



INTRODUCTION

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INTRODUCTION

This Compendium, prepared by the Construction Practice Group of ALFA International, was designed to serve as a single resource for ALFA clients regarding important construction law issues. This Compendium provides a synopsis of significant case law or statutes involving:

Mechanic's Lien Basics
Statutes of Limitation and Repose
Pre-suit Notice of Claim and Opportunity to Cure
Insurance Coverage and Allocation Issues
Contractual Indemnification
Contingent Payment Agreements
Damage Limitations
Case Law and Legislation Update

This Compendium should allow quick access to the relevant statutes and/or leading cases in each jurisdiction regarding these important topics and issues.

The Construction Practice Group Steering Committee communicated with our Client Advisory Board to determine issues of interest and subsequently communicated with all ALFA member firms in order to obtain information to compile this complete resource for your use.

We extend our thanks to our Client Advisory Board and to all contributing ALFA firms. This massive undertaking by the Construction Practice Group could not have been completed without their assistance.

The Construction Practice Group of ALFA hopes that the Compendium will be used frequently by you as a quick and easy reference for special construction law related issues. We are interested in any comments or feedback you wish to give us regarding this or future compendiums or topics that may be of interest to clients and counsel.

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I. Mechanic's Lien Basics

The Alabama mechanic's lien statute distinguishes between persons in privity of contract with the owner and lower-tier contractors and suppliers not in privity with the owner. Contractors in privity with the owner have "full price" lien rights.¹ Lower-tier contractors and suppliers not in privity with the owner have "unpaid balance" lien rights.² A "full price" lien is a lien to the full extent of the price of the prime contract with the owner. An "unpaid balance" lien is limited to the amount of the unpaid balance of the prime contract at the time the lienholder gives written notice of intent to lien.³ The notice and procedural requirements differ for full price and unpaid balance liens. Because mechanics' liens are not recognized in the common law or in equity, strict compliance with the notice and procedural requirements of the mechanic's lien statute is required.⁴

A. Requirements

1. Full Price Liens

Persons with a direct contractual relationship with the owner ("original contractors") have a right to a lien in the full amount of their contract with the owner, which is known as a "full price" lien. Material suppliers not in privity with the owner ordinarily have "unpaid balance" lien rights, but they may elevate their status from "unpaid balance" lienholder to "full price" lienholder by providing written notice to the owner in accordance with ALA. CODE § 35-11-210 before delivering any materials to the project site. Otherwise, there is no requirement that original contractors give written notice to the owner before filing a verified statement of lien.

¹ ALA. CODE § 35-11-210 (1975).

² *Id.*

³ *Valley Joist, Inc. v. CVS Corp.*, 954 So. 2d 1115 (Ala. Civ. App. 2006).

⁴ *Davis v. Gobble-Fite Lumber Co.*, 592 So. 2d 202 (Ala. 1991); *Hartford Accident & Indem. Co. v. American Country Clubs, Inc.*, 353 So. 2d 1147 (Ala. 1977).

To perfect a full price lien, the original contractor or the supplier who has given notice under ALA. CODE § 35-11-210 must file a verified statement of lien in the probate court in the county in which the work was performed.⁵ The verified statement of lien must be filed within six months after the last item of work was performed or the last item of material was furnished.⁶

2. Unpaid Balance Liens

Persons who are not in privity of contract with the owner, including materials suppliers who have not given advance notice under Alabama Code § 35-11-210, have unpaid balance lien rights. Unpaid balance lienholders must file a verified statement of lien in the probate court for the county in which the work was performed within four months of the date they last performed work or delivered material to the site.⁷ Before filing the verified statement of lien, unpaid balance lien claimants must notify the owner and construction lender in writing of their intent to file a lien. The requirements for this notice are set forth in Alabama Code § 35-11-218.

3. Filing Suit to Enforce the Lien

After the lien statement has been filed in probate court, original contractors and unpaid balance lienholders must file suit to enforce the lien within six months of the maturity of the entire indebtedness.⁸ To enforce the lien, the lien claimant must obtain a money judgment against the person or entity from whom the money is owed.⁹

B. Ability to Waive and Limitations on Lien Rights

The lien created by the Alabama statute may be subordinated, waived, or released by contract.¹⁰ Nevertheless, if a claimant has followed the formalities for obtaining a lien, it is presumed that the right to the lien exists. In that case, the burden is on the defendant to prove that the claimant knowingly surrendered or waived its lien.¹¹ An original contractor may also waive a lien if he fails to furnish to the owner a list of all materialmen, laborers, and employees who have provided labor or material to the project, pursuant to ALA. CODE § 35-11-219.

II. Statutes of Limitation and Repose

A. Statutes of Limitations

The time limitation for commencing actions against architects, contractors, and engineers for damage or injury as a result of defective design or construction is two years from the date the cause of action accrues.¹² A cause of action accrues when the damage or injury occurs, or in the case of latent defects, when the damage or injury is, or reasonably should have been, discovered.¹³ A cause of action accrues whether or not the full amount of damages is apparent at

⁵ ALA. CODE § 35-11-213.

⁶ ALA. CODE § 35-11-215; *Southern Sash of Huntsville, Inc. v. Jean*, 235 So. 2d 842 (Ala. 1970).

⁷ ALA. CODE § 35-11-215.

⁸ ALA. CODE § 35-11-221.

⁹ *Ex parte Grubbs*, 571 So. 2d 1119 (Ala. 1990).

