CONSTRUCTION RISK MANAGEMENT REPORTER

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ContrACT

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Owner Not Required to Respond to Contractor's Delay Claims Absent Express Contractual Terms

CAVAN S. BOYLE

Benjamin Franklin is credited with saying, "Remember that time is money". History may not include "builder" among Franklin's many accomplishments, but he certainly would have understood why most modern construction contracts contain provisions that govern the parties' entitlement to delay damages. Often, the contract also prescribes the manner in which an owner reviews and responds to those claims. But what happens when a contract does not state when, how, or even if, an owner must respond to a contractor's properly submitted delay claims? According to a recent First Department decision in *Tutor Perini Corp. v. City of New York*,[1] the answer is nothing, leaving that contractor in a tough spot.

The case involved a 2018 public construction project between Tutor Perini and the New York City Department of Transportation (the "City")[2] for the rehabilitation of the Broadway Bridge over the Harlem River.

The project was initially scheduled to finish in July 2021, but Tutor Perini claimed that significant owner-directed design changes pushed the likely substantial completion date to May

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Despite Change Order, County Evades Payment When Legislature Denies Funding

MICHAEL F. HIGGINS

Ernstrom & Dreste attorneys consistently warn of the dangers of proceeding without an executed change order, and of other ways public owners avoid paying for work performed.[1] But what about a situation where the public owner does not dispute ordering additional work, issues a change order with agreed compensation, accepts the benefit of the work, but then dodges payment because a legislative body failed to later approve release of the payment? The Appellate Division, Second Department recently approved just that.[2]

In *Atane*, a construction manager contracted with Nassau County to provide construction management-agent services on a "not to exceed" basis for a defined time. Delays ensued and the contract period and cap were extended via change order with the Department of Public Works ("DPW"). The change order funding was then authorized by the County Legislature and signed by the County Executive. As the first extension ended, the DPW issued a change order to further extend the time for performance and the cap. However, the Legislature never approved the funding for the change order and refused to pay.

The appellate court sided with the County, reasoning that the extended period of construction management required a new "stand alone contract." The legislature could not be forced to ratify the change order, said the court. The construction manager's other arguments, including breach of contract, were rejected because the court concluded there was no enforceable contract for the additional services. The County could not be compelled to pay for the services, even though it obtained them by inducing them with a change order.

The contract included a provision that empowered the DPW Commissioner to order extra services. The contract also contained language cautioning that approval of the contract may require approval by the County Legislature.[3] The contract had been duly approved by the legislature at inception and the extra services provision did not explicitly require legislative approval. The extra services provision only noted the "prior written approval of the Commissioner" was required. In other words, the fully vetted, legislatively approved and signed contract required only that the Commissioner issue prior approval for extra work (i.e. via change order).

The court, seemingly ignoring the Commissioner's power to issue change orders, went so far as to proclaim that a contractor's only option is to refuse to perform until an agreement is executed and fully approved as required. While that is the safest course, here the construction manager had a change order in hand and the County project representatives clearly intended and anticipated payment. The actions of the project-level parties were thus stymied by the County's later stance that the change was, instead, a new agreement requiring legislative approval.

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The Risk of Assumptions: Contract's Exculpatory Clause Defeats Claim

NELL M. HURLEY

A 2023 court decision highlights the dangers of a contractor's assumptions about work it is required to perform, especially in the face of contract exculpatory clauses that place the risk for that assumption directly on the contractor.[1]

The matter stems from a New York State Power Authority ("NYPA") construction contract with B.V.R Construction Company, Inc. ("BVR"), which then subcontracted the concrete demolition work for the project to Penn Hydro, Inc. ("Penn Hydro"). There was no information about the strength or "hardness" of the concrete contained in the prime contract or represented in project plans and specifications. Penn Hydro's written proposal, which was ultimately attached as an exhibit to the unit price subcontract, stated that its pricing was "based on" removal of approximately 4000 psi[2] concrete.

Soon after starting the demolition work, Penn Hydro learned that the concrete's hardness varied from place to place and was much more difficult to demolish than expected. This resulted in additional costs for manpower and equipment, and the work proceeded very slowly. Thereafter, Penn Hydro asked for, and BVR obtained, test boring samples showing the psi of the 5 concrete samples to be 9720, 5500, 5400, 8030, and 8490, much higher than either party likely expected.

