SHIELDS MOTT LUND L.L.P.
ATTORNEYS AND COUNSELLORS AT LAW

Louisiana Construction Law and News Update

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Construction Law Update

"Waive" good-bye without lifting a finger

Mutual "waiver of subrogation" clauses in construction contracts are commonplace. Essentially, those clauses provide that in the event one party causes damage to another which is covered by the damaged party's insurance, the damaged party has waived, on behalf of its insurance company, any right of its insurer to subrogate to (or assume) the rights of the injured party to pursue reimbursement from the party which caused the damage. In *Gray Insurance Company v. Old Tyme Builders,* 878 So. 2d 603 (La. App. 1st Cir. 2004), a subcontractor was successful in enforcing to its benefit (and to the benefit of its insurer) a mutual waiver contained in the general contract – that is, the contract between the owner and general contractor to which the subcontractor was not a party. The contract clause at issue – Article 11.3.7 of the A201-1987 (a corresponding provision exists in the 1997 version of A201 at Article 11.4.7) provides that the parties waive rights of subrogation against each other and "any of their subcontractors…" The court interpreted this provision to mean that the parties to the general contract each waived subrogation as regards their *own* subcontractors, and not just the subcontractors and agents of the other party.

There is no explanation from the court why it chose to extend the effect of the waiver as far as it did other than its reliance on the rather broad language contained in the AIA General Conditions. Since contractors and owners can handle the matter of whether they desire to waive subrogation against other parties with whom they contract in the other documents out of which those contracts arise, there appears to be no reason (especially in light of this court decision) for the subject article in A201 to be used in its unaltered form. As the AIA documents declare in the various instruction forms issued by the AIA that the forms are to be amended by the parties to fit the needs of particular projects, owners and contractors should take care to examine the cited provisions and, based in part upon this court decision, actively consider amending the waiver of subrogation to exclude the waiver as it pertains to each party's own subcontractors and agents.

Suppliers' lien preserved despite "abandonment" by intermediate subcontractor

The Louisiana First Circuit Court of Appeal in *Nu-Lite Electrical Wholesalers v. Alfred Palma, Inc.,* 878 So. 2d 660 (La. App. 1st Cir. 2004), ruled that the default by an electrical subcontractor – described by the general contractor as an "abandonment" – did not trigger the running of the thirty or sixty day period within which a material supplier on a private project was required to file its lien. The court interpreted the applicable statute, La. R.S. 9:4822(C)(2), to speak of "abandonment" in terms of abandonment of the entire project and not mere default by a single subcontractor on the work. While the decision is not a landmark in any sense, because it dealt with a 1999 construction project it is potentially problematic for the unwary reader because of changes in the law governing claims by suppliers lacking a direct contract with the general contractor.

Although added in 1999, La. R.S. 9:4802(G)(3) is a relatively overlooked provision. That portion of the Private Works Act (there is a corresponding Public Works Act statute as well) requires a seller of "movables" (that is, a supplier), in order to preserve its lien rights, to provide written notice of non-payment to the general contractor and to the owner "on or before seventy-five days from the last day of the month in which the material was

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Letter From the Partners

We are pleased to deliver to you the latest edition of "Louisiana Construction Law and News Update." This newsletter is provided to keep you and your company current on legal topics that affect the construction industry. The firm hopes you find this information insightful and relevant to your work.

The newsletter is published on a quarterly basis by the firm and is distributed to the construction industry. We encourage suggestions and ideas for articles from our readers so that this publication can be as current and useful as possible.

We appreciate the opportunity to provide this newsletter to you. If you know of others in the industry whom you think might enjoy receiving the publication, please let us know so that we can add them to our industry list.

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Surety Decisions and Non-Louisiana Cases

Angelo Iafrate Construction, LLC v. Potashnick Construction, Inc., 370 F. 3d 715 (8th Cir. 2004)

A district court entered partial summary judgment in favor of the surety on claims by a road surfacing contractor against the performance and payment bond provided on behalf of a road grading contractor for an Arkansas State Highway Commission project. Delays caused by the grading contractor ultimately operated to the detriment of the road surfacing contractor's work, which work was being performed under a separate and distinct general contract. The court of appeals affirmed the trial court's finding that the surety had no duty under the performance bond to disclose knowledge of its principal's (the grading contractor) potential financial difficulties prior to that contractor's default. Additionally, although the surety escaped liability in the trial court on the basis of the court's finding that the surety had undertaken in a reasonable manner to complete the grading work following the principal's default, the court of appeals took that ruling an additional step by declaring that neither the performance nor payment bond contemplated the road surfacing contractor as a potential beneficiary under the bond. Finally, the court refused to overturn the trial court's refusal to impose liability upon the surety based on a default judgment taken against its principal, focusing in large part upon the fact that the surety had obtained a judgment in its favor before the default judgment was rendered against the grading contractor.

