

CONSTRUCTION LAW BRIEFING



IN THIS ISSUE

Do what I say, not what I do

Bidding rules on public projects can be murky

Timing is everything

Statutory revisions affect outcome of homebuilding case

The fine line between construction contract and contract of sale

Meeting the specs

Successful bid claims begin with satisfying the proposal

Can claims outlive a statute of limitations?

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Bidding rules on public projects can be murky

Can a municipality be trusted not to bypass its own mandatory bidding rules? Not always, as an Alabama development company learned the hard way in *Bessemer Water Service v. Lake Cyrus Development Co.*

Here come the waterworks

Bessemer Water Service (BWS) is a department of the City of Bessemer, Ala. It entered into a water agreement with Lake Cyrus Development Company (LCDC) in 1998.

In 2004, as part of another case regarding water rates, BWS sought a judicial declaration that parts of the water agreement were invalid because the contract was not publicly bid. It also requested a determination of whether LCDC was obligated to return any of the funds it had previously received from BWS under the agreement.

Per that agreement, LCDC was to increase the size of the main water line within a residential development in the City of Hoover, Ala., which is adjacent to Bessemer. BWS was obliged to provide water to the development at the same rates, terms and conditions as it provided water service to all other customers.

Let's mix things up

Yet the terms and provisions weren't the same as those in the typical BWS water services contract.

For example, BWS usually funded the cost of a water main extension for a residential development to the point of the entrance, and the developer then paid the costs associated with bringing water from that point into the development, including construction of mains and lines.

Here, BWS agreed to pay LCDC \$273,000 as "partial deferment" of LCDC's costs incurred in installing the main extension, the submains and the water valves. BWS further agreed to reimburse LCDC on a monthly basis for all costs and expenses LCDC incurred in installing lateral water lines, and to remit monthly 100% of the tap fees collected from new customers in the development.

The Alabama Supreme Court identified several other requirements in the water agreement that deviated from the standard water services contract.

Eventually, the relationship between BWS and LCDC deteriorated. BWS withheld payments, and LCDC stopped work, resulting in delays in the development's construction. BWS sought relief in December 2004, but, in March 2005, the trial court found the water agreement to be valid.

"Public works" by any other name

On appeal, BWS argued that, because the agreement obligated it to at least partially fund the construction of the water lines in the development, the



IT'S ALL OR NOTHING

One interesting side note to *Bessemer Water Service v. Lake Cyrus Development Co.* (see main article) was that, after fighting to invalidate much of the water agreement, Bessemer Water Service (BWS) tried unsuccessfully to salvage some provisions it liked. It argued that the court should sever the invalid provisions of the agreement and enforce the remaining provisions.

BWS contended that would leave a standard water service contract that was fair to both parties. Not surprisingly, Lake Cyrus Development Company (LCDC) countered that, if the agreement is void, it's void in its entirety. The agreement contained a severance clause that would support such a contention, but BWS cited the court's policy of preserving as much of a contract as can survive its invalid provisions.

The court declined to apply the policy here. The agreement, it said, didn't merely incorporate invalid provisions; the agreement itself was void by statute. Under Alabama law, "all contracts for public works entered into in violation of [the competitive bidding requirements] shall be null, void, and violative of public policy." The court wouldn't attempt to prune certain provisions of a contract deemed void by the legislature.

construction represented a public works project under Alabama law. Therefore, BWS's payments to LCDC to complete the construction violated the state law that requires all public works projects to be advertised and bid out.

The relevant statute defines "public works" as "the construction, repair, renovation, or maintenance of public buildings, structures, sewers, waterworks ... on public property and to be paid, in whole or in part, with public funds ..."

The question was: Did the construction represent a public works project under Alabama law?

The Alabama Supreme Court noted that the agreement granted BWS "... all permanent, non-exclusive easements necessary for BWS to install water mains and otherwise provide water service to all areas of ..." the development.

BWS's easement on the property where the waterworks were built rendered it public property. Because the agreement also obligated BWS to pay, at least in part, for construction of the waterworks, the court

found that the project satisfied the definition of "public works."

LCDC disputed this, pointing out that the development was already under construction in Hoover, with plans to buy water from another source, when BWS representatives asked the development to use BWS for its water. LCDC claimed that the purchase of an ongoing project is not a public works job that should be let for bid.