¹⁰ *Vulcan Painters v. MCI Constructors*, 41 F.3d 1457 (11th Cir. 1995); *Ex parte Renovations Unlimited, LLC* 59 So. 3d 679 (Ala. 2010).

¹¹ *See Noland Co. v. Southern Dev. Co.*, 445 So. 2d 266 (Ala. 1984).

¹² ALA. CODE § 6-5-221(a).

¹³ *See* ALA. CODE § 6-5-220(e); *Jones v. Kassouf & Co., P.C.*, 949 So. 2d 136 (Ala. 2006).

the time of the first injury or damage.¹⁴ The time a cause of action accrues cannot be extended by the notion of a continuous wrong.¹⁵

ALA. CODE §6-5-221 applies to all claims for design or construction defects, regardless of legal theory. Otherwise, the statute of limitations for breach of a contract not under seal is six years¹⁶, breach of warranty involving the sale of goods is four years¹⁷, and negligence and fraud is two years¹⁸.

B. Statutes of Repose

The Alabama statute of repose for claims involving defective design or construction is seven years after substantial completion, unless the architect, engineer or builder had actual knowledge of the design or construction defect before the seven year period of repose expired and failed to disclose it.¹⁹

III. Pre-Suit Notice of Claim and Opportunity to Cure

Alabama does not have a “right to cure” or “right to repair” statute for construction defects.

IV. Insurance Coverage and Allocation Issues

There is a substantial body of law in Alabama addressing the kinds of insurance ordinarily involved in construction, including builder’s risk and other forms of property insurance, commercial general liability (“CGL”) insurance, excess and umbrella coverages, professional liability insurance, worker’s compensation and employer liability insurance and business interruption insurance.

A. General Coverage Issues

Generally, an insurer's duty to defend is determined by the allegations of the complaint. However, when the insurer is uncertain as to what the complaint is alleging, the insurer has a duty to investigate the facts surrounding the incident to determine its duty to defend.²⁰ The insurer’s duty to defend is broader and more extensive than its duty to indemnify.²¹

Damage or injury caused by defective construction or poor workmanship may be covered by a CGL policy in Alabama.²² Alabama courts have recognized that, under a CGL policy, poor workmanship can lead to an “occurrence” depending “on the nature of the damage” resulting

¹⁴ See *Dickinson v. Land Developers Constr. Co.*, 882 So. 2d 291 (Ala. 2003).

¹⁵ ALA. CODE § 6-5-220.

¹⁶ ALA. CODE § 6-2-34(4).

¹⁷ ALA. CODE § 7-2-725(1).

¹⁸ ALA. CODE § 6-2-38(l).

¹⁹ ALA. CODE § 6-5-221(a).

²⁰ *Great American Ins. Co. v. Baddley and Mauro, LLC*, 330 Fed.Appx. 174 (11th Cir. 2009); *Perkins v. Hartford Ins. Group*, 932 F.2d 1392 (11th Cir. 1991); *Porterfield v. Audubon Indem. Co.*, 856 So.2d 789 (Ala. 2002); *Blackburn v. Fidelity & Deposit Co.*, 667 So. 2d 661, 668 (Ala. 1995).

²¹ *United States Fid. & Guar. Co. v. Armstrong*, 479 So.2d 1164, 1168 (Ala. 1985).

²² See *U.S. Fid. and Guar. Co v. Bonitz Insulation Co.*, 424 So. 2d 569 (Ala. 1982).

from the occurrence.²³ Among other formulations, “faulty workmanship may lead to an occurrence if it subjects personal property or other parts of the structure to ‘continuous or repeated exposure’ to some other ‘general harmful condition.’”²⁴ Faulty workmanship itself, however, is not “property damage” “caused by” or “arising out of an occurrence.”²⁵ Coverage may exist for property damage accidentally caused by or resulting from faulty workmanship, but not for the faulty workmanship itself.²⁶

Where poor workmanship leads to an occurrence and property damage, the insured may still have to overcome the “Your Work” exclusion to obtain CGL coverage. The Alabama Supreme Court has recognized that a standard “Your Work” exclusion in a CGL policy applies only where the damage in question was both damage to the contractor’s work *and* damage included in the products-completed operations hazard.²⁷ If the policy provides for products-completed operations coverage, however, then the “Your Work” exclusion does not apply.²⁸ In addition, the “Your Work” exclusion combined with a “subcontractor exception” results in no coverage for damage caused by the insured contractor’s own forces, but allows coverage for damage caused by any subcontractors.²⁹

B. Trigger of Coverage and Notice

There are two main types of policies, “claims-made” policies and “occurrence” policies. The primary difference between these types of policies relates to the timing of coverage. A claims-made policy provides coverage for claims asserted during the policy period, regardless of when the accident or other loss occurred.³⁰ A claims-made policy is triggered when the claimant notifies the insurer of the claim.

An occurrence policy provides coverage for all losses that take place during the policy period, regardless of when the claim is made.³¹ An occurrence is deemed to have taken place when the claimant was damaged, not when the event causing the damage occurred.³²

An insurance policyholder must give notice within a reasonable time, if required by the insurance policy. When asserting a late notice defense, an insurer is not required to show prejudice resulting from a policyholder’s delay in giving notice.³³ The reason for the delay and the length of the delay in providing notice are factors considered by the court in determining whether notice was timely given.³⁴

²³ *Owners Ins. Co. v. Jim Carr Homebuilder, LLC*, --- So.2d---, 2014 WL 1270629 at *4 (Ala. 2014)(citing *Town & Country Prop., LLC v. Amerisure Ins. Co.*, 111So.3d 699, 705 (Ala. 2011)).