120 Greenwich Development Associates, LLC v. Reliance Insurance Company, 2004 WL 1277998 (S.D.N.Y.)

Defendant performance bond surety successfully opposed claims against it on the basis that the plaintiff failed to comply with the notice requirements of the bond. Ultimately, the plaintiff's demand of more than $6,800,000.00 in damages based upon several alleged defaults by the contractor/principal was dismissed.

The surety asserted several defenses, including that the action against it was time barred, having been commenced more than two years following the contractor's cessation of work on the project (the bond was a AIA form A312 bond). The court rejected this defense based upon disputed material facts, and similarly rejected the surety's argument that the obligee waived its rights under the bond when it unilaterally took certain steps in response to various shortcomings in the contractor's performance. Factual discrepancies also precluded summary judgment based upon a defense that the surety could not perform its obligations under its bond because of failure of notice from the obligee.

However, based upon the provisions in paragraph 3 of the bond – which provisions the court characterized as "conditions precedent" to the obligations of the surety under the bond – the court dismissed the suit on the basis that the obligee failed to provide the required notice. The surety bond provided that the surety's obligation under the bond "shall arise after" the obligee took certain steps detailed in the bond, including providing the surety with proper notification of the proposed default, requesting a meeting with the contractor and surety to resolve the problem, formal declaration of default and termination of the contractor's right to complete the contract and either payment of the balance of the contract price to the surety or selection of another contractor to complete the construction contract.

Appeal of Clauss Construction, 2004 WL 1080493 (ASBCA No. 53,953)

Claimant appealed the rejection by the Army Corps of Engineers for a constructive change related to the ACOE's refusal to allow the contractor to take advantage of certain salvageable materials during a demolition project. The contract in question gave the contractor title to the salvage property (including HVAC equipment, toilets, sinks, tubs, doors, windows and flooring). The Board of Contract Appeals held that a constructive change entitles the contractor to an equitable adjustment, even if the lost salvage rights are merely those of a subcontractor sponsored by the prime contractor (and despite the fact that the general contractor bid the project based upon an in-house salvage estimate and not subcontractor bids).

Associated Glass, Ltd. v. Eye Ten Oaks Investments, Ltd., 147 S.W. 3d 507 (Tex.App.-San Antonio 2004)

Noting that Texas law favors the joint resolution of multiple claims in order to prevent multiple determinations of the same matter, the court granted the relief sought by two subcontractors seeking to compel an owner (with whom the subcontractors were not in privity of contract) to arbitrate its disputes against the subcontractor. In the matter, the

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delivered…" Failure to provide the notice entails that the "seller shall lose his right to file a privilege or lien on the immovable property." It should be noted that the seventy-five day requirement applies only to projects for which the general contract is recorded.

Statutory employer status declared in an addendum to contract upheld by court

On the construction of a pipeline, the pipeline owner and contractor entered into an addendum to the general contract declaring a statutory employer relationship between the owner and the general contractor's employees. Plaintiff filed suit against the owner in tort alleging that the statutory employer designation should be held invalid for two reasons:

- The addendum should not be considered a part of the general contract; and
- The work in question should not be deemed to be a part of the owner's trade, business or occupation under the applicable statute, La. R.S. 23:1061.

Ruling in favor of the owner and dismissing the tort claim, the court in *Trent v. PPG Industries, Inc*., 865 So. 2d 1041 (La. App. 3rd Cir. 2004), held, first, that the plaintiff failed to rebut the testimony of representatives for both owner and contractor that the addendum was intended to be a part of the general contract. Second, the court noted that a proper declaration of a statutory employer relationship, per the cited statute, creates a presumption – albeit a rebuttable one – of a statutory employer relationship between the principal (here, the owner) and the contractor's employees. The court then examined evidence presented by the plaintiff attempting to show that the work was not an integral part of or essential to the ability of the owner to generate its principal goods, products or services, but found that the plaintiff failed to meet its burden of proof (noting that the construction, essentially, was directly related to the ability of the owner to conduct its business).

Special language should be placed in all construction contracts in order to take advantage of the statutory exclusion which protects both parties to the contract from tort liability to one of the opposite party's employees.

Completed operations coverage requires liability insurer to defend pile driver

In *Rando v. Top Notch Properties, L.L.C.*, 879 So. 2d 821, La. App. 4th Cir. 2004), the court of appeal reversed a summary judgment in favor of a liability insurer on claims by its insured asserting a demand for indemnity, defense and damages for bad faith failure to defend and provide coverage. After a painstaking review of the policy language, the court held that the claim for damage to an air conditioning system (that is, work other than that of the pile driver), which damages were alleged to have occurred during the policy period, triggered the duty to defend and potential coverage under the policy because the work of the pile driver was "completed" as contemplated by the policy provisions. While the typical work-product exclusion in a liability policy would exclude coverage for the cost to cure work improperly performed by the pile driver or the damage to the property caused thereby, the "products-completed operations" coverage was deemed to be an exception to the standard "work product" exclusion. The court noted at the outset of its decision that it shared the concern expressed by authors of a learned treatise on insurance that often courts misapply policies "…by seizing upon conclusions in earlier cases without realizing that the policy language had been revised" (citing to McKenzie and Johnson, 15 Civil Law Treatise (2nd Ed. 1996)).

