection before lights turned green. The magistrate considered untenable the design firm's claim that it was absolved of liability merely because a design change was instituted without its knowledge during the construction phase of the project. The fact that the design had been changed in some manner did not, standing alone, automatically relieve the design firm of liability.

In a 2011 decision, *Matter of Fort Totten Metrorail Cases, lead case Jenkins v. Washington Metropolitan Area Transit Authority, et al.*, the U.S. District Court for the District of Columbia addressed design liability issues arising from a major crash on the Washington Metro system during 2009.[213] One of the defendants, Alstom, a firm that had been involved in construction of the Metro system both as a designer and as a manufacturer, moved for dismissal. The court held that a statute of repose barred design claims arising more than 10 years after manufacture. The court also ruled, however, that the statute of repose did not bar claims for manufacturing defects that were not discovered until years later.

In another 2011 decision, *Drew County, Arkansas v. Joh Pas Murray Co.*, the U.S. District Court for the Eastern District of Arkansas had to deal with design liability issues arising from a situation considerably complicated by confusion over the legal standards and procedures governing procurement of design and construction services for a hospital project.[214] A municipal hospital's managers entered into negotiations with an out-of-state contractor under some confusion over whether the contractor, not licensed in the state as an engineering firm and initially not licensed in the state as a contractor either, would be acting as a design-builder or as a construction manager at risk. The hospital's board authorized the project, and the contractor began the planning phase of the project before any contract was signed. The hospital broke off dealing with the firm after the hospital's attorney concluded that design-build projects were not authorized by state law. The hospital then turned the planning work product that had been delivered to date over to a licensed architectural firm. The contractor then sued for the value of the planning work that had been performed to date. The court found that while the firm might have violated state law against practicing engineering without a license, the state law prohibiting that did not preclude recovery for services performed on the basis of express or implied contract. The court denied the hospital's motion for summary judgment, granted the contractor's motion for partial summary judgment precluding some of the hospital's defenses, and ordered further proceedings.

In a 2010 decision, *SEPTA v. AECOM USA, Inc.,* the U.S. District Court for the Eastern District of Pennsylvania dealt with design liability issues arising from an urban rail project.[215] The owner had hired an A/E firm to design a rail reconstruction project. The A/E firm hired subconsultants. After problems developed, the owner sued the A/E firm for failure to perform. The A/E firm brought a third-party complaint against its subconsultants. The subconsultants then cross-claimed against each other. The court denied one subconsultant's motion to dismiss, granted a motion to dismiss cross-claims for indemnification, but denied a motion to dismiss cross-claims seeking contribution.

[212] Sewell et al. v. Barge, Waggoner, Sumner & Cannon, Inc., et al., 2009 U.S. Dist. LEXIS 85233 (U.S. Dist. Ct. ND Alabama, magistrate judge, 2009).

[213] 793 F. Supp. 2d 133 (U.S. Dist. Ct. D.C. 2011).

[214] 2011 U.S. Dist. LEXIS 43947 (U.S. Dist. Ct. E.D. Ark. 2011).

[215] 2010 U.S. Dist. LEXIS 123097 (E.D. Pa., Nov. 19, 2010).

A number of other cases concerning the liability of design professionals have been decided since the 2005 update to the current volume, which will be summarized only briefly here, but may possibly prove relevant in certain situations.

In the 2009 case of *Auto-Owners Insurance Co. v. Ace Electrical Service, Inc., et al.*, the U.S. District Court for the Middle District of Florida dealt with a dispute involving a surety bond loss that resulted from the failure of a design for electrical work on a municipal project to meet code.[216]

In the 2008 case of *Holbrook v. Woodham et al.*, the U.S. District Court for the Western District of Pennsylvania dealt with design liability and other issues arising in a wrongful death case involving a construction accident on an airport runway extension and repaving project.[217]

In yet another 2008 case, *Quinn Construction, Inc. v. Skanska U.S.A. Building, Inc., et al.,* the U.S. District Court for the Eastern District of Pennsylvania addressed design liability issues arising from a university construction project.[218] In that case, a concrete subcontractor on the project sued the contractor and an architectural firm, alleging that continuous design changes, incomplete drawings, and failure to provide timely review of shop drawings caused the subcontractor to incur significant additional labor costs on the project. The contractor cross-claimed against the architectural firm for any liability to the subcontractor. The court denied a motion to dismiss that had been based on a state procedural requirement for the filing of a certificate of merit in support of any claim of failure to meet professional standards. The court reasoned that the subcontractor's negligent misrepresentation claim involved an ordinary standard of negligence, rather than more serious allegations of failure to meet professional standards.

In a 2007 case, *Southern New Jersey Rail Group, LLC at ano. v. Lumbermens Mutual Casualty Co.*, a magistrate judge of the U.S. District Court (Southern District of New York) dealt with design liability issues raised on cross-motions for summary judgment.[219] The case involved construction of a light rail transit line. The plaintiff sought to invoke a Construction, Engineering and Design Professional Liability Insurance Policy issued by the defendant. The magistrate recommended granting summary judgment to the defendant, dismissing the plaintiff's claim for design liability coverage under the policy, because plaintiff did not timely tender its claims under the policy to the defendant.

[216] 648 F. Supp. 2d 1371; 2009 U.S. Dist. LEXIS 75367 (U.S. Dist. Ct. Middle Dist. Fla. 2009).

[217] 2008 U.S. Dist. LEXIS 76268 (U.S. Dist. Ct. W.D. Pa. 2008).

[218] 2008 U.S. Dist. LEXIS 45980 (U.S. Dist. Ct. E.D. Pa. 2008).

[219] 2007 U.S. Dist. LEXIS 58510 (U.S. Dist. Ct. S.D.N.Y. 2007).

B. ALTERNATIVES TO LITIGATION—ALTERNATIVE DISPUTE RESOLUTION

1. The Alternative Dispute Resolution Process

The most popular form of alternative dispute resolution (ADR) is negotiation, which occurs when the parties resolve the issue themselves at the project level. Transportation agencies commonly use this method in many of the ADRs that will be discussed in this section.

An early resolution of a construction dispute is usually in the best interests of both the owner and the contractor. The adage, "Agree for the law is costly,"[220] has particular significance in heavy construction, one of the country's most adversarial and litigious industries.[221] A single dispute early in the project, if left unresolved, may escalate into a claim that ultimately leads to litigation.[222]

Because most construction disputes involve money, they are often viewed in purely economic terms. Viewed as a business judgment, it is often better to settle and avoid the costs and risks of litigation. An owner may, however, choose litigation rather than settle to uphold some principle, or to establish a judicial precedent. In the absence of these kinds of consideration, owners often choose to settle rather than litigate the dispute. Over the past decade, the construction industry has developed a variety of nondispute resolution methods, which can be used to facilitate settlement. These methods, which include mediation, mini-trials, and Dispute Review Boards (DRBs), have proven to be useful,[223] and if used proactively can minimize and prevent claims. Their success has tended to overcome the general resistance to bringing a third-party facilitator into the negotiation process or to referring the dispute to a neutral third party for a nonbinding, advisory decision.

ADR may enhance the quality of negotiation, acceptably minimize operational delays, and yield long-term savings in time and money.[224] ADR can improve the flow of information among the parties, which can in turn lead to a creative and superior outcome while maintaining the parties' control of the outcome. ADR helps to preserve existing relationships and avoid project disruption, while promoting long-term trust and understanding. The ADR process provide the parties with an opportunity to gain a clearer understanding of their own cases, the other parties' positions, and the underlying issues, which can lead to more efficient

[220] LEGAL BRIEFS 148 (McMillian–U.S.A. 1995).

[221] James P. Groton, *Alternative Dispute Resolution in the Construction Industry*, 52 DISP. RESOL. J. 48 (1997).

[222] *Id*.

[223] *Id*. About 85 percent of those who mediate their disputes settle. *See* Douglas E. Knoll, *A Theory of Mediation*, 56 DISP. RESOL. J. 16, 18, 26 (2001); John D. Coffee, *Dispute Review Boards*, 43 ARB. J. 58 (1988).

[224] CHARLES POU, JR., CURRENT PRACTICES IN THE USE OF ALTERNATE DISPUTE RESOLUTION (Legal Research Digest 50, Transportation Research Board, 2008).

hearings and resolutions. A neutral perspective on issues can provide a fresh perspective on positions and strategy, which can lead to a successful resolution.

There is no single form that nonbinding ADR methods must follow. The method may be predetermined by the contract,[225] or one ADR method may be combined with another. Combining mediation and arbitration into one process is an example.[226] Since nonbinding ADR is voluntary, the parties may develop various hybrids to suit their needs.[227] When and how nonbinding ADR is used is up to the parties. But whatever method is agreed upon, it should represent a good faith effort by the parties to try and settle their dispute, and not be used as a means of obtaining "free" discovery.

This subsection discusses the more commonly used methods of ADR such as mediation, mini-trials, and DRBs. Arbitration is also discussed as an alternative to litigation. The subsection concludes with an overview of the Partnering process as part of a dispute resolution system designed to minimize and even prevent claims.[228]

Federal Participation

FHWA will determine federal aid eligibility on a case by case basis on any contract claim arbitration or mediation proceeding, administrative board determination, court judgment, negotiated settlement, or other contract claim settlement. Federal funds will participate to the extent that the claim is supported by the facts and has a basis in state contract law.[229]

FHWA will not participate in attorney fees or anticipated profits. FHWA will, however, participate in interest if it is allowed by state law or specification and not the result of delays caused by dilatory action of the State or contractor, and if the interest rate does not exceed the rate provided by state law or specifications.[230]

2. Nonbinding ADR

a. Mediation

Mediation is a form of structured negotiations in which the parties seek to settle their disputes with the assistance of an impartial facilitator. It is an informal nonadversarial process. In mediation, decision-making authority rests with the parties. The role of the mediator is to assist the parties in identifying issues, evaluating each party's respective positions,[231] and exploring settlement alternatives.[232] The mediator provides assistance in resolving the dispute by narrowing and clarifying issues, but does not decide the dispute.[233]

The mediation process may be contractually required as a condition precedent to engaging in litigation or arbitration. In the absence of a contract provision requiring mediation, the contract may encourage, but not compel mediation.[234]

Mediation, as a form of structured negotiations, was often used when the parties—because of personality conflicts or hard feelings—were unable to resolve their disputes through face to face negotiations. Instead of attempting to negotiate directly with each other, the parties retained a neutral third person to conduct the negotiations, usually a skilled negotiator who had a construction law background. The process was usually quick, several days at most, and relatively inexpensive.[235] In the 1980s, mediation became popular as a way of resolving construction disputes. Studies have shown that mediation usually works. About 80 percent to 85 percent of the cases submitted to mediation settle.[236] These successes have led to the adoption of standard contract provisions providing for mediation. For example, the Arizona DOT has a standard specification that provides that the contractor may request the engineer to arrange for a mutually acceptable mediator, with the cost for the mediator's services to be shared equally by the state and the contractor. [237] The Ohio DOT actively uses DRBs, and provides for mediation as an additional method of dispute resolution.

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[225] The American Arbitration Association (AAA) Mediation Rules suggest that, as to disputes, the construction contract should require mediation before resorting to litigation or arbitration. The Associated General Contractors of America form 600, article 14.3, makes mediation optional. The sample DRB contract provision makes submittal of the dispute to the DRB a condition precedent to litigation; *see* para. C.1 of App. A, at 276, AMERICAN ARBITRATION ASSOCIATION, ADR, A PRACTICAL GUIDE TO RESOLVE CONSTRUCTION DISPUTES (Kendall/Hunt Publishing Co., 1994) (hereinafter "Practical Guide").

[226] *See* AMERICAN ARBITRATION ASSOCIATION, *supra* note 192, at 217–23.

[227] For one large construction claim, the parties agreed to combine mediation with a mini-trial format (I-90 floating bridge refurbishment project). The Oregon DOT used voluntary mediation to resolve a $4 million claim. (FHWA Report, TS-84-2098 (1993)).

[228] Steven Pinnell, *Partnering and the Management of Construction Disputes*, 54 DISP. RESOL. J. 16 (1999).

[229] FHWA, CONTRACT ADMINISTRATION CORE CURRICULUM PARTICIPANT'S MANUAL AND REFERENCE GUIDE 37 (2006); *see* http://fhwa.dot.gov/programadmin/contracts/coretoc.cfm.

[230] *Id.* at 38.

[231] As discussed later, these discussions are conducted in the private sessions.

[232] Beth Paulsen & Franker Sander, *Alternative Dispute Resolutions, An ADR Primer*, ABA Standing Committee on Dispute Resolution (1987).

[233] FHWA Report, *supra* note 227, at 39.

[234] *See* Practical Guide, *supra* note 192.

[235] Usually the mediator's fee is shared equally by the parties.

[236] AMERICAN ARBITRATION ASSOCIATION, *supra* note 192, at 72.

[237] Standard Specification 105.21 (2000); *see also* PRACTICAL GUIDE, *supra* note 225.

i. The Mediation Process.—The mediation process is simple and straightforward. The parties agree on a mediator or a process for selecting a mediator through an association such as the American Arbitration Association. The parties sign a mediation agreement, which they draft or which is furnished to them by the mediator, and then they mediate.[238]

Typically, the mediation process begins with a joint session between the parties presided over by the mediator. The mediator may share any preliminary thoughts he or she may have with the parties and outline the procedure that will be followed. Following the mediator's remarks, the parties have an opportunity to make opening statements in which each party presents its case to the mediator. The parties then split up and go to separate rooms for the private sessions, or caucuses.[239]

In the private sessions, the mediator meets privately with each party. The mediator seeks to elicit compromises from a party that may lead to settlement. The critical ground rule, in these sessions, is that the discussions are confidential and cannot be revealed to the opposing party unless the party making the statement authorizes its disclosure. The mediator engages in what is commonly called "shuttle-negotiations," going back and forth between the parties communicating offers of settlement that a party has authorized. This process continues until a settlement is reached, or it becomes apparent the negotiations have reached an impasse and further mediation would be a waste of time and money.[240]

ii. Selecting the Mediator.—The selection of a skilled and forceful negotiator is essential. The mediator is not just a messenger communicating offers made by the parties. An experienced mediator may play the role of a devil's advocate, often questioning and even challenging a party position to show that its position is not as strong as the party may believe, or to show that the opposing party's position also has merit.[241]

How do you find a skilled mediator? One way is to ask other attorneys and owners who have engaged in mediation for recommendations. Other sources for recommendations are construction expert witnesses who have been involved in major construction litigation. Often, such experts will attend a mediation and develop a perspective on whom to select and whom to avoid. The American Arbitration Association and similar dispute resolution organizations are other sources for recommendations.[242]

iii. The Opening Statement.—There are two opportunities during mediation of persuading the opponent to settle. The first is the opening statement in the joint session. The second is the information provided to the mediator during the private sessions, which the mediator can use to persuade the opponent to settle.

The opening statement by each party should be persuasive and a thorough presentation of that party's position. The real purpose of the opening statement is to persuade the opposing party that your case is strong and that you are likely to prevail if the claim is litigated or arbitrated. The opening statement should not be designed solely to educate the mediator. This can be done, as necessary, in the private session. "The opening statement in mediation should not be directed toward the mediator, rather it should be directed toward the opposing party."[243]

The opening statement is usually made by counsel, and may be augmented with presentations by key project personnel and expert witnesses, as appropriate.[244] The presentation should be well organized, accurate, and thorough. It should be supported by pertinent documents, such as CPM schedules, correspondence, change orders, photographs, diary entries, and inspection reports. The use of PowerPoint slides and overhead projector transparencies should be considered. Blown-up charts to depict key information and summarized arguments can be effective.[245]

Concerns about "free discovery" and educating the opposing party should not affect the thoroughness of the opening statement. First, if the claim doesn't settle and is tried or arbitrated, it is likely that the information will be obtained through discovery. Second, and more important, is the need to persuade the opposing party that it is in its interest to settle more on your terms than to stick with its initial position.

The opening statement should not be hostile or overbearing in tone. Instead, it should be civil and business like, focusing on the key points of the dispute. This type of presentation will help set the stage for the mediator in persuading the opposing party of the risks it faces if the case is tried, and the practical advantages it gains in settling the claim.

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[238] The mediation agreement is discussed in more detail later.

[239] Peter J. Comodeca, *Ready, Set, Mediate*, 56 DISP. RESOL. J. 32 (Dec. 2001–Jan. 2002).

[240] *Id.*; *see also* Timothy S. Fisher, CONSTR. MEDIATION, 49 DISP. RESOL. J. 8, (1994); and Note, *Protecting Confidentiality in Mediation*, 98 HARV. L. REV. 441 (1984); Wayne D. Brazil, *Protecting the Confidentiality of Settlement Negotiations*, 39 HASTINGS L.J. 955 (1988); *Preparing for Mediation and Negotiation*, 37 PRAC. LAW. 66 (1991); Ross R. Hart, *Improving Your Chance of Success During Construction Mediation*, 47 ARB. J. 14 (Dec. 1992).

[241] *Getting the Mediation Process Started*, GROTON, *supra* note 192. For a discussion of various mediator styles and theories of mediation, *see* Douglas E. Knoll, *A Theory of Mediation*, 56 DISP. RESOL. J. No. 2, at 78 (2001).

[242] Timothy S. Fisher, *Construction Mediation*, 49 DISP. RESOL. J. No. 1, at 12 (1994); *A Theory of Mediation*, *id.*; *How Do You Select A Mediator?,* ADR, A PRACTICAL GUIDE TO RESOLVE CONSTRUCTION DISPUTES, *supra* note 225, at 82–83,

[243] Comodeca, *supra* note 239, at 38.

[244] *See The Value of an Expert in Today's ADR Forum*, ch. 21, ADR, A PRACTICAL GUIDE TO RESOLVE CONSTRUCTION DISPUTES, *supra* note 192, at 302; Eric R. Galton, *Experts Can Facilitate a Mediation*, 50 DISP. RESOL. J. No. 4, at 64 (1994).

[245] *Preparing to Mediate*, ch. 8, ADR, A PRACTICAL GUIDE TO RESOLVE CONSTRUCTION DISPUTES, *supra* note 225, at 97.

iv. Case Evaluation.—A party should make its own evaluation of the case and determine a reasonable settlement range, rather than relying on the mediator to establish a settlement range. However, a party's settlement position should not be overly rigid. A party should be willing to reevaluate its settlement position based on new information that could significantly affect the outcome of the case if it were litigated. In this regard, it is important to know the case and its strengths and weaknesses to properly evaluate the new information.[246]

If the new information cannot be evaluated properly without further investigation, then it may be better to adjourn the mediation until the information can be verified. Usually, this is a better course of action than being overly influenced by new information and settling too high if you are the defendant, or too low if you are the claimant.[247]

v. Candor with the Mediator.—Information provided to the mediator is confidential and cannot be used in subsequent proceedings, if the mediation fails.[248] Also, anything said to the mediator in the private session cannot be revealed to the opposing party, unless the party making the statement authorizes disclosure.[249] Since communications with the mediator are protected, a party should be frank and cooperative in the private sessions and provide the mediator with an honest assessment of the claim. Creating this type of atmosphere will promote the negotiations and serve as a "reality check" to test the soundness of a party's position.

vi. The Mediation Agreement and Confidentiality — The parties should enter into a mediation agreement establishing the ground rules for the mediation. The agreement should identify the dispute that will be mediated and the name of the mediator. The agreement should address certain "housekeeping" matters such as the mediator's fee and expenses, how they will be shared by the parties, and when and where the mediation will be held.

The agreement may address the submission of position papers by the parties to the mediator, any limitations on their length, and whether the papers will be exchanged between the parties or submitted solely to the mediator in confidence. Usually the parties will exchange position papers. This is consistent with the notion that an important feature of mediation is for the parties to persuade each other of the merits of their respective positions.[250]

It is not necessary to outline in the agreement how the mediation will be conducted. Usually, this will be covered by the mediator in the joint session. The agreement should contain a clause granting immunity to the mediator from any liability for the mediator's participation in the mediation. The agreement should identify who will attend the mediation and identify the parties' representatives who have full settlement authority.

Perhaps the most important provision of a mediation agreement is the one dealing with the confidentiality of the proceedings.[251] A public agency should consider including a clause in the agreement that allows the agency to disclose the terms of any settlement involving public funds or public issues. In *Register Div. of Freedom Newspapers, Inc. v. County of Orange*,[252] the court held that documents relating to the settlement of a claim with public funds constitute public records that are subject to disclosure under the California Public Records Act.[253] Other jurisdictions have reached a similar result.[254]

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[246] Fisher, *supra* note 242.

[247] *See* GROTON, *supra* note 221, at 105–6. The authors suggest that postponing the mediation to investigate new issues is counterproductive. Instead, the party should keep the process moving by doing a quick investigation during a break or between sessions. As a practical matter, a party's choice to proceed or adjourn will be determined by the impact that the information has on the case, its reliability, and the time needed to verify its accuracy.

[248] John W. Hinchley, *Construction Industry: Building the Case for Mediation*, 47 ARB. J. No. 2 (1992); Some states have enacted statutes that make mediation proceedings confidential. Some examples: TEX. CIV. PROC. & REM. CODE ANN. § 154.53(c); NEB. STAT. 25-2914.

[249] GROTON, *supra* note 221, at 106.

[250] *See* GROTON, *supra* note 221, at 129 for an example of a basic mediation agreement.

[251] *See* 38 PRAC. LAW. No. 2, at 32–33 (1992) for an example of a confidentiality clause for a mediation agreement. *See also* the confidentiality provision in the mediation agreement referenced in note 250 *supra*.

[252] 205 Cal. Rptr. 92, 158 Cal. App. 893 (1984).

[253] Cal. Pub. Disclosure Act, CAL. GOV'T CODE, § 6520, *et seq*. Examples of other states that have similar public disclosure or "sunshine" laws are: Florida, FLA. STAT. ANN. § 119.01 (West), *et seq*; Georgia, GA. CODE. ANN. 50-18-170, *et seq*; Maryland, MD. STATE GOV'T CODE 10-011; Missouri, MO. STAT. 610-011, *et seq*; New York, N.Y. PUB. OFF. LAW § 84 (McKinney); Michigan, MICH. STAT. 15.231, *et seq*; Ohio, OHIO STAT. 149.43; South Carolina, S.C. CODE 30-4-10, *et seq*; Washington, WASH. REV. CODE 42.17.010, *et seq*.

[254] Daily Gazette Co. v. Withrow, 350 S.E.2d 738 (W. Va. 1986); Miami Herald Pub. Co. v. Collazo, 329 So. 2d 333 (Fla. App. 1976); Kingsley v. Berea Bd. of Ed., 653 N.E.2d 653 (Ohio App. 1990); Dutton v. Guste, 395 So. 2d 683 (La. 1981); Anchorage Sch. Dist. v. Anchorage Daily News, 779 P.2d 1191 (Ak. 1989); Yakima Newspapers v. City of Yakima, 890 P.2d 544 (Wash. App. 1995). Annotation, *What Are Records of Agency Which Must be Made Available Under State Freedom of Information Act*, 27 A.L.R. 4th 680 ("Settlement agreements and contracts") § 16, at 723–725 (1984).

vii. Other Guidelines.—

• A party should have one spokesman. Other party representatives should not speak unless called upon to do so by the spokesman. This guideline applies to both the joint and private sessions. It is critical that the attorneys have the presence of, or access to, the real decision makers of each of the parties, so that issues can be efficiently resolved and negotiations promptly concluded.

• After sufficient discovery is conducted to fill in any significant gaps in the case, the parties should consider a moratorium on discovery. This saves the cost of discovery and allows the parties to concentrate on preparing for the mediation, instead of being distracted by ongoing discovery, particularly depositions. This guideline applies where a lawsuit has been filed or a demand for arbitration has been made.

• When mediation is voluntary (not mandated by the contract), the owner should not agree to mediation until the owner is satisfied that it has sufficient information concerning the claim to be able to evaluate settlement positions during the mediation process.

• Once a settlement is reached, the principal terms of the settlement should be put in writing and signed by the parties. Counsel should prepare an outline of the important settlement terms in advance and bring them to the mediation.

viii. Advantages and Disadvantages.—Mediation has certain advantages in addition to creating an opportunity for the parties to engage in meaningful negotiations that may resolve their dispute. Mediation allows the parties to "test the waters" by having the mediator explore settlement possibilities with the opposing party. It allows the negotiations to be conducted by a skilled and impartial negotiator. The obvious drawback is the expense invested in the process, and to some extent "free discovery." In addition, a settlement may be too high or too low, because a party was overly influenced by the mediator to settle. However, the better a party understands the case, the better it will be able to evaluate the case and make an informed decision on whether to settle or proceed to litigation or arbitration.

ix. Authority To Mediate.—Do public agencies need statutory authority to engage in mediation? Generally, the power to contract, and to sue and be sued, carries with it the implied power to settle disputes arising out of the contract.[255] This should include mediation since it is simply a form of structured negotiations.

x. Mandatory Mediation.—Should mediation be contractually required as a condition precedent to arbitration or litigation, or should mediation be purely voluntary? Those who favor mandatory mediation argue that even if the mediation fails, the mediation process forces the parties to test their positions before a neutral mediator, which may lead to a settlement.[256] There are those, however, who believe that mediation should be voluntary.[257] If a party is not willing to compromise its position, it is unlikely that the claim can be settled. Why should a party who is unwilling to compromise be required to go through a process that, as a practical matter, will be meaningless? In rebuttal, some argue that mediation should be required by the contract because it creates an opportunity for settlement, and that is sufficient reason to require mediation as a condition of the contract.[258] But there is an old proverb that "you can lead a horse to water, but can't make it drink." The same is often true for a party who is unwilling to negotiate or compromise its position. The party can be forced to attend the mediation —to satisfy the condition precedent so that it can bring suit or demand arbitration—but it cannot be forced to negotiate.

b. The Mini-Trial

i. The Mini-Trial Process.—A mini-trial is a form of structured negotiations in which each party makes a summary or abbreviated presentation of its position to a panel composed of the parties' principals, who have authority to settle the claim. The parties' positions may be presented by witnesses, usually in narrative form. Cross-examination is limited, or not permitted, as determined by the parties. The hearing is confidential; nothing said can be used by the parties in subsequent proceedings. The hearing is adversarial; each party presents its best case. However, the presentations nevertheless should be civil in tone. After the mini-trial is concluded, the principles will try to negotiate a settlement. The process may be facilitated by a neutral who, serving as the moderator, keeps the process on track and running smoothly. The facilitator can also serve as a mediator when the principals try to negotiate a settlement of the claim.[259]

ii. History.—Mini-trials have been widely used for 2 decades in the private sector and in some federal agencies.[260] The U.S. Army Corps of Engineers has led the way among federal agencies in the use of mini-trials. The use of mini-trials as a voluntary method of resolving contract disputes received further encouragement with the enactment of the Disputes Resolution Act.[261] The mini-trial process has been used successfully to

[255] E.E. Tripp Excavating Contractor, Inc. v. Jackson County, 230 N.W.2d 556 (Mich. App. 1975). (Power to contract carries with it the power to adjust disputes in the manner deemed most expeditious by the public agency, unless the manner it chooses is prohibited by statute). M.S. Kelliher Co. v. Town of Wakefield, 195 N.E.2d 330 (Mass. 1964) (town had authority to agree to arbitration as a means of resolving contractual dispute rather than by litigation).

[256] Hinchley, *supra* note 248, at 40.

[257] For example, the AGC favors making mediation optional. *See* note 225 *supra*.

[258] The AAA recommends mandatory mediation in its Mediation Rules, note 225 *supra*.

[259] Lester Edleman & Frank Carr, *The Mini-Trial: An Alternative Dispute Resolution Procedure*, 42 ARB. J., No. 1, at 7 (1987); GROTON, *supra* note 221, at 233–43.

[260] POU, *supra* note 224, at 17.

[261] 5 U.S.C. § 581*, et seq*.

settle large construction claims.[262] Mini-trials have, however, not been in wide use in transportation agencies. As an exception, a mini-trial was used by PennDOT to settle a construction dispute on the Schuylkill Expressway Project. The parties were represented by participants who had authority to settle, including FHWA participants who had authority to approve the settlement.

iii. Mini-Trial Agreement.—The mini-trial agreement should set the ground rules on how the mini-trial will be conducted and contain a clause making the proceedings confidential. The agreement should identify the principals who will hear the presentations and the neutral who will serve as the facilitator. The agreement should contain a schedule of the proceedings and how the time for the presentations will be allocated between the parties. It should also address the immunity of the facilitator and the sharing of his or her fees by the parties.[263]

iv. Advantages and Disadvantages.—The primary advantage of the mini-trial is that it provides an opportunity for the parties to explore the strengths and weaknesses of their respective positions in a structured, confidential setting designed for settlement purposes. Its disadvantages are the time and expense invested in the process. Also, a mini-trial is not suitable if the outcome of the dispute turns mainly on the application of some legal precedent or legal principal.[264]

c. Dispute Review Boards

i. Purpose.—A Dispute Review Board (DRB) is a nonbinding ADR method that is established by the owner and the contractor to decide construction disputes that arise during the course of the project.[265] It involves a board of impartial professionals formed at the beginning of the project to follow construction progress, encourage dispute avoidance, and assist in the resolution of disputes for the duration of the project.[266] DRBs serve an important role in dispute avoidance. If a dispute occurs, the function of a DRB is to provide recommendations as to how a dispute should be resolved. The owner and the contractor can then use the recommendation in their settlement negotiations.[267] However, unlike other forms of nonbinding ADR, the recommendations, depending on contract specifications and provisions, may not be confidential.[268] Moreover, the DRB Specifications may provide that "…the written recommendations, including any minority reports will be admissible as evidence in any subsequent litigation."[269] Generally, a DRB serves as an ad hoc method of resolving disputes; disputes that if not resolved could fester and eventually lead to litigation or arbitration.

DRBs are commonly used on large, complex projects. The DRB process has been found to be successful in preventing disputes, and also in achieving early resolution when disputes occur, as it involves trusted expert neutrals who have the confidence of the parties, and whose objective decisions can administer a "dose of reality." [270]

History of DRBs

In 1975, the underground industry held the first DRB in connection with the second bore of the Eisenhower Tunnel on I-70 in Colorado. The DRB heard three disputes and was overwhelmingly successful, and all parties were pleased with the results. Other successful DRBs followed, and over the following 3 decades DRB usage spread rapidly throughout North America and the world. In 2010, DRBs were used in over 2,200 projects worth $150 billion in construction value.

The DRB issues a recommendation based upon an analysis of the provisions of the contract documents, applicable law, and the facts and circumstances of the dispute. It is not mediation or arbitration, and requires training to become familiar with the unique role and obligations of a DRB member.

DRBs at DOTs, Models of State Practice

Transportation agencies have used DRBs on numerous large bridge, tunnel, and highway projects with remarkable success. The Dispute Resolution Board Foundation (DRBF), a nonprofit corporation that promotes DRB usage, reports that 98 percent of DRB projects were completed without litigation or arbitration. The DRBF-published guide specifications and standard three party agreements are a useful resource. DRBs are in active use for DOTs in Alaska, California, Delaware, Florida, Hawaii, Idaho, New York, Ohio, Maine,

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[262] *See* the discussion of cases in which mini-trials were used successfully in Douglas H. Yarn, *Mini-Trial*, *in* ADR, A PRACTICAL GUIDE TO RESOLVE CONSTRUCTION DISPUTES 233–34. Several states have had success in using mini-trials to resolve construction claims. For example, the Pennsylvania Department of Transportation achieved settlement of a major construction claim on the Schoylkill Expressway ($38.4 million claim settled for $7.5 million), *State Laws and Regulations Governing Settlement of Highway Construction Contract Claims and Claim Disputes* (No. FHWA-TS-84-209 (1993)).

[263] *See* PUB. CONT. L.J. No. 3 71–75 (1995) for a sample mini-trial agreement.

[264] *See* Yarn, *supra* note 262, at 234–36.

[265] A sample DRB specification is shown in App. A to ch. 20, *Dispute Review Boards*, GROTON, *supra* note 221, at 274–80. A sample DRB three-party agreement is shown in App. B, at 281–94. A sample DRB guideline is shown in App. C, at 295–97.

[266] DRBF Administrative & Practice Workshop, Seattle, Washington, Sep. 2011.

[267] John D. Coffee, *Dispute Review Boards*, 43 ARB. J. No. 4, at 58 (1988); *Avoiding and Resolving Disputes During Construction*, The Technical Committee on Contracting Practices of the Underground Technology Research Council (1991).

[268] *Supra* note 198.

[269] *See* sample specification, § B11, at 276, App. A, note 265 *supra*, and American Society of Civil Engineers Model Specification at 338–44.

[270] POU, *supra* note 224, at 16.