²⁴ *Id.* at *5(citing *Town & Country Prop., LLC*, 111 So.3d at 706).

²⁵ *Id.* at *6.

²⁶ *Id.* at *5 (citing 9A *Couch on Insurance* § 129:4 (3d ed. 2005)).

²⁷ *Id.* at *7.

²⁸ *Id.*

²⁹ *Town & Country Prop., LLC*, 111 So.3d at 703.

³⁰ *Attorneys Ins. Mut. of Alabama, Inc. v. Smith, Blocker & Lowther, P.C.*, 703 So. 2d 866 (Ala. 1996).

³¹ *Id.*

³² *United States Fidelity & Guaranty Co. v. Warwick Dev. Co.*, 446 So. 2d 1021 (Ala. 1984).

³³ *U.S. Fid. and Guar. Co. v. Baldwin County Home Builder’s Ass’n*, 770 So. 2d 72 (Ala. 2000); *Southern Guaranty Ins. Co. v. Thomas*, 334 So. 2d 879 (Ala. 1976). *But see Midwest Employers Cas. Co. v. East Alabama Health Care*, 695 So. 2d 1169 (Ala. 1997) (holding that an excess insurance carrier must show prejudice).

³⁴ *U.S. Fid. and Guar. Co.*, 770 So. 2d 72.

C. Allocation Among Insurers

Where two or more insurers cover the same interest, subject matter, and risk, each will be liable for the percentage of total damages represented by that insurer's limits to the combined policy limits.³⁵ In exposure cases, when a defense arises under multiple policies, defense costs are to be apportioned pro rata among the carriers based upon the time on the risk.³⁶

V. Contractual Indemnification

Alabama does not have an anti-indemnity statute. In Alabama, when two parties "knowingly, evenhandedly, and for valid consideration" enter into an agreement in which one party, through "clear and unequivocal language," agrees to indemnify the indemnitee for its own wrongdoings, the indemnity provisions will be read and construed so as to give them the meaning the parties have expressed.³⁷ But these provisions are only enforceable if (a) "the contract clearly indicates an intention to indemnify against the consequences of the indemnitee's negligence," (b) "such provision was clearly understood by the indemnitor," and (c) "there is not shown to be evidence of a disproportionate bargaining position in favor of the indemnitee."³⁸

Alabama does not recognize comparative fault, common-law indemnity, or contribution,³⁹ but parties may agree to apportion their respective liability in an indemnification provision.⁴⁰ Nonetheless, indemnity provisions that assign percentages of fault for injuries or damages must be carefully drafted.

VI. Contingent Payment Agreements

Alabama courts treat "pay when paid" and "pay if paid" clauses somewhat differently. "Pay when paid" clauses do not make the contractor's receipt of payment from the owner a condition precedent to the contractor's payment to the subcontractor; rather, these clauses serve as a timing mechanism for payment. Under a "pay when paid" clause, the contractor cannot delay payment to a subcontractor indefinitely. A contract containing a "pay when paid" clause obligates the contractor to pay the subcontractor within a reasonable time.⁴¹ In addition, a "pay when paid" clause cannot be asserted by a payment bond surety as a defense to a claim against the payment bond.⁴²

"Pay if paid" clauses, on the other hand, condition the contractor's payment to the subcontractor on first receiving payment from the owner for the work performed by the subcontractor. Alabama courts will enforce a carefully drafted "pay if paid" clause according to

³⁵ *Nationwide Mut. Ins. Co. v. Hall*, 643 So. 2d 551 (Ala. 1994).

³⁶ *Commercial Union Ins. Co. v. Sepco Corp.*, 765 F.2d 1543 (11th Cir. 1985).

³⁷ *See Holcim (US), Inc. v. Ohio Cas. Ins. Co.*, 38 So. 3d 722 (Ala. 2009).

³⁸ *Indus. Tile, Inc. v. Stewart*, 388 So. 2d 171, 175 (Ala. 1980).

³⁹ *Humana Med. Corp. v. Bagby Elevator Co.*, 653 So. 2d 972 (Ala. 1995); *Parker v. Mauldin*, 353 So. 2d 1375 (Ala. 1977).

⁴⁰ *Holcim*, 38 So. 3d at 728-29.

⁴¹ *Federal Ins. Co. v. I. Kruger*, 829 So. 2d 732 (Ala. 2002).

⁴² *Id.*

its terms, but the clause should state explicitly that the owner's payment to the contractor is an express condition precedent to the contractor's obligation to pay its subcontractor.⁴³

VII. Damage Limitations

A. Attorney's Fees

In general, attorney's fees will only be awarded to the prevailing party as an element of damages when authorized by statute or case law, provided for in a contract, or otherwise allowed during an equitable proceeding.⁴⁴ Alabama's prompt payment law, the "Deborah K. Miller Act," provides that in a civil action for violation of the prompt payment law, the prevailing party may recover reasonable attorneys' fees.⁴⁵

B. Consequential Damages

As in all contract cases in Alabama, damages must be reasonably certain to support an award. To recover consequential damages, the claimant must prove that the damages were reasonably within the contemplation of the parties at the time of contracting.⁴⁶ But the claimant may only recover consequential damages to the extent they are "capable of ascertainment with reasonable, or sufficient, certainty."⁴⁷ Lost profits that are speculative or remote are usually not recoverable.⁴⁸

C. Delay and Disruption Damages

Liquidated damages provisions will be enforced by the courts if they are construed as reasonable attempts to measure prospective damages rather than a penalty. One seeking to enforce a liquidated damages provision must prove that (a) the liquidated amount is reasonable and (b) the nature and amount of the damages resulting from the delay were not capable of adequate computation at the time of contracting.⁴⁹ If the evidence shows that a liquidated damages clause was intended to compel or incentivize timely completion instead of intended to compensate for delay damages, the clause may be stricken as an unenforceable penalty.⁵⁰

A contractor seeking delay damages from an owner must prove the extra costs were incurred as a result of the owner's breach or action which gave rise to a breach claim or a claim for equitable adjustment.⁵¹ Where the total amount of damages is comprised of amounts for which both the owner and the contractor are responsible, the contractor must provide a reasonable basis for apportioning the extra costs.⁵²

⁴³ *Lemoine Co. v. HLH Constructors, Inc.*, 62 So.3d 1020, 1026 (Ala. 2010).