The court disagreed. It held that BWS is a public utility and was required to comply with the competitive bid law. Because it didn't, the water agreement was null and void.

Shortcut goes nowhere

In the end, LCDC wasn't entitled to any payment for the work it performed under the agreement. It also lost its option under the water agreement to repurchase waterlines it had previously tendered to BWS. And, as of this writing, the Alabama attorney general is seeking the return of \$882,822 from LCDC to BWS.

This case illustrates the risk of accepting a contract awarded directly, outside of a bidding process. Before accepting a contract, contractors and developers need to work with an experienced construction attorney who can identify the precise type of a project and ensure they adhere to applicable statutory requirements. *T*

Timing is everything

Statutory revisions affect outcome of homebuilding case

Thanks to a change in the law governing homeowners' claims, an Oregon homebuilder reaped the benefits of some fortuitous timing. Although the circumstances in *Strizver v. Wilsey* were unusual, they teach an important lesson on how statutory revisions may or may not apply to a given situation.

Defects discovered

According to the Strizvers, in April 2003 they entered into a contract under which the Wilseys, neighborhood contractors, would build them a house.

The contract included a provision requiring the Strizvers to notify the Wilseys of any claims for defective work within one year of the date of completion. It also required any claim arising from the contract to be brought within one year of the date of completion.

The Strizvers moved into the house in September 2003. They subsequently discovered it hadn't been built to specifications in several respects, and they found a number of defects. They notified the contractors of the defects in the fall of 2003, in accordance with the contract terms, but received no response.



On Jan. 1, 2004, a new Oregon statutory procedure took effect. It imposed requirements related to prosecution of homeowners' complaints against residential contractors, subcontractors and suppliers. In particular, homeowners can't commence a new arbitration or court action unless they first follow several notice and inspection procedures.

Nine months after the law took effect, the Strizvers filed suit against the contractors. The contractors moved to dismiss the case because the Strizvers failed to comply with the new statutory provisions before filing. The Douglas County Circuit Court dismissed the case without prejudice, meaning the Strizvers could refile the lawsuit within the statute of limitations period.

The court compares

On appeal, the Strizvers argued that the requirements shouldn't apply to them retroactively because the parties entered the contract before the statute became effective. Further, the house was built and defects were discovered before it went into effect.

According to the Court of Appeals of Oregon, the issue came down to whether the relevant provisions were "remedial" or "substantive" in nature. If remedial, they presumptively would apply retroactively; if substantive, they presumptively would apply only prospectively. Remedial statutes, as the name hints, affect a plaintiff's remedy, while substantive laws affect rights and duties.

The statute at issue required homeowners to send would-be defendants a notice of defect by registered mail, with specified information, before commencing their action. It also imposed other requirements and timelines.

The court concluded the provisions were remedial and thus applied retroactively. It found that the provisions were intended to require homeowners and contractors to attempt to settle their differences before initiating court action. In other words: "If the owner was unable to comply previously because the statutory requirements did not yet exist, the owner must comply now."

Confusion reigns

The contractors here benefited from confusion over the application of new laws. Of course, much of the favorable outcome can be attributed to good timing rather than legal knowledge. Generally, the best defense against coming out on the losing end of a similar predicament is quality workmanship — and expert legal advice. *T*

The fine line between construction contract and contract of sale

It may seem insignificant, but the legal characterization of a contract can dramatically affect the remedies available in the case of a breach. The plaintiff in *Kevin's Restaurant, LLC v. Fire Tech, Inc.*, can surely attest to this.

Troubles with the hood

Kevin's Restaurant contracted with FireTech to install a hood ventilation system. FireTech quoted a price of almost \$21,000, and the equipment was installed before the restaurant opened.

Soon after the opening, the restaurant experienced problems with the hood system, leading to a two-day shutdown of the business on one occasion. FireTech failed to remedy the problem, and the restaurant hired others to solve it.

Kevin's filed suit, alleging negligent installation of the hood ventilation system. The 21st District Court found the system was not, at least initially, "reasonably fit for ordinary use." Even after repair, the court said, the system's condition continued to diminish its usefulness to the degree that the restaurant would have purchased it only at a lower price.

The court ruled that a price reduction of \$10,000 was an adequate remedy for the restaurant, along with lost profits for the two-day closure.