Maryland, Massachusetts, Nevada, Oregon, Virginia, Washington, West Virginia, and Wisconsin. Caltrans uses DRBs for all contracts over $10 million, and has adopted either three-member or single-member DRBs for most of its construction program. Florida uses DRBs for all contracts over $10 million, and uses regional DRBs for most of the other construction projects, which has resulted in drastic reductions in claim litigation. Ohio uses DRBs for all projects over $25 million. One of the nation's highest profile projects, the Central Artery Tunnel Project ("Big Dig") in Boston, used DRBs on 24,000 issues with 500 meetings of the DRB, and only 31 issues were raised to formal hearings.[271]

DRBs also have been, and are, in active use in many transit projects for WMATA, New York City Metropolitan Transit Authority, and Miami International Airport.

DRBF's best practices provide:

1. DRB members are neutral and subject to the approval of both parties.
2. DRB members sign a three-party agreement obliging them to serve both parties equally.
3. DRB fees and expenses are shared equally by the parties.
4. The DRB is organized when work begins, before there are any disputes.
5. The DRB keeps abreast of job developments by reviewing relevant documentation, and by making regular visits to the site.
6. Either party can refer a dispute to the DRB.
7. If a dispute is referred to a DRB, an informal and comprehensive hearing is convened promptly.
8. The written recommendation of the DRB is nonbinding, although admissible in later litigation.

ii. Selection and Disclosure.—The composition of a DRB is specified in the contract documents. Typically, a DRB is composed of three members:[272] one member selected by the owner and approved by the contractor, one member selected by the contractor and approved by the owner, and a third member selected by the other two board members who also must be approved by the owner and the contractor. The member usually serves as the chairperson.[273] The contract specifications also require that all DRB members must be experienced with the type of construction involved in the project.[274] Essential elements of the DRB process are that the DRB members must be experienced and technically qualified, must be impartial and have no conflict of interest, and must be trained in the DRB process. Many transportation agencies insist that prospective board members be trained in DRB operations and practices, and often offer DRBF training for the attorneys, engineers, contractors, and consultants involved in a project. Replacement members are to be appointed in the same manner as the original members were appointed.[275] After the DRB members are selected, the owner, the contractor, and the DRB members must sign a three-party agreement, which governs the operations of the DRB.[276]

iii. DRB Operations.—The function of the DRB is spelled out in the contract, and in the operating procedures adopted by all the parties. After the DRB is formed and all parties sign the three-party agreements, DRB operating procedures are reviewed and signed by all parties. The DRB is an advisory body assisting the parties in the resolution of contract disputes,[277] and may issue formal recommendations after formal submissions and a hearing, or informal oral advisory opinions after brief informal presentations. The DRB provides written recommendations to the owner and the contractor. These recommendations, while advisory and nonbinding, are admissible as evidence in subsequent litigation or arbitration proceedings.[278] Generally, lawyers do not make the presentations, but are available to address legal issues if both parties agree. The Ohio DRB model, however, prefers lawyers to serve as DRB chairs. The DRB's recommendation, if not accepted by all parties, is usually used as the basis of future negotiations, which contributes to DRBs' 98 percent success rate.

Generally, the DRB procedure is similar to arbitration, although the DRB's recommendations are advisory and not binding. The party that has the dispute goes first, followed by the other party. Each party is permitted to rebut what the other has said until all aspects of the dispute are thoroughly covered. Each party may call witnesses. Presentations are made narratively, and the witnesses may use exhibits to support or to illustrate

[271] *Id.* at 16.

[272] A DRB could consist of one member to reduce costs, or as many as five members, as was done on the English Channel Tunnel Project. It is important to have an odd number of members to ensure a majority decision and avoid a tie, which could happen with an even numbered panel if there was a split decision.

[273] Sample DRB specification, § E, DRB Members, App. A, *supra* note 265, at 277.

[274] *Id*. The goal in selecting the third member is to complement the experience of the other two members. Dispute Review Board Three Party Agreement, § II.A, App. B, *supra* note 265, at 282.

[275] *Id*.; App.B, § F, at 283.

[276] App. B, *supra* note 265.

[277] App. A, § D, *supra* note 265.

[278] App. A, § B.11, *supra* note 265. There is not unanimity as to whether the DRB's recommendations should be admissible in evidence in subsequent dispute resolution proceedings. Daniel D. McMillan, *An Owner's Guide to Avoiding the Pitfalls of Dispute Review Boards on Transportation Related Projects*, 27 TRANSP. L.J. 181, at 198–99 (Spring 2000) (Discussing why owners should consider deleting the provision concerning admissibility of DRB recommendations). The majority view, that the recommendation should be admissible, is based on the premise that the parties are more inclined to accept the DRB's recommendation when the contract provides that the recommendation will be admissible in any subsequent litigation or arbitration. "Alternative Dispute Resolution in the Construction Industry," *supra* note 221, at 53.

their testimony. There is no cross-examination by the opposing party, and the formal rules of evidence do not apply, but the DRB members may ask questions. A refusal by a party to provide information requested by the DRB may be considered by it in making its findings and recommendations.[279]

After the hearing is concluded, the DRB meets in private to discuss and decide the dispute. Its findings and recommendations are then submitted as a written report, including a minority report if a member dissents, to both parties. Either party may request the DRB to reconsider its recommendation based on new evidence.[280] Although DRB reports are admissible in future proceedings, three-party DRB agreements generally provide that DRB members cannot be called to testify, nor can DRB members' notes be admissible.

If a party refuses to attend a DRB hearing, the party requesting the hearing may seek a court order to compel the recalcitrant party's attendance.[281]

iv. Canon of Ethics.—

Ethical Considerations

Because the DRB's recommendations are not binding and may be rejected by the owner or the contractor, it is essential that both parties have confidence in the DRB process and in each of its members.[282] If either party loses confidence in the DRB, a party is unlikely to give weight to an unfavorable recommendation, making the DRB process ineffective.[283]

DRBF members subscribe to five Canon of Ethics, which provide that:

1. DRB members shall disclose any interest or relationship that could possibly be viewed as affecting impartiality or create the appearance of partiality or bias. This obligation is a continuing obligation throughout the life of the contract.

2. Board members shall be above reproach; there shall be no *ex parte* communication except as provided in operating procedures.

3. Board members should not disclose confidential information.

4. Board members should conduct meetings and hearings in an expeditious, diligent, orderly, and impartial manner.

5. A DRB shall consider all claims and disputes referred to it. Reports shall be based solely on the provisions of the contract documents and facts of the dispute.

v. History and Popularity of the DRB Concept.—DRBs owe their popularity to the fact that the DRB's recommendations have generally been accepted by the contracting parties.[284] While the DRB concept is popular, it is not a panacea for all construction disputes. DRBs are well suited for the resolution of construction issues that invariably crop up during the course of the work. The fact remains, however, that the DRB concept has proven to be a useful tool in resolving construction disputes. Moreover, the establishment of a DRB tells potential bidders that the owner believes in trying to resolve disputes by engaging neutrals, who are experts in construction, to assist the parties in resolving their disputes. This could result in lower bids by reducing contingent amounts included in bids for anticipated legal costs in litigating construction claims.[285]

d. Hybrid ADR

While mediation and mini-trials are the more common ADR methods, the parties are free to create other ways of resolving their contract disputes. Mediation combined with arbitration (Med-ARB) is an example.[286] Under this hybrid, the parties mediate the dispute and if the dispute is not resolved, it is referred to arbitration for a binding resolution. The person who served as the mediator may or may not serve as the arbitrator.[287]

Mediation can be combined with a mini-trial format in which presentations are made by witnesses to the mediator in a joint session. The mediator can use the information obtained during the mini-trial to provide each party, in the private sessions, with a confidential assessment of the claim and the probable outcome if the parties proceed to litigation or arbitration.[288] A variation of this method is fact-based mediation. In this method, the mediator, after making a thorough investigation of the claim, issues a detailed, confidential report

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[279] App. C, Dispute Review DRB Guidelines, *supra* note 265, at 295.

[280] *Id*.

[281] "An Owner's Guide to Avoiding the Pitfalls of Dispute Review Boards on Transportation Related Projects," *supra* note 278, at 200. The article also discusses the pros and cons of proceeding with a DRB hearing in the absence of one of the parties.

[282] The requirement in the contract that each party must approve the other's member, and the third member selected by the two members, is designed to establish neutrality and make the DRB function as an objective, impartial, and independent body. *See* CONSTRUCTION DISPUTE REVIEW BOARD MANUAL 27–30, 40 (McGraw Hill 1995).

[283] L.A. County Metro. Transp. Auth. v. Shea-Kiewit-Kenny, 59 Cal. App. 4th 676, 69 Cal. Rptr. 2d 431 (1997) (DRB specification only allowed a DRB member to be terminated for cause. Owner terminated its member for cause when the member told the owner, during the second day of the hearing, that it should settle because it was going to lose. The court found that the owner had cause to terminate its member). Ex parte communications between DRB members and the owner or contractor are prohibited. The DRB members are specifically forbidden to give consulting advice to either party. CONSTRUCTION DISPUTE REVIEW BOARD MANUAL, *supra* note 282.

[284] Groton, *supra* note 221.

[285] ADR, A PRACTICAL GUIDE TO RESOLVE CONSTRUCTION DISPUTES, *supra* note 225, at 272.

[286] *Id*. ch. 16, Med-ARB, at 217.

[287] *Id*. Serving as both the mediator and arbitrator could affect the parties' willingness to make compromises and be candid with the mediator.

[288] *Supra* note 227.

to each party stating a recommended settlement figure and the factual basis for the recommendation. The parties can then use the report for further negotiations.[289]

Some transportation agencies use a hybrid ADR process. In South Dakota, an in-house expert outside adjuster (similar to an engineering neutral) who is selected by the agency and reports to the agency recommends appropriate resolutions to the Secretary of Transportation. In South Dakota, 10 cases annually utilize this process to assist the agency and the contractor to reach a negotiated result.[290] In Vermont, the Agency of Transportation Board provides appellate review of contract claims.[291]

In short, there is no single format that ADR must follow. Since ADR is consensual, the parties are free to create any process that suits their needs in resolving construction disputes.[292]

3. Arbitration of Construction Claims

a. Overview

Arbitration has become the most widely used method of resolving construction disputes between private contracting parties.[293] Most states have enacted arbitration statutes modeled after the Uniform Arbitration Act adopted by the National Conference of Commissioners on Uniform State Laws.[294] The Federal Arbitration Act (FAA) authorizes enforcement of arbitration agreements that affect interstate commerce.[295] However, arbitration is not authorized for dispute resolution when the Federal Government is one of the disputing parties. Contract disputes involving the Federal Government are resolved in accordance with the procedures specified in the Contract Disputes Act.[296]

Arbitration is generally favored by the courts as an expeditious means of resolving contract disputes.[297] This was not true under the common law. The common law viewed arbitration as an improper attempt to deprive or oust the courts of jurisdiction to hear contract disputes.[298] This view is now generally obsolete. With the enactment of statutes providing for judicial enforcement of arbitration agreements and a change in judicial attitude, arbitration agreements are entitled to be enforced on the same terms as any other contractual undertaking.[299]

b. The Arbitration Process

Litigation and arbitration are governed by rules. Litigation is conducted in accordance with the civil rules of procedure and the rules of evidence in effect in the jurisdiction where the case is filed. Arbitration, although less formal, is governed by the rules specified in the arbitration clause, normally the Construction Industry Arbitration Rules of the American Arbitration Association.[300] These rules, which were revised in 1996, create three classes of claims:

1. Fast track (claims less than $50,000).
2. Regular track (claims $50,000 to $1 million).
3. Large, complex case track (claims over $1 million).

The new rules are designed to speed up and streamline the arbitration process. While arbitration is not as formal as a trial, it would be a mistake to approach arbitration as some sort of "fact-finding" process, where each party tells its story and then leaves it up to the arbitrator or arbitrators to sort out the truth and reach a fair result. It would also be a mistake to regard arbitration as a Solomonic process in which the arbitrators invariably "split the baby." Instead, one should prepare for arbitration much like one would prepare for a trial. The key to successful arbitration, like successful litigation, is sound and thorough preparation.[301] In an arbitration proceeding, direct and cross-examination usually follow a question-and-answer format.[302]

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[289] ADR, A PRACTICAL GUIDE TO RESOLVE CONSTRUCTION DISPUTES, *supra* note 225, "Considering Fact-Based Mediation," at 96.

[290] POU, *supra* note 224, at 16.

[291] *Id.*

[292] While research has not disclosed any laws that mandate a particular form of nonbinding ADR that state transportation agencies must follow, a few states require arbitration as the sole remedy for the final resolution of a public works contract dispute, if the parties cannot settle the dispute through negotiations. *See generally* table in § 6.3.B.

[293] ADR, A PRACTICAL GUIDE TO RESOLVE CONSTRUCTION DISPUTES, *supra* note 225, at 71.

[294] *See, e.g.*,: CONN. GEN. STAT. 52-412; GA. CODE ANN. 9-9-9; HAW. REV. STAT. 658-76; TEX. ANN. CIV. STAT. art. 224; UTAH CODE ANN. 78-31A; WASH. REV. CODE ch. 7.04.

[295] 9 U.S.C. § 2. The meaning of "interstate commerce" as used in the Act is broadly construed, *In re Gardner Zemke Co*., 978 S.W.2d 624 (Tex. App. 1998); St. Lawrence Explosives Corp. v. Worthy Bros. Pipeline Co., 916 F. Supp. 187 (N.D.N.Y. 1996); *see also* Indemnity Ins. Co. of N.A. v. ABA Power, 925 F. Supp 705 (S.D.N.Y. 1996) (preemption of state law when the arbitration agreement specified that state law will apply).

[296] 41 U.S.C. 601, *et seq*. *See* 16 PUB. CONT. L.J. 66; 50 YALE L.J. 458.

[297] Maross Constr., Inc. v. Central N.Y. Regional Transp. Auth., 488 N.E.2d 67 (N.Y. 1985).

[298] *Id*.; L.H. Lacy Co. v. City of Lubbock, 559 S.W.2d 348 (Tex. 1977).

[299] Hetrick v. Friedman, 602 N.W.2d 603, 610 (Mich. App. 1999).

[300] *The General Conditions of the Contract for Construction*, American Architect Institute (AIA) Document A201, incorporates the Construction Industry Arbitration Rules of the AASAZ. The following state transportation agencies that employ arbitration use the AAA rules: Arizona, Connecticut, Delaware, Oregon, and Washington. *See* table § 6.B.3.

[301] "How to Win at Arbitration," ch. 12, ADR, A PRACTICAL GUIDE TO RESOLVE CONSTRUCTION DISPUTES, *supra* note 225, at 157–75.

[302] *Id*. *See also* "The Expert in ADR," *id.* at 303–05, suggesting a narrative form of expert testimony where it is necessary to explain technical issues to the panel. However, the panel's expertise should be kept in mind by the attorney and the ex-

The presentation to the panel, which is usually made by counsel, should be organized, interesting, and credible. The use of models, photographs, videos, and other demonstrative exhibits to illustrate the testimony help accomplish this goal. Affidavits should be used to establish routine facts that the opposing party is unwilling to stipulate to. Another technique is to use affidavits for direct testimony, leaving live testimony for cross-examination.[303] Although the rules of evidence do not apply in arbitration, objections to questions that are unfair or improper should be made. Objections should also be made to testimony that is clearly out-of-bounds.[304]

The use of summaries should be considered as a method of presenting voluminous information. The party offering a summary should give the opposing party the opportunity to review the underlying data on which the summary is based in advance of the hearing. Documents that will be used as exhibits should be pre-numbered and, if possible, stipulated to in advance of the hearing. Bulky documents, such as the contract plans and specifications, should be available in the hearing room. Less bulky documents that have been agreed to, such as correspondence, change orders, excerpts from reports, diary entries, memoranda, and inspection reports should be placed in notebooks in numerical order, according to how they are pre-numbered, for use by the arbitrators, the witnesses, and counsel. Each arbitrator should have his or her own notebook for use during the hearing.

Briefs should be submitted after the evidentiary hearing is closed.[305] Documents referred to in the brief should be identified by their number in the notebook. Arbitrators should not be forced to sift through a mass of documents in the notebooks to find some document referred to in the brief just by its description or title. Legal authority should be used wisely. Citing case after case is usually ineffective. It is better to cite a case that is a precedent than cite a string of cases from other jurisdictions. Copies of cases that are cited should be attached as an appendix to the brief. Important language in the case should be highlighted. The brief should explain why the law applies, how its application dictates the result that the party is seeking, and why that result is fair and furthers public policy.[306] The brief should be written in clear, plain English; the use of legalese should be avoided. The brief should be accurate, persuasive, and supported by references to the record. In this sense, what persuades judges should also persuade arbitrators, although arbitrators, unlike judges, are not bound by legal precedent. In short, a good post-hearing brief should serve as a map that the arbitrators can use in reaching their decision.

Arbitration may be waived by failing to demand it within the time required by the contract,[307] by commencing litigation,[308] or by failing to plead the agreement to arbitrate as an affirmative defense in an answer to a complaint in a lawsuit.[309] Also, arbitration may be time-barred when the demand for arbitration is filed after the statute of limitations has expired.[310]

Generally, an arbitrator's decision on questions of fact or law is conclusive,[311] and can only be modified or vacated in accordance with the grounds specified in the state's arbitration act.[312] An arbitrator's decision may collaterally estop another party in a subsequent proceeding[313] or bar a later claim based on *res judicata*.[314]

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pert in presenting expert testimony. Construction arbitration panels are usually knowledgeable about construction issues, project delays, and damages. *See also* James J. Meyers, *10 Techniques for Managing Arbitration Hearings*, 51 DISP. RESOL. J., No. 1., at 28 (Jan.–March 1996). The author discourages the use of expert witnesses except where an issue cannot be resolved without them, at 29.

[303] *10 Techniques for Managing Arbitration Hearings*, *id.* at 28.

[304] Handling Objections, ADR, A PRACTICAL GUIDE TO RESOLVE CONSTRUCTION DISPUTES, *supra* note 225, at 170–71.

[305] In addition to a post-hearing brief, a pre-hearing brief containing a short, concise statement of the party's position is also helpful, and should be given to the arbitrators in advance of the hearing. The pre-hearing brief can be amplified by a brief opening statement, *Id.* at 162–64 (Opening Briefs and Statements), 173 (Closing Statements), 174.

[306] *See*, *e.g.*, Foster Wheeler Enviresponse v. Franklin County Convention Facilities, 678 N.E.2d 519, 528 (Ohio 1997) (purpose and public policy served by a contract provision requiring written authorization by the owner for alterations in a construction contract).

[307] Capitol Place I Ass'n L.P. v. George Hyman Constr. Co., 673 A.2d 194 (D.C. 1996). *See* 25 A.L.R. 3d 1171 (1969).

[308] Modren Piping, Inc. v. Blackhawk Auto Sprinklers, Inc., 581 N.W.2d 616 (Iowa 1998).

[309] S&R Co. of Kingston v. Latona Trucking, Inc., 159 F.3d 80 (2d Cir. 1998).

[310] Zufari v. Arch. Plus, 914 S.W.2d 756 (Ark. 1996). *See* 94 A.L.R. 3d 533 (1979); *see also* Har-Mar, Inc. v. Thorsen and Thorshov, Inc., 218 N.W.2d 751 (Minn. 1974) (arbitration not barred by statute of limitations).

[311] Garrison Assocs. v. Crawford Constr., 918 S.W.2d 195 (Ark. App. 1996).

[312] Stockdale Enters. v. Ahl, 905 P.2d 156 (Mont. 1995). Reasons for vacation of an award are narrow, and include fraud, undisclosed bias, ultra vires determinations that were not arbitrable, or misconduct on the part of the arbitrators. The court's review of an arbitration proceeding is limited to whether or not the statutory grounds for vacation exist. Mike's Painting, Inc. v. Carter Welsh, Inc., 975 P.2d 532 (Wash. App. 1999); Bennett v. Builders II, Inc., 516 S.E. 808 (Ga. App. 1999).

[313] QDR Consultants & Dev. Corp. v. Colonial Ins. Co., 675 N.Y.S.2d 117 (N.Y. App. 1998) (determination that the general contractor was liable to the subcontractor collaterally estopped the subcontractor's action against the general contractor's surety).

[314] TLT Constr. Corp. v. A. Anthony Tappe and Assocs., Inc., 716 N.E.2d 1044 (Mass. App. 1999) (arbitration decisions in favor of city barred contractor's claim against city's retained architect who was in privity with city); *see* Res Judicata and Collateral Estoppel, ADR, A PRACTICAL GUIDE TO RESOLVE CONSTRUCTION DISPUTES, *supra* note 225, at 193–98.

A question may arise as to whether a dispute is subject to arbitration.[315] Normally, this is a question for judicial determination.[316] But if arbitrability is debatable, the clause generally will be construed in favor of arbitration.[317] This view is consistent with that public policy favoring arbitration.

A party to an arbitration agreement cannot vitiate the arbitration hearing by refusing to attend. The arbitration may proceed in the absence of a party who, after notice of the hearing, fails to be present or fails to obtain a continuance from the arbitrator.[318]

c. State Transportation Agencies and Arbitration

i. Authority to Arbitrate.—Some state transportation agencies include arbitration clauses in their contracts. In Delaware[319] and North Dakota,[320] arbitration is the exclusive method for resolving contract disputes. In California, arbitration is required by statute, although the State and the contractor may agree, in writing, to waive arbitration and litigate the claim.[321] In Connecticut, the contractor has the option of electing either arbitration or litigation.[322] A few states use a mix of arbitration and litigation.[323]

In California, the California Public Works Contract Arbitration Program established an arbitration program of public work construction. The program, codified in 1981, provides "a fair and equitable resolution" of disputes between public agencies and contractors, in an attempt to reduce court congestion. Caseload in recent years has approached 20 to 25 cases.[324] Caltrans's strong adoption of the DRB process has no doubt reduced the arbitration caseload.

In the absence of express legislation authorizing arbitration as a means of resolving contract disputes, may a state contracting agency agree to arbitrate? Generally, the answer to this question is yes. A number of jurisdictions have held that the express statutory authority to contract, and to sue or be sued, waives sovereign immunity and includes, by implication, the implied power to agree to arbitration as a means of resolving contract disputes. For example, in *Dormitory Authority v. Span Electric Corp.*,[325] the New York Court of Appeals said: "…we hold that the state itself is not insulated against the operation of an arbitration clause because the power to contract implies the power to assent to the settlement of disputes by means of arbitration."

Other jurisdictions have followed the view expressed by the New Court of Appeals in cases where public agencies have attempted to avoid arbitration by contending that they lacked statutory authority to include arbitration clauses in their contracts.[326]

Statutes that expressly authorize state contracting agencies to arbitrate contract disputes may be strictly construed. Only disputes of the kind specified in the statute are subject to arbitration. If there is a serious question as to whether the dispute is arbitrable, the statute will be construed against arbitration and in favor of the state's interpretation that the claim is not subject to arbitration under the statute. In *Department of Public Works v. Ecap Const. Co.*,[327] the Connecticut Supreme Court held that the public works arbitration statute did not apply to a claim that the State had breached a settlement agreement. The statute only applied to actual construction disputes. It would not be construed to cover a claim that an agreement settling a

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[315] Department of Public Works v. Ecap Constr. Co., 737 A.2d 398 (Conn. 1999). While the state could be compelled to arbitrate whether it breached a settlement agreement of that claim, the state statute providing for arbitration only made claims directly involving the work arbitrable.

[316] *Id.*

[317] In United Steel Workers of America v. Warrior & Gulf Nav. Co., 363 U.S. 574, 585 (U.S. Ala. 1960), the court said that only the "most forceful evidence of an intention to exclude a dispute from arbitration" will be sufficient to find against arbitrability. Accord: Munsey v. Walla Walla College, 906 P.2d 988 (Wash. App. 1995); Jenkins v. Percival, 962 P.2d 796 (Utah 1998).

[318] AAA Rule 29; E.E. Tripp Ex. Con., Inc. v. City of Jackson, 230 N.W.2d 556 (Mich. App. 1975). *Contra*, see Pinnacle Constr. Co. v. Osborne, 460 S.E.2d 880 (Ga. App. 1995) (invalidating arbitration agreement in an effort to oust courts of jurisdiction—following early common law rule, which is now rejected by most courts); *see* Maross Constr. Co. v. Cent. Regional Trans. Auth., *supra* note 297, and Hetrick v. Freidman, *supra* note 299.

[319] 10 Del. C. § 5723 (1999) *et seq*.

[320] N.D.C.C. 24-02-31.

[321] State Contract Act, pt. 2, Public Contract Code, Article 7.2, § 10240.10, Waiver of Arbitration.

[322] C.G.S.A. § 4-61 (1998).

[323] Arizona: STAT. 12-1518; Missouri: STAT. 485-350; see Murray v. Highway Trans. Comm'n, 37 S.W.3d 228 (Mo. 2001), (arbitration of negligence case); Mississippi: STAT. 435-350; New Mexico: STAT. 12-8A-3; Oregon: STAT. 20-330 (acknowledging Dep't of Transportation's authority to include arbitration clauses in its contracts); Rhode Island: R.I. GEN. LAWS, § 37-16-1, *et seq*.; Washington: WASH. REV. CODE 39.04.240 (recognizing state agency's authority to use arbitration clauses in its construction contracts).

[324] POU, *supra* note 224, at 18.

[325] 218 N.E.2d 693, 696 (N.Y. 1966).

[326] Watkins v. Department of Highways of Com. of Ky., 290 S.W.2d 28 (Ky. 1956); Pytko v. State, 255 A.2d 640 (Conn. Super 1969); City of Hartford v. American Arb. Ass'n, 391 A.2d 137 (Conn. Super. 1978); Charles E. Brohawn Bros. v. Bd. of Trustees of Chesapeake College, 304 A.2d 819 (Md. 1973); State by Spannaus v. McGuire Architects-Planners, Inc., 245 N.W.2d 218 (Minn. 1976); Paid Prescriptions v. State Dep't of Health & Rehabilitative Services, 350 So. 2d 100 (Fla. App. 1977); Holm-Sutherland Co. v. Town of Shelby, 982 P.2d 1053 (Mont. 1999); E.E. Tripp Ex Con, Inc. v. City of Jackson, 230 N.W.2d 556 (Mich. App. 1975); Annotation, 20 A.L.R. 3d 569 (1968); City of Atlanta v. Brinderson Corp., 799 F.2d 1541 (11th Cir. Ga. 1986); 4 AM. JUR. 2D *Alternative Dispute Resolution* § 106 (1995).

[327] *Supra* note 315. Statutes that waive sovereign immunity are strictly construed. This rule applies to statutes that authorize arbitration as a means of resolving public contract disputes.

construction dispute had been breached by the State.

ii. Advantages and Disadvantages.—Contract disputes that remain unresolved often develop into a claim leading to litigation or arbitration. The forum selected to resolve the claim usually depends upon the final dispute resolution method specified in the contract or by a statute.[328] Which forum is better for an owner—arbitration or litigation? Those who favor arbitration agree that arbitration is quicker, cheaper, and more efficient than litigation. Those who favor litigation argue that litigation has better safeguards because of the rules of evidence, the application of legal precedent, and broader appeal rights. There doesn't seem to be any absolute answer as to which forum is better. Each has its own advantages and disadvantages, as depicted in the "DRBs on ADR Continuum" chart, and in Table B, on the following pages.[329]

[328] For example, the California State Contract Act specifies arbitration as the required dispute resolution method unless the state and the contractor agree to litigation, *supra* note 287.

[329] *See generally* Judge Marjorie O. Rendell, *ADR vs. Litigation*, 55 DISP. RESOL. J., No. 1, at 69 (Feb. 2000); John A. Harding, Jr., *Dealing With Mandatory ADR*, 39 TRIAL LAW. GUIDE 38 (1995); 4 AM. JUR. 2D *Alternative Dispute Resolution* §§ 8 and 11 (1995).

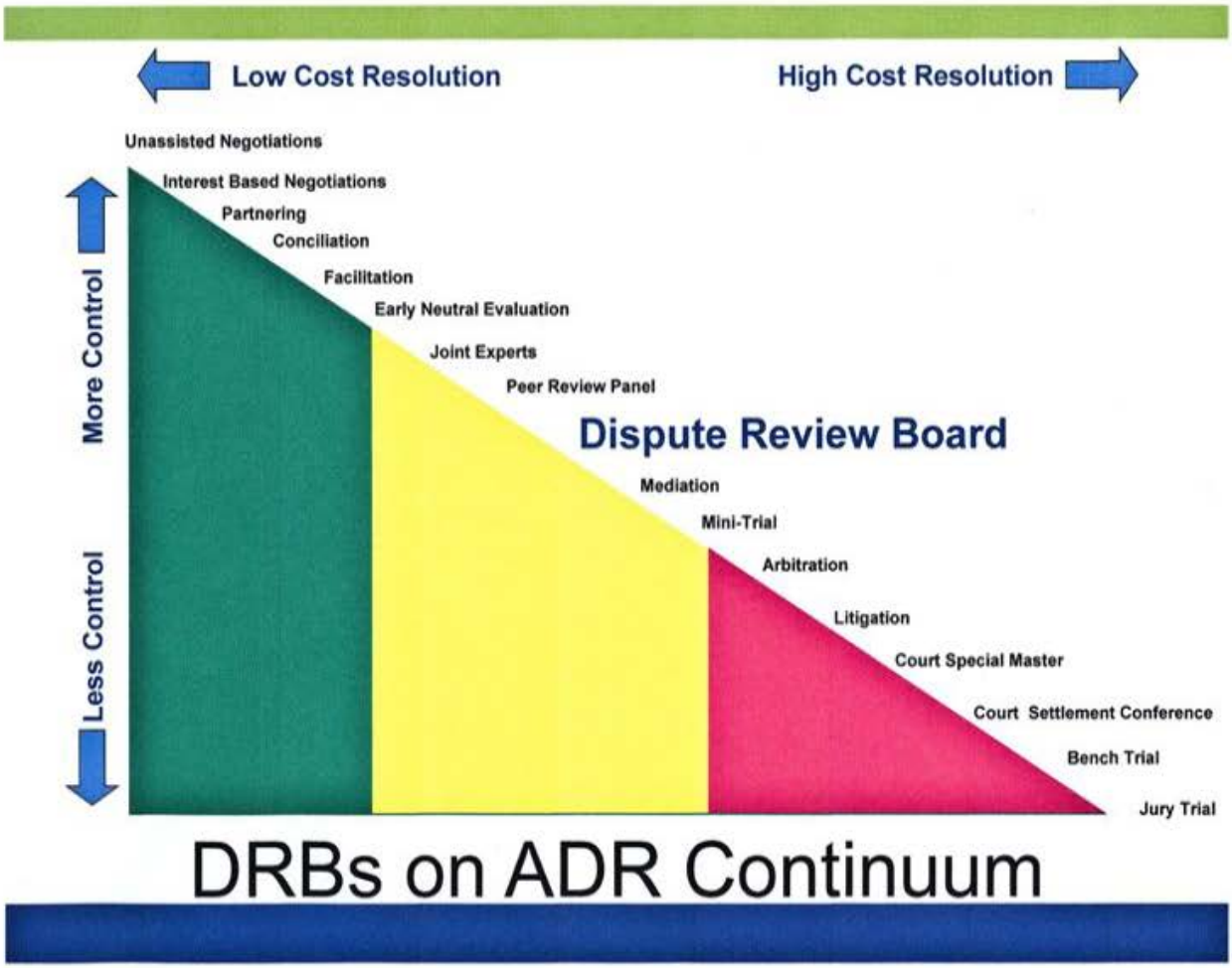
Low Cost Resolution
High Cost Resolution
More Control
Less Control
Unassisted Negotiations
Interest Based Negotiations
Partnering
Conciliation
Facilitation
Early Neutral Evaluation
Joint Experts
Peer Review Panel
Dispute Review Board
Mediation
Mini-Trial
Arbitration
Litigation
Court Special Master
Court Settlement Conference
Bench Trial
Jury Trial
DRBs on ADR Continuum

Table B. Arbitration, Litigation, and DRB Comparisons by Features.

Feature	Arbitration	Litigation	DRBs
Discovery	Restrictive	Liberal	None
Motion practice	Little if any.	Civil rules allow pre-trial motions to dismiss claims and limit evidence.	None
Evidence	Rules of evidence do not govern admissibility.	Rules of evidence apply.	Rules of evidence do not govern.
Basis for decision	Leans toward fairness—Not bound by legal precedent, favors a party who has the "equities."	Governed by legal precedent, although jury may be influenced by what it believes to be fair.	Based on facts, circumstances, and applicable law.
Complex engineering and technical issues	Arbitrators usually selected for their knowledge and technical expertise.	Decisionmaker—judge or jury—usually lacks technical expertise.	Three-person DRB.
Scheduling	More flexible and easier to schedule hearings, although this is not always true when three arbitrators are involved.	Less flexible and harder to schedule hearings because of court congestion.	Flexible.
Expense and time required for hearing	Generally less expensive, and more expeditious; however, the cost and time to resolve large, complex omnibus claims involving a three-member arbitration panel may be more expensive and time consuming than a courtroom trial.	Generally takes longer and is more expensive than arbitration.	Inexpensive.
Appeal from adverse decision	Limited—grounds for vacation of award are usually governed by statute.[330]	Broader appeal rights based on substantial evidence and conformity to legal precedent.	Limited only as to new material.