⁴⁴ *Shelby County Comm'n v. Smith*, 372 So. 2d 1092 (Ala. 1979).

⁴⁵ ALA. CODE § 8-29-6.

⁴⁶ *HealthSouth Rehab. Corp. v. Falcon Mgmt. Co.*, 799 So. 2d 177 (Ala. 2001).

⁴⁷ *Goolesby v. Koch Farms, LLC*, 955 So. 2d 422 (Ala. 2006).

⁴⁸ *Paris v. Buckner Feed Mill, Inc.*, 182 So.2d 880, 882 (Ala. 1966).

⁴⁹ See *Stonebrook Dev., L.L.C. v. Matthews Bros. Const. Co.*, 985 So. 2d 960 (Ala. Civ. App. 2007) (quoting *Camelot Music, Inc. v. Marx Realty & Improvement Co.*, 514 So. 2d 987 (Ala. 1987)).

⁵⁰ *Southern Elec. Corp. v. Utilities Bd.*, 643 F.Supp.2d 1302, 1307-08 (S.D. Ala. 2009).

⁵¹ *U.S. For Use and Benefit of Gray-Bar Elec. Co., v. J.H. Copeland & Sons Constr., Inc.*, 568 F.2d 1159 (5th Cir. 1978).

⁵² *Id.*

A no-damages-for-delay clause is enforceable in Alabama, apparently subject to certain exceptions such as delays not contemplated by the parties or active interference with performance.⁵³

D. Economic Loss Rule

Alabama recognizes the economic loss rule as a bar to certain tort actions where a defective product damages itself but does not cause personal injury or damage to any other property.⁵⁴ That said, the Supreme Court has refused to apply the rule in commercial construction cases.⁵⁵

E. Interest

Whether a claimant can recover interest in addition to the damages awarded depends largely on the ability to determine the underlying damages with certainty. For instance, where the measure of damage cannot be determined with certainty or is discretionary, prejudgment interest cannot be awarded.⁵⁶

Yet, where the damages can be ascertained with some certainty, a successful claimant may receive interest in addition to the damages already awarded. In tort cases, the interest is measured from the date of the injury and is assessed at the statutory rate.⁵⁷ In contract cases, the damages may be increased by the contractual interest rate from the date of the breach until recovery.⁵⁸ Where no contractual interest rate is stated, the statutory rate is applied.⁵⁹

Under Alabama's prompt payment law, the Deborah K. Miller Act, an owner, contractor or subcontractor who fails to make payments in accordance with the Act owes twelve percent interest, per annum, on the amount owed.⁶⁰

F. Punitive Damages

Alabama does not allow punitive damages in cases of breach of contract or simple negligence.⁶¹ Punitive damages are not recoverable as a matter of right unless provided by statute.⁶² Except in wrongful death actions, punitive damages are awarded for tort claims where plaintiff proves by clear and convincing evidence that the defendant consciously or deliberately engaged in statutorily defined "oppression, fraud, wantonness or malice" toward the plaintiff.⁶³

⁵³ *RaCON, Inc. v. Tuscaloosa County*, 953 So.2d 321 (Ala. 2006); *E.C. Ernst, Inc. v. Manhattan Constr. Co.*, 387 F.Supp. 1001 (S.D.Ala. 1974), *aff'd in part, vacated in part*, 551 F.2d 1026, 1029 (5th Cir. 1977), *cert denied*, 434 U.S. 1067 (1978).

⁵⁴ *Vesta Fire Ins. Corp. v. Milam & Co. Constr., Inc.* 901 So. 2d 84 (Ala. 2004).

⁵⁵ *Pub. Bldg. Auth. v. St. Paul Fire and Marine Ins. Co.*, 2010 WL 3937962 (Ala. 2010).

⁵⁶ *Goolsby*, 955 So. 2d at 429.

⁵⁷ *See Nelson v. AmSouth Bank, N.A.*, 622 So. 2d 894 (Ala. 1993); *see also* ALA. CODE § 8-8-10.

⁵⁸ *See Hunt v. Ward*, 79 So. 2d 20 (Ala. 1955).

⁵⁹ ALA. CODE § 8-8-10.

⁶⁰ ALA. CODE § 8-29-5.

⁶¹ *Exxon Mobil Corp. v. Alabama Dep't of Conservation and Natural Res.*, 986 So. 2d 1093 (Ala. 2007); *Bradley v. Walker*, 93 So. 634 (Ala. 1922).

⁶² *Alabama Power Co. v. Rembert*, 208 So. 2d 205 (Ala. 1968).

⁶³ ALA. CODE § 6-11-20(a).