A question of "redhibition"

Both parties appealed the court's decision. The restaurant wasn't satisfied with the price reduction for the defective system and sought rescission of the sale altogether. FireTech argued that the contract at issue was a construction contract rather than a sale and thus not covered by state laws on "redhibition."

Louisiana law defines "redhibition" as the avoidance of a sale because of a defect that renders the item sold either absolutely useless or so inconvenient and imperfect

that the buyer wouldn't have bought it had he or she known of the defect.

The court rejected the idea that approval for occupancy was the equivalent of finding the hood system free of defects.

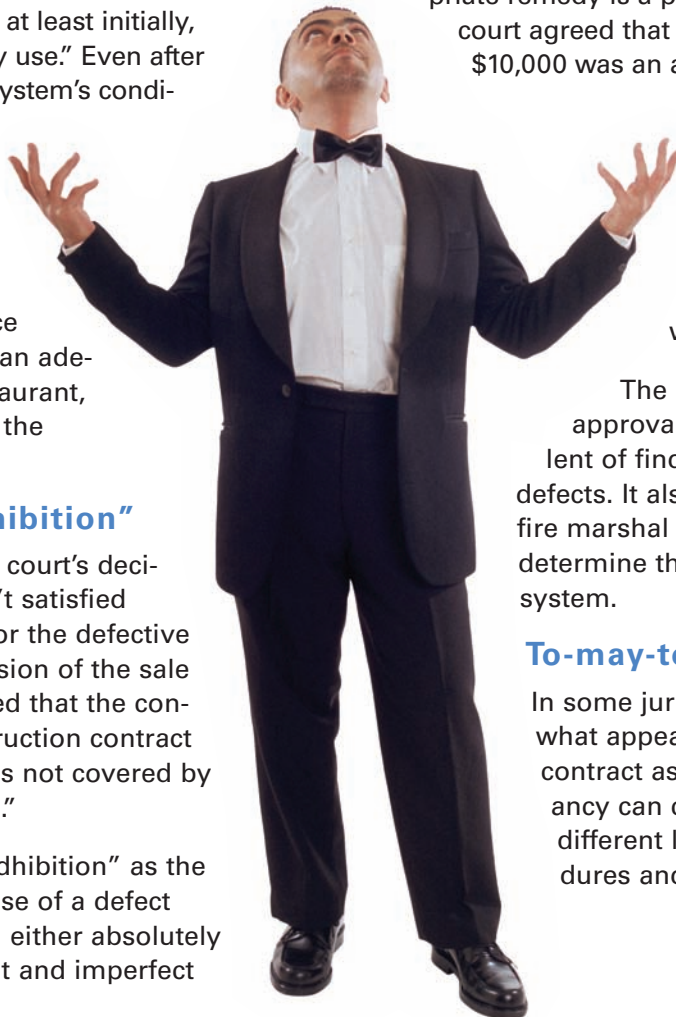
The appellate court held the arrangement was obviously a contract of sale, "whereby a person transfers ownership of a thing to another for a price in money." It explained that, when defects exist that merely diminish the value or usefulness of the thing sold, the appropriate remedy is a price reduction, not rescission. The court agreed that the trial court's reduction of \$10,000 was an adequate remedy.

It's worth noting that FireTech also argued that the trial court erred in finding the hood system defective. After all, it contended, the fire marshal had approved the building (fitted with the system) for occupancy.

The court rejected the idea that approval for occupancy was the equivalent of finding the hood system free of defects. It also dismissed the assertion that the fire marshal held exclusive jurisdiction to determine the existence of any defects in the system.

To-may-to v. To-mah-to

In some jurisdictions, a court may regard what appears on its face to be a construction contract as a contract for sale. The discrepancy can cause critical repercussions, as different laws may trigger different procedures and remedies. ↑



Meeting the specs

Successful bid claims begin with satisfying the proposal

Just as they do with nonpublic projects, contractors bidding on public projects still must meet the bid specifications before they have any legal recourse. A Louisiana construction equipment company was reminded of this in *State Machinery v. Iberville Parish Council*.

Bid history

In early 2005, the town of Iberville published advertisements soliciting bids for the purchase of an excavator and wheel loader. Because the estimated cost of each piece of equipment exceeded \$20,000, the bids were subject to the Louisiana Public Bid Law.

State Machinery submitted a timely bid and came in as low bidder on both items. Nonetheless, Iberville rejected the bids because they didn't satisfy a specification for both pieces that the machine and engine come from the same manufacturer.