[330] The California State Contract Act provides that a court must vacate the arbitration award if it is not supported by substantial evidence, or it is not decided in accordance with state law. Public Contract Code, art. 7.2, § 10240.12.

Generally, arbitration has been the forum of choice for resolving smaller claims. Several states have implemented this view. Arizona requires mandatory arbitration for claims not exceeding $200,000.[331] Oregon requires mandatory arbitration for claims under $25,000.[332] Washington requires mandatory arbitration for claims not exceeding $250,000.[333] Each state specifies that the arbitration hearing will be conducted in accordance with the Construction Industry Arbitration Rules promulgated by the American Arbitration Association.[334]

d. Consolidation of Arbitration Proceedings

Ordinarily, courts will not compel consolidation of separate arbitration proceedings where the arbitration agreements do not contain provisions permitting consolidation.[335] The rule is based on the rationale that arbitration is consensual and thus parties cannot be compelled to arbitrate matters that they did not agree to arbitrate.[336] However, when a party signs a contract containing an arbitration clause, it waives its right to litigate disputes covered by the clause and it can be compelled to submit those disputes to arbitration.[337]

Owners who favor arbitration, and would like the flexibility of being able to join the contractor and the owner's design engineer in a single arbitration proceeding, should provide for joinder and consolidation in both the construction contract and the design contract.[338] The California public works arbitration statute authorizes such joinder of "any supplier, subcontractor, design professional, surety or other person who has so agreed and if the joinder is necessary to prevent a substantial risk of the party otherwise being subjected to inconsistent obligations or decisions."[339] A "flow-down" clause in a subcontract may incorporate an arbitration clause in the prime contract.[340] The arbitration clause will not be incorporated in the subcontract, however, unless it is clear that the subcontractor intended to submit to arbitration.[341]

4. Partnering and Use of Facilitation in Construction Administration

Partnering is not an ADR method, but is a change in the attitude and relationship between the contractor and owner.

Partnering is a nonbinding process initiated at the outset of the construction project. The process involves a workshop attended by the owner and the contractor. The workshop may be conducted by a professional facilitator who guides the discussions. The workshop is designed to accomplish several goals: First, it encourages the parties to recognize that it is in their interest to resolve problems as they arise rather than let them fester and grow into bigger problems. Partnering encourages the parties to trust each other and try to resolve their disputes through negotiations, rather than by litigation.

The cost of partnering sessions is typically shared equally by the owner and contractor, and federal funds may be used to reimburse owners for their shares of the costs.[342]

The partnering process was developed by the U.S. Army Corps of Engineers in the 1980s for a major construction project on the Columbia River. The purpose of partnering has been described as follows:

> Partnering is the creation of an owner-contractor relationship that promotes achievement of mutually beneficial goals. It involves an agreement in principle to share the risks involved in completing the project, and to establish and promote a nurturing partnership environment. Partnering is not a contractual agreement, however, nor does it create any legally enforceable rights or duties. Rather, Partnering seeks to create a new cooperative attitude in completing government contracts. To create this attitude, each party must seek to understand the goals, objectives, and needs of the other—their "win situations—and seek ways that these objectives can overlap."[343]

In partnering, key managers meet early in a workshop to establish a working relationship, identify common objectives, and agree on what is needed to achieve objectives and solve problems. The partnering facilitator ensures that all issues are brought up, including the dispute resolution process to be used. Follow-up meet-

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[331] Stand. Spec. 105.22 (2000).

[332] Stand. Spec. 00199.40 (1996).

[333] Stand. Spec. 1-09.13 (3) (2000).

[334] The "fast track" rules apply to claims that do not exceed $50,000. The "regular track" rules apply to claims over $50,000, but less than $1 million. The rules are available from the AAA Customer Service Dept., 140 W. 51st., N.Y., N.Y. 10020-1203; Telephone: (212) 484-4000; Fax: (212) 765-4874; email: usadrsrv@arb.com.

[335] Hyundai American, Inc. v. Meissner & Wurst GmbH & Co., 26 F. Supp. 2d 1217 (N.D. Cal. 1998); Hartford Accident and Indem. Co. v. Swiss Reinsurance America Corp., 87 F. Supp. 2d 300 (S.D.N.Y. 2000).

[336] AJM Packing Corp. v. Crossland Constr. Co., 962 S.W.2d 906 (Mo. App. 1998); Diersen v. Joe Keim Builders, Inc., 505 N.E.2d 1325 (Ill. App. 1987); City and County of Denver v. Dist. Ct., 939 P.2d 1353 (Colo. 1997).

[337] Maross Constr. v. Cent. Regional Trans., *supra* note 297; 3A Indus. v. Turner Constr. Co., 869 P.2d 65 (Wash. App. 1993).

[338] *See* § 7.10.c., *supra*, discussing considerations regarding the joinder of the owner's architect/engineer in the litigation between the owner and the contractor.

[339] California State Contract Act, Public Contract Code, art. 7.2, § 10240.9.

[340] 3A Indus. v. Turner Constr. Co., 869 P.2d 65 (Wash. App. 1993).

[341] Gen. Railway Signal Corp. v. L.K. Comstock & Co., 678 N.Y.S.2d 208 (N.Y.A.D. 1998).

[342] FHWA, CONTRACT ADMINISTRATION CORE CURRICULUM PARTICIPANT'S MANUAL 160, available online at http://www.fhwa.dot.gov/programadmin/contracts/cacc.pdf, last accessed July 22, 2012.

[343] U.S. Army Corps of Engineers, *Partnering* (Pamphlet – 91-ADR-P-4).

ings are held at regular intervals to evaluate goals, objectives, and concerns. Partnering has been adopted by 46 transportation agencies, and is believed to reduce contract disputes. Arizona DOT estimates partnering has resulted in an annual cost savings of $5 million.[344]

Several transportation agencies, including Arizona, California, and Texas, have developed partnering field manuals and training activities.

Although partnering is a method of avoiding disputes rather than resolving them, it is still regarded as part of a dispute management system.[345] The partnering process has been used by a number of state transportation agencies.[346] The partnering workshop usually concludes with the parties signing a memorandum or partnering agreement.[347] The agreement provides that the contractor and the owner, with a positive commitment to honesty and integrity, agree that:

1. Each will function within the laws and statutes applicable to their duties and responsibilities.
2. Each will assist in the other's performance.
3. Each will avoid hindering the other's performance.
4. Each will proceed to fulfill its obligations diligently.
5. Each will cooperate in the common endeavor of the contract.[348]

New innovations in partnering involve "Alignment Partnering," in which facilitators align the parties' interests to improve communication and promote "project first thinking."

Partnering is not a quick fix for adversarial attitudes and antagonistic relationships that may exist between owners and contractors. Yet it can be a positive step toward improving communications between the parties and establishing a nonadversarial process aimed at resolving problems as they occur, rather than letting them fester and become worse.

5. Conclusion

The high cost of litigation and arbitration for large, complex claims has caused owners and contractors to explore alternative means of resolving their disputes, other than through litigation or arbitration. The most valuable ADR techniques are those that prevent or resolve disputes as early as possible through the efforts of individuals directly involved at the project level. Innovative owners and contractors have developed variations in traditional ADR techniques, such as hybrid mediation, specifically tailored to meet the parties' needs. In the private sector, the trend has been toward greater use of the ADR process to resolve construction disputes. Many public contracting agencies have joined this trend.

As ADR becomes even more sophisticated, it is likely this trend will increase and more public contracting agencies will take advantage of the opportunities that ADR offers.

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[344] POU, *supra* note 224, at 15.

[345] Steven Pinnell, *Partnering and the Management of Construction Disputes*, 54 DISP. RESOL. J. No. 1, at 16 (1999); James H. Kill, *The Benefits of Partnering*, 54 DISP. RESOL. J., No. 1, at 29 (1999). (This article discusses the use of partnering by the Puerto Rico Dep't of Transportation in fashioning an ADR system for the *Tren Urbano* project, a regional rail transit system in San Juan.)

[346] The following states have used partnering: Alaska, Arizona, California, Idaho, Kansas, Minnesota, Montana, North Carolina, North Dakota, New Mexico, Oregon, Texas, Utah, Washington, Wisconsin, and Wyoming. Source: Resolutions International, email: Norman Anderson@msn.com.

[347] A partnering agreement does not change the terms of the contract, or alter the legal relationship of the parties to the contract, Arizona Standard Specification 104.01 (2000).

[348] Arizona Standard Specification 104.01. The Specification provides that cost of the workshop will be shared equally by the owner and the contractor. The Arizona DOT partnering specification (104.01) is quoted in 52 DISP. RESOL. J. No. 3 (1997), at 52, *supra* note 221.

APPENDIX A

PUBLICATION REQUIREMENTS FOR INVITATIONS TO BID ON TRANSPORTATION CONSTRUCTION CONTRACTS

STATE & CITATION	PUBLIC NOTICE	OTHER REQUIREMENTS
ALA. CODE § 39-2-2	Publication once each week for 3 consecutive weeks in newspapers of general circulation in counties where project will be located.	
ALASKA STAT. § 36.30.130 2 ALASKA ADMIN. CODE § 12.130	May include newspaper publication "calculated to reach prospective bidders."	Must be posted on the Alaska Online Public Notice System at least 21 days before the bid opening date. May include posting in public place where work is to be performed or materials furnished.
ARIZ. REV. STAT. § 28-6923	Once a week for not less than 2 consecutive weeks in weekly newspaper of general circulation in state, or twice in daily newspaper, not less than 6 nor more than 10 days apart.	
ARK. CODE § 19-11-229	Must advertise not less than 5 nor more than 30 days prior to bid opening by publishing at least once in at least one newspaper of general circulation in the state or posting by electronic media.	
CAL. PUB. CONT. CODE § 10140	Publication once a week for 2 consecutive weeks, unless longer period deemed necessary by department, in newspaper of general circulation in county where project is located.	Publication for 2 consecutive weeks in construction trade journal of general circulation in San Francisco or Los Angeles for projects in those vicinities.
COLO. REV. STAT. 24-92-103(3), 24-92-104.5, 43-1-105(4)	Advertisement 14 days prior to for bid opening, may be published in newspaper of general circulation.	May include online publication, including Internet.
CONN. GEN. STAT. § 4a-57 Conn. DOT Construction Contract Bidding and Award Manual, VII.A and IX.B	Notice on the State Contracting Portal, at least 5 days before final date of bid submission.	.
29 DEL. CODE § 6962(b)	Publication at least once a week for 2 consecutive weeks in newspaper	May include mailing to registry of prospective bidders.

STATE & CITATION	PUBLIC NOTICE	OTHER REQUIREMENTS
	circulated in each county in state. Public advertising shall require electronic publication accessible to the public for 2 consecutive weeks.	
D.C. CODE § 2-354.02	Public notice for 14 days on the Internet and may include publication in newspaper of general circulation and in appropriate trade publications with provision for shorter notice of not less than 3 calendar days.	Shall maintain Internet site that provides vendors with notice of opportunities to bid as well as notice of awards.
FLA. STAT. § 337.11	For contracts under $250,000, publication in newspaper of general circulation in county where proposed work is located, once a week for at least 2 consecutive weeks, with first publication no less than 14 days prior to deadline for submission of bids.	For contracts greater than $250,000, bid solicitation notice to prequalified contractors at least 2 weeks before bids to be received.
GA. CODE ANN. 32-2-65	Advertise for at least 2 weeks, in newspapers "as will ensure adequate publicity," with one ad at least 2 weeks prior to bid opening and another 1 week after first notice.	May advertise in other publications in addition to or instead of newspaper, so long as there is adequate publicity.
HAW. REV. STAT. § 103D-302(c)	Advertise in a reasonable time before bid opening pursuant to regulations adopted by procurement policy board.	
IDAHO CODE § 40-902	Advertisement in at least two consecutive weekly issues in a weekly newspaper, in the county where the work is to be done.	
ILL. COMP. STAT. § 30 500/20-10	Publication in Illinois Procurement Bulletin at least 14 days before the date set for bid opening.	
IND. CODE § 8-23-9-1	Secure Internet bidding on Indiana Department of Transportation website.	
IOWA CODE § 313.10	Current notice to bidders and other bid letting information available on Iowa Department of Transportation website	Also advertises in Des Moines Register and in local areas.
KAN. STAT. § 68-408	Publication once per week for 2 consecutive weeks in Kansas Register.	Other notice as the Secretary deems necessary and proper.

STATE & CITATION	PUBLIC NOTICE	OTHER REQUIREMENTS
KY. REV. STAT. §§ 176.070; 424.130(1)(b)	Publication at least once by legal notice not more than 21 days nor less than 7 days prior to bid opening, in qualified newspaper.	May be published two or more times.
LA. REV. STAT. § 48:252	Publication in official journal of the state once a week for 3 weeks, first ad at least 21 days prior to bid opening.	Must also be published on electronic bidding system that is accessible to general public.
23 ME. REV. STAT. § 4243	Maine Department of Transportation engages in 100% electronic advertising currently available on its website.	
MD. STATE FIN. & PROC. CODE § 13-103(c)	Must give reasonable notice for 10 days prior to bid opening; published in "eMaryland" Marketplace; may publish in newspapers.	May publish in periodicals or trade journals.
MASS. GEN. L. ch. 81, § 8	Publish in two or more newspapers published in each county in which the highway lies, and in three or more daily newspapers published in Boston.	
MINN. STAT. § 161.32	For trunk highway construction, Publication in newspaper of general circulation once each week for 3 weeks.	Must be published on Internet.
MISS. CODE § 65-1-85	Publication once per week for 2 successive weeks in newspaper of general state circulation published in Jackson, no less than 14 days nor more than 60 days after the publication of the first notice.	May also be published in metropolitan newspaper or trade publication.
MO. REV. STAT. § 227.100.1	Advertisement published in county where work is to be done.	May be advertised in such other publications as the commission determines.
MONT. CODE § 18-2-301	Advertisement published weekly for 3 consecutive weeks, in newspaper of seat of government and in newspaper in county where work is performed.	
NEB. REV. STAT. § 39-1348	Not less than 20 days prior to opening bids, advertise once a week for 3 consecutive weeks in the official county newspaper designated by county board	

STATE & CITATION	PUBLIC NOTICE	OTHER REQUIREMENTS
	in county where work will be done, and in such additional newspapers as may appear necessary to department.	
NEV. REV. STAT. § 408.327	Once a week for 2 consecutive weeks in newspaper of general circulation in county where major part of work will be done; also, once a week for 2 consecutive weeks in one or more daily newspapers of general circulation in State; first publication not less than 15 days before bid opening.	
N.H. REV. STAT. § 237:14	Once a week for 2 consecutive weeks in newspaper of general circulation in state, first advertisement not less than 14 days prior to bid opening.	
N.J. STAT. § 27:7-29	Once a week for 3 weeks prior to bid opening in each of two newspapers printed in county or counties where project is located, and in one newspaper published in Trenton..	May publish notice in one or more American engineering periodicals.
N.M. STAT. §§ 13-1-104; 67-3-43	Published at least once, not less than 10 calendar days prior to bid opening, in at least three newspapers of general circulation where agency central office is located.	Agency may adopt other procedures, including publication electronically and in trade journals.
N.Y. HIGH. LAW, 3 § 38	Once a week for 2 successive weeks in newspaper published in county where work will be done; and in other newspapers as commissioner designates. If county has no newspaper, publication in paper of adjoining county designated similarly.	May also publish in trade journals.
19A N.C. ADMIN. CODE § 2D.0803	Advertised in widely circulated newspapers in the state prior to bid opening.	Invitations to bid made available on North Carolina Department of Transportation website to prospective bidders, , and other interested parties on day of publication.
N.D. CENT. CODE § 24-02-19	Once in official newspaper of county where project located, at least three weeks prior to bid opening.	Publication in other daily newspaper of general circulation where project is located; trade journals; written solicitations to those on bidders' list.

STATE & CITATION	PUBLIC NOTICE	OTHER REQUIREMENTS
OHIO REV. CODE § 5525.01	Publication for 2 consecutive weeks in newspaper of general circulation published in county where project is all or partially located; or, if none, newspaper having general circulation in adjacent county.	May advertise in other publications director considers advisable.
61 OKLA. STAT. § 104	Publication in two consecutive weekly issues of newspaper of general circulation published in county where work will be done, with first notice not less than 20 days prior to bid opening.	May be published in trade journals.
OR. REV. STAT. 26 § 279.055	Publication at least once in at least one newspaper of general circulation in area of project, and in as many additional publications as the contracting agency may determine..	. May also use electronic publication instead of newspaper publication.
62 PA. CONS. STAT. § 512	Must give adequate notice, which may include notice in newspaper of general circulation.	May also use notice by electronic publication available to general public; notice in trade publications; notice to mailing list; or notice to prequalified contractors' list.
R.I. GEN. LAWS §§ 24-8-12; 37-2-18; 37-2-17.1	Once in a newspaper of statewide circulation at least 7 days before the final date for receiving bids and not more than 28 days before the date set for opening of the bids, unless waived.	Invitations for bids may be accessed electronically in accordance with the Rhode Island vendor information Program
S.C. CODE § 57-5-1620	Publication for at least 2 weeks in one or more daily newspapers in the State.	May advertise for longer time and in other publications.
S.D. CODIFIED LAWS § 31-5-10 S.D. Admin. R. 70:07:01, *et. seq*.	Advertising required; department may adopt rules governing advertising.	
TENN. CODE § 54-5-114	Publication for at least 2 weeks prior to the date set for receiving bids in newspaper published in county where work will be performed and in one widely circulated daily newspaper in that area of state. If no paper published in county, publication in newspaper in adjacent county.	Bid proposals may be requested electronically.

STATE & CITATION	PUBLIC NOTICE	OTHER REQUIREMENTS
TEX. TRANSP. CODE §§ 223.002, 223.003.	Electronic Bidding System	Notice may be mailed to those contractors who have requested to be on mailing list.
UTAH CODE ANN. § 63G-6a-405 UTAH ADMIN. CODE § 33-3-104	Publication in newspaper of general or local circulation of area directly impacted or within jurisdiction at least 10 days before deadline for submission of bids; or at least 10 days before day of deadline for submission of bids. Publication notice also on main website of purchasing unit or state website	Ten day period may be reduced by authority
VT. STAT. 19, chap. 1 § 10 Code of Vt. Rules § 14-010-010	Weekly posting of bidding opportunities by VTrans contract administrative staff on department website	
VA. CODE §§ 2.2-4301, 33.1-185	Public notice of invitation for bids at least 10 days prior to date set for receipt of bids in newspaper of general circulation.	Posting on Internet procurement Web site designated by the Department of General Services is required. May be posted in designated public place. Bid opening may be postponed for one week if bid call has been advertised for two consecutive weeks.
WASH. REV. CODE § 47.28.050	Once a week for 2 consecutive weeks preceding date for receiving bids in at least one trade journal of general circulation in State, or if project is less than $50,000, in one newspaper of general circulation in county where major part of work will be done.	
W. VA. CODE § 17-4-19	At least once weekly for two successive weeks in area, county, or municipality in which work will be done. At least once in at least one daily newspaper published in Charleston.	May publish in such other journals and magazines as deemed advisable by commissioner.
WIS. STAT. ANN. § 84.06(2)(a); Roadway Standards 102.1	Prequalification system for bidders. Prequalification statement on department's form must be submitted at least 10 business days before time set for opening proposals.	Department may determine that prequalification is not necessary and advertise in a manner determined by the department.

WYO. STAT. § 24-2-108 Wyoming DOT Construction Manual, § 8.01	Public notice required by statute; department policy is to advertise weekly for 3 weeks prior to bid opening. WYDOT maintains electronic bid letting information available on its website.	Department will mail invitations for bids to bidders requesting to be on mailing list.

APPENDIX B

BID SECURITY

STATE & CITATION	AMOUNT OF SECURITY	FORM OF SECURITY	TERMS FOR RETURN OF SECURITY
ALA. CODE §§ 23-1-2; 39-2-4, 39-2-5	Not less than 5 percent of awarding authorities estimate or of bid amount, but not more than $10,000.	Certified or cashier's check or bid bond.	All except those of three lowest bids returned immediately after determination of low bidder; others returned after contract and contractor bond executed.
ALASKA STAT. § 36.30.120	At least 5 percent of bid.	Bond or other form acceptable to commissioner.	
ARIZ. REV. STAT. § 34-201	Ten percent of bid amount.	Certified check, cashier's check, or surety bond.	Returned to those whose proposals are not accepted, and to successful bidder upon execution of contract and surety bond.
ARK. CODE § 19-11-235	Bid security may be required by regulations.		
CAL. PUB. CONT. CODE §§ 10167, 10184	At least 10 percent of bid amount.	Cash, cashier's check, certified check, or bid bond.	Returned within 10 days after award; second and third low bidders' security may be retained until a contract is executed.
Colo. Code of Regulations §§ 2-CCR-601-10-1.05 (nn); 2CCR-601-10-4.21	Amount specified in bid invitation.	Cashiers check, certified check, or bid bond.	Proposal guarantees for three lowest bids, held until award, then two unsuccessful bidders' security returned immediately; successful bidder's is held until execution of contract and bond.
CONN. GEN. STAT. § 13a-95 (1998) Conn. Standard Specifications, §§ 1.02.07, 1.03.03	One third of contract price, or annual bid bond in amount of one-third of amount of all current bids by that bidder; or amount set by commissioner and	Surety bond.	Returned to unsuccessful bidders within 3 calendar days after award of contract. If award not made within 10 days after bid opening, bonds of all but three lowest bidders

STATE & CITATION	AMOUNT OF SECURITY	FORM OF SECURITY	TERMS FOR RETURN OF SECURITY
	stated in invitation for bids.		are returned.
29 DEL. CODE § 6962(d)(8)	Equal to or greater than 10 percent of bid amount.	Surety bond.	Returned to unsuccessful bidders upon award or rejection of all bids; returned to successful bidder upon contract execution.
D.C. CODE § 2-357.01.	Required for all contracts over $100,000 (subject to revision by regulations), at least 5 percent of bid.	Surety bond, cash or equivalent, or other form acceptable to director.	Surety authorized to do business in district.
FLA. STAT. § 337.17	On contracts over $150,000, not to exceed 10 percent of preliminary estimate of project cost.	Certified check, cashier's check, bank draft, money order, or surety bond.	
GA. CODE ANN. § 32-2-68	Amount deemed necessary "to insure that the successful bidder will execute the contract on which he bid."	Certified check, "or other acceptable security."	Returned to unsuccessful bidders upon determination of lowest reliable bidder.
HAW. REV. STAT. § 103D-323 (2002)	At least 5 percent of amount of bid as established by policy board.	Cash or surety bond, or form of security specified by rules.	Irrevocable for period specified in invitation for bids.
IDAHO CODE § 40-902(2)	Five percent of the bid amount.	Cashier's check, certified check, or surety bond.	Returned to unsuccessful bidders when contract is awarded.
44 ILL. ADMIN. CODE § 6.160(d)	Amount stated in invitation for bids.	Certified check, cashier's check, money order, irrevocable letter of credit, or surety bond.	
IND. CODE § 8-23-9-9	Five percent of bid price.	Surety bond.	
Iowa Stan. Specs. §§	Form and amount of bid	Certified check, bank	Returned to unsuccessful

STATE & CITATION	AMOUNT OF SECURITY	FORM OF SECURITY	TERMS FOR RETURN OF SECURITY
1102.11, 1103.03	guaranty as prescribed in notice to bidders.	draft, cashier's check, bid bond, surety bond.	bidders after approval for award has been made. Successful bidder's guaranty returned after the filing of contract documents.
KAN. GEN. STAT. § 68-1114	Five percent of bid amount	Bid security in form prescribed by Board of Commissioners.	
KY. REV. STAT. § 176.080 (2002)	Amount set by department, guaranteeing that contractor will execute contract.	Certified check or surety bond.	
LA. REV. STAT. § 48:253	Five percent of official bid amount for projects in excess of $50,000.	Surety bond qualified to do business in state.	
23 ME. REV. STAT. § 753	Amount specified in bid invitation, determined by department to be sufficient to guarantee that bidder will execute contract if awarded.	Surety bond.	
MD. STATE FIN. & PROC. CODE § 13-207	At least 5 percent of bid.	Surety bond, cash, or other form of security allowed by regulation.	None required if expected price is $100,000 or less.
MASS. L. ch. 30, § 39M	Five percent of value of bid.	Surety bond, cash, certified check, cashiers check, or treasurer's check.	
Minn. Stan. Specs. §§ 1208, 1304	Amount specified in bid invitation.	Certified check, surety bond.	Returned to unsuccessful bidders "immediately" following opening and checking of proposals, except for two lowest bidders, whose bonds are retained until contract is executed.
MISS. CODE § 65-1-85	Not less than 5 percent	Cashier's check, certified	Bid bonds not returned, but checks will be returned

STATE & CITATION	AMOUNT OF SECURITY	FORM OF SECURITY	TERMS FOR RETURN OF SECURITY
Stan. Specs. § 103.04	of bid amount.	check, or surety bond.	following bid opening except for two lowest bidders, which will be returned 10 days after award.
MO. REV. STAT. § 227.100	Five percent of amount of bid.	Certified check, cashier's check, or surety bond.	Returned to successful bidder upon execution of contract and bond, and to unsuccessful bidders under terms of proposal.
MONT. CODE ANN. §§ 18-1-202; 203; 18-2-302	Not less than 10 percent of bid amount.	Cash; cashier's check, certified check, bank money order or bank draft drawn and issued by bank insured by FDIC; bid bond, guaranty bond, or surety bond.	Bid security of unsuccessful bidders returned after bid opening.
Neb. Stan. Specs. § 102.15	At least 5 percent of bid amount.	Surety bond.	
NEV. REV. STAT. § 408.337	At least 5 percent of bid amount.	Cash, certified check, or surety bond.	Returned to unsuccessful bidders within 10 days after award. Guaranties of second and third lowest bids may be held until after contract is executed.
N.H. Stan. Specs. §§ 102.09, 103.04	Character and amount specified in bid invitation.	Surety bond or certified check.	Returned to unsuccessful bidders within 7 days after bids are opened, except two lowest bidders' guaranties, which are returned after contract award.
N.J. STAT. ANN. §§ 27-7-31, 27-7-33	Amount to be determined by commissioner, not to exceed 50 percent of bid.	Surety bond.	Returned to unsuccessful bidders within 3 days after bids received, except two lowest bidders.
N.M. STAT. § 13-1-146 Standard Specifications 102.11	At least 5 percent of bid amount.	Surety bond or cash equivalent, cashiers check, certified check, postal money order, or bank money order.	Checks returned to all but two lowest bidders; lower of two returned after award; lowest bidder's check returned after contract execution. Bonds returned upon request.

STATE & CITATION	AMOUNT OF SECURITY	FORM OF SECURITY	TERMS FOR RETURN OF SECURITY
N.Y. HIGH. LAW § 38	Amount fixed by Commissioner and set out in advertisement.	Certified check, cashier's check, or surety bond.	Returned to unsuccessful bidders following bid opening, except two lowest bidders whose security is retained until contract bond is filed.
N.C. Stan. Specs. §§ 102-10; 103-6	At least 5 percent of bid amount.	Surety bond, certified check, or cashier's check.	All bid bonds retained until bonds are executed by successful bidder, after which they are destroyed. Checks, other than those of three lowest bidders, returned within 10 days after bid opening. Checks of three lowest bidders returned when contractor bonds furnished by successful bidder.
N.D. CENT. CODE § 24-02-20 (1970) Std. Specs. §§ 102.09, 103.04	Five percent of bid amount if check is used; 10 percent if bond is used.	Certified check or cashier's check on solvent bank, or surety bond.	Bonds and checks returned upon bid opening except for lowest three bidders; lowest bidder's security returned after execution of contract, other two after determination made for award.
OHIO REV. CODE § 5525.01	Five percent of bid amount up to $50,000 if by check, etc., or 10 percent of bid amount, if by bid bond.	Certified check, cashier's check, electronic funds transfer, or surety bond.	Returned to unsuccessful bidders "forthwith" following contract award, and to successful bidder after bidder has executed contract and provided contractor bonds.
61 OKLA. STAT. § 107	Five percent of bid amount for contracts over $50,000.	Certified check, cashier's check, surety bond, or irrevocable letter of credit.	Unsuccessful bidders' security returned according to terms of bid solicitation; successful bidder's security returned upon execution of contract and bonds.
OR. REV. STAT. §§ 279C.365; 279C.385	Not more than 10 percent of bid amount.	Certified check, cashier's check, surety bond, or irrevocable letter of credit.	Returned to unsuccessful bidders when bids have been opened and contract has been awarded; returned to successful bidder upon execution of

STATE & CITATION	AMOUNT OF SECURITY	FORM OF SECURITY	TERMS FOR RETURN OF SECURITY
			contract and bond.
62 PA. CONS. STAT. § 902	In the minimum amount or percentage of the amount of bid as specified in the invitation for bids	Certified check, cashier's check, surety bond authorized to do business in the commonwealth, or another form as specified in the invitation for bids.	Returned to unsuccessful bidders within 30days after bid opening, except for that of low bidder and next to low bidder, which is returned upon contract execution.
R.I. GEN. LAWS § 37-2-40; Procurement Regulations §§ 12.102.06, 12.103.04 General Conditions of Purchase, number 32.	Not less than 5 percent of bid amount, as designated in notice to contractors.	Cash or surety bond in form satisfactory to the state for contracts over $50,000.	All returned at time of bid opening except three lowest bidders. Unsuccessful bidders' bonds returned 10 days after award and lowest three after contract and bond executed.
S.C. Stan. Specs. §§ 102.9; 103.4	Five percent of submitted bid.	Surety bond.	All retained until contract is executed, then are destroyed unless bidder has requested that it be returned.
S.D. CODIFIED LAWS §§ 5-18B-2; 5-18B-4	No less than 5 percent of bid amount for bond.	Surety bond; cashier's check or certified check.	Returned to unsuccessful bidders "immediately"; and to successful bidder upon execution of contract and bond. Must be returned within 30 days after bid opening.
TENN. CODE § 54-5-115 Stan. Specs. §§ 1.02.05, 1.03.02	"Proper bond" or proposal guaranty must accompany bid.		Returned to unsuccessful bidders upon opening, except for those likely to considered for award, which are returned upon execution of contract and bond.
TEX. STAT. §§ 223.014, 223.015 43 Tex. Admin. Code R-9.14(d)	Amount specified in bid form.	Electronic fund transfer, cashier's check, money order, bid bond, trust account, or other form satisfactory to department. Department may establish escrow accounts for prepayment of bid guarantees and use of credit cards for	

STATE & CITATION	AMOUNT OF SECURITY	FORM OF SECURITY	TERMS FOR RETURN OF SECURITY
		electronic fund transfer.	
UTAH CODE § 63G-6-504	At least 5 percent of bid amount.	Surety bond, cash, or form acceptable to state.	
Vt. Agency of Transportation Policies and Procedures of Prequalification, Bidding and Award of Contracts §§ 7.07 and 8.03	Must be for amount and of character indicated in bid invitation.	With electronic bids, electronic corporate surety bond	Lowest two bidders' security retained until contract and bond executed. Others returned to unsuccessful bidders "as soon as possible."
Va. Stan. Specs. § 102.07,	Five percent of bid amount.	Surety bond, with exact wording as department form.	
WASH. REV. CODE § 47.28.090 Wash. Stan. Specs. §§ 1-02.7, 1-03.6	Five percent of bid amount.	Certified check, cashier's check, surety bond either physical or electronic, or cash.	Bonds or guaranties accompanying proposals not eligible for further consideration returned after bid opening; others returned after contract execution.
W. VA. CODE § 17-4-19(e) Stan. Specs. §§ 102.8, 103.4	Amount specified in bid invitation, but not less than $500, nor more than 5 percent of bid, specified in advertisement.	Certified check, cashier's check, or surety bond.	Returned to unsuccessful bidders immediately following opening and checking of bids, except security of two lowest bidders; second lowest returned within 10 days after award, and successful bidder's security returned after execution of contract and bond.
Wis. Stan. Specs. §§ 102.8; 103.4	Amount specified in bid notice to contractors.	Certified check, cashier's check, postal money order, bid bond.	Returned to unsuccessful bidders immediately following bid opening,. Security of low bidder returned after execution of contract.
Wyo. Stan. Specs. §§ 101.5; 101.5	Ten percent of bid.	Certified check, cashier's check, or bank money order, surety bond.	All bid bonds returned after receipt of performance bond and contract.