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I. CONTRACT IS “KING”

The Arizona Supreme Court has accepted quite a number of construction-related cases recently and essentially ruled that Arizona courts will enforce the parties' contracts.¹ However, manipulation of contract arrangement(s) will not be permitted to thwart a residential buyer's implied warranty rights against the builder for construction defects.²

II. MECHANICS' LIEN AND STOP NOTICE BASICS

A. Mechanics' Lien Statutes

Unpaid providers of services, labor, materials, fixtures and equipment used for construction of improvements to real property in Arizona have the opportunity to secure payment through placement of a mechanics' lien on the improved property.³ A perfected mechanics' lien can be foreclosed on, compelling the sale of the improved property to generate funds to pay lienholders. A payment bond may be substituted for the lien right.⁴

Mechanics' liens are creatures of statute that are available only on private construction projects, and which are granted preferential rights over certain other encumbrances.⁵ However, mechanics' liens may be obtained against owner-occupied dwellings only where the lien claimant contracts in writing directly with the owner-occupant.⁶

Lien claims should be processed with care as property owners can sue for damages resulting from the recording of an invalid mechanics' lien.⁷

B. Requirements for Imposing a Mechanics' Lien

To impose a valid mechanics' lien, the lienor must:

1. Have a written contract with the owner, or with an architect/engineer or general contractor who has an agreement with the owner, or for mechanics' liens against owner-occupied dwellings, have a written agreement directly with the owner-occupant;⁸
2. Have a contracting license where required, or registration, in the case of an architect or engineer;⁹ and

3. Timely comply with the statutes requiring a preliminary 20-day notice and proof of service.¹⁰ (See Section D *infra*.)

C. Stop Notices

In addition to mechanics' liens, which essentially allow resort to a foreclosure sale of the lien property, Arizona law also provides for stop notices to the project owner or the construction lender that can tie up project funds until the claimant is paid.¹¹ A stop notice claimant must comply with the 20-day pre-lien notice statute, and serve the stop notice by the statutory deadlines for notices and claims of lien.¹² As with mechanics' liens, stop notices apply only to private projects.

D. The Pre-Lien Notice

The pre-lien notice must be given no later than 20 days after beginning work or supplying material.¹³ If more than 20 days passes, a pre-lien notice can still be given to secure payment for services, materials or equipment provided to the site during the past 20 days and thereafter.¹⁴ Owners receiving a 20-day pre-lien notice should require waivers from all noticing parties before paying their contractor.

The format for the pre-lien notice is prescribed by statute, which specifies that the pre-lien notice substantially follow the format below:¹⁵

Arizona Preliminary Twenty Day Lien Notice

In accordance with Arizona Revised Statutes § 33-992.01, this is not a lien. This is not a reflection on the integrity of any contractor or subcontractor.

The name and address of the owner or reputed owner are:

This preliminary lien notice has been completed by (name and address of claimant):

Date: _____

By: _____

Address: _____

The name and address of the original the contractor are: will

You are hereby notified that claimant has furnished or

furnish labor, professional services, materials, machinery, fixtures or tools of the following general description:

The name and address of any lender or reputed lender and assigns are: structure or

In the construction, alteration or repair of the building,

improvement located at:

The name and address of the person with
whom the claimant has contacted are:
certain lot(s)

And situated upon that

or parcel(s) of land in _____
County, Arizona, described as
follows:

An estimate of the total price of the
labor, professional services,
materials, machinery, fixtures or
tools furnished or to be furnished is:
\$ _____

(The following statement shall be in bold-faced type.)

Notice to Property Owner

If bills are not paid in full for the labor, professional services, materials, machinery, fixtures or tools furnished, or to be furnished, a mechanic's lien leading to the loss, through court foreclosure proceedings, of all or part of your property being improved may be placed against the property. You may wish to protect yourself against this consequence by either:

1. Requiring your contractor to furnish a conditional waiver and release pursuant to [Arizona Revised Statutes § 33-1008, subsection D](#), paragraphs 1 and 3 signed by the person or firm giving you this notice before you make payment to your contractor.

2. Requiring your contractor to furnish an unconditional waiver and release pursuant to [Arizona Revised Statutes § 33-1008, subsection D](#), paragraphs 2 and 4 signed by the person or firm giving you this notice after you make payment to your contractor.

3. Using any other method or device that is appropriate under the circumstances.

(The following language shall be in type at least as large as the largest type otherwise on the document.)

Within ten days of the receipt of this preliminary twenty day notice the owner or other interested party is required to furnish all information necessary to correct any inaccuracies in the notice pursuant to Arizona Revised Statutes § 33-992.01, subsection I or lose as a defense any inaccuracy of that information.

Within ten days of the receipt of this preliminary twenty day notice if any payment bond has been recorded in compliance with [Arizona Revised Statutes § 33-1003](#), the owner must provide a copy of the payment bond including the name and address of the surety company and bonding agent providing the payment bond to the person who has given the preliminary twenty day notice. In the event that the owner or other interested party fails to provide the bond information within that ten day period, the claimant shall retain lien rights to the extent precluded or prejudiced from asserting a claim against the bond as a result of not timely receiving the bond information.

Dated: _____

(Company name)

By: _____
(Signature)

(Title)

(Acknowledgement of receipt language from [Arizona Revised Statutes § 33-992.02](#) shall be inserted here.)¹⁶

The pre-lien notice must give an estimated value of the claim and a general description of what is to be supplied to the property.¹⁷ If the lien is to be perfected, the actual price of the services or materials or equipment supplied may not exceed the estimate by more than 20 percent. If there is a change during the project that will increase the price by more than 20 percent, a new pre-lien notice should be served.