Iberville eventually awarded the contract to the next lowest responsive bidder. That bid, which used Volvo equipment, met all of the specifications for both pieces.

State Machinery subsequently sued Iberville, requesting preliminary, permanent and mandatory injunctions and, in the alternative, damages. It alleged that the equipment described in its bid was the "functional equivalent" of the equipment in the bid specifications.

State Machinery also claimed that, because it submitted the lowest responsible and responsive bid, state law required Iberville to award it the contract.

The 18th Judicial District Court ruled in Iberville's favor. It identified several objective reasons for rejecting the bid, including the bidder's failure to satisfy the requirement that the engines and machines be manufactured by the same company.

Louisiana lowdown

Under the Louisiana Public Bid Law, a public entity may reject any and all bids for just cause. And while the law requires a public entity to award a public contract to the "lowest responsible bidder," that doesn't mean the entity must accept the lowest monetary bid. As the court observed, "... simply submitting the

lowest monetary bid will not demonstrate the entitlement to an award of the contract."

Rather, when a bidder seeks injunctive relief from the rejection of its bid, it must show that, in addition to submitting the lowest monetary bid, its bid complied with the advertised specifications. If the bid deviates from those specifications, the bidder must explain the deviations and satisfy the court that the differences are "insignificant, pretextual or insubstantial, and thus could not constitute 'just cause' for rejection."

Obvious deviation

State Machinery's bids consisted of Hyundai machines with Cummins engines — an "obvious deviation" from the specification, in the court's view. State Machinery argued that only Volvo could meet the bid specifications. If so, even though the specifications didn't state a manufacturer by name, the effect was the same as an improper closed-specification bid.

This court had agreed with similar arguments in a 1999 case that State Machinery brought against another Louisiana parish, but it drew distinctions with the current case. The evidence here didn't establish that Volvo equipment was the only type that could meet the specifications.



The court also recognized other reasonable objectives for this equipment, including ease of repair and the ability to service both the engine and the corresponding machine at one location under a single warranty.

In the court's view, the State Machinery equipment wasn't the functional equivalent of the equipment described in Iberville's specifications. On this basis alone, it declared, Iberville had just cause to reject the bid.

A Quixotic pursuit

It's difficult to understand why a company that knew of the just-cause provision would even bother contesting the rejection of a bid that clearly didn't satisfy the specifications. Whatever the case may be, any contractor who is going to assert a closed-specification bid argument should be able to prove that only one type of product can satisfy the specifications. Failing in such an effort could scuttle any attempted claim. *T*

Can claims outlive a statute of limitations?

A statute of limitations typically offers some protection from tardy lawsuits. But it's not unqualified protection. Case in point: *Red Dirt Properties v. Prime Building Co.*, which took place in North Carolina.

The facts on the ground

Prime built a manufacturing facility on Red Dirt's property in 2000. The contract required off-site disposal of brush and stumps cleared from the site.

In November 2000, a subcontractor alerted Red Dirt that clearing and grubbing material may have been buried under an area designated for future expansion. Prime promised to investigate and later assured Red Dirt that there was no issue. The contract was completed in July 2001.

In 2003, a large amount of land-clearing debris was discovered under the soil when Red Dirt began grading in the expansion area. The presence of the material prevented construction of the building, and Red Dirt sued Prime for breach of contract.

Limits on limitations

North Carolina has a three-year statute of limitations for breach of contract actions. In an action for physical damage to property, however, it doesn't start to run until the damage becomes apparent or should reasonably have become apparent to the plaintiff. Red Dirt filed its action more than three years after the contract was completed but within a year of the discovery of the unsuitable debris material.

Prime argued that the statute of limitations started running when the subcontractor gave notice in 2000. The Wake County Superior Court and the North Carolina Court of Appeals both found Prime couldn't wield the statute of limitations defense because of the affirmative assurances it had given Red Dirt at that time.

Specifically, the appeals court found fraud in the inconsistent position subsequently taken by Prime — in other words, that Red Dirt had notice of the hidden defect beneath the soil. The evidence supported a finding that Red Dirt, having relied on Prime's assurances, couldn't have been expected to discover the hidden defect until it launched construction in the expansion area.

The lesson

It appears Prime may have rolled the dice in hopes its breach would evade detection until too late in the game. Let this be a lesson to any contractor prone to such gambles.