APPENDIX C

REQUIREMENTS FOR COMPETITIVE BIDDING AND CRITERIA FOR AWARD OF HIGHWAY CONSTRUCTION CONTRACTS

STATE & CITATION	CLASSES OF CONTRACTS	CRITERIA FOR AWARD	AUTHORITY TO REJECT ALL BIDS
ALA. CODE § 39-2-6	Public works contracts exceeding $50,000.	Lowest responsible and responsive bidder, unless awarding authority finds bid unreasonable or it is not in awarding authority's interest to accept any of the bids.	If all bids are unreasonable and it is not in awarding authority's interest to accept any, bids may be rejected and work done by force account by awarding authority.
ALASKA STAT. §§ 19.10.170; 36.30.170(a) 2 AAC § 12.860 – 870	All highway construction with estimated cost exceeding $100,000. For construction costing less than $100,000, department may perform work directly; however, for work over $5,000, commissioner must make written findings that state forces will be less expensive than contracting.	Lowest responsible and responsive bidder whose bid conforms in all material respects to the requirements and criteria set out in the invitation to bid.	
ARIZ. REV. STAT. § 28-6923		Lowest responsible bidder whose proposal is satisfactory.	All bids may be rejected for any reason the contracting agent determines.
ARK. CODE § 27-67-206	All new construction, and all other construction costing $10,000 or more; except for discretionary authority to contract with railroads for signals and safety devices at grade crossings, or grade crossing elimination. All materials purchased for road work.	Lowest responsible bidder.	Commission has right to reject any or all bids.
CAL. PUB. CONT. CODE §§ 10105; 10180; 10185	As of 2010, all work over $250,000, which amount is adjusted every 2 years by California construction index.	Lowest responsible bidder.	May reject all bids if found to be not for best interest of the State to accept them; must state reasons for rejecting bids.
COLO. REV. STAT. §§	All construction contracts.	Low responsible bidder	All bids may be rejected

STATE & CITATION	CLASSES OF CONTRACTS	CRITERIA FOR AWARD	AUTHORITY TO REJECT ALL BIDS
24-92-103; 24-92-105		whose bid meets the requirements and criteria set forth in the invitation for bids.	when in best interest of state; reasons must be stated in contract file.
CONN. GEN. LAWS ANN. § 13a-95	Construction, alteration, improvement, reconstruction, relocation, widening, or change of grade of State highways or bridges.	Lowest bidder deemed responsible.	Commissioner may reject any and all bids for cause.
29 DEL. CODE § 6923	Contracts exceeding amount set by Contracting and Purchasing Advisory Council, unless Secretary of Transportation and Budget Commission determine it to be in best interests of state to enter into contract without bidding.	Lowest responsive and responsible bidder whose bid conforms in all material respects to the requirements and criteria set forth in the invitation to bid.	May reject all bids if it is advantageous to the state.
D.C. CODE §§ 2-354, et. seq.	Construction contracts over $100,000.	Responsible and responsive bidder whose bid is most advantageous to District, considering price and other factors.	May reject all bids if in best interest of District.
FLA. STAT. § 337.11	All construction contracts exceeding $250,000.	Lowest responsible bidder, or in the instance of a time-plus-money contract, the lowest evaluated responsible bidder.	May reject all bids and readvertise project, or perform work.
GA. CODE §§ 32-2-61; 32-2-64; 32-2-69	Any construction or maintenance contract over $200,000.	Lowest reliable bid.	May reject any and all such bids, and readvertise, perform work directly, or abandon project.
HAW. REV. STAT. §§ 103D-301; 103D-302	All construction contracts.	Lowest responsible and responsive bidder whose bid meets the requirements and criteria set forth in the invitation for bids.	
IDAHO CODE § 67-280	Public works construction	Lowest responsible bidder.	May reject any or all bids.

STATE & CITATION	CLASSES OF CONTRACTS	CRITERIA FOR AWARD	AUTHORITY TO REJECT ALL BIDS
30 ILL. COMP. STAT. 500/20-5; 500/30-15; 500/20-20; 500/20-40 44 Ill. Admin. Code §§ 6.220; 6.240	All construction contracts over $30,000, to be adjusted for inflation.	Lowest responsible and responsive bidder whose bid meets the requirements and criteria set forth in the invitation for bids.	All bids may be rejected when in best interest of State, in accordance with administrative rules.
IND. CODE §§ 8-23-9-2; 8-23-9-3; 8-23-9-4	All contracts for construction, improvement or maintenance of roads.	Lowest and best bidder, provided not more than 15 percent over engineer's estimate and in best interests of state.	May reject all and all bids for cause.
IOWA CODE ANN. §§ 313.10; 314.1	Construction contracts over $1,000.	Bid price to be considered with financial responsibility, experience, equipment, and performance in similar work.	May reject any or all bids, and relet job without conducting an additional public hearing.
KAN. STAT. § 68-410	All State contracts for highway construction, improvement, reconstruction, and maintenance of State highway system involving more than $1,000.	Lowest responsible bidder.	
KY. REV. STAT. §§ 176.080; 180.060	Construction and maintenance on State highways, bridges, and bridge approaches.	Lowest and best bidder.	May reject any or all bids if in best interest of State, and readvertise.
LA. REV. STAT. §§ 48:205; 48:255	Construction contracts over $25,000.	Lowest responsible bidder.	May reject any and all bids if no satisfactory bids are received.
23 ME. REV. STAT. § 4243	Construction of state highways.	Lowest responsible bidder.	May reject any and all bids if there is deemed to be in the best interests of the department of transportation.
MD. STATE FIN. & PROC. CODE §§ 13-102; 13-103; 13-206.	All State highway construction.	Lowest responsible bidder, or lowest evaluated bid price if that process is noted in invitation for bids.	May reject all bids if in best interest of state.
MASS. LAWS ch. 30, § 39M; ch. 81, § 8	Construction, alteration, reconstruction, or repair in	Lowest eligible responsible bidder.	Invitation for bids reserves right to reject

STATE & CITATION	CLASSES OF CONTRACTS	CRITERIA FOR AWARD	AUTHORITY TO REJECT ALL BIDS
	excess of $10,000.		all bids.
MICH. COMP. LAWS § 247.661c	All highways, streets, and bridges whose cost exceeds $100,000, unless department affirmatively finds that another method is in public interest.		
MINN. STAT. § 161.32; 161.3410	May use state forces or contract.	Lowest responsible bidder, considering conformity with specifications, delivery terms, and other conditions imposed in bid notice; may also use life-cycle costing.	May reject any and all bids. If no satisfactory bids received, commissioner may readvertise or perform work directly.
MISS. CODE §§ 65-1-85	All contracts for construction, reconstruction, or other public work, and purchase of materials and supplies.	Lowest responsible bidder.	Director, with approval of Transportation Commission, may reject any and all bids.
MO. REV. STAT. § 227.100	All construction contracts.	Lowest responsible bidder.	Commission may reject all bids and do work under own supervision.
MONT. REV. CODE § 18-2-301; 18-1-102; 60-2, 11, 112, 135-137	Construction for $75,000 or more.	Lowest responsible bidder.	If no responsible bids received after two attempts, may reject and contract in manner that is cost-effective to the state.
NEB. REV. STAT. § 39-1349	Contracts for construction, reconstruction, improvement, maintenance, and repair of State roads and bridges.	Lowest responsible bidder.	May reject any or all bids, and cause work to be done as directed by department.
NEV. REV. STAT. §§ 408.317; 408.323; 408.343	All construction, improvement, and maintenance on State highway system, except where director can justify that limited work can be done more economically or in other satisfactory manner by other means.	Lowest responsible bidder who has qualified and submitted bid in accordance with statute.	May reject any and all bids if, in the department's opinion, such bids are unbalanced, incomplete, irregular, or for other good cause.
N.H. REV. STAT. §§ 228:4; 228:4-a;	All major State highway projects over $25,000, except	Lowest responsible bidder.	Right reserved to reject all bids or negotiate

STATE & CITATION	CLASSES OF CONTRACTS	CRITERIA FOR AWARD	AUTHORITY TO REJECT ALL BIDS
228:4(1)	normal maintenance and improvements.		with lowest responsible bidder.
N.J. STAT. § 27:7-30	Construction contracts for State highway system.	Lowest responsible bidder.	May reject any and all bids.
N.M. STAT. § 67-3-43	All construction, reconstruction, and maintenance on State highway system, except work performed directly by State Highway Department.	Lowest responsible bidder.	May reject any and all bids if such bids are unbalanced, or for other good cause.
N.Y. HIGH. LAW § 38	Contracts for construction or improvement of state highways.	Lowest responsible bidder as will best promote the public interest.	May reject any and all bids and readvertise if State's best interest will be promoted thereby.
N.C. GEN. STAT. ;§§ 136-28.1; 28.11	Contracts for highway construction or repair exceeding $1.2 million. Contracts under that amount require three informal bids, without advertising.	Lowest responsible bidder.	Right is reserved to reject all bids.
N.D. CENT. CODE §§ 24-02-17, 18; 24-02-23	Construction or improvements exceeding $20,000.	Responsible bidder submitting the lowest and best bid.	May reject all bids.
OHIO REV. CODE §§ 5517.02; 5525.01; 5525.10	State highway construction, improvement, and repair; bridge, culvert, and traffic signal projects over $50,000; maintenance over $25,000 per mile of highway.	Lowest competent and responsible bidder.	May reject any and all bids. No contract may be awarded that exceeds the estimate by more than 5 percent.
61 OKLA. STAT. §§ 102, 103, 111, 119	All construction work on State highway system.	Lowest responsible bidder.	Agency may reject all bids and readvertise if in best interest of state.
OR. REV. STAT. §§ 279A.383.2796; 279B.055; 279B.100; 279C.300; 279C.335, 279C.383;	All public contracts, except those declared exempt by Public Contract Review Board as (1) not likely to substantially diminish competition, (2) result in saving to contracting agency; or (3) if prompt action needed to deal with emergency.	Lowest responsible bidder.	May reject any or all bids for cause, and readvertise.

STATE & CITATION	CLASSES OF CONTRACTS	CRITERIA FOR AWARD	AUTHORITY TO REJECT ALL BIDS
62 PA. CONS. STAT. §§ 512(g); 3911	All work done by contract.	Lowest responsible bidder.	May reject any and all bids.
R.I. GEN. LAWS §§ 24-8-12; 24-8-12; 37-2-18; 37-2-22	All highway construction or improvements over $10,000.	Lowest responsible and responsive bidder.	Right reserved to reject all bids.
S.C. CODE § 57-5-1620	Contracts for construction work on State highways involving $10,000 or more.	Lowest qualified bidder.	
S.D. CODIFIED LAWS § 31-5-10	Contacts of State Highway Commission for highway improvements on trunk highway system.	Lowest competent and responsible bidder, unless bid is deemed unreasonable.	
TENN. CODE §§ 54-5-116; 54-5-118	Contracts of State Department of Transportation relating to highways.	Best and most advantageous offer. Lowest bid to be accepted.	
TEX. TRANSP. CODE §§ 223.004; 223.005	Contracts of highway department relating to State highway system over $25,000.	Lowest bidder.	May reject any and all bids.
UTAH CODE §§ 72-6-107; 72-6-109; 63-56-20	Contracts of State Department of Transportation for construction or improvement of State highways.	Lowest responsible bidder.	Any or all bids may be rejected.
Code of Vt. Rules § 14-010-010 Vt. Agency of Trans. Policies, Procedures of Prequalification, bidding and Award of Contracts. §§ 103.01; 103.02; 7.06, 8.02	Agency of Transportation authorized to contract on such terms as it deems to be for best interest of State for construction, repair, and maintenance of State highways, and for use of machinery and equipment for road work, etc.	Lowest responsible bidder.	May reject bids if found to be on altered form, irregular, incomplete, conditional, or if bid is obviously unbalanced.
VA. CODE §§ 33.1-185; 2.2-4306; 2.2-	All contracts let by Commonwealth	Lowest responsive and responsible bidder.	May be canceled or rejected.

STATE & CITATION	CLASSES OF CONTRACTS	CRITERIA FOR AWARD	AUTHORITY TO REJECT ALL BIDS
4319; 2.2-4303	Transportation Board for construction or other necessary work; agency may use competitive negotiation at its option.		
WASH. REV. CODE §§ 47.28.090; 47.28.100	Contracts for construction on State highway system.	Lowest responsible bidder.	May reject lowest bid for good cause, and may reject all bids if in best interest of state.
W. VA. CODE § 17-4-19 Stan. Specs. § 103.2	Contracts of State Highway Department for road work, materials, and supplies exceeding $3,000.	Lowest responsible bidder.	May reject all bids, and perform work directly.
WIS. STAT. § 84.06 Stan. Specs. §§103.1; 103.2	All contracts for construction, reconstruction, and rehabilitation of highways.	Lowest competent and responsible bidder.	All bids may be rejected if lowest bid exceeds estimated reasonable value of work, or if bids not in public interest.
WYO. STAT. § 24-2-108	Contracts for highway improvements exceeding $200,000.	Lowest responsible qualified bidder.	Transportation Commission may reject any or all bids, and readvertise.

APPENDIX D

SUMMARY OF STATE LAWS RELATING TO LICENSING CONTRACTORS

STATE	LICENSING AGENCY	SCOPE OF REQUIREMENT	EXAM	CRITERIA	CLASSIFICATIONS	PERIOD	CAUSES OF REVOCATION
ALASKA STAT. § 08.18.011-171	Department of Community and Economic Development	Person who undertakes or offers to perform or submits a bid to construct, alter, repair, move, or demolish a building, highway, road, railroad, or any type of fixed structure.	No	Surety bond and proof of insurance.	General Specialty Mechanical Residential Electrical		Failure to comply with insurance and bond requirement.
ARIZ. REV. STAT. §§ 32-1101 to 32-1169	Registrar of Contractors	Person who for compensation undertakes or offers to construct, alter, repair, add to, subtract from, improve, move, wreck, or demolish any building, highway, road, railroad, excavation or other structure, project, development, or improvement.	May be required.	1. Good standing with corporation commission. 2. Compliance with rules regarding workers' compensation. 3. Submission of bond and fee. 4. Financial resources. 5. Good character and reputation.	General commercial building General dual licensed General engineering General residential Specialty commercial Specialty dual licensed Specialty residential	2 years	1. Abandonment of contract. 2. Disregard of plans and specs. 3. Disregard of registrar's rules. 4. Disregard of rules regarding social security, workers' compensation, or unemployment compensation. 5. Failure to pay taxes. 6. Misrepresentation of material fact in obtaining license. 7. Fraudulent act that results in substantial injury to another. 8. Conviction of felony. 9. Failure to complete a project for the price stated/ 10. Aiding or abetting an unlicensed person to evade licensing law. 11. Failure to pay bills for

							labor and materials when due and when able to pay, in excess of $750. 12. Failure to comply with labor or safety codes. 13. False or deceptive advertising 14. Knowingly contracting beyond classification 15. Contracting while license suspended.
ARK. CODE §§ 17-25-101 *et seq*; 17-25-301 *et seq*.	Contractors' Licensing Board	Person who for compensation, contracts to construct, erect, alter, or repair any building, highway, sewer, utility, grading, or any other improvement or structure on public or private property for lease, rent, resale, public access, where project is over $20,000.	Yes	1. Experience. 2. Ability. 3. Character. 4. Manner of performance of previous contracts. 5. Financial condition. 6. Equipment. 7. Any fact tending to show ability and willingness to conserve public health and safety. 8. Default in complying with licensing laws or any other state laws.		1 year	1. Fraud or deceit in obtaining a license. 2. Aiding or abetting any contractor or person to violate the provisions of this chapter. 3. Gross negligence. 4. Incompetence. 5. Misconduct in the conduct of the contractor's business.
CAL. BUS. & PROF. CODE § 7000–7145.5	Contractors' State License Board Department of Consumer Affairs	All contractors, or anyone who for compensation undertakes, offers to undertake, or purports to have capacity to construct, alter, repair, add to, subtract from, improve, move, or	Yes	Knowledge and experience in the classification applied for, and such general knowledge of the building, safety, health, and lien laws of the state and of the administrative	General engineering General building Specialty building	2 years	1. Abandonment of work without legal excuse 2. Diversion of funds. 3. Fraud, gross negligence, or disregard of specifications or accepted trade standards.

		demolish any building, highway, road, railroad, or other structure, project, development, or improvement.		principles of the contracting business necessary for the safety and protection of the public; knowledge of pertinent state laws and the contracting business and trade.		4. Willful violation of building laws or rules of construction, labor, or safety. 5. Failure to carry workers' compensation insurance. 6. Failure to keep records. 7. Misrepresentation in obtaining license. 8. Aiding or entering into contract with unlicensed contractor. 9. Commission of crime related to duties as contractor. 10. Failure to complete work at specified price. 11. Aiding evasion of license law. 12. Failure to cooperate in investigation by Registrar. 13. Failure to pay bills.
CONN. GEN. STAT. ch. 393 § 20-341gg Conn. Regs. §§ 20:341gg–1 through 7	Department of Consumer Protection	Person doing construction, structural repair, structural alteration, dismantling or demolition of a structure or addition that exceeds statutory threshold limits.	No	1. Credit references. 2. References re work. 3. General liability insurance. 4. Certificate of good standing from Secretary of State if incorporated.	Major contractors	1. Conviction of a felony. 2. Gross incompetence. 3. Malpractice or unethical conduct. 4. Knowingly makes false, misleading, or deceptive representations regarding work. 5. Violation of regulations adopted under this chapter. 6. False statement in obtaining license. 7. Performing work beyond scope of license.

							8. Employ unlicensed contractor.
HAW. REV. STAT. §§ 444-1 to 444-36	Contractors Licensing Board	Person who undertakes to improve any realty or construct, alter, repair, add to, subtract from, improve, move, or demolish any building, highway, road, railroad, excavation, or other structure, project, development, or improvement, including specialty contractors and subcontractors.	May be required	1. Workers compensation insurance. 2. Liability insurance. 3. Bond.	General engineering General building Specialty	2 years	1. Dishonest, fraudulent, or deceitful acts. 2. Unfair or deceptive practice. 3. Abandonment of project without legal excuse. 4. Diversion of funds. 5. Willful disregard of plans and specifications. 6. Willful violation of law. 7. Failure to keep records. 8. Misrepresentation of material fact in obtaining license. 9. Failure to complete project for agreed price. 10. Failure to pay bills. 11. Failure to carry workers compensation insurance. 12. Failure to complete with diligence.
IDAHO CODE §§ 54-1901 to 54-1924 Stan. Specs § 107.03	Public Works Contractors License Board	Person who undertakes any construction, repair, or reconstruction of any public work under contract with the state of Idaho or any agency or public or quasi public corporation.	Yes	Such degree of experience, and such general knowledge of the building, safety, health, and lien laws of the state, and of the rudimentary administrative principles of the contracting business, as may be deemed necessary by the board for the safety and	Eight classes based on amount of work licensee may bid on: Class Unlimited License $5 million or more AAA— not more than $5 million AA—up to $3 million A—up to $1,250	12 calendar months	1. Abandonment of project without legal excuse. 2. Diversion of funds or property received. 3. Willful disregard of plans or specifications. 4. Willful disregard of valid building laws, or safety, labor, or compensation insurance laws.

				protection of the public; good character, shown by past performance of work and reputation for honesty and integrity; has never been refused a license or had a license revoked.	million B—up to $600,000 CC—up to $400,000 C- up to $200,00 D- up to $50,000		5. Material misrepresentation in obtaining a license. 6. Aiding or abetting an unlicensed person to evade provisions of this chapter. 7. Material failure to comply with this chapter. 8. Knowingly entering into contract with unlicensed contractor on public works project. 9. Willful failure without legal excuse to finish project with reasonable diligence, causing material injury to another. 10. Willful failure to pay for materials or services. 11. Change in financial circumstances impairing financial responsibility.
IOWA CODE § 91C	Labor Commissioner, Division of Labor Services	Person who engages in business of construction.	No	Application and payment of fee; evidence of workers' compensation insurance; surety bond required for payment of taxes if out-of-state contractor for contracts.		1 year	1. Violation of requirement that contractor be registered. 2. Violation of requirement that registration information be substantially complete and accurate. 3. Failure to file bond with the division of labor services (if out of state contractor).
LA. REV.	State	Person who	Yes, but	1. Financial statement	1. Building.	1 year	1. Dishonest or fraudulent

STAT. §§ 37:2150–37:2164	Licensing Board for Contractors	undertakes to or submits a bid to construct or supervise construction, alteration, repair, improvement, movement, demolition, or furnishing labor, for any building, highway, road, railroad, utility, grading, excavation, pipeline, housing, development, or other commercial construction of $50,000 or more.	may be waived	showing net worth of at least $10,000. 2. Examination, unless waived.	2. Highway, street, and bridge. 3. Heavy construction. 4. Municipal and public works. 5. Electrical. 6. Mechanical. 7. Plumbing. 8. Hazardous materials. 9. Specialty. 10. Residential.	act causing substantial damage to another. 2. Willful misrepresentation of material fact in obtaining license. 3. Willful failure to comply with this Chapter. 4. Entering into contract with unlicensed contractor. 5. Permitting contractor's license to be used by unlicensed person. 6. Failure to maintain a qualifying party to represent the licensee. 7. Insolvency or involuntary cessation of business. 8. Failure to continue to fulfill requirements for original licensure. 9. Problems relating to ability to engage in business of contracting, as demonstrated by prior experience. 10. Disqualification or debarment by any public entity.

MISS. CODE §§ 31-3-1 to 31-3-23 Standard Specs. § S-102.01	State Board of Contractors	Person contracting or undertaking as prime contractor, subcontractor of any tier to do erection, building, construction, reconstruction, repair, maintenance, or related work on any public or private project.	Yes	1. Experience and ability. 2. Character. 3. Performance of previous contracts. 4. Financial condition. 5. Equipment. 6. Personnel. 7. Work completed and work on hand. 8. Default in complying with law. 9. Results of objective, standardized examinations.		1 year	Finding of nonresponsibility.
NEV. REV. STAT. §§ 624.040 – 624.361	State Contractors' Board	Person who for compensation undertakes or submits a bid to construct, alter, repair, add to, subtract from, improve, move, wreck, or demolish any building, highway, road, railroad, excavation, or other structure, project, development, or improvement.	Yes	1. Financial responsibility; experience; knowledge of building, safety, health, and state lien laws; and qualifications of the applicant. 2. Proof of industrial insurance. 3. Good character. 4. Surety bond.	General engineering General building Specialty	2 years	1. Abandonment of project. 2. Disregard of plans or specifications. 3. Diversion of funds. 4. Failure to maintain records. 5. Failure to maintain bond. 6. Failure to establish financial responsibility. 7. Misuse of license or evasion of law. 8. Acting beyond scope of license. 9. Contracting with unlicensed person. 10. Fraudulent or deceptive act; criminal conviction.
N.C. GEN. STAT. §§ 87-1 to 15.1	State Licensing Board for General	Person who for compensation bids upon or constructs or manages construction	Yes	1. Good character. 2. Competency and ability.	Building Residential Highway	Expires on the first day of	1. Fraud or deceit in obtaining a license. 2. Gross negligence.

	Contractors	of any building, highway, public utilities, grading or any improvement or structure costing $30,000 or more.		3. Integrity. 4. Financial responsibility. 5. Has not committed act that would be grounds for suspension or revocation of license. 6. Has not committed act of dishonesty, fraud, or deceit. 7. Has never been refused a license as a general contractor nor had such license revoked in any state. 8. Has not been convicted of felony involving moral turpitude, relating to building or contracting, or involving embezzlement or misappropriation of funds or property.	Public Utilities Specialty	December after its issuance	3. Incompetency. 4. Misconduct. 5. Willful violation of any provision of this Article.
N.D. CENT. CODE 43-07	Secretary of State	Person who constructs, repairs, alters, dismantles, or demolishes any highways, roads, streets, buildings, airports, dams, drainage or irrigation facilities, utilities, and all other structures, projects,	No	1. Experience and qualifications, under oath. 2. Liability insurance. 3. Workers' compensation insurance.	Class A—no dollar limit. Class B—up to $250,000. Class C—up to $120,000. Class D—up to $50,000.	1 year	1. Abandonment of contract without legal excuse. 2. Diversion of funds or property. 3. Committing any fraudulent act in which another is injured. 4. False statement in application for license.

		developments, or improvements over $2,000.					
S.C. CODE §§ 40-11-5 to 40-11-430	Contractor's Licensing Board	General or mechanical contracting work, the cost of which is greater than $5,000.	Yes	1. Financial condition and bank reference. 2. Qualifying party who is full time employee and certified in classification.	General Mechanical groups setting contract limits are based on contractor's net worth.	2 years	1. Negligence or incompetence. 2. Abandonment of a contract without legal excuse. 3. Fraud or deceit in obtaining a license or certification. 4. Violation of licensing laws. 5. Conviction of forgery, embezzlement, or similar crime. 6. Conviction of crime involving moral turpitude in connection with contract. 7. False, misleading, or deceptive advertising. 8. Failure to obtain a building permit. 9. Failure to maintain net worth requirements. 10. Contracting outside classification.
TENN. CODE §§ 62-6-101 to 62-6-132	State Board for Licensing Contractors	Person who undertakes to or submits bid to construct or supervise construction, alteration, repair, improvement, movement, demolition, or furnishing labor to install material or equipment for any building, highway,	Written and/or oral	1. Letter of reference from past client, employer, or codes administration official. 2. Financial statement. 3. Affidavit that applicant is not performing construction work	1. Commercial 2. Industrial 3. Heavy 4. Highway 5. Municipal & Utility 6. Mechanical 7. Electrical 8. Environmental	2 years	1. Gross negligence. 2. Incompetence. 3. Fraud, dishonest dealing, and/or misconduct in contracting. 4. Failure to observe the terms and conditions of license.

		railroad, sewer, grading, excavation, pipeline, public utility structure, housing, or improvement; $25,000 or more.		and has not offered to perform work exceeding $25,000.	9. Residential		
UTAH CODE §§ 58-55-101 to 58-55-604	Construction Services Commission	Any person who for compensation other than wages as an employee undertakes any work in the construction, plumbing, or electrical trade.	Yes	1. Financial responsibility. 2. Knowledge and experience in the construction industry and knowledge of the principles of contracting business reasonably necessary for protection of the public.	1. General building. 2. General engineering. 3. Electrical. 4. Plumbing. 5. Residential. 6. Specialty.	2 years	1. Unlawful or unprofessional conduct.
VA. CODE §§ 54.1-1100 to 54.1-1117 18 VA. ADMIN CODE § 50.22	Board for Contractors	Person that for compensation undertakes to bid upon contracts for performing, managing, or superintending the construction, removal, repair, or improvement of any building or structure.	Oral or written	1. Past performance record. 2. Compliance with contracting and business laws. 3. Financial information.	Class A–single projects of $120,000 or more, or total in one year or $750,000 or more. Class B–single projects $7,500 but less than $12,000, or total in one year between $150,000 and $500,000. Class C–projects over $1,000 but less than $7,500.	2 years	Violation of statutes or regulations governing licensed contractors.
WASH. REV. CODE §§	Department of Labor and	Person who as independent business	No	1. Workers' compensation	General	2 years	1. Unsatisfied final judgment for work within scope of

18.27.010-340	Industries	undertakes to or submits a bid to construct, alter, repair, add to, subtract from, improve, move, wreck or demolish, for another, any building, highway, road, railroad, excavation or other structure, project, development, or improvement.	insurance. 2. Insurance or financial responsibility. 3. Surety bond.	Specialty	this chapter. 2. Not maintaining valid unified business identifier number for department of revenue. 3. Loss of insurance. 4. Loss of surety bond.

APPENDIX E

SUMMARY OF STATE LAWS AND REGULATIONS RELATING TO QUALIFICATION OF BIDDERS

STATE	CERTIFYING AGENCY	APPLICATION AND OTHER DOCUMENTS; PERIOD OF CERTIFICATION	EXEMPTION FROM CERTIFICATION	CRITERIA FOR CERTIFICATION
ALA. CODE § 23-1-56	Department of Transportation	Application submitted annually 14 days prior to bid opening Statement under oath on forms prescribed by Department. Financial statements certified by CPA. Inventory of equipment. Lists of previous projects and sureties from previous 3 years.		1. Sufficient net worth. 2. Competent and responsible. 3. Compliance with workers' compensation laws.
2 ALASKA ADMIN CODE § 12.500 Alaska Standard Specifications § 102-1.01	Department of Transportation and Public Facilities	Contractors questionnaire. Contractor registration and license (for state funded projects). Bidder registration form submitted annually.		1. Satisfactory record of performance. 2. Legally qualified to contract in state. 3. Availability of necessary financing, equipment, personnel, facilities, expertise, and business and technical organization.
ARIZ. ADMIN. CODE R §§ 17-3-201 through 204	Contractor Prequalification Board (appointed by State Highway Engineer)	Application and financial statement compiled by independent CPA or public accountant registered and licensed by any state submitted 15 days prior to bid opening. 15 month certification period		1. Key personnel and their work experience. 2. Organizational structure. 3. History of past or current projects and contracts. 4. Company affiliations. 5. Equipment owned or controlled. 6. Any applicable licenses. 7. Type of work requested. 8. Individuals authorized to act on behalf of the contractor. 9. Any prequalification or bidding disputes with a government agency. 10. Financial condition.

STATE	CERTIFYING AGENCY	APPLICATION AND OTHER DOCUMENTS; PERIOD OF CERTIFICATION	EXEMPTION FROM CERTIFICATION	CRITERIA FOR CERTIFICATION
ARK. CODE § 19-11-235 Ark. Standard Specifications § 102-01	State Highway Commission	Financial statement and experience record on questionnaire forms specified by Commission, certified by certified or registered public accountant submitted 5 days prior to time rating is made. Period of certification equal to 1 year plus grace period of 4 months.	Contractor's license under ARK. STAT. § 17-22-101 not required for contracts of less than $20,000, but must still prequalify.	1. Evidence contractor has been regularly engaged in type of work being bid and length of time. 2. Evidence of necessary capital, machinery, material, and expert workers.
CAL. PUB. CONTRACT CODE §§ 10160-10165	Department of Transportation	Standard questionnaire and Financial statement. Application must be submitted at least 5 days prior to bid opening; must have been prequalified for at least 1 day prior to bid opening.	Prequalification is at option of department, but if required for one bidder must be required for all bidders on a given project.	1. Financial responsibility. 2. Experience. 3. Any previous disqualification or debarment. 4. Safety record.
COLO. REV. STAT. § 24-92-107 2 COLO. CODE. Reg. § 601-10	Department of Transportation	Application and supporting information, including financial statement submitted 10 days prior to bid opening. Certification good for 1 year.		1. Financial responsibility. 2. Equipment. 3. Experience of organization and personnel. 4. Whether previously debarred in any jurisdiction. 5. Past record on DOT contracts.
CONN. GEN. STAT. § 13a-95 Conn. DOT Construction Contract Bidding and Award Manual, Chapter VI.	Department of Transportation	Contractor's prequalification statement and financial statement attested by CPA submitted 30 days prior to requesting bid proposal form. Certification for 16 months from end of contractor's previous fiscal year. Must reapply at least 30 days prior to expiration.		1. Financial condition and resources. 2. Plant and equipment. 3. Organization. 4. Prior experience. 5. Financial interest in any other construction business. 6. Statement describing circumstances of any violation, nonresponsibility determination, or debarment.

STATE	CERTIFYING AGENCY	APPLICATION AND OTHER DOCUMENTS; PERIOD OF CERTIFICATION	EXEMPTION FROM CERTIFICATION	CRITERIA FOR CERTIFICATION
29 DEL. CODE § 6962(c)	Department of Transportation	Contractor questionnaire and any supplemental information requested. Audited financial statement. Period of Certification equal to 1 year.		1. Experience. 2. Performance reviews on previous contracts. 3. Civil judgments and criminal history, suspension or debarment, bankruptcy, or license revocation. 4. Organization. 5. Financial ability.
D.C. CODE §§ 2-353.01; 2-353.02 Code of D.C. Regs. Title 27 § 2200.4 Standard Specifications § 102.01	Chief Procurement Officer, Office of Contracting and Procurement	Period of Certification equal to 1 year	Bidders who have not done comparable work for the District within the past 5 years may be required to prequalify at contracting officer's discretion; also prequalification approval in another State may be considered as alternative to filing D.C. qualification forms.	1. Adequate financial resources. 2. Ability to comply with schedule, taking all other commitments into account. 3. Satisfactory performance record. 4. Satisfactory record of integrity and business ethics. 5. Organization. 6. Experience. 7. Accounting and operational controls. 8. Technical skills. 9. Compliance with district licensing and tax regulations. 10. Necessary equipment and facilities. 11. Other qualifications necessary to receive award.
FLA. STAT. § 337.14 FLA. ADMIN. CODE § 14-22.002	Department of Transportation	Annual application, audited financial statement. Department is allowed 30 days to process. Certification expires 16 months after date of last audited financial statement.	Prequalification not required to bid on contracts under $250,000.	1. Financial responsibility. 2. Equipment. 3. Organizational personnel. 4. Satisfactory work performance record.