Penn Hydro sought unsuccessfully to recover its additional costs from BVR, ultimately filing the lawsuit. BVR denied Penn Hydro's claim and moved for summary judgment relying on subcontract language it said placed responsibility for the higher psi concrete on Penn Hydro. The motion court ruled for Penn Hydro and denied BVR's motion. On appeal, however, the lower court's decision was reversed, and Penn Hydro's breach of contract action for additional compensation was dismissed.

While the parties agreed that the terms of the subcontract governed the claim, the court concluded that Penn Hydro's pricing proposal "assumption" (work "based on" 4000 psi concrete) was not a condition of the subcontract. The court reasoned that because the subcontract failed to provide any "cognizable formula" by which a different price could be ascertained for removal of harder concrete, the values in the proposal established a set price for the work, not contingent on psi strength.

The court then determined that the subcontract's "investigations clause" (aptly rebranded by BVR as an "assumption of risk" clause) placed the risk of the harder concrete on Penn Hydro. Pursuant to that provision, decided the court, Penn Hydro accepted responsibility for inspecting "the conditions that could affect the [s]ubcontract [w]ork at the [p]roject site" and was properly charged with the knowledge such an inspection would have revealed, including concrete psi higher than anticipated. Thus, the decision means those costs must be borne by Penn Hydro.

Significant to this outcome may have been the lack of representations by the NYPA or BVR regarding concrete psi. New York law may permit recovery based upon a "qualitative change" in the contract work in certain circumstances, but typically requires that some significant contract term has changed. Here, the psi strength "term" was nothing more than an assumption by Penn Hydro, according to this decision.

There are actions a contractor can take to protect itself. Understand that "investigations clauses" are designed to transfer risk to the contractor (or subcontractor). Be sure to fully review all important assumptions upon which contract work is based. In the case here, even without test borings, a substantial disparity in concrete strength likely could have been detected before the subcontract was signed. In preparing pricing where an important variable is unknown, but must be assumed in the bid/proposal, set forth alternate parameters that permit, or even require, an adjustment if that assumption turns out to be erroneous. And finally, remember that a mere staple attaching a proposal to the subcontract as an exhibit does not automatically make all its terms a part of the contract – for that you need language in the contract that expressly incorporates the exhibit and its specific terms. E&D

1 *Penn Hyrdro, Inc. v. B.V.R. Constr. Co., Inc.*, 218 AD3d 1253 (4th Dept 2023).

2 Psi stands for pounds per square inch, a standard measure of hardness for concrete.

In July, Brian Streicher, third from (R), joined other Board Members of Rochester JBX (Junior Builders Exchange) to present a $4,000 donation to the Al Sigl Community of Agencies, the result of JBX charity fundraisers.

CONTINUED "DESPITE CHANGE ORDER, COUNTY EVADES PAYMENT WHEN LEGISLATURE DENIES FUNDING"

Atane risks upending the expectation that contractors will be paid for their work on public jobs. It also runs counter to long-settled court recognition that changes requested by a public owner do not make the contract invalid. The New York Court of Appeals has observed that if the existence of a change order provision in a public construction contract was sufficient to void a contract where the execution of change orders pushes the total indebtedness over the appropriated limit, then every public construction contract in New York State is potentially void. Further, *Atane* appears to violate State Law and the New York Constitution's mandate that government entities pledge their full faith and credit for the payment of indebtedness. Change orders should not be treated as new contracts, and government entities should not be permitted to escape payment for authorized and accepted extra work performed under previously approved public contracts.

Atane reiterates that contractors risk non-payment for additional work until all contractual requirements are fully completed, and that a change order may not be enough. Must contractors now research whether legislative approval is required, risking work stoppages until the slow-moving cogs of government turn to finalize any required secondary approvals? Although wrongly decided, *Atane* indeed prompts prudent contractors to refuse performance of additional work until all contractual (and now County Charter or similar) requirements for changes, extensions, or amendments of the contract are fully performed. E&D

1 Contracts often mandate full change order execution before proceeding under pain of non-payment, and various other bars or forfeitures of rights abound.

2 *Atane Engineers, Architects and Land Surveyors, D.P.C. v Nassau County*, 227 AD3d 708 (2d Dept 2024).

3 "The County shall have no liability under this [contract] Agreement (including any extension or other modification of this Agreement) to any Person unless (i) all County approvals have been obtained, including, if required, approval by the County Legislature and (ii) this Agreement has been executed by the County Executive (as defined in this Agreement)." The County Charter contained similar terms.