Arizona statutes prescribe the following format for proof of mailing a preliminary 20-day notice and to substantiate its receipt:

Signature of sender

Acknowledgment of receipt of preliminary twenty day notice

This acknowledges receipt on (insert date) of a copy of the preliminary twenty day notice at (insert address).

Date: _____
(Date this acknowledgment is executed)

Signature of person acknowledging receipt,
with title if acknowledgment is made on behalf

of another person¹⁸

If the recipient does not return the acknowledgement, proof of mailing may be made by affidavit of the sender meeting the requirements of A.R.S. §33-992.02.B.

E. Perfecting a Mechanics' Lien

To enforce a mechanics' lien, a notice and claim of lien must be timely recorded. The deadline for recording, and the format and contents of the notice and claim of lien, are given in the statute.¹⁹ After perfection of the lien, title to the property can be cleared by substituting a bond for the lien.²⁰

The format for a notice and claim of mechanics' lien is given by statute as follows:

1. Notice and Claim of Lien

The notice and claim of lien must contain:

1. The legal description of the lands and improvements to be charged with a lien.
2. The name of the owner or reputed owner of the property concerned, if known, and the name of the person by whom the lienor was employed or to whom he furnished materials.
3. A statement of the terms, time given and conditions of the contract, if it is oral, or a copy of the contract, if it is written.
4. A statement of the lienor's demand, after deducting just credits and offsets.
5. A statement of the date of completion of the building, structure or improvement, or any alteration or repair of such building, structure or improvement.
6. A statement of the date the preliminary twenty day notice required by § 33-992.01 was given. A copy of such preliminary twenty day notice and the proof of mailing required by § 33-992.02 shall be attached.²¹

2. Notice of Completion to Shorten Time for Recording Liens

An owner can shorten the time for filing a notice and claim of lien from 120 to 60 days by serving and recording a notice of completion, which also has a format prescribed by statute:

Notice of Completion

Notice is hereby given that:

1. The undersigned is owner of the interest or estate stated below in the property hereinafter described, or the undersigned is the owner's agent.

2. The full name of the undersigned is _____.

3. The full address of the undersigned is _____.

4. The nature of the interest or estate of the owner is: in fee. _____ (If other than fee, strike "In Fee" and insert, for example, "Purchaser Under Contract of Purchase" or "Lessee.")

5. The full names and full addresses of all persons, if any, who hold interest or estate with the undersigned such as joint tenants or tenants in common are:

Name	Address
_____	_____
_____	_____
_____	_____
_____	_____

6. The full names and full addresses of the predecessors in interest of the undersigned, if the property was transferred after the beginning of the work or improvement:

Name	Address
_____	_____
_____	_____
_____	_____
_____	_____

7. The nature of the improvements to the real property _____.

8. The work of improvement on the property hereinafter described was completed in accordance with the definition of completion in Arizona Revised Statutes § 33-993, subsection C. (Fill in the appropriate completion date as defined in Arizona Revised Statutes § 33-993, subsection C.)

(a) Date _____
(Thirty days after written final acceptance by

governmental body)

(b) Date _____
(Sixty days after cessation of labor)

9. The name of the original contractor, if any, for such work or improvement is _____. (if no contractor, insert "none")

10. The street address of the property is _____
_____. (include both address and city with zip code)

11. The legal description of property described above _____
_____. (attached exhibit if necessary)

Verification

I, the undersigned, certify that I am the owner, the owner's agent for the property or another interested party in the property, described in the above notice, or I certify that I am the original contractor of the improvements to the real property described in the above notice. I have read the foregoing notice and know and understand the contents thereof, and the facts stated therein are true and correct. I declare under penalty of perjury that the foregoing is true and correct.

Executed on _____ (date) at _____
(place where signed), Arizona.

(print name)

(personal signature)

(title)

(Acknowledgement)

Each notice of completion shall contain the following language in type at least as large as the largest type that otherwise appears on the document:

In order to shorten the lien period pursuant to Arizona Revised Statutes § 33-993, subsection A, a copy of the notice of completion and a written statement of

the date of recording and the county recorder's record location information shall be served by certified or registered mail, postage prepaid, to the owner, the original contractor and all persons from whom the person recording this notice has previously received a preliminary twenty day notice as prescribed by Arizona Revised Statutes § 33-993, subsection I.

Notice: Receipt of a notice of completion may alter the time you have to impress and secure a lien in accordance with Arizona Revised Statutes § 33- 993, subsection A.²²

F. Foreclosure of Mechanics' Lien

A recorded notice and claim of mechanics' lien is good for six months, after which the lienor loses the right to file an action to foreclose the lien.²³ When a foreclosure action is filed, a *lis pendens* must also be timely recorded.²⁴

G. Duty to Defend

Contractors must defend lien foreclosure actions brought by claimants “beneath” them (i.e., the general contractor must defend lien claims by subcontractors; subcontractors must defend lien claims by materialsmen or sub-subcontractors, etc.).²⁵

H. Waiver and Release of Lien Rights

Arizona statutes prescribe the forms for waivers and releases of lien rights as follows:

1. Conditional waiver and release on progress payment

Project: _____
Job No.: _____

On receipt by the undersigned of a check from _____ (Maker of Check) in the sum of \$_____ (Amount of Check) payable to _____ (Payee or Payees of Check). And when the check has been properly endorsed and has been paid by the bank on which it is drawn, this document becomes effective to release any mechanic's lien, any state or federal statutory bond right, any private bond right, any claim for payment and any rights under any similar ordinance, rule or statute related to claim or payment rights for persons in the undersigned's position that the undersigned has on the job of _____ (Owner) located at _____ (Job Description) to the following extent. This release covers a progress payment for all labor, services, equipment or materials furnished to the jobsite or to _____ (Person with whom undersigned contracted), through _____ (Date) only and does not cover any retention, pending modifications and changes or items furnished after that date. Before any recipient of this document relies on it, that person should verify evidence of payment to the undersigned.