STATE	CERTIFYING AGENCY	APPLICATION AND OTHER DOCUMENTS; PERIOD OF CERTIFICATION	EXEMPTION FROM CERTIFICATION	CRITERIA FOR CERTIFICATION
GA. CODE § 32-2-66 Ga. Admin. Rules, ch. 672-5	Department of Transportation	Application and questionnaire submitted 10 days prior to bid opening, must be updated and submitted annually. Financial statement. List of equipment Letters of reference from three other public agencies if no work done for DOT in previous 5 years.	Required only for any individual contracts in excess of $2 million.	1. Financial responsibility. 2. Major plant and equipment. 3. Organization and personnel. 4. Experience over past 3 years.
HAW. REV. STAT. § 103D-310 Standard Specifications § 102.01	Procurement Policy Board	Financial statement and Standard Questionnaire, after notice of intent to submit bid filed 10 days prior to bid opening.		1. Financial ability. 2. Resources. 3. Skills, capability. 4. Business integrity.
IDAHO CODE §§ 54-1903; 54-1910 Standard Specifications §§ 102.11	Public Works Contractors License Board	Annual sworn application. Financial statement, which may include letter from bonding company. Oral or written examination, or both, required. Must be licensed prior to bid opening.	1. Officers of court acting in scope of office. 2. Public utilities. 3. Work on federal land. 4. Irrigation or drainage ditches. 5. Licensed architects or engineers. 6. Construction costing $10,000 or less. 7. Governmental entity. 8. Installation of finished products, not fixtures. 9. Personal property. 10. Solid waste disposal sites.	1. Experience and general knowledge of building safety, health and lien laws, and basic administrative principles of contracting business. 2. Good character. 3. Contractor has not previously been refused a license.
44 ILL. ADMIN. CODE , Part 650	Department of Transportation	Completed application, Statement of Experience, Equipment, and Financial Condition submitted 21	Department has authority to waive prequalification for specialized	1. Financial resources. 2. Performance. 3. Experience.

STATE	CERTIFYING AGENCY	APPLICATION AND OTHER DOCUMENTS; PERIOD OF CERTIFICATION	EXEMPTION FROM CERTIFICATION	CRITERIA FOR CERTIFICATION
		days prior to bid opening.	contracts.	4. Equipment. 5. Capacity to perform.
IND. CODE §§ 8-23-10-1 through 8-23-10-8	Department of Transportation	Prequalification application and financial statement, if for contract over $1 million, must be audited. Certification period of 2 years. Commission may investigate any aspect of application or statement.	Subcontracts of less than $300,000.	1. Financial resources are adequate. 2. Competent and responsible.
IOWA CODE § 314.1	Department of Transportation	Prequalification application form supplied by department submitted at least 5 calendar days prior to bid opening. Certification period of 18 calendar months.		1. Financial Responsibility. 2. Equipment. 3. Experience.
KAN. STAT. § 75-37,104 KSDOT Contractor's Prequalifi-cation and Experience Questionnaire	Department of Transportation,	Application, including financial statement submitted at least 7 days prior to bid opening.		1. Financial rating. 2. Amount of required equipment. 3. Experience of organization and key personnel.
KY. REV. STAT. §§ 176.130, 176.140, 176.150 603 KY. ADMIN. RULES, 2:015	Department of Highways	Application, including financial statement at least 15 days prior to bid opening. Certificate expires 120 days after end of applicant's fiscal year. Contractor expected to re-apply no later than 90 days after end of fiscal year.		1. Financial status. 2. Experience and organization. 3. Adequacy of plant and equipment. 4. Business ability. 5. Previous record.
LA. REV. STAT. §§ 37:2151 through 37:2163	State Licensing Board for Contractors	Financial statement prepared by auditor. References. License expires on December 31 of year in which it was issued.	1. Contracts for less than $50,000. 2. Work on land owned by federal government. 3. Licensed	1. Financial responsibility. 2. Experience. 3. Equipment. 4. Organization and personnel.

STATE	CERTIFYING AGENCY	APPLICATION AND OTHER DOCUMENTS; PERIOD OF CERTIFICATION	EXEMPTION FROM CERTIFICATION	CRITERIA FOR CERTIFICATION
Standard Specifications §§ 102.01, 102.02			engineers and architects. 4. Supervising work on own property. 5. Public utilities.	
23 ME. REV. STAT. § 4243 MDOT Contractor Prequalifi--cation Form	Department of Transportation	Financial statement and experience record at least 10 days prior to bid opening. Period of Certification equal to 3 years	Contracts under $300,000. Contractor previously prequalified and has completed two projects in last prequalification period. May be waived by commissioner.	1. Sufficient experience. 2. Past record and personnel. 3. Record on safety, environmental, and civil rights. 4. Financial responsibility. 5. Previous denials or prequalification. 6. Claims history.
MASS. LAWS c. 29 § 8B 720 CODE MASS. Reg. 5.00	Commissioner of Highways	Application. Financial statement. Period of Certification equal to 1 year.	Contracts of less than $50,000.	1. Financial responsibility. 2. Bonding capacity. 3. Experience. 4. Equipment. 5. Size and completion dates of other jobs. 6. Past performance on similar jobs.
MICH. ADMIN. CODE §§ 247.1 through 247.53	Department of State Highways and Transportation	Application and financial statement submitted at least 15 days prior to bid opening. Certification expires 15 ½ months after end of fiscal year. Must reapply annually.		1. Past performance on work of similar nature. 2. Financial resources. 3. Construction equipment and facilities. 4. Experience and key personnel.
Minn. Standard Specifications §§ 1201, 1213	Department of Transportation	Prequalification not required for bid submission; however, a written statement may be required prior to consideration of a bid or award showing experience of bidder and amount of capital and equipment available.		

STATE	CERTIFYING AGENCY	APPLICATION AND OTHER DOCUMENTS; PERIOD OF CERTIFICATION	EXEMPTION FROM CERTIFICATION	CRITERIA FOR CERTIFICATION
MISS. CODE §§ 31-3-15; 31-3-21 Rules and Regulations of State Board of Contractors, Rule 1.1 Code of Miss. Rules 50-023-001	State Board of Contractors	Application on form provided by Board, to be submitted with payment of special privilege tax. Financial statement signed by CPA. Certificate of general liability insurance. Documents submitted annually. Period of Certification equal to 1 year	Contracts of $50,000 or less.	1. Experience, ability, and character. 2. Manner of previous performance. 3. Equipment. 4. Personnel. 5. Work completed and work on hand. 6. Apparent ability to satisfactorily perform work currently under contract. 7. Written or oral examination results. 8. Financial condition. 9. Any previous default under contractor licensing laws.
MO. REV. STAT. §227.105 7 MO. CODE REGS. §§ 10-15.010, 10-18.010	Department of Transportation	Audit report from bonding company. Prequalification contractor questionnaire form available online Period of Certification equal to 1 year Documents submitted at least 7 days prior to bid opening.	Contracts under $2 million. Contractors who have performed work for department within preceding 5 years.	1. Experience of contractor and key personnel. 2. Ability to complete work satisfactorily and on time. 3. Type of work contractor qualified to perform. 4. Designation of resident agent. 5. Value of works in progress. 6. Equipment available. 7. Insurance coverage. 8. Audit from bonding company.
MONT. ADMIN. R. § 18.3.201	Department of Transportation	Does not require prequalification; requires only registration with Department of Labor. Responsibility determined at time of bidding.		1. Financial resources adequate. 2. Adequate equipment, material, personnel, and facility. 3. Satisfactory record of integrity. 4. Legally qualified to contract with Commission. 5. Satisfactory record of

STATE	CERTIFYING AGENCY	APPLICATION AND OTHER DOCUMENTS; PERIOD OF CERTIFICATION	EXEMPTION FROM CERTIFICATION	CRITERIA FOR CERTIFICATION
				performance.
NEB. REV. STAT. §§ 39-1351, 39-1352 Standard Specifications § 102.01	Department of Roads	Statement under oath showing qualifications. Financial statement certified by CPA. Letter of credit acceptable in lieu of financial statement for contracts under $250,000. Documents submitted not less than 10 days prior to bid opening. Period of Certification equal to 15 months.		1. Financial resources. 2. Equipment. 3. Experience. 4. Performance record.
NEV. REV. STAT. § 408.333	Department of Transportation	Prequalification financial statement, questionnaire verified under oath submitted in sufficient time for processing prior to bid opening.		Financial ability and experience in performing public works of similar nature.
N.H. CODE ADMIN. R. Tra-401	Department of Transportation	Questionnaire and financial statement meeting standard set out in rule submitted at least 8 days prior to bid opening. Period of Certification equal to 1 year. Expires a year and 3 months from date of last financial statement.		1. Financial resources. 2. Experience. 3. Record of completed proj ects, whether any de faults.
N.J. STAT. ANN. §§ 27:7-35.2 through 27:7-35.12 Department Regulations § 16:44	Department of Transportation	Questionnaire with statement under oath.and certified financial statement submitted at least 15 days prior to bid opening. Period of Certification equal to 18 months		1. Financial ability. 2. Adequacy of plant, equipment, and organization. 3. Record of prior performance.
				4.
N.M. STAT. § 13-1-134 18 N.M. ADMIN. CODE §§ 27.5.3 through 27.5.15	Highway and Transportation Department	Questionnaire under oath submitted not less than 7 days prior to bid opening.		1. Financial resources. 2. Production or service facilities. 3. Personnel. 4. Service reputation. 5. Experience. 6. Must be licensed in New

STATE	CERTIFYING AGENCY	APPLICATION AND OTHER DOCUMENTS; PERIOD OF CERTIFICATION	EXEMPTION FROM CERTIFICATION	CRITERIA FOR CERTIFICATION
				Mexico.
N.Y. Standard Specifications § 103-01	The bidder must present evidence of ownership, corporate structure, ability, and financial standing, and a statement as to equipment.			
N.C. Standard Specifications § 102-2	Department of Transportation	Experience questionnaire and additional material requested by Department submitted at least 2 weeks prior to bid opening. Period of Certification equal to 24 months.		1. Sufficient ability and experience. 2. History of successful and timely performance. 3. Financial ability to furnish bonds. 4. Sufficient equipment. 5. Available experienced personnel. 6. List of related completed work. 7. Identity of ownership. 8. Financial ability to complete work. 9. Safety Index Rating form.
N.D. CENT. CODE § 43-07-15 Standard Specifications § 102.01	Department of Transportation	Financial statement, record of experience and equipment submitted at least 7 days prior to bid opening. Period of Certification equal to 12 months	Not required for landscaping, rest areas, or electrical or other specialty work.	1. Financial responsibility. 2. Organization. 3. Plant and equipment. 4. Previous experience.
OHIO REV. CODE §§ 5525.02 through 5525.09 OHIO ADMIN. CODE §§ 5501:-2-3-1 through 10	Department of Transportation	Application form supplied by department. Certificate of compliance with affirmative action programs. Department has 30 days to process application. Period of Certification equal to 12 months.	Not required for environmental remediation or specialty work for which no classes are established.	1. Net current assets or working capital to indicate ability to execute contract and meet obligations. 2. Equipment. 3. Past performance. 4. Experience. 5. Personnel and organization.
61 OKLA. STAT. § 118 OKLA. ADMIN.	Transportation Commission and Transportation	Audited financial statement, certified by CPA and experience questionnaire submitted 14 days prior to bid	Department may waive requirement when in best	1. Financial resources. 2. Technical expertise.

STATE	CERTIFYING AGENCY	APPLICATION AND OTHER DOCUMENTS; PERIOD OF CERTIFICATION	EXEMPTION FROM CERTIFICATION	CRITERIA FOR CERTIFICATION
CODE § 730:25-3-1	Authority	opening. Period of Certification equal to 12 months after initial prequalification, then 2 years from acceptance of contractor's last project.	interest of state and increase competition, and for work such as environmental or landscaping or other work that does not involve highway construction.	
OR. REV. STAT. §§ 279B.110; 279B.120	Department of Transportation	Financial statement, record of experience, and equipment submitted 10 days prior to bid opening. Period of Certification equal to 12 to 36 months.	Contracts under $50,000.	1. Financial ability. 2. Sufficient equipment, material, personnel, and expertise. 3. Satisfactory record of performance. 4. Satisfactory record of integrity. 5. Legal ability to contract.
62 Pa. C.S. § 532; 67 Pa. Code, chapter 457 Standard Specifications § 102.01(a)	Department of Transportation	Statement under oath on form supplied by department, including financial statement, contractor's organization and experience statement, and affirmative action statement submitted at least 10 working days prior to bid opening. Period of Certification equal to 30 months from contractor's last balance sheet.	Demolition contracts estimated at less than $25,000; "miscellaneous work" determined to be not within purview of the law may be excluded by Deputy Secretary for Highway Administration, and so stated in bid advertisement.	1. Financial capacity. 2. Adequacy of plant and equipment. 3. Prior and current experience. 4. Organization and personnel. 5. Record of work done in past 5 years, and any liens, stop-work orders, or claims in last 5 years. 6. Whether ever failed to complete work, ever denied prequalification, or disqualified, or convicted of crime.
R.I. GEN. LAWS § 37-2-26 R. I. Procurement Regs. § 12. 102.01	Department of Transportation	List of equipment. Names of supervisory personnel and their qualifications. Financial statement and financial references. Certificate of		1. Financial resources. 2. Experience. 3. Equipment.

STATE	CERTIFYING AGENCY	APPLICATION AND OTHER DOCUMENTS; PERIOD OF CERTIFICATION	EXEMPTION FROM CERTIFICATION	CRITERIA FOR CERTIFICATION
		nondiscrimination.		
S.C. CODE § 57-5-1650 S.C. CODE of REG. §§ 63-300 through 63-307	Department of Transportation	Sworn statement on form supplied by Department submitted 7 days prior to bid opening. Period of Certification equal to 12 months		1. Prior performance. 2. Recent past references on performance. 3. Financial stability. 4. Experience on similar projects.
S.D. CODIFIED LAWS § 31-5-10 S.D. ADMIN. R. § 70:07:02. Standard Specifications § 2.1	Department of Transportation	Prequalification application with statement under oath, and financial information, which may be audited financial statement or certificate of surety from bonding firm.	Not required on contracts less than $100,000.	1. Equipment. 2. Organization. 3. Prior experience. 4. Financial resources. 5. Any pending debarment proceedings.
TENN. CODE § 54-5-117 Standard Specifications § 102.01	Department of Transportation	Form supplied by department with statement under oath submitted 14 days prior to bid opening. Period of Certification equal to 18 months.		1. Financial responsibility. 2. Experience. 3. Organization and equipment. 4. Work currently underway.
43 TEX. ADMIN. CODE § 9.12	Department of Transportation	Questionnaire, CPA-audited financial statement if for project over $300,000; may be unaudited if under that amount, and Certificate of Eligibility for federal aid projects submitted by noon on day prior to bid letting. Period of Certification equal to 12 months plus 3-month grace period for renewal.		1. Financial condition. 2. Equipment. 3. Experience.
UTAH CODE § 63G-6-401(8) Standard Specifications § 001201.6	Department of Transportation	Annual application and financial statement certified by CPA. Agency is allowed 10 working days to process application.	Contracts of less than $1.500,000.	1. Financial resources and liabilities. 2. Equipment. 3. Past record. 4. Personnel.
VT.	Agency of	Experience questionnaire and		1. Financial ability.

STATE	CERTIFYING AGENCY	APPLICATION AND OTHER DOCUMENTS; PERIOD OF CERTIFICATION	EXEMPTION FROM CERTIFICATION	CRITERIA FOR CERTIFICATION
Transportation Policies and Procedures for Prequalifi-cation, Bidding and Awarding of Contracts § 2-6 VDOT Contractor's Experience Questionnaire	Transportation	financial statement certified by CPA submitted 5 working days prior to bid opening. Period of Certification equal to 12 months. Certificate expires 3 months after end of contractor's fiscal year.		2. Adequacy of plant and equipment. 3. Organization. 4. Prior experience.
VA. CODE § 33.1-12(b) Road and Bridge Specifications §§ 102.01, 102.8 VDOT Application Rules Governing Prequalificatio n and Certification)	Department of Transportation Comm.	Application, financial statement, workers' compensation certificates of insurance, and report of work underway submitted 30 calendar days prior to bid submission. Period of Certification equal to 12 months.	Not required for specialty items.	1. Financial ability. 2. Organization. 3. Experience. 4. Equipment. 5. Work underway.
				6.
WASH. REV. CODE §§ 18.27; 47.28.070 WASH. ADMIN. CODE §§ 468-16-010 through 150 Standard Specifications § 1-02.1	Department of Transportation	Standard questionnaire with statement under oath and financial statement submitted 15 days prior to bid opening. Period of Certification equal to 12 months.		1. Adequacy of financial resources. 2. Necessary experience. 3. Organization and technical competence. 4. Ability to meet performance schedule. 5. Satisfactory record of performance. 6. Integrity and skill on part of employees.
W. VA. CODE, § 17-4-19	Division of Highways	Financial statement; record of experience and equipment submitted 15 days prior to bid opening.		1. Financial resources available. 2. Equipment, property, and

STATE	CERTIFYING AGENCY	APPLICATION AND OTHER DOCUMENTS; PERIOD OF CERTIFICATION	EXEMPTION FROM CERTIFICATION	CRITERIA FOR CERTIFICATION
				other assets. 3. Organization and personnel. 4. Record of work accomplished. 5. Past experience.
W. Va. Code of State Rules § 157-3-4 Stan. Specs. § 102.1 WVDOT Prequalification-tion Form (Contract Form SC 421)				
Standard Specifications § 102.1	Department of Transportation	Application on form supplied by department.		1. Financial ability. 2. Adequacy of plant and equipment. 3. Organization. 4. Prior experience.
WYO. STAT. § 24-2-108 Transportation Rules and Regulations, ch. 6 WCWR-045-000-006	Department of Transportation	Financial statement; record of experience submitted no sooner than 30 days or less than 5 days prior to bid letting. Period of Certification equal to 15 months.	Contracts of less than $200,000.	1. Financial ability. 2. Adequacy of plant and equipment. 3. Organization. 4. Past experience. 5. “Other pertinent or material facts as may be desirable in the judgment of the Highway Superintendent.”

APPENDIX F

STATE LAWS RELATING TO SUSPENSION AND DEBARMENT

STATE AND CITATION	BASIS FOR SUSPENSION, DISQUALIFICATION, OR DEBARMENT
ALA. CODE § 23-1-56 Standard Specifications § 102.02 ALDOT Prequalification Questionnaire	1. Lack of competency, plant, equipment, or machinery. 2. Uncompleted work that might hinder performance. 3. Failure to pay all bills for labor and materials on other jobs. 4. Failure to comply with prequalification regulations. 5. Default or unsatisfactory work on prior contracts. 6. Disqualification by FHWA. 7. DBE violations. 8. Collusion. 9. Failure to reimburse state for overpayment or forfeited proposal guarantee. 10. Affiliated with contractor who has been suspended or debarred. 11. Making false or fraudulent statements in application or in administrative or judicial proceeding.
ALASKA STAT. §§ 36.30.635-685 2 ALASKA ADMIN. CODE §§ 12.620-670 Alaska Standard Specifications §§ 102-1.01, 102-1.12	Disqualification: 1. Evidence of bid rigging or collusion. 2. Fraud or dishonesty in performance of previous contracts. 3. More than one proposal submitted. 4. Unsatisfactory performance on previous contract. 5. Failure to pay or settle all bills due on previous contract. 6. Uncompleted work that might hinder current contract. 7. Failure to reimburse state for money owed on previous contract. 8. Default under previous contract. 9. Failure to comply with any department qualification requirements. Debarment / Suspension 1. Conviction of criminal offense in obtaining or performing a public contract. 2. Conviction of offense such as embezzlement or bribery that indicates lack of business integrity. 3. Serious violation of contract terms such as knowing failure to complete on time or unsatisfactory performance. 4. Violation of ethical standards. 5. Violation of public contract laws.
ARIZ. ADMIN. CODE §§ 17-3-201 through 204 ADOT Application for	1. Contractor falsifies documents. 2. Failure to enter into contract awarded by department. 3. Default on previous contract with any public agency. 4. Unsatisfactory work performance record with department. 5. Failure to notify department within 30 days of any change in ownership, corporate officers, bankruptcy, receivership, or judgment adverse to contractor.

STATE AND CITATION	BASIS FOR SUSPENSION, DISQUALIFICATION, OR DEBARMENT
Contractor Prequalification	
ARK. CODE §§ 19-11-235, 19-11-245 Ark. Standard Specifications § 102-01	Disqualification: 1. Failure to comply with prequalification requirements. 2. Lack of competency or plant and equipment. 3. Uncompleted work that might hinder performance. 4. Failure to satisfactorily settle all bills on previous jobs. 5. Serious misconduct that affects contractor's ability to perform future work. 6. Suspension or debarment in effect. 7. Failure to reimburse state for money owed on previous contract. 8. Previous failure to execute contract or provide bonds. 9. Unsatisfactory performance on previous contract. 10. Liquidated damages currently being assessed under current contract. 11. Default under previous contracts.
CAL. PUB. CONT. CODE §§ 10160-10166; 10285-10285.5	1. Inadequate safety record. 2. Conviction of contractor or principal of fraud, bribery, collusion, conspiracy, or violation of antitrust laws.
COLO. REV. STAT. § 24-92-107 2 Colo. Code. Reg. §§ 601-10	1. Contractor declared in default on any contract. 2. Making false or deceptive statements on prequalification application or any other information provided to DOT. 3. Failure to report significant decreases in capabilities or limitations on performing work. 4. Lack of integrity in contract-related matters. 5. No longer meets criteria for prequalification.
Conn. Gen. Stat. § 31-57c	1. Unsatisfactory record of compliance with state and federal laws. 2. Unethical conduct or criminal conduct. 3. Suspended or debarred by another agency. 4. Lacks necessary skills, equipment, organization, experience, or employees to timely complete project in accordance with contract. 5. Unsatisfactory record of performance on previous projects. 6. Lack of financial resources. 7. Lack of experienced management. 8. Making false representations to or about department. 9. Reason to doubt that contractor will fulfill all contract and legal requirements; that it has necessary financial, managerial, and other resources; that it will exhibit integrity, honesty, cooperativeness, professionalism, and skill in performing contract.

STATE AND CITATION	BASIS FOR SUSPENSION, DISQUALIFICATION, OR DEBARMENT
29 DEL. CODE §§ 6962(c), (d)(14)	Disqualification 1. Inadequate expertise, labor, or experience. 2. Failure to provide supplemental information requested. Suspension/Debarment 1. Failure to supply adequate labor. 2. Inadequate financial resources. 3. Poor performance.
D.C. CODE § 2-2-359.07 Standard Specifications § 102.01	1. Conviction of criminal offense relating to obtaining or performing public contract. 2. Conviction for fraud or other crime indicating lack of business integrity. 3. Conviction of antitrust violation. 4. False assertion of DBE status. 5. Any other cause affecting responsibility.
FLA. STAT. § 337.16 FLA. ADMIN. CODE § 14-22.002(2)	1. Contractor delinquent on previously awarded contract. 2. Making false or deceptive statements in prequalification application, bid proposal, certificate or payment, or of judicial proceeding. 3. Insolvency or bankruptcy. 4. Failure to comply with contract requirements. 5. Submission of more than one bid on the same project by contractor affiliates. 6. Wrongfully employing or offering compensation or otherwise wrongfully attempting to influence department employee. 7. Failure to register motor vehicles operated in the state.
GA. CODE § 32-2-66 Ga. Admin. Rules §§ 672-5.04, 672-5.16	1. Work not being prosecuted diligently. 2. Refusal to execute contract and forfeiture of bid bond. 3. Contractor's actions have lessened competition or damaged integrity of bidding process. 4. Conviction of crimes involving restraint of trade.
HAW. REV. STAT. § 103D-310	1. Bidder not fully qualified and able to perform intended work. 2. Unreasonable failure to promptly provide information regarding inquiry on responsibility.
IDAHO CODE §§ 54-1910, 54-1914	1. Abandonment of construction project without legal excuse. 2. Diversion of funds or property received for construction project. 3. Willful disregard of plans and specifications. 4. Willful disregard of building, safety, labor, or compensation insurance laws. 5. Misrepresentation of material fact in obtaining license.

STATE AND CITATION	BASIS FOR SUSPENSION, DISQUALIFICATION, OR DEBARMENT
	6. Aiding or abetting unlicensed person with intent to evade contractor licensing law. 7. Willful or deliberate failure to complete project. 8. Willful or deliberate failure to pay for labor or materials. 9. Change in financial circumstances that may impair financial responsibility.
44 ILL. ADMIN. CODE §§ 6.520	1. Lack of business integrity or honesty, such as bribery. 2. Material false statement in application for prequalification or affidavit. 3. Material violation of rule or procurement procedure. 4. Material false statement with respect to quality of cost of work done or procurement procedures. 5. Doing business with suspended contractor. 6. Debarment or suspension by another state agency or agency of other state.
IND. CODE § 8-23-10-8 105 IND. ADMIN. CODE §§ 11-1-1 through 11-2-12	1. Making false statement to department with respect to net worth in any other document filed with department. 2. Work unsatisfactory 3. Apparent that work will not be completed on time 4. Contractor fails to adequately document current or previous contract.
IOWA Standard Specifications §§ 1102.01, 1102.03	1. Failure to repair or replace work found not in conformity with contract documents. 2. Failure to carry out work in acceptable manner or in reasonable time. 3. Failure to perform required work with own organization, or assigning work without approval. 4. Forfeiture of proposal guaranty and failure to enter into awarded contract. 5. Failure to comply with EEO and affirmative action requirements. 6. Failure to pay subcontractor progress payments and retainage. 7. Safety concerns. 8. Contractor default. 9. Material change in financial condition.
KAN. STAT. §§ 75-37, 103 Kan. Admin. Rules § 36-31-2 through 36-31-5	1. Conviction or admission of fraud or criminal offense in connection with obtaining or performing contract; anti-trust violation; embezzlement, theft, forgery, falsification of documents, making false statements, obstruction of justice; wage and hour laws; or violation of laws indicating lack of business integrity. 2. Violation of contract terms, including failure to perform in accordance with specifications, or record of unsatisfactory performance. Debarment not to exceed 3 years and suspension not to exceed 3 months.
KSDOT Contractor's Prequalifi-cation and Experience	

STATE AND CITATION	BASIS FOR SUSPENSION, DISQUALIFICATION, OR DEBARMENT
Questionnaire	
KY. REV. STAT. §§ 176.130, 176.140, 176.150 603 KAR § 2:015	1. Failure to perform satisfactorily. 2. Failure to adhere to laws and regulations.
LA. REV. STAT. §§ 37:2156 through 37:2158 Standard Specifications §§ 102.01; 102.02	1. Dishonest or fraudulent act determined by a court to have caused substantial damage to another. 2. Willful misrepresentation of material fact in applying for license. 3. Willful failure to comply with licensing rules. 4. Entering into contract with unlicensed contractor. 5. Permitting contractor license to be used by unlicensed person. 6. Failure to maintain registered agent. 7. Failure to fulfill licensing requirements. 8. Insolvency or involuntary cessation of business. 9. Problems relating to ability to engage in business of contracting. 10. Debarment by any other agency.
17 Maine Admin. Rules § 102	1. Bribery, attempted bribery, or conspiracy to bribe. 2. Conviction for fraud, embezzlement, theft, forgery, destruction or falsification of records. 3. Antitrust or RICO conviction.
Code of Md. Regs. §§ 21-08.02 through 21.08.03 MDOT Contractor Prequalification Form	1. Conviction of a bidding crime. 2. Conviction of any crime indicating lack of moral or business integrity. 3. Debarment by any state or federal agency. 4. Making false or deceptive statements on any documents submitted to department.
MASS. LAWS ch. 29, § 29F 720 MASS. REGS. CODE 5.00	1. Conviction of willfully making false or fraudulent statement in application. 2. Collusion.

STATE AND CITATION	BASIS FOR SUSPENSION, DISQUALIFICATION, OR DEBARMENT
MICH. ADMIN. CODE §§ 247.22	1. Submission of false statements. 2. Failure to comply with rules and with requirements of prequalification. 3. Factors that affect responsibility or ability to perform work.
Minn. Stat. § 161.32 Minn. Standard Specifications § 1213	1. Debarment by federal agency under 49 C.F.R. pt. 29. 2. Submission of more than one proposal on a project. 3. Evidence of collusion.
MISS. CODE §§ 31-3-15; 31-3-21 Rules and Regulations of State Board of Contractors (CMSR) 50-023-001	1. Finding of nonresponsibility by board. 2. Submission of bid outside of classification.
MO. REV. STAT. §§ 227.100; 227.105 7 MO. CODE REGS. §§ 10-15.010, 10-18.010	1. Submission of more than one proposal for same project. 2. Collusion. 3. Conviction or civil judgment for fraud, criminal offense in attempting to obtain bid, antitrust, embezzlement, theft, bribery, perjury, assault, false statements or claims, obstruction of justice. 4. Violation of terms of public contract so serious as to affect the integrity of the project. 5. Debarment by a local, state, or federal agency.
MONT. ADMIN. R. §§ 18.3.101-106	1. Conviction of fraud or criminal offense in obtaining or performing a contract; antitrust violation; crime such as embezzlement, theft, or obstruction of justice; conspiracy or collusion; or any crime indicating lack of business integrity. 2. Filing false or fraudulent claim. 3. Violation of contract terms such as willful failure to comply with specifications; history of failure to perform or unsatisfactory performance. 4. Failure to reimburse department for money owed under previous contract. 5. Willful violation of applicable statute or regulation. 6. Serious or repeated violation of wage requirements. 7. DBE violation. 8. Doing business with debarred or suspended contractor.

STATE AND CITATION	BASIS FOR SUSPENSION, DISQUALIFICATION, OR DEBARMENT
	9. Nonpayment of taxes.
Standard Specifications for Highway Construction § 102.18	Disqualification: 1. Submission of more than one proposal for a project. 2. Collusion among bidders. 3. Bid obviously or materially unbalanced, signature is missing from affidavit, or bid not accompanied by bid bond. Debarment: 1. Indictment or conviction of bidding crime. 2. Conviction of offense involving lack of moral or ethical integrity. 3. Debarment by another state or federal agency. 4. Materially false statements on bid proposal.
NEV. REV. STAT. § 408.333	May be disqualified if responses to questionnaire are insufficient.
N.H. ADMIN. R. Part Tra-401.12	1. Materially false, deceptive, or fraudulent statements on application or on bid proposal form. 2. Conviction for antitrust violations. 3. Debarment by other state or federal agency. 4. Factors that materially affect contractor's ability to perform, including poor performance history.
N.J. STAT. ANN. §§ 27:7-35.2 through 27:7-35.12 Department Regulations § 16:44	Making false, deceptive, or fraudulent statement in application for prequalification, or in hearing relating to prequalification, commission of criminal offense, violation of discrimination, labor, or any laws governing the conduct of business, willful failure to perform in accordance with specifications, or fee laws.
N.M. STAT. 13-1-134 18 N.M. ADMIN. CODE §§ 27.5.3.14; 28.4.3 through 28.4.10	1. False, deceptive, or misleading statements in application. 2. Conviction for bidding crime, embezzlement, theft, forgery, bribery, falsification or destruction of records, or receiving stolen property. 3. Conviction of antitrust violation arising out of submission of bid proposal. 4. Willful failure to perform contract, or history of failure to perform. 5. Willful violation of state procurement code.
N.C. Standard Specifications §§ 102-2; 102-15	1. Unsatisfactory safety record. 2. Unsatisfactory progress on work or being declared in default. 3. Uncompleted contracts that might hinder additional work. 4. Failure to comply with prequalification requirements.