Recent Decisions on Toxic Mold Claims

Smith v. State Farm Insurance Company, 869 So. 2d 909 (La. App. 4th Cir. 2004).

Following the infamous New Orleans area hailstorm of January 23, 2000, plaintiffs made a roof damage claim to their property insurer. Roof repairs were made to the property on two separate occasions, although leaks continued to manifest themselves, causing water damage to the home. Eventually, the plaintiffs noticed the growth of mold and notified the insurer, which retained a consulting group to inspect the property for the presence of mold. In September of 2001, the consultant inspected the property and reported the results to the insurer only. Six months later – in March of the next year – the insurer notified the plaintiffs that the inspection confirmed "the presence of toxic mold."

Based upon the passage of time from the inspection until the reporting of the purportedly toxic substance, the plaintiffs sued the insurer and the consultant for failing to warn plaintiff of the mold, and, as regards the consulting group, for falling below the standard of care required of such groups. The consultant sought summary judgment and was dismissed from the case by the trial court. The court of appeal, in affirming the dismissal of the consultant, held that the contract solely between the insurer and the consultant was not a contract which provided a *stipulation pour autrui,* or a third party benefit, to the plaintiff. Concurrently, the court rejected plaintiff's arguments that a unique relationship existed between the consultant and the plaintiff which created a duty of the consultant to inform the plaintiff regarding the consultant's findings. The case noticeably lacks any mention of ill health effects suffered by the plaintiff or his family, or an indication that expert testimony was received regarding what negative health effects might result from exposure to "toxic" mold, or a discussion of when the duty of a consulting firm with a knowledge of an actual potential hazard would arise.

News and Notes

The Daily Journal of Commerce reported in its December 22, 2004, edition that the construction industry outlook for 2005 is "good," noting that the industry appeared to have found the light at the end of the proverbial tunnel during 2004. The DJC cited the 29th annual "CIT Construction Industry Forecast" as its source, a study performed by financial services provider CIT Equipment Finance. The article indicated that two thirds of the regions surveyed showed "increased optimism" for growth in 2005, including the areas encompassing Louisiana's west south central region and Mississippi's east south central region. The forecast projected new equipment purchases to more than double the average for those in 2004, with average median sales volume for contractors to increase 11%. The article also noted a significant increase in contractors shifting their focus from residential to commercial construction, with 21% of contractors responding declaring commercial construction to be their niche for 2005 (as opposed to 15% in 2004).

Happy New Year!!

Upcoming Construction and Labor Law Seminars

Shields Mott Lund L.L.P. is pleased to announce these upcoming seminars presented by its lawyers:

The ABC's of Contract Review and Negotiating for Construction Professionals (Lorman Education Services), February 16, 2004, New Orleans, Louisiana, 8:30 am – 4:30 pm)

Construction Delay Claim Seminar (Lorman Education Services), February 23, 2005, New Orleans, Louisiana, 9:00 am – 4:30 pm

Zoning, Subdivision and Land Development Law (Lorman Education Services), April 7, 2005, New Orleans, Louisiana, 9:00 am – 4:30 pm

Employment Related Records (Lorman Education Services), April 27, 2005, New Orleans, Louisiana, 9:00 am – 4:30 pm

Development, Implementation and Legal Issues of Construction Scheduling (Lorman Education Services), May 12, 2005, New Orleans, Louisiana, 9:00 am – 4:30 pm

Employee Discharge and Documentation (Lorman Education Services), July 13, 2005, New Orleans, Louisiana, 9:00 am – 4:30 pm

These seminars are designed to address the legal issues that the construction industry faces and to zero in on the options that make the best legal sense. Understanding these issues and choices and being prepared for potential problems are the best ways to avoid pitfalls. We sincerely hope you can attend one of these seminars. Additional information on the seminars can be obtained by contacting Dan Lund at Shields Mott Lund (504-581-4445) or Lorman on-line at www.lorman.com.

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owner had filed suit in court against the general contractor and the general contractor filed third party claims against two subcontractors seeking contribution from them. The owner then sued the subcontractors directly in tort (*i.e.*, negligence) for their work on the project.

Overruling the owner's defense that it could not be bound by the arbitration agreements because it was not a party to the subcontracts, the court found that the owner could be required to arbitrate because the owner asserted claims which required "reliance on the terms of the written agreement containing the arbitration provision." The court found that all the factual allegations regarding the tort claims arose out of or were related to the duties of the subcontractors under the subcontracts, and bound the owner to the arbitration clauses therein contained. The court also ultimately required that the third party claims of the general contractor against the subcontractors be arbitrated (a result more obviously entailed by the fact of the existence of a contract between the parties and containing an arbitration clause).

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