The undersigned warrants that he either has already paid or will use the monies he receives from this progress payment to promptly pay in full all of his laborers, subcontractors, materialmen and suppliers for all work, materials, equipment or services provided for or to the above referenced project up to the date of this waiver.

Date: _____

(Company Name)

By: _____
(Signature)

(Title)

* * *

2. Unconditional waiver and release on progress payment

Project: _____
Job No.: _____

The undersigned has been paid and has received a progress payment in the sum of \$_____ for all labor, services, equipment or material furnished to the jobsite or to _____(Person with whom undersigned contracted) on the job of _____(Owner) located at _____(Job Description) and does hereby release any mechanic's lien, any state or federal statutory bond right, any private bond right, any claim for payment and any rights under any similar ordinance, rule or statute related to claim or payment rights for persons in the undersigned's position that the undersigned has on the above referenced project to the following extent. This release covers a progress payment for all labor, services, equipment or materials furnished to the jobsite or to _____(Person with whom undersigned contracted) through _____(Date) only and does not cover any retentions, pending modifications and changes or items furnished after that date. The undersigned warrants that he either has already paid or will use the monies he receives from this progress payment to promptly pay in full all of his laborers, subcontractors, materialmen and suppliers for all work, materials, equipment or services provided for or to the above referenced project up to the date of this waiver.

Date: _____

(Company Name)

By: _____
(Signature)

(Title)

(Each unconditional waiver shall contain the following language, in type at least as large as the largest type otherwise on the document:)

Notice: This document waives rights unconditionally and states that you have been paid for giving up those rights. This document is enforceable against you if you sign it, even if you have not been paid. If you have not been paid, use a conditional release form.

* * *

3. Conditional waiver and release on final payment

Project: _____

Job No.: _____

On receipt by the undersigned of a check from _____ (Maker of Check) in the sum of \$ _____ (Amount of Check) payable to _____ (Payee or Payees of Check) and when the check has been properly endorsed and has been paid by the bank on which it is drawn, this document becomes effective to release any mechanic's lien, any state or federal statutory bond right, any private bond right, any claim for payment and any rights under any similar ordinance, rule or statute related to claim or payment rights for persons in the undersigned's position, the undersigned has on the job of _____ (Owner) located at _____ (Job Description). This release covers the final payment to the undersigned for all labor, services, equipment or materials furnished to the jobsite or to _____ (Person with whom undersigned contracted), except for disputed claims in the amount of \$ _____. Before any recipient of this document relies on it, the person should verify evidence of payment to the undersigned.

The undersigned warrants that he either has already paid or will use the monies he receives from this final payment to promptly pay in full all his laborers, subcontractors, materialmen and suppliers for all work, materials, equipment or services provided for or to the above referenced project up to the date of this waiver.

Date: _____

(Company Name)

By: _____

(Signature)

(Title)

* * *

4. Unconditional waiver and release on final payment

Project: _____

Job No.: _____

The undersigned has been paid in full for all labor, services, equipment of material furnished to the jobsite or to _____(Person with whom undersigned contracted), on the job of _____(Owner) located at _____(Job Description) and does hereby waive and release any right to mechanic's lien, any state or federal statutory bond right, any private bond right, any claim for payment and any rights under any similar ordinance, rule or statute related to claim or payment rights for persons in the undersigned's position, except for disputed claims for extra work in the amount of \$_____.

The undersigned warrants that he either has already paid or will use the monies he receives from this final payment to promptly pay in full all of his laborers, subcontractors, materialmen and suppliers for all work, materials, equipment or services provided for or to the above referenced project.

Date: _____

(Company Name)

By: _____

(Signature)

(Title)

(Each unconditional waiver shall contain the following language in type at least as large as the largest type otherwise on the document:)

Notice:

This document waives rights unconditionally and states that you have been paid for giving up those rights. This document is enforceable against you if you sign it, even if you have not been paid. If you have not been paid, use a conditional release form.²⁶

III. STATUTES OF LIMITATION AND REPOSE

A. Statutes of Limitation

General statutes of limitation that may apply to construction-related lawsuits are the six-year limitations period for breach of contract claims²⁷ and the two-year limitations period for tort-based property damage claims.²⁸ The four-year statute of limitations under the Arizona Uniform Commercial Code may apply to claims concerning defective materials.²⁹

B. Statute of Repose for Construction Defect Claims

The statute of repose for economic losses resulting from construction defects bars *contract* actions against developers, builders, designers and the like after eight years from substantial completion of the project, unless a latent defect is discovered in the eighth year, in which case suit may be filed no later than nine years from substantial completion.³⁰ The statute of repose applies only to contract actions, and not, for instance, to tort or common law indemnity actions.³¹ Where there is contractual privity between the plaintiff and defendant, a claim for economic losses is a contractual claim, unless the contract expressly reserves tort remedies for purely economic losses.³²

IV. DWELLING ACTIONS: PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

Arizona requires prior notice of a lawsuit “arising out of or related to the design, construction, condition or sale” of a dwelling,³³ unless the contract for sale conspicuously provides for alternative dispute resolution procedures.³⁴

A homeowner must serve a notice of claim 90 days before a dwelling action may be filed.³⁵ The prospective defendant must thereafter be given access to the property for inspection, and within 60 days of receiving the notice, make a good faith response and offer.³⁶ The owner then has 20 days to respond to the offer.³⁷ If the homeowner rejects an offer, the “defendant to-be” has 10 days to make a good faith best and final offer.³⁸

An award of attorneys’ fees is mandated to the successful party in a “dwelling action.”³⁹

V. COVERAGE AND ALLOCATION ISSUES

For coverage of a claim by typical Commercial General Liability (CGL) policies, there must be property damage occurring during the policy period.⁴⁰ The subsidiary issues are (1) what is “property damage,” and (2) what is an “occurrence”?