STATE AND CITATION	BASIS FOR SUSPENSION, DISQUALIFICATION, OR DEBARMENT
	5. Submission of more than one bid for a project. 6. Evidence of collusion, or failure to submit non-collusion affidavit. 7. Failure to comply with written order of state engineer. 8. Failure to comply with DBE requirements. 9. Failure to comply with subletting and assignment requirements. 10. Failure to return overpayments. 11. Failure to maintain safety index. 12. Recruitment of department employees. 13. Department has not received amount due under forfeited bid bond or on performance bond.
N.D. CENT. CODE § 43-07-06 Standard Specifications §§ 102.01; 102.13	1. More than one proposal submitted for a project. 2. Collusion among bidders.
OHIO ADMIN. CODE §§ 5501:2-3 through 10	1. Contractor in default on any department project. 2. Debarment or suspension by other state or federal agency. 3. Conviction of crimes involving fraud. 4. Bankruptcy. 5. Submission of false or misleading statements in connection with prequalification or contract. 6. Collusion with other bidders. 7. Violation of DBE requirements. 8. Failure to pay prevailing wages. 9. Poor contractor evaluations.
OKLA. ADMIN. CODE § 730:25-3-5	1. Conviction of bidding crime or other crime involving lack of moral or ethical integrity. 2. Unsatisfactory performance of contract. 3. Disqualification or debarment by another state or federal agency. 4. Failure or refusal to comply with terms or obligations of contract.
OR. REV. STAT. §§ 279B.130; 279C.440 OR. ADMIN. R., 734-010-0270	1. Conviction of crime related to bidding or performance of public contract. 2. Conviction of offense involving lack of moral integrity, such as bribery or embezzlement. 3. Conviction under antitrust statutes. 4. Failure to perform contract or unsatisfactory performance. 5. Failure to have workers' compensation and unemployment compensation insurance.
67 PA. CODE §§ 457.13 through	1. Commission of embezzlement, theft, forgery, bribery, falsification or destruction of records, making false statements, or receiving stolen property.

STATE AND CITATION	BASIS FOR SUSPENSION, DISQUALIFICATION, OR DEBARMENT
457.17	2. Commission of fraud in obtaining public contract. 3. Violation of antitrust statutes. 4. Violation of campaign contribution laws. 5. Violation of environmental laws. 6. Violation of labor laws, including prevailing wage. 7. Violation of workers' compensation act. 8. Violation of anti-discrimination laws. 9. Suspension or debarment by another state or federal agency. 10. Three or more instances when contractor has been found ineligible to bid. 11. Unsatisfactory performance of contract, including being declared in default; untimely performance; making false statements.
R.I. GEN. LAWS § 37-2-26 Standard Specifications §§ 102.01, 102.12 Rules and Regulations of R.I. Department of Transportation Regarding Contractor and Subcontractor Debarment, Suspension, and Sanctions	1. Submission of more than one bid on a project. 2. Collusion among bidders or violation of antitrust laws. 3. Making false statements on prequalification materials. 4. Failure to comply with prequalification requirements. 5. Debarment by another state or federal agency. 6. Failure to provide contract bond. 7. Lack of competency or inadequacy of equipment. 8. Uncompleted work that might hinder additional work. 9. Failure to pay all bills due for labor or materials. 10. Default or unsatisfactory performance on previous contract. 11. Failure to reimburse state for money owed under previous contract. 12. Failure to comply with post-qualification regulations imposed by state. 13. Conviction or admission of bid-related crime. 14. Crime involving lack of moral or ethical integrity. 15. Failure to comply with state or federal regulations.
S.C. CODE § 11-35-4220 S.C. CODE REGS. §§ 63-304-306	1. Unsatisfactory work. 2. Conviction of any crime indicating lack of business integrity. 3. Civil judgment or administrative decision, or any act or omission, indicating lack of business integrity. 4. Willful violation of contract provision. 5. Persistent failure to perform contract, or incompetent performance. 6. Knowingly allowing suspended or disqualified person to act as subcontractor. 7. Failure to cooperate in department or law enforcement investigation.
S.D. ADMIN. CODE §§	1. Lack of competency or inadequate machinery.

STATE AND CITATION	BASIS FOR SUSPENSION, DISQUALIFICATION, OR DEBARMENT
70:07:02; 70:07:04.01 through 70:07:04.19 Standard Specifications §§ 2.1, 2.3	2. Uncompleted work that department believes will hinder additional work. 3. Failure to pay or settle legal obligations due. 4. Failure to comply with prequalification regulations. 5. Default on previous contract. 6. Unsatisfactory performance, including noncompliance with specifications or failure to complete on time. 7. Failure to provide adequate safety measures. 8. Questionable moral integrity. 9. Failure to reimburse state for money due. 10. Conviction for contract crime. 11. Conviction of antitrust violation.
TENN. CODE § 54-5-117 Standard Specifications § 102.01	1. Default on existing contract. 2. Work on existing contract is behind schedule. 3. Failure to file prequalification statement
43 TEX. ADMIN. CODE §10.101	1. Debarment by federal agency. 2. Conviction of or admission of bidding crime. 3. Conviction of offense indicating lack of moral or ethical integrity, such as bribery. 4. Failure to execute contract or honor bid guaranty. 5. Default on highway improvement contract. 6. Conflict of interest violation 7. Debarment in another state
UTAH CODE § 63-56-20 Standard Specifications §§ 1.1; 1.15; 1.17-1.20	Disqualification: 1. More than one proposal submitted for one project. 2. Evidence of collusion among bidders. Disbarment: 1. Conviction, public admission, or guilty plea to contract-related crime. 2. Submission of false, deceptive, or fraudulent information in prequalification, bidding, or contract performance. 3. Anti-trust violation. 4. Lack of integrity in performing public projects. 5. Debarment of contractor or affiliate by another agency. 6. Collusion regarding DBE compliance. 7. Default on previous contract. 8. Unsatisfactory performance, including failure to complete on time, noncompliance, need for substantial corrective work, failure to provide adequate safety measures and traffic control. 9. Questionable moral integrity.

STATE AND CITATION	BASIS FOR SUSPENSION, DISQUALIFICATION, OR DEBARMENT
	10. Failure to reimburse state for money owed under previous contract.
Code of Vt. Rules § 14-010-004 VDOT Contractor's Experience Questionnaire VT Transportation Policies and Procedures on Prequalification, Bidding and Award of Contracts §§ 7.06; 7.12	Disqualification: 1. Work exceeds prequalification rating. 2. Unsatisfactory performance on past contracts. 3. Unsatisfactory performance or progress on current contracts. 4. Uncompleted work might hinder performance of new work. Suspension and Debarment: 1. Fraud or criminal offense in obtaining public contract. 2. Criminal offense indicating lack of business integrity. 3. Violation of law in performance of state contract. 4. Violation of settlement agreement under prequalification rules. 5. Making false statement to influence state. 6. Violation of conflict of interest laws. 7. Outstanding criminal indictment. 8. Willful or serious failure to perform contract. 9. Disqualification by federal agency or other state.
VA. CODE § 33.1-12 Road and Bridge Specifications §§ 102.01; 102.8 DOT Rules Governing Prequalification and Certification DOT Board Policy for Debarment and/or Suspension Policy	Disqualification (Enjoinment): 1. Project behind schedule. 2. Poor workmanship, until defective work corrected. 3. Submission of more than one bid on a project. 4. Incompetence or inadequacy of plant or equipment. 5. Unsatisfactory workmanship or progress on past projects for the department or other agencies. 6. Uncompleted work for the department that might hinder new job. 7. Failure to pay all bills for labor, materials, and equipment. 8. Failure to comply with prequalification regulations. 9. Failure to cooperate with department representatives. 10. Default on a contract. Enjoined from bidding: 1. Failure to meet DBE requirements. Debarment: 1. Proof of involvement in bidding crime. 2. Conviction of offense involving lack of moral or ethical integrity. 3. Debarment by another state or federal agency. 4. Flagrant violations of OSHA regulations. Debarment may be imposed for any length of time.
WASH. REV. CODE §§ 18.27.030;	Disqualification: 1. More than one bid submitted for project. 2. Evidence of collusion with other bidders.

STATE AND CITATION	BASIS FOR SUSPENSION, DISQUALIFICATION, OR DEBARMENT
47.28.070 WASH. ADMIN. CODE §§ 468-16-180; 468-16-190 Standard Specifications §§ 1-02.1; 1-02.14	3. Record of unsatisfactory performance. 4. Uncompleted work that might hinder performance. 5. Failure to pay or settle outstanding bills. 6. Failed to complete previous contract. 7. Conviction of bidding crime. 8. Not registered to do business in Washington. Suspension: 1. Incompetence detrimental to timely completion or safety. 2. Inadequate performance. 3. Infractions of regulations or specifications. 4. Finding of noncompliance and refusal to take corrective action. 5. Uncompleted work that may hinder completion of new work. 6. Failure to comply with DBE requirements. Revocation: 1. Conviction or admission of antitrust laws. 2. Knowingly concealing deficiency in prior contract performance. 3. Falsification of information relating to prequalification or contract performance or destruction of records. 4. Debarment by a federal or state agency. 5. Willful disregard for applicable law. 6. Default on previous contract within 3 years. 7. Bankruptcy. 8. Breach of contract. 9. Having been suspended two or more times in 2-year period.
W. VA. CODE, §§ 17-4-19; 5A-3-33d W. Va. Code of State Rules §§ 157-3-4; 157-3-13 Standard Specs. for Roads & Bridges § 102.13	Disqualification: 1. More than one proposal submitted by bidder. 2. Collusion with another bidder. Suspension/Debarment: 1. Conviction of offense involving fraud or offense regarding obtaining public contract. 2. Conviction of antitrust violation. 3. Conviction of an offense involving embezzlement, theft, forgery, bribery, falsification or destruction of records, making false statements, or receiving stolen property in connection with the performance of a contract. 4. Conviction of offense that indicates lack of business integrity or honesty. 5. Default on obligations owed state, such as state tax and revenue laws, unemployment compensation, and workers' compensation. 6. Contractor not in good standing with licensing board. 7. Willful failure to perform public contract or violation of standards of law or of generally accepted practices of the trade, amounting to intentionally deficient or grossly negligent performance. 8. Use of substandard materials or defects in construction amounting to gross negligence. 9. Willful misconduct demonstrating wanton indifference to interest of public.
WIS. STAT. §§	1. Submission of falsified statement.

STATE AND CITATION	BASIS FOR SUSPENSION, DISQUALIFICATION, OR DEBARMENT
66.0901; 84.06 Standard Specifications § 102.12 Policy on Prequalifi-cation of Bidders	2. Conviction of violation of federal or state law. 3. Collusion or restraint of trade.
WYO. STAT. § 24-08 Transportation Rules and Regulations, ch. 6 WCWR-045-000-006	1. Default on contract. 2. False, deceptive, or fraudulent statement on questionnaire. 3. Disqualification, suspension, or debarment by another government agency. 4. Attempt to influence department through gifts or gratuities, or by hiring agency employees. 5. Inability to meet WYDOT requirements for specifications and contracts.

APPENDIX G

STATE LAWS RELATING TO SCOPE AND COVERAGE OF CONTRACTOR BONDS

STATE & CITATION	SCOPE OF BOND OBLIGATION	AMOUNT OF COVERAGE	SPECIAL REQUIREMENTS
ALA. CODE § 39-1-1	Performance Bond: faithful performance of contract. Payment Bond: labor, materials, or supplies for or in the prosecution of the work provided in the contract. Exemption: contracts under $50,000.	100 percent of contract price. 50 percent of contract price.	Payment bond must provide for payment of reasonable attorney fees for successful claimant on bond.
ALASKA STAT. § 36.25.010 Standard Specs. § 103-1.05	Performance Bond: perform and complete all obligations and work under the contract. Payment Bond; payment of all claims for labor performed and materials and supplies furnished. Applies to contracts over $100,000.	50 percent of amount of contract less than $1 million; 40 percent of amount of contract over $1 million; over $5 million, bond amount is $2.5 million. Amount of performance bond shall be amount of payment bond.	Corporate surety must be authorized to do business in state, or at least two individual sureties.
ARIZ. STAT. §§ 34-221, 34-222 Standard Specs. § 103.07	Performance Bond: faithful performance of the contract in accordance with plans, specifications, and conditions, solely for protection of agency. Payment Bond: for payment of labor, materials, and supplies furnished to contractor or subcontractors.	100 percent of contract amount for each payment and performance bond.	Surety must have authority to transact business in the State. Bond must provide for payment of attorney fees for prevailing party.
ARK. CODE § 27-67-206 Standard Specs. § 103.05	Performance Bond: faithful performance of the contract. Payment Bond: In form acceptable to department.	Statute requires at least 25 percent of contract price. Standard Specs require 100 percent of contract amount for performance bond, and 80 percent of contract amount for payment bond.	
CAL. PUB. CONT. CODE §§ 10221-10225	Performance bond: Guarantee faithful performance of contract. Payment Bond: For payment of claims of laborers mechanics or materialmen employed under the contract.	At least 50 percent of contract price for each bond.	

STATE & CITATION	SCOPE OF BOND OBLIGATION	AMOUNT OF COVERAGE	SPECIAL REQUIREMENTS
COLO. REV. STAT. §§ 38-26-106; 24-105-202	Performance bond: Satisfactory to the state. Payment Bond: Payment for any labor, materials, team hire, sustenance, provisions, provender, or other supplies used or consumed by the contractor or his or her subcontractor in performance of the work contracted to be done, or supplier or laborers, rental machinery, tools, or equipment. Exceptions: Contracts under $50,000.	50 percent of contract amount.	Certified or cashier's check or bank money order may be accepted in lieu of surety bond.
CONN. GEN. STAT. § 49-41 Stand. Specs § 1.03.04	Performance Bond: Agency may require. Payment bond: For the protection of persons supplying labor or material in the prosecution of the work. Exceptions: Contracts under $50,000 do not require payment bond; contracts under $25,000 do not require performance bond.	Full amount of the contract.	
29 DEL. CODE § 6927 Standard Specifications § 103.05	Performance Bond: Compliance and performance by the successful bidder of each and every term and condition of the contract and the proposal, plans and specifications thereof; payment in full to every person furnishing materiel or performing labor in the performance of the contract, of all sums of money due the person for such labor and material. Exceptions: Bond may be waived for contract under threshold amount set by Contracting and Purchasing Council, or may be waived at discretion of State.	100 percent of contract price.	Bond must also indemnify and save harmless the State and the agency from all costs, damages, and expenses growing out of or by reason of the successful bidder's failure to comply and perform the work and complete the contract.
D.C. CODE § 2-357.02	Performance Bond: To ensure the protection of the District government. Payment Bond: For the protection of all businesses supplying labor and materials, including lessors of equipment to the extent of the fair rental value of the equipment, to the contractor or a subcontractor in the performance of the work provided for by the contract. Exceptions: Contracts under $100,000.	Amount equal to 100 percent of the portion or the contract price that does not include the cost of operation maintenance and finances.	Surety must be authorized to do business in District. In lieu of bond, may provide cash or other satisfactory security.

STATE & CITATION	SCOPE OF BOND OBLIGATION	AMOUNT OF COVERAGE	SPECIAL REQUIREMENTS
FLA. STAT. § 337.18	Payment and Performance Bond: prompt, faithful, and efficient performance of the contract according to plans and specifications and within the time period specified, and for the prompt payment of all persons furnishing labor, material, equipment, and supplies therefore. Exceptions: Department may waive requirement for contracts of $150,000 or less.	Amount of contract.	Department may require alternate security if bond is waived; surety must be registered to do business in state.
GA. CODE §§ 32-2-70; 13-10-40; 13-10-60.	Performance Bond: Required for construction contracts over $100,000, with discretion to require for contracts less than $100,000. Payment Bond: For the use and protection of all subcontractors and all persons supplying labor, materials, machinery, and equipment in the prosecution of the work provided for in the contract. Exemptions: Contracts under $50,000.	Amount of contract.	State may accept a cashier's check, certified check, or cash.
HAW. REV. STAT. § 103D-324	Performance Bond: Faithfully perform, and fully complete the contract in strict accordance with its terms. Payment Bond: For every person who furnishes labor or material to the contractor for the work provided in the contract. Exceptions: contracts $25,000 or less.	100 percent of contract price.	May be a single payment and performance bond that satisfies requirements for each.
IDAHO CODE § 54-1926 Stand. Specs. § 103.04	Performance Bond: Faithful performance of the contract in accordance with its plans, specifications, and conditions. Bonds shall be solely for protection of contracting agency. Payment Bond: Solely for protection of persons supplying labor or materials, or renting, leasing, or otherwise supplying equipment to the contractor or subcontractor in prosecution of the work provided for in the contract.	Not less than 85 percent of contract amount.	Government obligations may be given in lieu of surety bond if they meet statutory criteria in IDAHO CODE § 54-1901.
30 ILL. COMP. STAT. § 550/1 44 Ill. Admin. Code	Performance and Payment Bond: For the completion of the contract, for the payment of material used in such work, and for all labor performed in such work, whether by subcontractor or	Full amount of contract.	Sureties selected by contractor, but subject to right of reasonable approval or disapproval of

STATE & CITATION	SCOPE OF BOND OBLIGATION	AMOUNT OF COVERAGE	SPECIAL REQUIREMENTS
§ 6.290	otherwise.		agency.
IND. CODE §§ 8-23-9-8; 8-23-9-9 Stan. Specs § 101.35	Performance Bond: Faithful performance of the work, in accordance with the profile, plans, and specifications set forth in the proposal; payment by the contractor and by all subcontractors for all labor performed or materials furnished or other services rendered in the construction. Exceptions: Commissioner may waive bond requirements for contracts under $200,000.	Amount not less than contract price.	Commissioner has right to approve surety.
IOWA CODE §§ 573.2–573.5 Stan. Specs. § 1103.05	Contract Bond: Faithful performance of the contract and for fulfillment of other requirements as provided by law. Exceptions: Contracts under $25,000; may be required for contracts under that amount.	Not less than 75 percent of the amount of the contract unless contract provided that no payments are due until completion, in which case only 25 percent of the contract amount must be covered by the bond. Standard specifications require 100 percent of contract price.	Bonding company must be authorized to do business in the state. In lieu of surety bond, the contractor may deposit cash, certified check, or bonds issued by federal, state, or local agencies.
KAN. STAT. §§ 68-410, 68-704 Stan. Specs. § 103.05	Contractor Bond: Faithfully perform such contract in every respect, and pay all indebtedness incurred for supplies, materials, or labor furnished, used or consumed in connection with or in or about the construction of the project for which the contract has been let, including gasoline, lubricating oils, fuel oils, greases, coal, and similar items used or consumed and used directly in carrying out the provisions of the contract. Exceptions: Binding for construction contracts in an amount in excess of $40,000.	Amount not less than contract price.	Surety must be authorized to do business in state and approved by the secretary.
KY. REV. STAT. § 45A.190	Performance Bond: Satisfactory to state.	100 percent of contract price.	

STATE & CITATION	SCOPE OF BOND OBLIGATION	AMOUNT OF COVERAGE	SPECIAL REQUIREMENTS
Stan. Spec. § 103.05	Payment Bond: For the protection of all persons supplying labor and material to the contractor or subcontractors. Exceptions: Contracts under $25,000.		
LA. REV. STAT. §§ 38:2216; 39:2241, 48:255	Performance Bond: For faithful performance of contractor's duties. Payment Bond: For payment to claimants as defined in § 38:2242. Exceptions: No payment bond required for contracts under $25,000. No performance bond if under $50,000. On contracts of $200,000 or less, qualified small businesses required to furnish only half of required bond amount.	Not less than 50 percent of contract amount.	
14 ME. REV. STAT. § 871 Standard Specs § 110.2.1	Performance Bond: Faithful performance of the contract in accordance with the plans, specifications, and conditions thereof. Payment Bond: Solely for the protection of claimants supplying labor or materials to the contractor or the contractor's subcontractor in the prosecution of the work provided for in the contract, including rental equipment. Exceptions: Contracts under $100,000.	100 percent of contract amount.	
MD. CODE STATE FIN. & PROC. §§ 13-216; 17-101 MD. REGS. CODE §§ 21.07.02.10; 21.06.07.10	Performance Bond: Performance of contract. Payment Bond: Payment for labor and materials, including leased equipment, under a contract for construction. Exceptions: Contracts under $100,000.	100 percent of contract amount.	Bond amounts may be reduced if state decides that self-insuring for part of risk is in best interest of state.
MASS. LAWS ch. 149, § 29 Stan. Specs § 3.04	Performance Bond: Performance of the contract. Payment Bond: Payment by contractor or subcontractor for labor performed or furnished and material used or employed in the work, including lumber not yet incorporated into or wholly consumed, specially fabricated material, transportation costs, equipment rental charges, and sums due under collective bargaining agreements regarding labor performed under the contract.	100 percent of contract amount.	
MICH. COMP. LAWS §§ 129.201, 129.202,	Performance Bond: Faithful performance of the contract in	Sufficient security, but not less than 25	

STATE & CITATION	SCOPE OF BOND OBLIGATION	AMOUNT OF COVERAGE	SPECIAL REQUIREMENTS
129.203	accordance with the plans, specifications, and terms thereof. Payment Bond: Claimants, as defined in statute, supplying labor or materials to the principal contractor or subcontractors in the prosecution of the work. Exceptions: Contracts under $50,000.	percent of contract amount.	
MINN. STAT. § 574.26	Performance Bond: For the use and benefit of the public body to complete the contract according to its terms, and conditioned on saving the public body harmless from all costs and charges that may accrue on account of completing the specified work. Payment Bond: for the use and benefit of all persons furnishing labor and materials engaged under, or to perform the contract, conditioned for the payment as they become due, of all just claims for labor and materials.	Not less than 100 percent of contract amount.	
MISS. CODE §31-5-51 Stan. Specs. § 103.05	Performance Bond: Full and faithful performance of the contract. Payment Bond: Prompt payment of all persons supplying labor or material used in the prosecution of the work under the contract. Exceptions: Performance bond not required for lump-sum contracts under $25,000.	Full amount of contract.	Surety must be authorized to do business in state.
MO. REV. STAT. § 107.170.2 Stan. Specs § 103.4.1	Contractor Bond: Payment of any and all materials, incorporated, consumed, or used in connection with the construction of such work, and all insurance premiums, both for compensation, and for all other kinds of insurance, said work, and for all labor performed in such work whether by subcontractor or otherwise. Exceptions: Contracts under $25,000.	Amount equal to contract price.	
MONT. CODE §§ 18-2-201, 18-2-203	Performance security: Faithfully perform all of the provisions of the contract and pay laborers, mechanics, subcontractors, and material suppliers and all persons who supply contractor or subcontractor with provisions, provender, material, or supplies for performing the work.	Full contract price.	In lieu of bond, state may accept cash, cashier's check, certified check, bank money order, certificate of deposit, money market certificate, or bank

STATE & CITATION	SCOPE OF BOND OBLIGATION	AMOUNT OF COVERAGE	SPECIAL REQUIREMENTS
	Exceptions: Contracts under $50,000.		draft issued by federally or state-chartered bank or savings & loan insured by FDIC.
NEB. REV. STAT. § 52-118	Payment Bond: Payment of all laborers and mechanics for labor that is performed and for the payment of material and equipment rental that is actually used or rented in the erecting, furnishing, or repairing of the public structure or improvement or in performing the contract. Exceptions: Contracts $10,000 or less.	Full amount of contract price.	Must be corporate surety.
NEV. REV. STAT. § 408-357 Stan. Specs. § 103.05	Performance Bond: Guarantee faithful performance of the contract in accordance with the plans, specifications, and terms of the contract. Must be maintained for 1 year after the date of completion. Payment Bond: Payment of state and local taxes; industrial insurance and unemployment compensation premiums; claims for labor, materials, provisions, implements, machinery; means of transportation or supplies furnished upon or used for performance of contract.	Full contract price.	Surety must be corporate surety approved by department, and authorized to do business in state.
N.H. REV. STAT. § 447:16 Stan. Specs. § 103.05	Performance Bond: For the faithful performance and completion of the work to be done under the contract. Payment Bond: For all labor performed or furnished; for all equipment hired, including trucks; for all material used; and for fuels, lubricants, power, tools, hardware and supplies purchased and used in carrying out the contract, and for labor and parts furnished upon the order of the contractor for the repair of equipment used. Exceptions: Contracts under $35,000, for which bonds are optional.	100 percent of contract amount.	
N.J. REV. STAT. § 2A:44-143 Stan. Specs §	Payment and Performance Bond: For the payment by the contractor, and by all subcontractors, for all labor performed or materials, provisions, provender or other supplies; teams,	Amount not to exceed 100 percent of contract amount, but may be set by agency depending on	

STATE & CITATION	SCOPE OF BOND OBLIGATION	AMOUNT OF COVERAGE	SPECIAL REQUIREMENTS
103.05	fuels, oils, implements or machinery used or consumed in, upon, for or about the construction, erection, alteration or repair of public buildings or public works. Exceptions: Contracts not exceeding $200,000, requirement may be waived.	risk.	
N.M. STAT. §§ 13-4-18; 13-4-20 Stan. Spec. § 103.6	Performance Bond: Performance of the contract. Payment Bond: For the protection of all persons supplying labor and material to the contractor or its subcontractors for the performance of the work. Exceptions: Agency may waive bonds for contracts $25,000 and under.	100 percent of contract price.	New or additional bond required for insolvency of surety. Agency may elect to reduce bonds to not less than 50 percent of contract price, and self-insure for remaining risk if more advantageous to state.
N.Y. HIGH. LAW § 38 N.Y. STAT. FIN. LAW § 137	Performance Bond: Perform the work in accordance with the terms of the contract and the plans and specifications, and commence and complete the work within the time prescribed, protect against any direct or indirect damage suffered or claimed on account of such construction or improvement during the time thereof. Labor and Material Bond: Contractors and subcontractors shall promptly pay all moneys due for furnishing labor and material to the project.	100 percent of contract price.	Sureties must be approved by highway department. In lieu of bonds, contractor may agree to have 20 percent of the entire contract price retained until entire job is completed and accepted.
N.C. GEN. STAT. § 44A-26	Performance Bond: Faithful performance of the contract, in accordance with plans, specifications, and conditions, solely for the protection of the contracting body. Payment Bond: Solely for the protection of the persons furnishing materials or performing labor for which a contractor or subcontractor is liable. Exceptions: Contracts $50,000 and under.	100 percent of contract amount.	Surety must be authorized to do business in state.
N.D. CENT. CODE §§ 24-02-23; 24-02-17	Contract Bond required on contracts over $20,000.	Total amount of contract.	Surety must be a "responsible surety" approved by state

STATE & CITATION	SCOPE OF BOND OBLIGATION	AMOUNT OF COVERAGE	SPECIAL REQUIREMENTS
Stan. Specs § 103.05			DOT.
OHIO REV. CODE § 5525.16	Performance Bond: Perform the work upon the terms proposed, within the time prescribed, and in accordance with the plans and specifications; will indemnify the state against any damage that may result from any failure of the contractor to so perform. Payment Bond: Payment by the contractor and all subcontractors for labor or work performed of materials furnished in connection with the work, improvement, or project.	100 percent of estimated cost.	Surety must be authorized to do business in state.
OKLA. STAT. tit. 61, §§ 1, 113	Performance Bond: Proper and prompt completion of work in accordance with the contract. Payment Bond: Payment of all indebtedness incurred for subcontractors and all suppliers of labor, material, rental of machinery or equipment, and repair of and parts for equipment as are used or consumed in the performance of the contract. Exceptions: Contracts under $50,000, for which contractor must supply affidavit that subcontractors and suppliers have been paid.	Total amount of contract price.	Contractor must have liability and workers' compensation insurance during construction. In lieu of surety bond, contractor may deposit an irrevocable letter of credit.
OR. REV. STAT. § 279C.380 OR. Admin. R. 731-005-0770	Performance Bond: Faithful performance of the contract and statutory obligations.	100 percent of contract price.	In lieu of bond, may submit cashier's check or certified check.
62 PA. C.S 903 8 P.S. § 193	Performance Bond: Conditioned on faithful performance of contract in accordance with the plans, specifications, and conditions. Payment Bond: Conditioned upon the prompt payment for all materials furnished or labor supplied or performed in the prosecution of the work. Labor or materials include public utility services and reasonable rentals of equipment for the periods when the equipment is actually used at the site.	100 percent of contract price.	Surety must be authorized to do business in the state.

STATE & CITATION	SCOPE OF BOND OBLIGATION	AMOUNT OF COVERAGE	SPECIAL REQUIREMENTS
R.I. GEN. LAWS § 37-12-1	Contract Bond: Conditioned that contractor shall perform the covenants, conditions, and agreements in the contract at the time and manner therein specified, and indemnify the state; and shall promptly pay for all labor performed or furnished and for all materials and equipment furnished in carrying out the contract. Exceptions: May be waived for contracts under $50,000.	Not less than 50 percent nor more than 100 percent of contract price.	Applies to construction managers as well as prime contractors.
S.C. CODE § 57-5-1660	Performance and Indemnity Bond: For the protection of DOT. Payment Bond: For the protection of all persons supplying labor and materials in the prosecution of the work provided for in the contract. Exception: Contracts under $10,000.	100 percent of contract amount. Payment bond not less than 50 percent of contract amount.	Surety must be satisfactory to agency.
S.D. CODIFIED LAWS § 5-21-1, 31-23-1	Performance Bond: Faithful performance of the contract; promptly pay all persons supplying him with labor or material in the prosecution of the work provided for in the contract.	100 percent of contract price.	
TENN. CODE § 54-5-119 Standard Specs § 103.06	Contract Bond: For the full and faithful performance of every part and stipulation of the contract, especially the payment for all materials purchased and for all labor employed in the contemplated work.	100 percent amount of contract. May use letter of credit.	Bond must be approved by department.
TEX. GOV'T CODE § 2253.021 Tex. Trans. Code § 226.006	Performance Bond: Faithful performance of the work in accordance with the plans, specifications, and contract documents. Payment Bond: Solely for the protection and use of payment bond beneficiaries who have a direct contractual relationship with the prime contractor or a subcontractor to supply public work labor and material. Exception: Performance Bonds, contracts under $100,000. Payment Bonds, contracts under $25,000.	Amount of contract.	
UTAH Standard Specs., §1.10	Performance Bond: For faithful performance of contract.	100 percent of contract amount.	Bonds must be satisfactory to the

STATE & CITATION	SCOPE OF BOND OBLIGATION	AMOUNT OF COVERAGE	SPECIAL REQUIREMENTS
	Payment Bond: For the protection of each person supplying labor, service, equipment, or material for the performance of the work provided for in the contract.		state.
VT. STAT. tit 19, ch. 1 §§ 10(8), (9) Vt. Agency of Transportation Policy and Procedures of Prequalification, Bidding and Award of Contracts §§8.04; 8.08	Performance Bond: Guarantees the faithful performance and completion of the work to be done under the contract as well as with all provisions of the contract. Labor and Materials Bond: Conditioned on payment, settlement, liquidation and discharge of the claims of all creditors for material, merchandise, labor, rent, hire of vehicles, power shovels, rollers, concrete mixers, tools and other appliances, professional services, premiums and other services used or employed in carrying out the terms of the contract; for the payment of state and municipal taxes, and contributions to commissioner of employment and training. Exceptions: Contracts under $100,000, performance bond may be waived.	Amount set by agency.	Surety must be authorized to do business in the state. May accept other security in lieu of bond.
VA. CODE § 2.2-4337	Performance Bond: Faithful performance of the contract in strict conformity with the plans, specification, and conditions of the contract. Payment Bond: For protection of claimants who have and fulfill contracts to supply labor or materials to the prime contractor to whom the contract was awarded, or to any subcontractors in the prosecution of the work provided for in the contract, and shall be conditioned upon the prompt payment for all such material furnished or labor supplied or performed in the prosecution of the work.	Equal to the sum of the contract amount.	One or more sureties must be authorized to do business in state.
WASH. REV. CODE § 39.08.010 Stan. Specs. § 1-03.4	Contract Bond: Conditioned on faithful performance of all provisions of the contract, and payment of all laborers, mechanics, subcontractors, materialmen, and all persons who supply contractors and subcontractors with provisions and supplies for carrying out the contract.	Full contract amount.	Surety must be subject to jurisdiction of state.
W. VA. CODE §§ 17-	Contract Bond: Conditioned that	102 percent of	Security bond, but

STATE & CITATION	SCOPE OF BOND OBLIGATION	AMOUNT OF COVERAGE	SPECIAL REQUIREMENTS
4-20 Stan. Specs § 103.5	contractor will perform contract and pay in full to the persons entitled for all material, gas, oil, repairs, supplies, tires, equipment, rental charges for equipment, and charges for use of equipment, and labor used by the contractor.	contract price.	may deposit a cash bond.
WIS. STAT. § 779.14	Performance Bond: Faithful performance of the contract. Payment Bond: Promptly make payment to every person, including every subcontractor or supplier, of all claims that are entitled to payment for labor performed and materials furnished to the contractor for the purpose of making the public improvement or performing the public work. Exceptions: Contracts under $10,000.	Not less than contract price.	Surety must be licensed to do business in state. Bond must be approved by agency.
WYO. STAT. §§ 16-6-112 Stan. Specs. § 103.05	Contract Bond: Payment of all taxes, excises, licenses, assessments, contributions, penalties, and interest lawfully due the state; for use and benefit of any person performing any work or labor or furnishing any materials or goods of any kind that were used in the execution of the contract, conditioned for the performance and completion of the contract according to its terms, compliance with all the requirements of law and payment as due of all just claims for work or labor performed and material furnished. Exceptions: Contracts under $7,500.	Amount set by agency.	Other form of guarantee may be allowed by state for contracts under $150,000.