CONTINUED "OWNER NOT REQUIRED TO RESPOND TO CONTRACTOR'S DELAY CLAIMS"

2027. As a result, Tutor Perini faced millions of dollars in delay-related costs that would continue to accrue over the project's duration, and the prospect of the City asserting $7,000 per day in potential liquidated damages for late completion. Over the next one and a half years, Tutor Perini properly submitted notices of its delay and extension claims to the City, without receiving any response or determination. Frustrated with the City's silence, Tutor Perini filed a declaratory judgment lawsuit asking the court to find the City obligated to "timely and reasonably address" its delay claims.

Tutor Perini made three main arguments. First, the contract's notice of claim provisions were designed to require a response, particularly since the contract included a six-month contractual limitations period. Second, that failing to respond to the claims violated the covenant of good faith and fair dealing implied in every contract. Third, the City's failure to respond violated the prevention doctrine by frustrating Tutor Perini's ability to carry out its agreement.

The court disagreed and instead found that because there was no specific language that required the City to respond to Tutor Perini's delay claims, the City had no such obligation. "Silence does not equate to contractual ambiguity," the court said, and it refused to "write into a contact conditions the parties did not include." The court noted, "[Tutor Perini] is not totally deprived of the benefit of the contract" because "no provision in the contract states that [it] must wait to file delay claims until after review or rejection of those claims," leaving open the immediate opportunity for Tutor Perini to sue the City for breach of contract. Thus, the court rejected Tutor Perini's arguments that the City's lack of response had violated the implied covenant of good faith and fair dealing and the prevention doctrine.

The City asserted that it typically did not process contract claims, including delay claims, until after the project was substantially complete. While this flies in the face of the very purpose of the contract's immediate notice provisions placed on Tutor Perini,[3] that did not impact the court's determination that no action whatsoever was required by the City in response to those notices.

Contractors that find themselves in this position face the difficult task of quantifying financial exposure and determining how (and maybe even whether) to proceed.[4] In such circumstances, how long must the contractor wait before legal action would succeed? Might the owner then paradoxically argue that the lawsuit is premature because there has been no denial of the contractor's claims or that damages are undeterminable? On the other hand, the owner's non-responsiveness could implicate applicable limitations periods for suit if the owner's conduct is later deemed a constructive denial.

With such high-stakes questions hanging in the balance, a contractor in this situation is best served by continuing to "document its claim" with ongoing written claim updates to the owner and seeking immediate counsel with experienced construction attorneys. E&D

1 225 AD3d 439 (1st Dept 2024).

2 The City acted on behalf of NYCDOT and was a named defendant.

3 The logical purpose of such provisions is to provide the owner with prompt notice so that efficient owner investigation may be made, the validity of the claim determined, and steps taken to avoid or minimize the delay.

4 Depending on the contract, the contractor may have the right to terminate the contract but then runs the risk of itself being held in breach if it turns out to be wrong.

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Ernstrom & Dreste, LLP also publishes the Fidelity and Surety Reporter. If you would like to receive that publication as well, please contact Clara Onderdonk at conderdonk@ed-llp.com. Copies of ContrACT Construction Risk Management Reporter and The Fidelity and Surety Reporter can also be obtained at Ernstrom & Dreste, LLP's website (ernstromdreste.com).

FIRM NEWS

Ernstrom & Dreste, LLP was featured by the Rochester Business Journal in an article about boutique law firms published July 26, 2024, noting E&D's 30-plus years of success as a Construction and Surety Law firm.

John Dreste presented at the AGC NYS webinar on "*Managing the New Contractor/Subcontractor Registration Law*" on June 27, 2024.

Brian Streicher and Cavan Boyle participated in the 2024 Isaiah House Annual Golf Tournament held at Penfield Country Club on July 29. The event was sponsored by Schuler-Haas Electric Corp. Ernstrom & Dreste was a Bronze Sponsor.

Kevin Peartree, Martha Connolly, and Brian Streicher presented "*Controlling Risk in Construction and Project Delivery Systems*" to the AGC NYS Construction Leadership Academy at a session in Rochester, New York on May 16, 2024.

Todd Braggins (L) at the Philadelphia Surety Claims Association's Annual Golf Outing in June, joined by Rachel Walsh (Liberty Mutual Surety), Christine Alexander (Arch Surety) and Dennis O'Neill (Beacon Consulting). Ernstrom & Dreste was a hole sponsor.