APPENDIX H

Appendix H

50-STATE SURVEY OF TRANSPORTATION AGENCY DESIGN-BUILD AUTHORITY AS OF JULY 1, 2013*

	State[1]	Transportation Agencies with Authority	Citation[2]	DOT Procurement Process
1.	AL	Authorization for the Alabama Toll Road, Bridge and Tunnel Authority to use design-build.	ALA. CODE §§ 23-2-144, 145	Proposals to be evaluated based on qualifications of participants or best value or both taking interest of the state into consideration. (ALA. CODE § 23-2-145)
2.	AK	Authorization for all agencies to use design-build for projects using state funds.	ALASKA STAT. § 36.30.200	Competitive sealed proposals if appropriate findings are made; otherwise, competitive sealed bids. (ALASKA STAT. § 36.30.200)
3.	AR	Authorization for DOT to use design-build (through July 16, 2023) on two projects that require state highway revenues; each project must cost more than $50 million. The State Highway Commission has the authority to enter into design-build contracts.	ARK. CODE § 27-67-206 ARK. CODE § 27-65-107(c)	To be established by the Commission; contract awarded "on a qualification basis that offers the greatest value for the state". (ARK. CODE § 27-67-206(j)(2)(A), (C))
4.	AZ	Authorization for DOT to use design-build (through December 31, 2025) if it makes a determination in writing that it is appropriate and in the department's best interests.	ARIZ. REV. STAT. §§ 28-7361, 28-7363, 28-7364, 28-7365	Two-phase solicitation procedure to be established by DOT. Phase One: the department shall prepare documents for RFQ; the selection team shall evaluate the design-build qualifications of responding firms and shall compile a short list of firms in accordance with technical and qualifications-based criteria. Phase Two: the department shall issue a RFP to the design-builders on the short list. Award is to lowest score when price is divided by technical score; time valued adjustments may be made to score. (ARIZ. REV. STAT. § 28-7365)

1 This survey includes states with existing transportation agency design-build authority. It does not include states with sunsetted statutes authorizing design-build.

2 This survey identifies legislation specifically permitting agencies to enter into design-build contracts and exclusive development agreements, and also identifies legislation permitting agencies to use a best value procurement process for construction contracts (thus allowing design-build procurements to proceed without concern about differences between procurement requirements applicable to design and construction contracts). This survey does not necessarily address authorizing legislation for franchise agreements or similar public-private partnerships.

	State[1]	Transportation Agencies with Authority[2]	Citation[3]	DOT Procurement Process
5.	CA	Authorization for the California Transportation Commission to authorize 15 design-build projects (10 for Caltrans and 5 for local transportation agencies). The Riverside County Transportation Commission, if authorized by the commission, may utilize design-build procurement for the State Route 91 Corridor Improvements Project on the state highway system. Authorization for transit agencies to use design-build until January 1, 2015, unless extended.	CAL. PUB. CONT. CODE §§ 6800 to 6809, 6811-6813; CAL. STS. & HIGH. CODE § 143 CAL. PUB. CONT. CODE § 6802 (c)(1) CAL. PUB. CONT. CODE §§ 20209.5 – 20209.14	Three-Step Procurement Process: RFP (including competitive sealed proposals), prequalification requirements, selection. (CAL. PUB. CONT. CODE § 6805) For non-rail transit projects that exceed $2.5 million, the transit operator may award the project to the lowest bidder or by using best value method; in no case may the transit operator award a contract to a design-build entity pursuant to the authority granted under the Public Contract Code for a capital maintenance or capacity-enhancing rail project unless that project exceeds $25 million in cost; no cost threshold for acquisition and installation of technology applications or surveillance equipment. (CAL. PUB. CONT. CODE § 20209.7)
6.	CO	Authorization for DOT to use design-build. Specific authorization for new High Performance Transportation Enterprise to use design-build for surface transportation projects, such as reversible highways.	COLO. REV. STAT. §§ 43-1-1401 *et seq.* COLO. REV. STAT. § 43-4-806	Two-Phase "Adjusted Score" Process; shortlist followed by proposals; preference allowed to Colorado residents (suspended if it would cause denial of federal funds); contract awarded to proposal providing best value to department. (COLO. REV. STAT. § 43-1-1401)
7.	CT	Authorization for the Commissioner of Transportation to designate specific projects to be completed using a (1) construction-manager-at-risk contract with a guaranteed maximum price, or (2) design-build contract.	CONN. GEN. STAT. § 13a-95b	Selection process based on competitive proposals and contract awarded based on predetermined metrics provided in advance to proposers. This metric may be unique to each project, but shall consist of a combined score of qualifications and past performance of the proposer, technical merit of the proposal and cost. (CONN. GEN. STAT. § 13a-95b(c))
8.	DC	Authorization for Chief Procurement Officer to use various project delivery methods for construction projects including design-build.	D.C. CODE § 2-356.01 *et seq.*	Competitive sealed bidding shall be used to procure construction in design-build procurements or by competitive sealed proposal (i.e. submission of written technical and price proposals and evaluation of in accordance with evaluation criteria) when competitive sealed bidding is not practicable or advantageous to District. (D.C. CODE § 2-354.03)
9.	DE	Authorization for the Secretary of Transportation to solicit proposals from and enter into agreements with private entities, or consortia involving, inter alia, design, construction, leasing, financing, operation, and maintenance of transportation systems, which proposals may provide for the design-build mode of infrastructure development.	2 DEL. C. § 2003	Each proposal to be weighed on its own merits and ranked according to selection criteria stipulated in the request for proposals. (2 DEL. C. § 2003 (e)(1))

	State[1]	Transportation Agencies with Authority[2]	Citation[3]	DOT Procurement Process
10.	FL	Authorization for DOT to use design-build for buildings, major bridges, limited access facilities, and rail corridor projects. DOT also authorized to use design-build for projects that are a part of the "innovative" practices package; before using design-build for these projects, DOT must document in writing the need for design-build and identify what benefits the traveling public and the affected community are anticipated to receive; the annual contracting monetary cap for these "innovative" projects is $120 million.	FLA. STAT. ANN. § 337.11(7) FLA. STAT. ANN. § 337.025	Governed by rules adopted by DOT (which must include prequalification requirements, public announcement procedures, scope of service requirements, letters of interest requirements, short-listing criteria and procedures, bid proposal requirements, technical review committee, selection and award processes, and stipend requirements). (FLA. STAT. ANN. § 337.11(7)(b))
11.	GA	Authorization for DOT to use design-build for buildings, bridges and approaches, rail corridor, limited or controlled access projects, projects within existing right of way with a clear scope of work or when it can obtain significant savings in project delivery time.	GA. CODE ANN. § 32-2-81	Governed by rules adopted by DOT (which must include shortlisting and price proposal phases); DOT to select the lowest qualified bidder; in contracting for design-build projects, DOT limited to no more than 50% of total amount of construction projects awarded the previous fiscal year. (GA. CODE ANN. § 32-2-81(d))
12.	HI	Authorization for all governmental bodies to solicit construction projects through a RFP to use the design-build method.	HAW. REV. STAT. § 103D-303(i)	Proposals shall be solicited through an RFP to select a short list of no more than three offerors; proposal evaluation criteria, terms of payment of conceptual design fee etc to be stated n the RFP. (HAW. REV. STAT. § 103D-303(i))
13.	ID	Authorization for Idaho Transportation Department to use design-build firms for appropriately sized design build projects. No more than 20% of annual highway construction budget can be used for design-build and construction manager/general contractor contracts combined.	IDAHO CODE § 40-904	Two step selection process for all projects using RFQ and RFP. DB selection may be best value, fixed price-best design or, in limited circumstances, lowest price-technically acceptable. (IDAHO CODE §§ 40-904(11))
14.	IL	Authorization for DOT to use design-build. Authorization for state agencies to use design-build. Authorization for Regional Transportation Authorities to use design-build. Authorization for Capital Development Board to use design-build. Authorization for Public Building Commission to use design-build for public buildings and any roads incident to the buildings.	630 ILL. COMP. STAT. § 5/20 30 ILL. COMP. STAT. § 535/75 70 ILL. COMP. STAT. §§ 3615/1.01 *et seq.* 30 ILL. COMP. STAT. §§ 537/5 *et seq.* 50 ILL. COMP. STAT. §§ 20/2.5 *et seq.*	The DOT has determined that the referenced statutes do not provide sufficient authority to undertake a procurement for a design-build project. (630 ILL. COMP. STAT. § 5/20) Procurements for Public Building Commission and Capital Development Board must use a 2-phase evaluation: shortlist based on qualifications then proposals and award based on technical criteria and cost. (30 ILL. COMP. STAT. 537/30; 50 ILL. COMP. STAT. 20/20.5)

	State[1]	Transportation Agencies with Authority[2]	Citation[3]	DOT Procurement Process
15.	IN	Authorization for DOT to use low bid design-build for road construction, improvement or maintenance contracts. Authorization for pubic agencies to use design-build for designing, constructing, reconstructing, altering, or renovating airport facilities, but not highways.	IND. CODE §§ 8-23-9-3 to 4.5 IND. CODE § 5-30-1-1 *et seq.*	The DOT may let contracts to the lowest and best bidder, and the best bid may not be for a greater sum than the estimated cost of the project. (IND. CODE § 8-23-9-3)
16.	KS	Authorization for one highway demonstration project in Johnson or Wyandotte county for the purpose of evaluating the design-build concept.	KAN. STAT. § 68-2314b(b)	Multi-phase evaluation process premised on Kan. Stat. Ann. §75-5001 *et seq.* including the evaluation of statement of qualifications and selection of at least three of the most qualified firms; selection of a single firm and the negotiation of a contract with such firm. (KAN. STAT. § 68-2314b(b)(4))
17.	KY	Authorization for all state agencies to use design-build,. To use this authority, state agencies must receive approval from the Secretary of the Finance and Administration Cabinet. The Secretary must compare the design-bid-build and design-build delivery methods and find that design-build offers the best value to taxpayers.	KY. REV. STAT. § 45A.045; KY. REV. STAT. §§ 45A.180 *et seq*; KY. REV. STAT. § 45A.494	Multi-phase selection process based on qualifications, experience, technical requirements, guaranteed maximum price and other criteria set forth in the request for proposals. (KY. REV. STAT. § 45A.182(1)(a)) Prior to award, a resident bidder shall be given a preference against a nonresident bidder registered in a state that gives preference to bidders from that state. (KY. REV. STAT. § 45A.494)
18.	LA	Department of Transportation and Development may formulate, develop, and implement design-build for transportation facility or facilities, including but not limited to highways, interchanges, or bridges into a single contract. Secretary must determine that use of design-build is in the best interest of taxpayers, and the House and Senate transportation, highways, and public works committees approve its use. Design-build authorized for construction of the new Mississippi River Bridge at St. Francisville (connection to U.S. Hwy. 61) including approach structures and connecting roadways.	LA. REV. STAT §§ 48:250.2 *et seq*; LA. REV. STAT § 48:442.1 LA. REV. STAT § 48:250.2(B)	Two-phase selection process; DOT will identify the specific requirements for the second phase depending on the complexity of the project; the selection method uses an adjusted score determined by three components: (1) technical score; (2) time value; and (3) the price proposal; DOT must submit any project selected for design-build to the House and Senate Transportation, Highways and Public Works Committees for approval. (LA. REV. STAT § 48:250.3)
19.	MA	Authorization for Department of Highways to use design-build for projects approved by the inspector general.	MASS. GEN. LAWS. ANN. ch. 149A, §§ 14 *et seq.*	Two-phase selection process: RFP shall identify the cost basis, low-bid or best value, by which the awarding authority will evaluate proposals submitted in response to said RFP. For projects to be awarded on a best-value basis, the scoring process, quality criteria and relative weight thereof must be contained in the RFP.
20.	MD	Authorization for governmental bodies to use design-build on capital projects.	MD. CODE ANN., STATE FIN. & PROC. § 3-602(g)(1); COMAR 21.05.03.03	Competitive sealed proposal process allows best value selection; award must be advantageous to the state considering price and other evaluation factors set forth in the request for proposals. (COMAR 21.05.03.03)

	State[1]	Transportation Agencies with Authority[2]	Citation[3]	DOT Procurement Process
21.	ME	Authorization for DOT to use design-build contracting to deliver projects on either a best-value or low-bid basis.	ME. REV. STAT. ANN. TIT. 23, § 4244	Low-bid award or best-value award; If the scope of work requires substantial engineering judgment, the quality of which may vary significantly, then the basis of award must be the best value. If best value is used, award should be submitted to the department in two components – technical and sealed price proposal. Proposer must be prequalified to be eligible to submit a proposal. (ME. REV. STAT. TIT. 23 § 4244 (3) – (7))
22.	MI	Authorization for state transportation department to use alternative procurement process for highway, street, road and bridge projects that exceed $100,000.	MICH. COMP. LAWS § 247.661c	Award by means other than competitive bidding is allowed if Department affirmatively finds that it is in the public interest; Department must report these findings to the State Transportation Commission and Appropriations Committees. Statutes do not include many details and give agencies discretion in choosing procurement processes.
23.	MN	Authorization for streets, highways, bicycle paths, bicycle trails and pedestrian facilities, trunk highways, and DOT projects. The number of design-build contracts awarded by DOT in any fiscal year may not exceed ten percent of the total number of transportation construction contracts awarded by the commissioner in the previous fiscal year. Hennepin County Board of Commissioners authorized to use design-build for a county road, bridge, or other infrastructure relating to a county roadway. Either the Metropolitan Council or the state of Minnesota may use a design-build method of project development and construction for light rail transit.	MINN. STAT. §§ 13.72 subd.11-12; 160.262 subd. 4-5; 161.32 subd. 1b; 161.3410, -12, -14, -16, -18, -20; 161.3422 -161.3428; 473.3993 MINN. STAT. §§ 383B.158, 1581–85 MINN. STAT. § 473.3993	Trunk highway construction design-build contracts must be awarded to the lowest responsible bidder, taking into consideration conformity with the specifications, the purpose for which the contract or purchase is intended, the status and capability of the vendor, and other considerations imposed in the call for bids. (MINN. STAT. § 161.32 subd. 1b) DOT authorized to procure design-build contracts using either a two-step best value selection process or a low bid process. (MINN. STAT. § 161.3420) Light rail contracts may be awarded on the basis of the RFQ or RFP without bids. (MINN. STAT. § 161.3426) Commissioner shall submit a list of executed design-build contracts to the Governor each year. (MINN. STAT. § 161.3428)
24.	MO	Authorization for the State Highways and Transportation Commission to enter into highway design-build contracts through July 1, 2018; the number of design-build contracts entered into each fiscal year shall not exceed 2% of the total number of highway system projects listed in the approved Statewide Transportation Improvement Project for that fiscal year.	MO. REV. STAT. § 227.107; 7 CSR §§ 10-24 *et seq.*	The Commission is required to use a two-phase procurement process. The first phase results in the Commission shortlisting firms and the second phase includes the evaluation of proposals based on price, technical solutions and other factors. Oral presentations are allowed. A minimum of two and a maximum of five proposers to be shortlisted. (7 CSR §§ 10-24.030, 100, 110 & 200)
25.	MS	Authorization for DOT and the Mississippi Development Authority to jointly use design-build for two projects per fiscal year costing no more than $10 million, and one project per fiscal year costing more than $50 million.	MISS. CODE ANN. § 65-1-85	DOT shall establish detailed criteria for the selection of the design-build contractor; for each project, DOT must file a report with the Legislature evaluating the design-build method of contracting by comparing it to the to the low-bid method. (MISS. CODE § 65-1-85 (11)(c) – (d))

	State[1]	Transportation Agencies with Authority[2]	Citation[3]	DOT Procurement Process
26.	MT	Authorization for DOT to use design-build for projects that department has determined are part of the design-build contracting program.	MT. CODE ANN. §§ 60-2-111, -112, -137	Two-phase proposal process; first phase involves evaluation of qualifications and second phase involves evaluation of technical and price proposals. (MT. CODE ANN. §§ 60-2-111(2) – (3))
27.	NC	Authorization for DOT to award contracts each fiscal year for construction of transportation projects on a design-build basis. For projects with a construction cost in excess of $50 million, DOT shall present to the Joint Legislative Transportation Oversight Committee the reasons the development of the project on a design-build basis will best serve the public interest. Authorization for Turnpike Authority to use alternative procurement process. Specific authorization for DOT to use design-build on Accelerated Pilot Toll Bridge Project and the Herbert C. Bonner Bridge Replacement Project.	N.C. GEN. STAT. § 136-28.11 N.C. GEN. STAT. § 136-89.180 *et seq.* N.C. GEN. STAT. § 136-89.183A–B	Design-build contracts may be awarded after a determination by the DOT that delivery of the projects must be expedited and that it is not in the public interest to comply with normal design and construction contracting procedures. (N.C. GEN. STAT. § 136-28.11(d))
28.	ND	Authorization for DOT to authorize one signal light project and one box culvert structure project before Dec. 31, 2013.	N.D. CENT. CODE § 24-02-47	DOT, in conjunction with the appropriate and affected professionals and contractors, shall adopt policies for procuring the projects. (N.D. CENT. CODE § 24-02-47(5))
29.	NH	Authorization for DOT to use design-build for statewide transportation improvement program projects not exceeding $25 million. Design-build is permitted for projects in excess of $25 million if the department demonstrates that it benefits the state more than conventional methods.	N.H. REV. STAT. ANN. § 228:4(I)(c) – (d)	Selection to be based on objective standard and measurable criteria for evaluation of proposals. (N.H. REV. STAT. ANN. § 228:4(I)(c))
30.	NJ	Authorization for New Jersey Transit Corporation to use design-build.	N.J. STAT. § 27:25-11	Design-build projects shall be bid and contracts awarded in accordance with applicable regulations promulgated by the New Jersey Transit Corporation. (N.J. STAT. § 27:25-11(c)(2))
31.	NM	Authorization for DOT to use design-build project delivery for projects with a maximum allowable cost of more than $50 million if funded in whole or in part by grants from the American Reinvestment and Recovery Act of 2009.	N.M. STAT. ANN. § 13-1-119.2	Two-phase RFP process using best value; stipend to unsuccessful bidders. (N.M. STAT. ANN. § 13-1-119.2(C))

	State[1]	Transportation Agencies with Authority[2]	Citation[3]	DOT Procurement Process
32.	NV	Authorization for any public agency to contract with a design-build team for the construction of a public work project (including a road, highway, street or alley) whose cost exceeds $5 million. Authorization for DOT to contract with design-build team to construct a project if DOT determines that (i) cost is in excess of $10 million (ii) construction can be accomplished for a significantly lower cost than using a different method and (iii) method will result in shorter construction time. DOT may use design-build twice a year for projects costing between $5 million and $10 million if Department satisfies the three factors listed above. Authorization for regional transportation commission to use a turnkey procurement process (which includes having one entity both design and build) for a fixed guideway project after first evaluating whether such a procurement is the most cost-effective method of constructing the project on schedule and in satisfaction of its transportation objectives.	NEV. REV. STAT. §§ 338.1711, -15, -17, -19, -21, -23, -24, -25, -27 NEV. REV. STAT. §§ 408.3875 – 408.3887 NEV. REV. STAT. § 277A.280	Request for preliminary proposals followed by issuance of request for final proposals to "finalists"; award based on most cost effective and responsive proposal using criteria and weight assigned to each factor; preference for local contractors if not federally funded. (NEV. REV. STAT. § 408.3882)
33.	NY	Authorization for New York State Thruway Authority, Department of Transportation, Office of Parks, Recreation and Historic Preservation, Department of Environmental Conservation and the New York State Bridge Authority to use the design-build delivery method for capital projects costing at least $1.2 million.	2011 SESS. LAWS OF N.Y. Ch. 56, Part E, Section 4 – 5 (S.50002)	Two-step best value evaluation method that optimizes quality, cost and efficiency, price and other performance criteria. (2011 SESS. LAWS OF N.Y. Ch. 56, Part E, Section 5)
34.	OH	Authorization for DOT to establish a program to expedite the sale and construction of special projects that combines the design and construction elements of a bridge or highway into a single project; the total value of the contracts shall not exceed $1 billion per fiscal year. A county engineer may combine the design and construction elements of a bridge, highway, or safety project into a single contract but only if the cost of the project as bid does not exceed $1.5 million dollars.	OHIO REV. CODE ANN. § 5517.011 OHIO REV. CODE ANN. § 5543.22.	A value-based selection process may be used combining technical qualifications and competitive bidding elements, including consideration for minority or disadvantaged businesses that may include joint ventures. (OHIO REV. CODE ANN. §§ 5517.011)

	State[1]	Transportation Agencies with Authority[2]	Citation[3]	DOT Procurement Process
35.	OK	Authorization to use design-build with approval of the Director of the Office of Management and Enterprise Services for projects constructed for a state agency. These projects include highways, bridges, airports, railroads and tunnels that are related or appurtenant to a structure.	OKLA. STAT. TIT. 61, § 202.1	
36.	OR	Authorization for DOT to enter into design-build contracts with private entities for the construction of tollway projects	OR. REV. STAT. §§ 383.005 – 383.017	Award of toll contracts either by competitive process or by "private negotiation with one or more entities" or by a combination of competition and negotiation. (OR. REV. STAT. § 383.017)
37.	PA	Authorization for DOT to use design-build for projects to be financed with bond proceeds and all other DOT construction projects.	74 PA. CONS. STAT. § 9109; 75 PA. CONS. STAT. § 9511.5	The responsible offeror whose proposal is determined in writing to be the best value for and in the best interests of the public entity, taking into consideration all evaluation factors, shall be selected for contract negotiation. (74 PA. CONS. STAT. § 9109)
38.	RI	The state of Rhode Island and any of its departments or agencies and public agencies is authorized to use any type of contract which will promote the best interests of the state.	R.I. GEN. LAWS § 37-2-31	
39.	SC	Authorization for DOT to award highway construction projects using design-build procedure. Authorization for state to use design-build for procurements relating to public roads and streets, highways, public parking facilities, public transportation systems, terminals, rolling stock, rail, air, and water port structures.	S.C. CODE ANN. § 57-5-1625 S.C. CODE ANN. § 11-35-3005	Selection criteria shall include project cost and may include contractor qualifications, time of completion, innovation, design and construction quality or other related criteria. (S.C. CODE ANN. § 57-5-1625(B))
40.	SD	Authorization for all public agencies (including DOT) to award construction projects using design-build procedure.	S.D. CODIFIED LAWS § 5-18b-20	The particular agency must establish the procurement procedures prior to issuing any design-build requests for proposals. According to the Bureau of Administration Procedures for Design-Build Procurement, selection criteria include experience, financial and bonding capacity, managerial resources, past performance, capacity to meet time and budget requirements, workload, ability to complete work in timely manner and submitted pre-qualification form.
41.	TN	Authorization for DOT to use design-build for up to 15 projects in a fiscal year if the contract is less than $1 million and not more than five projects if the contract is in excess of $1 million; certain limitations apply to contracts estimated to be in excess of $70 million.	TENN. CODE ANN. § 54-1-119	Selection criteria shall include cost, qualifications, time of completion, innovation, design and construction quality, design innovation, or other technical or quality related criteria, as determined by the Department; Department must file report with the Legislature on the effectiveness of design-build once three projects have been completed with a total contract cost in excess of $1 million. (TENN. CODE ANN. § 54-1-119(b), (e))

	State[1]	Transportation Agencies with Authority[2]	Citation[3]	DOT Procurement Process
42.	TX	Authorization for DOT to use design-build for highway projects with a construction cost of $50 million or more but limited to three contracts in any fiscal year (Expires August 1, 2015); comprehensive development agreement authorization for TxDOT, Texas Turnpike Authority (a division of TxDOT) and regional mobility authorities.	TEX. TRANSP. CODE ANN. §§ 223.001 *et seq.* (Subchapter A); §§ 223.201 *et seq.* (Subchapter E); §§ 223.241 *et seq.* (Subchapter F); §§ 370.001 *et seq.*	May solicit proposals or accept unsolicited proposals; if an unsolicited proposal is received, DOT must request competing proposals and qualifications; selection is based on "best value". Subchapter F procurement is a two-step evaluation process including shortlisting of at least two firms and evaluation of technical an d cost proposals with 70% weighted to cost.
43.	UT	Authorization for transportation agencies, including the DOT, to award a design-build transportation project contract for any transportation project that has an estimated cost of at least $50,000,000.	UTAH CODE ANN §§ 63G-6a-1402, 1403; UTAH ADMIN. CODE (U.A.C.) R916-3 *et seq.*	Two phase process: pre-qualification then proposals; after considering price and other identified factors, award is to the proposal that is most advantageous to the state. (UTAH CODE ANN. §§ 63G-6a-1402(4)-(9)) Utah Administrative Code contains additional procurement requirements (i.e. RFQ must identify maximum number that could be shortlisted). (UTAH ADMIN. CODE (U.A.C.) R916-3 *et seq.*)
44.	VA	Authorization for the Commonwealth Transportation Board to award contracts on a design-build basis. General design-build authorization for state agencies. Counties, cities, and towns may award contracts for the construction of transportation projects on a design-build basis.	VA. CODE ANN. § 33.1-12(2)(b) VA. CODE ANN. §§ 2.2-4303, -4306, -4308 VA. CODE ANN. § 33.1-223.2:16	Award to be based on competitive sealed bidding or a two-step competitive negotiation process; award determined by objective criteria adopted by Commonwealth Transportation Board; objective criteria to include requirements for pre-qualification and competitive bidding; additional proposal requirements for contracts in excess of $100 million. (VA. CODE ANN. §§ 33.1-12(2)(b))
45.	VT	Authorization for Agency of Transportation to use design-build contracting to deliver projects.	19 VT. ST. ANN. §2601 *et seq.*	May evaluate proposals on either a best-value or a low-bid basis. For best-value awards, Proposer must submit sealed technical and price proposal. After evaluation and scoring of technical proposal, price proposal will be opened and separately evaluated and scored to determine the proposal that represents the best value to the agency.
46.	WA	Authorization for DOT for projects over $10 million and for five pilot projects costing between $2 and $10 million dollars. Authorization for Regional Transportation Investment District (a corporation created by county legislative authority to implement a regional transportation investment plan) to use the design-build procedure for transportation projects developed by it.	WASH. REV. CODE §§ 47.20.780, 47.20.785 WASH. REV. CODE § 36.120.110	Requires DOT to develop a process for awarding design-build contracts for projects over $10 million; this process must, at a minimum, include the scope of services, contractor prequalification requirements, criteria for evaluating technical information and project costs, contractor selection criteria and issue resolution procedures. (WASH. REV. CODE §§ 47.20.780) If DOT uses design-build for the Olympic region project, it must follow the design-build process for public works projects under chapter 39.10 RCW.

	State[1]	Transportation Agencies with Authority[2]	Citation[3]	DOT Procurement Process
47.	WI	Authorization for DOT to use design-build for specific bridge projects.	WIS. STAT. ANN. §§ 84.11(5n) *et seq.*	The design-build contract is awarded through a competitive selection process that utilizes, at a minimum, contractor qualifications, quality, completion time and cost as award criteria. In order to be eligible to participate in the selection process, the contractor must be prequalified by the department as a design consultant and as a contractor. (WIS. STAT. ANN. §§ 84.11(5n)(b)(1))
48.	WV	All state departments, agencies, authorities, quasi-public corporations and all political subdivisions, including cities, counties, boards of education and public service districts are authorized to use design-build. Authorization for the Division of Highways to use design-build on no more than thirteen projects by June 30, 2013; may spend up to $75 million per year. If any of the $75M is unused, it may be applied to the next year, for an aggregate maximum amount of $150 million.	W. VA. CODE §§ 5-22A-1 *et seq.* W. VA. CODE §§ 17-2D-1 *et seq.*	Award shall be based on low-bid or value-based selection process combining technical qualifications and competitive bidding elements.
49.	WY	Design-build broadly permitted for all agencies.	WYO. STAT. ANN. §§ 15-1-113, 16-6-701, -707, -708	RFQ process then shortlist selected to respond to fixed scope RFP or fixed price RFP depending on size of project; contract awarded based on best overall value.

APPENDIX I

OVERVIEW OF STATES WITH SIGNIFICANT TRANSPORTATION PUBLIC PRIVATE PARTNERSHIP ("PPP") AUTHORITY (As of June 2011)

State	Statute	Comments
1. AK	ALASKA http://wwwcf.fhwa.dot.gov/exit.cfm?link=http://www.knikarmbridge.com/documents/HB0471Z_000.pdf STAT. § 19.75 http://www.knikarmbridge.com/documents/AmendedAS19.75BYSCSCSHB471.pdf	Authorizes the Knik Arm Bridge and Toll Authority (KABATA) to utilize a PPP to finance, design, construct, operate and maintain the Knik Arm bridge to connect the Municipality of Anchorage and the Matanuska-Susitna Borough. KABATA has authority to set and collect tolls.
2. AL	ALA. CODE §§ 23-1-80 to 23-1-95 http://www.legislature.state.al.us/CodeofAlabama/1975/132328.htm. ALA. CODE § 23-2-144 http://law.onecle.com/alabama/highways-roads-bridges-and-ferries/23-2-144.html	§§ 23-1-80: Authorizes the Alabama Department of Transportation and county commissions to establish toll roads, toll bridges, ferries or causeways or allow for their operation by private parties. No express provision regarding unsolicited proposals. § 23-2-144: Authorizes the Alabama Toll Road, Bridge and Tunnel Authority to enter into agreements for design-build, DBOM, DFBOM, leases, licenses, franchises, concessions and other PPP forms for toll road, bridge or tunnel projects.
3. AZ	ARIZ. REV. STAT. § 28-7701 et seq. http://www.azleg.state.az.us/FormatDocument.asp?inDoc=/ars/28/07701.htm&Title=28&DocType=ARS	Authorizes the Arizona Department of Transportation to provide for the development and operation of eligible facilities using a broad range of PPP models, including pre-development agreements, design-build, DBOM, DBFOM and long-term concessions. Sets forth flexible procurement and selection guidelines, and authorizes unsolicited proposals from private entities.

State	Statute	Comments
		Authorizes flexible tolling arrangements and imposes no toll limitations (e.g., no limit on type of vehicle or hour restrictions); allows the Department to accept less than 100 percent performance bonds; exempts PPPs from state, local and property taxes; requires all projects be subject to Arizona's Five Year Transportation Facilities Construction Program; limits initial concessions terms to 50 years, which may be extended; authorizes eminent domain in favor of a PPP project.
4. CA	CAL. PUB. CONT. CODE §§ 6800 to 6813 http://www.leginfo.ca.gov/cgi-bin/displaycode?section=pcc&group=06001-07000&file=6800-6813 CAL. STS. & HIGH. CODE § 143 http://www.leginfo.ca.gov/cgi-bin/displaycode?section=shc&group=00001-01000&file=90-155.6. CAL. GOV. CODE §§ 5956 to 5956.10 http://www.leginfo.ca.gov/cgi-bin/displaycode?section=gov&group=05001-06000&file=5956-5956.10. CAL. PUB. UTIL. CODE § 130242 http://www.leginfo.ca.gov/cgi-bin/displaycode?section=puc&group=130001-131000&file=130220-130245 CAL. PUB. CONT. CODE §§ 20360 to 20369 http://www.leginfo.ca.gov/cgi-bin/displaycode?section=pcc&group=20001-21000&file=20360-20369 CAL. PUB. UTIL. CODE § 40075 http://www.leginfo.ca.gov/cgi-bin/displaycode?section=puc&group=400	PCC 6800: Expands existing Design-Build Demonstration Program. Authorizes state and local transportation entities, if authorized by the California Transportation Commission, to use design-build on up to five local and ten state projects. S&H 143: Authorizes regional transportation agencies, and the California Department of Transportation (Caltrans) in collaboration with regional transportation agencies, to enter lease agreements with public or private entities for transportation projects; solicited and unsolicited proposals authorized. GC 5956: Authorizes a government agency to solicit proposals from and enter into agreements with private parties for the design, construction, reconstruction or lease of fee-producing infrastructure, including commuter and light rail systems, highways, bridges and tunnels. Precludes use of state funding. Limits lease terms to 35 years. PUC 130242: Authorizes the Los Angeles Metropolitan Transportation Authority to procure a combination of professional services, such as design, construction, operations and maintenance, under one contract. Requires low-bid selection. PCC 20360: Authorizes the Los Angeles County Transportation Commission to enter into contracts with private entities for various services, including planning, design and construction of rail transit projects. Projects may not be funded from local tax revenues or statements, although such funds may be used for credit enhancement; must include system linking LAX and Palmdale airports. PUC 40075: Authorizes the Orange County Transportation Authority (OCTA) to contract with

State	Statute	Comments
	01-41000&file=40070-40081 CAL. PUB UTIL. CODE § 40183 http://www.leginfo.ca.gov/cgi-bin/displaycode?section=puc&group=40001-41000&file=40180-40187	any private corporation to operate or make improvements to transit services, facilities, equipment or operations. PUC 40183: Authorizes OCTA to lease or contract use of its transit facilities to any operator, including any private corporation.
5. CO	COLO. REV. STAT. § 32-9-128.5 COLO. REV. STAT. §§ 43-1-1201 to 43-1-1209 COLO. REV. STAT. § 43-3-202 to 202.5 COLO. REV. STAT. § 43-4-806 http://www.michie.com/colorado/lpext.dll?f=templates&fn=main-h.htm&cp	§ 32-9-128.5: Authorizes the Regional Transportation District to issue Private Activity Bonds (PABs) and loan proceeds from such PABs to private businesses so that private businesses can finance mass transit projects. §§ 43-1-1201 to 43-1-1209: Authorizes the Colorado Department of Transportation to use PPPs to design, finance, construct, operate, maintain or improve a broad range of projects including toll roads, turnpikes and high-occupancy toll lanes. Authorizes solicited and unsolicited proposals. § 43-3-202.5: Authorizes the Colorado Department of Transportation to use PPPs to design, finance, construct, operate, maintain, reconstruct or improve a turnpike project, including new and existing highways, tunnels, toll tunnels, bridges and toll houses. § 43-4-806: Creates a High-Performance Transportation Enterprise, within the Colorado Department of Transportation, to seek out a broad range of PPP opportunities, including design-build and concession agreements, to complete surface transportation projects.
6. DE	DEL. CODE ANN. tit. 2, §§ 2001 to 2012 http://delcode.delaware.gov/title2/c020/index.shtml	Authorizes the Delaware Department of Transportation to receive solicited and unsolicited proposals for PPP projects, including highway, bridge, maritime port, rail and other transit systems.

State	Statute	Comments
7. FL	FLA. STAT. § 334.30 http://www.flsenate.gov/Laws/Statutes/2010/334.30 FLA. STAT. §§ 338.22 to 338.251 http://www.leg.state.fl.us/STATUTES/index.cfm?App_mode=Display_Statute&URL=Ch0338/titl0338.htm&StatuteYear=2009&Title=-_2009-_Chapter 338	§ 334.30: Authorizes the Florida Department of Transportation to receive or solicit PPP proposals to build, operate, own or finance transportation facilities. The Department may use PPPs for both new toll facilities and long-term leases of existing facilities; the Florida Legislature must approve leases of existing toll facilities. Limits PPP agreements to 50-year terms. Authorizes 75-year terms if authorized by the Secretary of Transportation; authorizes longer terms if approved by the Florida Legislature. Authorizes the Department to use eminent domain for PPP projects. §§ 338.22 to 338.251: Authorizes the Florida Turnpike Enterprise to contract with private entities to develop, construct, improve, maintain, operate and manage the Florida Turnpike System (which includes limited access toll highways and associated feeder roads).
8. GA	GA. CODE. ANN. §§ 32-2-78 to 32-2-81 http://www.lexis-nexis.com/hottopics/gacode/default.asp	Authorizes Georgia DOT to solicit proposals for PPPs for projects identified by Georgia DOT and reported to the State Transportation Board that (1) (a) are on the state-wide transportation improvement program or (b) otherwise identified, that afford the greatest gains in congestion mitigation or promotion of economic development, and (2) have not been initiated within two years of the report and lack funding. § 32-2-81 provides design-build authority.
9. IN	IND. CODE § 8-15.5 http://www.in.gov/legislative/ic/code/title8/ar15.5/ IND. CODE § 8-15.7 http://www.in.gov/legislative/ic/code/title8/ar15.7/ IND. CODE §§ 8-23-7-22 to 8-23-7-25 http://www.in.gov/legislative/ic/code/title8/ar23/ch7.html	§ 8-15.5: Authorizes the Indiana Financing Authority to enter into toll road PPPs with private entities. Under a PPP, a private entity may be responsible for a broad range of project delivery services, including planning, design, finance, construction, operation, maintenance and improvement. § 8-15.7: Authorizes the Indiana DOT to use PPPs to develop, finance or operate a transportation facility. Authorizes private entities to impose user fees. Authorizes the Indiana DOT to use revenue from one PPP project to develop, finance and operate other PPP projects. §§ 8-23-7-22 to 8-23-7-25: Sets forth the process for the Indiana DOT and the Indiana Finance Authority to convert free highways into toll roads; all conversions require governor approval. If the Indiana DOT decides to convert a free highway into a toll road, it may enter into a public-private partnership pursuant to § 8-15.7.

State	Statute	Comments
10. KS	KAN. STAT. ANN. § 68-2314a; §§ 75-5801 et seq. http://kansasstatutes.lesterama.org/Chapter_68/Article_23/68-2314a.html http://kansasstatutes.lesterama.org/Chapter_75/Article_58/	Authorizes the Kansas Department of Transportation to use design-build methodology for innovative pavement management demonstration projects.
11. LA	LA. REV. STAT. § 48:2072 http://www.legis.state.la.us/lss/lss.asp?doc=103018 LA. REV. STAT. §§ 48:2084 to 48:2084.15 http://www.legis.state.la.us/lss/lss.asp?folder=122	Authorizes the Louisiana Transportation Authority to pursue PPPs; authorizes user-fee based funding sources. Authorizes the Authority to approve solicited and unsolicited PPP proposals. The Authority's approval is subject to the private entity's entering into a comprehensive agreement with the Authority. Authorizes the Authority to accelerate selection, review, and documentation timelines for certain proposals if the Authority deems projects have a high probability of success and require no substantial state funding. Authorizes the Authority to convey public property to the private entity and use eminent domain acquire property for a project.
12. MA	MASS. GEN. LAWS ch. 6C §§ 62-73 http://www.mass.gov/legis/laws/seslaw09/sl090025.htm	Creates the Massachusetts Department of Transportation and authorizes the Department in conjunction with the Public-Private Partnership Infrastructure Oversight Commission, to enter into DBOM and DBFOM contracts for the sale, lease, operation and maintenance of a transportation facility within the commonwealth. Limits PPPs to 50-year terms; longer terms authorized if approved in writing by the governor. Authorizes solicited and unsolicited proposals. The Department must protect private entities' confidential or proprietary information.

State	Statute	Comments
13. MD	MD. CODE REGS. 11.07.06 http://www.dsd.state.md.us/comar/subtitle_chapters/11_Chapters.htm. TRANSPORTATION PUBLIC-PRIVATE PARTNERSHIP (TP3) GUIDELINES, http://www.mdta.maryland.gov/About/tp3Guidelines.html	Creates the Transportation Public-Private Partnership Program which authorizes the Maryland Transportation Authority (MdTA), on behalf of the Maryland Department of Transportation, to enter into PPPs for new, expanded, or rehabilitated transportation facilities, including railroads and transit systems. [1] Additional legislative authority, however, may be needed depending on the form of the transaction. There is also no express provision regarding the acceptance of unsolicited proposals for highway projects. Provides PPP guidelines for the use of MdTA.
14. ME	ME. REV. STAT. ANN. TITLE 23 § 4251 http://www.mainelegislature.org/legis/statutes/23/title23sec4251.html	Authorizes the Maine DOT to enter into a PPP for the financing, development, operation, management, ownership, leasing or maintenance of a transportation facility. The law applies to projects when the Maine DOT estimates that the capital cost of the project are $25,000,000 or more, or when it would involve placing tolls on existing transportation facilities. Maine DOT may accept solicited and unsolicited proposals. Maine DOT must obtain approval by the legislature before entering into an agreement with a private entity.

1 According to a 1996 Attorney General opinion referenced in the annotations to this statute, MdTA has authority to construct toll roads using certain forms of PPPs. See MD 81 Op. Att'y Gen. (issued 2/2/96).

State	Statute	Comments
15. MI	MICH. COMP. LAWS § 472.1 to 472.36 http://www.legislature.mi.gov/(S(wcuneino4w4cuj55ftscn2zc))/mileg.aspx?page=getObject&objectName=mcl-Act-35-of-1867 MICH. COMP. LAWS § 124.401 to 124.406 http://www.legislature.mi.gov/(S(t0pftg55chnxmwiz3ukejoq2))/mileg.aspx?page=getObject&objectName=mcl-124-406 2009 Michigan State Budget, § 384(1)	Sets forth requirements for forming nonprofit street railway companies (i.e., light rail). One or more persons may organize a street railway for the purpose of acquiring, owning, constructing, furnishing, equipping, completing, operating, improving, and maintaining a street railway system. Provides for the establishment of transit development finance zones to finance projects. Authorizes metropolitan transportation authorities to enter service contracts and agreements with private parties for construction or operation of public transportation facilities. Authorizes $2.5 million for the Michigan Department of Transportation to continue preliminary legal, financial, traffic and revenue studies, permitting, engineering and other ancillary work for the Department to solicit PPP proposals for the Detroit River International Crossing.[2]
16. MN	MINN. STAT. ANN. §§ 160.85 http://www.revisor.leg.state.mn.us/revisor/pages/statute/statute_chapter_toc.php?chapter=160.	Authorizes a Road Authority to solicit proposals or accept unsolicited proposals from and enter into development agreements with private operators to develop, finance, design, construct, improve, rehabilitate, own, and operate toll facilities.
17. MO	MO. REV. STAT. §§ 227.600 to 227.699 http://www.house.mo.gov/billtracking/bills091/biltxt/truly/HB0683T.HTM MO. REV. STAT. §§ 238.300 to 238.367 http://www.moga.state.mo.us/STATUTES/C238.HTM MO. REV. STAT. §§ 238.400 to 238.412 http://www.moga.state.mo.us/STATUTES/C238.HTM	Expands Missouri's Public-Private Partnership Transportation Act, authorizing the Highways and Transportation Commission to preliminarily approve PPPs for pipeline, ferry, river port, airport, railroad, light rail or other mass transit facilities. The Commission requires approval by popular vote to pursue project types not specifically authorized by legislation (e.g., highways). All projects must be approved by majority vote of the state's Joint Committee on Transportation Oversight. No express provision authorizes solicited and unsolicited proposals. Establishes the Missouri Transportation Corporation Act, which authorizes the creation by private parties of special purpose non-profit corporations, or transportation corporations, to obtain rights-of-way for and assist in the planning and design of transportation facilities, including mass transit facilities. No express provision authorizes solicited and unsolicited proposals. Authorizes transit authorities to plan, construct, operate, maintain, or lease to or contract with others for operation and maintenance of infrastructure facilities including passenger

2 The Michigan Department of Transportation plans to submit PPP proposals to the legislature by May 1, 2010; the Michigan Legislature plans to adopt or reject authorizing legislation by the full legislative bodies by June 1, 2010.

State	Statute	Comments
		transportation systems. This statute does not mention either design-build or PPPs.
18. MS	MISS. CODE ANN. § 65-43-1 http://law.justia.com/codes/mississippi/2010/title-65/43/65-43-1/ MISS. CODE ANN. § 65-43-3 http://law.justia.com/codes/mississippi/2010/title-65/43/65-43-3/ MISS. CODE ANN. § 65-43-7 http://billstatus.ls.state.ms.us/2007/pdf/history/SB/SB2375.htm#title	Authorizes a governmental entity to construct, operate and maintain new toll road and toll bridges. Tolled facilities authorized only if built alongside alternate, free facilities. Authorizes a government entity to contract with private entities for designing, financing, constructing, operating or maintaining toll roads or toll bridges. Solicited and unsolicited proposals are authorized. Best-value selection process is authorized. Limits contract term to 50 years; no extensions permitted. Toll collection must cease upon termination of contract. Authorizes board of supervisors, counties or municipalities to borrow money to fund projects. Authorizes use of project revenues, including grants or contributions from the federal government, to service bond debt.
19. NC	N.C. GEN. STAT. §136-18 (39) http://www.ncga.state.nc.us/enactedlegislation/statutes/html/bysection/chapter_136/gs_136-18.html N.C. GEN. STAT. § 136-28 (Westlaw cite: SB 648, NC LEGIS. 2009-235 (2009)) N.C. GEN. STAT. §§ 136-89.180 to 136-89.198 http://www.ncleg.net/EnactedLegislation/Statutes/HTML/ByArticle/Chapter_136/Article_6H.html	Authorizes the North Carolina Department of Transportation to enter into PPPs with private entities to finance transportation infrastructure and to plan, design, develop, acquire, construct, equip, maintain, and operate existing rail and rail-adjoining properties. Authorizes the Department to form PPPs to engineer, design or construct improvements to the state highway system. The Department's authority under SB 648 expires December 31, 2011. Authorizes the North Carolina Turnpike Authority to develop, construct, operate and maintain up to nine toll facilities, including a toll bridge. Unsolicited proposals not authorized.

State	Statute	Comments
20. NJ	N.J. STAT. ANN. §§ 27:25-1 et seq.	Authorizes New Jersey Transit to award contracts, based on competitive proposals, to the proposer that submitted the proposal determined to "be the most advantageous to the State, price and other factors considered."[3]
21. NV	NEV. REV. STAT. §§ 338.161 to 338.168 http://www.leg.state.nv.us/NRS/NRS-338.html#NRS338Sec161.	Authorizes public bodies to accept unsolicited proposals to develop, construct, improve, maintain or operate transportation facilities. Toll bridge and toll road projects prohibited under this statute.
22. OH	OHIO REV. CODE ANN. § 5531.09 http://codes.ohio.gov/orc/5531 OHIO REV. CODE ANN. § 5531.12 http://codes.ohio.gov/orc/5531	Authorizes the director of transportation to develop financing techniques that maximize private and local participation in financing projects. Authorizes the director to use the state infrastructure bank to provide financial assistance to public and private entities for qualified projects; such assistance shall be in the form of loan, loan guarantees, letters of credit, leases, lease-purchase agreements, interest rate subsidies, debt service reserves or other forms the director deems appropriate. A qualified project is any public or private transportation project including any project involving the maintaining, repairing, improving, or construction of any public or private highway, road, street, parkway, public transit, aviation, or rail project, and any related rights-of-way, bridges or tunnels. Creates State Transportation Finance Commission within the Ohio Department of Transportation and authorizes it to approve toll projects at locations approved by the director of transportation. Tolls not authorized on existing non-tolled facilities.

3 New Jersey Transit used this authority for Hudson-Bergen LRT and River LINE DBOM projects.

State	Statute	Comments
23. OR	OR. REV. STAT. §§ 367.800 to 367.826. http://www.leg.state.or.us/ors/367.html. OR. REV. STAT. §§ 383.001 to 383.019 http://www.leg.state.or.us/ors/383.html.	Establishes the Oregon Innovative Partnerships Program which authorizes the Oregon Department of Transportation to solicit and accept unsolicited proposals for PPPs for transportation projects, including transit. Authorizes the Department to solicit and accept unsolicited PPPs for tollway projects.
24. PR	P.R. LAWS ANN. tit. 9, §§ 2001 to 2021	This Spanish language statute establishes a toll transportation facility authority with broad powers to authorize private participation in public highway projects.
25. SC	S.C. CODE ANN. §§ 57-3-200 http://www.scstatehouse.net/code/titl57.htm.	Authorizes the South Carolina Department of Transportation to enter into agreements to finance, construct and maintain highways, roads, streets, and bridges.
26. TN	TENN. CODE ANN. § 54-3-101 et seq. http://www.michie.com/tennessee/lpext.dll?f=templates&fn=main-h.htm&cp=tncode	Authorizes the Tennessee Department of Transportation to contract with private parties, the federal government, or other governmental agencies for the purpose of developing or operating a toll way or toll facility. Design-build is expressly authorized. Tolling authority limited to Pilot Program projects which include either: two highways or two bridges; or one highway and one bridge.
27. TX	TEX. TRANSP. CODE ANN. §§ 223.001 to 223.209; 227.001 to 227.083; 228.001 to 228.254; 370.001 to 370.365 http://tlo2.tlc.state.tx.us/statutes/tn.toc.htm. TEX. TRANSP. CODE ANN. §§ 451.801 to 451.812	Authorizes the Texas Department of Transportation, the Texas Turnpike Authority, and Regional Mobility Authorities to accept solicited and unsolicited proposals for PPPs, and to enter into comprehensive development agreements. If the agreement provides for collection of tolls by the private entity, the terms of the agreement may not exceed 50 years, except that the terms may be increased to 70 years if certain requirements are satisfied.[4] Authorizes Metropolitan Transit Authorities to use a “hybrid delivery system” to procure transit facilities.

4 On July 2, 2009, Texas rejected SB17 and SB404, bills that would allow TxDOT to enter into long-term leases with private companies (the current law allowing for the 50 year contracts mentioned above expires Sept. 1, with the exception of a short list of proposed roads that have until 2011). The new law does authorize a $2 billion transportation bonding bill but does not place bond revenues back in the fund.

State	Statute	Comments
	http://tlo2.tlc.state.tx.us/statutes/tn.toc.htm TEX. LOC. GOV. CODE ANN. §§ 271.181 to 271.199 http://tlo2.tlc.state.tx.us/statutes/lg.toc.htm	Authorizes local governmental entities to use best-value criteria to select design-builders for construction, rehabilitation, alteration, or repair of civil works projects, including transit projects.
28. UT	UTAH CODE ANN. §§ 63-56-502.5; 72-6-118; 72-6-201 to 72-6-206 http://www.le.state.ut.us/~code/TITLE63/63_29.htm; http://www.le.state.ut.us/~code/TITLE72/72_06.htm.	Authorizes the Utah Department of Transportation, with approval from the Transportation Commission, to accept solicited and unsolicited proposals for PPPs involving toll way facilities through the use of "toll way development agreements."
29. VA	VA. CODE ANN. §§ 56-556 to 56-575 http://leg1.state.va.us/cgi-bin/legp504.exe?000+cod+TOC560000000022000000000000.	Establishes Public-Private Transportation Act of 1995 which authorizes PPPs for transportation facilities, including mass transit facilities. This statute authorizes solicited and unsolicited proposals, and contains detailed guidelines to assist VDOT and other public entities in implementing PPPs.
30. WA	WASH. REV. CODE §§ 47.29.010 to 47.29.900 http://apps.leg.wa.gov/rcw/default.aspx?Cite=47.	Authorizes PPPs for transportation projects, which include capital or operating transit projects. Revenue-negative transit projects can be pursued under this statute, but if they are to be operated as public facilities, any indebtedness must be issued by the state treasurer.

APPENDIX J

FALSE CLAIM STATUTES

Comparative table or chart of state statutes

STATE AND MUNICIPAL FALSE CLAIMS STATUTES				
STATE	**CITATION(S)**	**GOV'T. CIVIL ACTIONS**	**QUI TAM ACTIONS**	**CRIMINAL PENALTIES**
Alaska	Alaska Stat. § 36.30.687	Yes	No	Yes, Class C felony, plus forfeiture of claim
Arizona	Ariz. Rev. Stat. § 47-9527 Arizona also has a Medicaid FCA	No	Yes, treble damages	No
California	Cal. Gov't. Code §§ 12650 et seq. enacted 1987, as amended through Stats. 2009, c.277. California also has a Medicaid FCA	Yes, treble damages plus costs plus civil penalty up to $10,000; must be filed within 3 years after discovery and 10 years after occurrence	Yes, and relator may receive 15 to 33% of recovery, plus attorneys' fees and costs; State AG may intervene, and may receive up to 33% of recovery	No
City of Chicago	Chicago Municipal Code §§ 1-22-010 et seq. See also: Chicago Municipal Code § 2-152-171 (Whistle blower protection) and Chicago Municipal Code § 1-21-010 et seq. (False stmts.)			

STATE	CITATION(S)	GOV'T. CIVIL ACTIONS	QUI TAM ACTIONS	CRIMINAL PENALTIES
Delaware	6 Del. Code Ann. §§ 1201 et seq. Enacted in 2000	Yes, treble damages, plus attorneys' fees and costs, plus civil penalty of up to $11,000; must be filed within 3 years after discovery and 6 years after occurrence	Yes, and relator may receive 15 to 25% of recovery (up to 30% if alone); plus attorneys' fees, costs, and expenses; State Dept. of Justice may intervene	No
Florida	Fla. Stat. Ann. §§ 68.081 et seq. Enacted in 1994	Yes, treble damages, plus attorneys' fees, costs and expenses, plus civil penalty up to $11,000; must be filed within 3 years after discovery and 10 years after occurrence	Yes, and relator may recover 15 to 25% (up to 30% if alone), plus attorneys' fees and costs; State Dept. of Legal Affairs or State Dept. of Financial Svcs. may intervene	No
Hawaii	Haw. Rev. Stat. Ann. §§ 661-21 et seq. (false claims–state), enacted in 2000; 46-171 et seq. (false claims–local); §§ 378-61 et seq. (whistleblowers)	Yes, treble damages plus civil penalty of up to $10,000, plus attorneys' fees and costs; must be filed within 6 years after discovery and 10 years after occurrence	Yes, and relator may recover 15 to 25% (up to 30% if alone), plus attorneys' fees and costs; State may intervene	No
Idaho	Idaho St. §§ 6-2101 et seq.	No	Whistleblower protection for public employees only	No
Illinois	740 Ill. Comp. Stat. Ann. §§ 175/1 et seq.	Yes, treble damages, plus civil penalty of up to $11,000, plus attorneys' fees, costs and expenses; must be filed within 3 years after discovery and 10 years after occurrence	Yes, and relator may recover 15 to 25% (up to 30% if alone), plus attorneys' fees, costs, and expenses; State may intervene	No
Indiana	Ind. Code 5-11-5.5	Yes, civil penalty of at least $5,000 and up to treble damages, plus costs; AG and IG have concurrent jurisdiction to investigate; must be filed within 3 years after discovery and 10 years after occurrence; AG and IG may use CIDs	Yes, and relator may recover 15 to 25% (up to 30% if alone), plus attorneys' fees, costs and expenses; State may intervene	No

STATE	CITATION(S)	GOV'T. CIVIL ACTIONS	QUI TAM ACTIONS	CRIMINAL PENALTIES
Kansas	Kan. Stat. Ann. 75-7501 et seq.; enacted Laws 2009, ch. 103, § 1, eff. April 30, 2009	Yes, treble damages, plus civil penalties of up to $11,000, plus attorneys' fees and costs; must be filed within 3 years after discovery and 10 years after occurrence; per Kan. Stat. Ann. 75-7508(a)(2), a portion of the recovery goes to the defrauded state agency	No; Kan. Stat. Ann. 75-7504 expressly rules out all private causes of action except for whistleblower retaliation suits authorized by Kan. Stat. Ann.75-7506	No
Louisiana	Two separate statutes: La. Rev. Stat. Ann. 38:2260, penalties for violation of provisions on public contracts for purchase of materials; La. Rev. Stat. Ann. 39:2151, Hurricane Relief Programs Integrity Act of 2006. Louisiana also has a Medicaid FCA.	La. Rev. Stat. Ann. 38:2260, no; La. Rev. Stat. Ann. 39:2151, yes, Treble damages, plus civil fine of up to $10,000, plus attorneys' fees, costs and expenses; must be filed within 1 year after discovery and 10 years after occurrence	La. Rev. Stat. Ann. 38:2260, no; La. Rev. Stat. Ann. 39:2151, yes, relator may receive up to 20 percent of recovery (up to 30 percent if alone), plus attorneys' fees, costs, and expenses	La. Rev. Stat. Ann. 38:2260, yes, misdemeanor, fine of up to $500; La. Rev. Stat. Ann. 39:2151
Massachu-setts	Mass. Gen. Laws Ann. ch. 12, §§ 5 et seq., enacted in 2000. Massachusetts also has a Medicaid FCA.	Yes, treble damages (incl. consequential damages) plus civil penalty up to $10,000, plus attorneys' fees, experts' fees, costs of investigation; State recoveries go to False Claims Prosecution Fund; must be filed within 3 years after discovery and 10 years after occurrence	Yes, and relator may recover 15 to 25% (up to 30% if alone), plus attorneys' fees and costs; State may intervene	No
Michigan	Mich. Comp. Laws §§ 15.361 et seq.	No	Whistleblower protection for public employees only	No

STATE	CITATION(S)	GOV'T. CIVIL ACTIONS	QUI TAM ACTIONS	CRIMINAL PENALTIES
Minnesota	Minn. Stat. §§ 15C.01 et seq.— **NEW**, effective July 1, 2010	Yes, treble damages, plus civil penalties of up to $11,000, plus attorneys' fees, experts' fees and costs; must be filed within 3 years after discovery and 10 years after occurrence; actual damages credited to fund that sustained damages, portion of balance to false claims account for litigation expenses	Yes, and relator may recover 15 to 25% (up to 30% if alone), plus attorneys' fees, experts' fees and costs; State may intervene	No
Montana	Mont. Code Ann. 17-8-401 et seq., (false claims–state); Mont. Code Ann. § 7-6-4311 (false claims–local) Montana also has a Medicaid FCA.	Yes, treble damages, plus civil penalties of up to $10,000, plus attorneys' fees, costs, and expenses; must be filed within 3 years after discovery and 10 years after occurrence	Yes, and relator may recover 15 to 25% (up to 30% if alone), plus attorneys' fees, costs, and expenses; State may intervene	No
Nebraska	Neb. Rev. St. § 23-135.01. Nebraska also has a Medicaid FCA.	No	No	Yes, Class IV felony
Nevada	Nev. Rev. Stat. §§ 357.010 et seq., enacted by ch. 824, Laws of 1999	Yes, treble damages, plus civil penalties of up to $10,000 plus costs, with joint and several liability; if AG commences, 33 percent of recovery to false claims investigation fund	Yes, and relator may recover 15 to 33% (up to 50% if alone), plus attorneys' fees, experts' fees, expenses, and costs; State may intervene	No

STATE	CITATION(S)	GOV'T. CIVIL ACTIONS	QUI TAM ACTIONS	CRIMINAL PENALTIES
New Jersey	N.J. Stat. Ann. 2A:32C-1 et seq.; enacted by Laws of 2007, ch. 265, eff. March 13, 2008	Yes, treble damages, plus same civil penalties as allowed under federal FCA as adjusted for inflation, plus attorneys' fees, expenses and costs; AG receives 10% of proceeds to special fund to support false claims investigations and prosecutions; must be filed within 3 years after discovery and 10 years after occurrence; AG authorized to subpoena records and witnesses, enforceable by arrest warrants	Yes, and relator may recover 15 to 25% (up to 30% if alone), plus attorneys' fees, expenses, and costs; State may intervene	No (except that persons failing to comply with AG subpoenas may be arrested)
New Mexico	N.M. Stat. Ann. 1978 §§ 44-9-1 et seq., enacted by L. 2007 ch. 40, eff. July 1, 2007	Yes, treble damages plus civil penalties of up to $10,000, plus attorneys' fees and costs; AG may investigate or delegate investigative authority to agency defrauded; joint and several liability; actual damages returned to fund defrauded, portion of other proceeds to AG for false claims investigations and prosecutions; no statute of limitations, except that underlying conduct must have occurred on or after July 1, 1987	Yes, and relator may recover 15 to 25% (up to 30% if alone), plus attorneys' fees and expenses; State may intervene	No
New York City	N.Y.C. Admin. Code §§ 7-801 et seq. Enacted by Local Law No. 53 of 2005			

STATE	CITATION(S)	GOV'T. CIVIL ACTIONS	QUI TAM ACTIONS	CRIMINAL PENALTIES
New York State	N.Y. State Finance Law §§ 187 et seq., enacted L. 2007 c. 58, eff. April 1, 2007	Yes, treble damages, plus civil penalties of up to $12,000, plus attorneys' fees, expenses, and costs; must be filed within 3 years after discovery and 10 years after occurrence	Yes, and relator may recover 15 to 25% (up to 30% if alone), plus attorneys' fees, expenses, and costs; State may take over action or intervene	No
North Carolina	N.C. Gen. Stat. Ann. Art. 51 §§ 1-605 et seq. and Art. 2 §§ 108A-63.1 et seq., enacted by Session Law 2009-554, Aug. 28, 2009, eff. Jan. 1, 2010 Note: appears to reflect FERA amendments to Federal FCA. North Carolina also has a Medicaid FCA.	Yes, treble damages, plus costs, plus civil penalty of up to $11,000; AG may retain a portion of recovery as reimbursement for costs; AG authorized to issue CIDs; must be filed within 3 years after discovery and 10 years after occurrence	Yes, and relator may recover 15 to 25% (up to 30% if alone), plus attorneys' fees, costs, and expenses, if alone); State may intervene	No
Ohio	Ohio Rev. Code Ann. §§ 4113.52 et seq. Ohio also has a Medicaid FCA.	No	Whistleblower protection only	No
Rhode Island	R.I. Stat. §§ 9-1.1-1 et seq., Enacted P.L. 2007, ch. 73, eff. Feb. 15, 2008	Yes, treble damages plus civil penalties of up to $10,000, plus costs; must be filed within 3 years after discovery and 10 years after occurrence; AG or State Police may issue subpoenas; recoveries deposited into special State False Claims Act fund	Yes, and relator may recover 15 to 25% (up to 30% if alone), plus attorneys' fees, expenses, and costs; State may intervene	No

STATE	CITATION(S)	GOV'T. CIVIL ACTIONS	QUI TAM ACTIONS	CRIMINAL PENALTIES
Tennessee	Tenn. Code Ann. §§ 4-18-101 et seq., enacted by ch. 367 Laws of 2001 Tennessee also has a Medicaid FCA	Yes, treble damages, plus civil penalty of up to $10,000, plus costs; AG receives 33% of recoveries to support ongoing investigation and prosecution of false claims; must be filed within 3 years after discovery and 10 years after occurrence	Yes, and relator may recover 25 to 33% (35 to 50% if alone); State may intervene	No
Virginia	Va. Code Ann. §§ 8.01-216.1 et seq., enacted by ch. 842 of the Laws of 2002, eff. Jan. 1, 2003	Yes, treble damages, civil penalty up to $11,000, plus attorneys' fees and costs; must be filed within 3 years after discovery and 10 years after occurrence; AG may use CIDs	Yes, and relator may recover 15 to 25% (up to 30% if alone), plus attorneys' fees and costs; State may intervene	No
Washington, D.C.	D.C. Code Ann. §§ 2-308.14 et seq.			
Wyoming	Wyo. Stat. 1977 § 6-5-303	No	No	Yes, felony, prison up to 2 years, fine of up to $2,000, or both

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INDEX OF CASES

THE NATIONAL ACADEMIES

Advisers to the Nation on Science, Engineering, and Medicine

The **National Academy of Sciences** is a private, nonprofit, self-perpetuating society of distinguished scholars engaged in scientific and engineering research, dedicated to the furtherance of science and technology and to their use for the general welfare. On the authority of the charter granted to it by the Congress in 1863, the Academy has a mandate that requires it to advise the federal government on scientific and technical matters. Dr. Ralph J. Cicerone is president of the National Academy of Sciences.

The **National Academy of Engineering** was established in 1964, under the charter of the National Academy of Sciences, as a parallel organization of outstanding engineers. It is autonomous in its administration and in the selection of its members, sharing with the National Academy of Sciences the responsibility for advising the federal government. The National Academy of Engineering also sponsors engineering programs aimed at meeting national needs, encourages education and research, and recognizes the superior achievements of engineers. Dr. C. D. Mote, Jr., is president of the National Academy of Engineering.

The **Institute of Medicine** was established in 1970 by the National Academy of Sciences to secure the services of eminent members of appropriate professions in the examination of policy matters pertaining to the health of the public. The Institute acts under the responsibility given to the National Academy of Sciences by its congressional charter to be an adviser to the federal government and, on its own initiative, to identify issues of medical care, research, and education. Dr. Harvey V. Fineberg is president of the Institute of Medicine.

The **National Research Council** was organized by the National Academy of Sciences in 1916 to associate the broad community of science and technology with the Academy's purposes of furthering knowledge and advising the federal government. Functioning in accordance with general policies determined by the Academy, the Council has become the principal operating agency of both the National Academy of Sciences and the National Academy of Engineering in providing services to the government, the public, and the scientific and engineering communities. The Council is administered jointly by both Academies and the Institute of Medicine. Dr. Ralph J. Cicerone and Dr. C. D. Mote, Jr., are chair and vice chair, respectively, of the National Research Council.

The **Transportation Research Board** is one of six major divisions of the National Research Council. The mission of the Transportation Research Board is to provide leadership in transportation innovation and progress through research and information exchange, conducted within a setting that is objective, interdisciplinary, and multimodal. The Board's varied activities annually engage about 7,000 engineers, scientists, and other transportation researchers and practitioners from the public and private sectors and academia, all of whom contribute their expertise in the public interest. The program is supported by state transportation departments, federal agencies including the component administrations of the U.S. Department of Transportation, and other organizations and individuals interested in the development of transportation. **www.TRB.org**

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