Most CGL insurers do not cover the cost to repair bad work by the insured, i.e., the insurer does not cover an insured’s breach of contract. However, the Arizona courts have recently held that a contractual liability exclusion in a CGL policy will not preclude coverage for the insured’s liability to its customers unless the policy very specifically excludes such liability.⁴¹ An “occurrence” requires “actual damage.”⁴² Issues in defining “occurrence” occur (no pun intended) in situations where damage accrues over time. Where damage is ongoing, “the

relevant date for coverage purposes is the date the property damage occurs, even if that damage is incremental.”⁴³ In the event of an “occurrence” with ongoing incremental damage, “insurers must provide coverage for ongoing property damage that occurs during the policy period even if other similar damage preceded that damage.”⁴⁴ There may be coverage under a policy purchased by the contractor itself, or policies where it is an endorsed additional insured. If there are multiple policy periods with different insurers, the trial court has the unenviable job of allocating damages to the different policy periods and among the various insurers.⁴⁵

Construction project participants may have claims brought against them under an indemnification theory, either by express contractual provision, or under a common law implied indemnification theory. It is important that contractors obtain insurance that is commensurate with their contractual undertaking in the project, including express provisions for indemnification, or indemnification liability that may be imposed by law.

VI. CONTRACTUAL INDEMNIFICATION

A. Statutory Limitations on the Scope of Contractual Indemnity

By statute, parties to construction contracts on private projects may not agree to indemnify the other for losses resulting from the sole negligence of the indemnitee; such provisions are void as against public policy.⁴⁶ This limitation does not apply to most contracts with governmental bodies.⁴⁷ A.R.S. §32-1159 voids, as against public policy, indemnification provisions for losses resulting from the sole negligence of the indemnitee, in construction contracts between private parties.⁴⁸

The Arizona Supreme Court has held that a contract capping an owner’s recovery to the amount of the fee for engineering services did not offend Arizona’s anti-indemnity statute because the statute concerns attempts to contract away all liability for one’s own negligence, but not to provisions that limit liability unless “the cap on potential recovery . . . [is] so low as to eliminate the incentive to take precautions”⁴⁹

B. No Common Law Indemnity Where There Is Express Indemnity Provision

Where the parties’ contract includes an express provision for indemnity, there can be no recovery under common law implied indemnity principles.⁵⁰

C. Limited/Intermediate/Broad Forms of Contractual Indemnity

In a construction project/injury case, a recent Arizona District Court opinion used the terms “limited,” “intermediate” and “broad” to describe the various types of contractual indemnity, rather than the more frequently used terms, “general” or “specific,” explaining:

Arizona law “permits a party to protect itself contractually by shifting liability for its fault to another via the mechanism of indemnity.” **There are three types of indemnities: the “limited form indemnity,” the “intermediate form indemnity,” and the “broad form indemnity.”** The limited form indemnity requires the indemnitor to save and hold harmless the indemnitee only for the *indemnitor’s* own negligence. The intermediate form indemnity requires the

indemnitor to indemnify for all liability, *excluding* that which arises out of the indemnitee's sole negligence. Finally, the broad form indemnity obligates the indemnitor to save and hold harmless the indemnitee from *all* liability arising from the project, "regardless of which party's negligence caused the liability."⁵¹

Under the narrow (or limited) form of indemnity, the indemnitor does not have a duty to indemnify in advance of a determination of indemnitor's fault.⁵²

D. Duty to Defend

The indemnitor's duty to defend is broader than the duty to indemnify:

"The duty to defend ... is not the same as the duty to indemnify. The duty to defend arises at the earliest stages of litigation and generally exists regardless of whether the insured is ultimately found liable." In evaluating whether [the carrier] had a duty to defend, the question whether the alleged liability of [the builder] "arose out of" [the subcontractor's] work must be determined initially from the allegations in the complaint against [the builder] and the facts known at that time. It is possible that the requisite nexus ("arising out of") could be established for the duty to defend but not for the duty to indemnify. ("[T]he insurer would have the duty to defend a suit alleging facts that, if true, would give rise to coverage, even though there would ultimately be no obligation to indemnify if the facts giving rise to coverage were not established.")⁵³

However, where a subcontract included a narrow form of indemnity, but did not mention defense, there is no duty to defend in advance of a determination of the indemnitor's fault.⁵⁴ The damages for breach of the duty to defend is payment of the indemnity's defense costs.⁵⁵

VII. RIGHTS IMPLIED BY LAW

A. Implied Warranties

An implied warranty of workmanship and habitability applies to new home construction and may be brought by the original home buyer and subsequent purchasers.⁵⁶ Implied warranty rights may be assigned.⁵⁷

Implied warranty claims sound in contract and may be sued on only where the claimant is in privity of contract with the defendant.⁵⁸

B. Implied Indemnity

Rights of implied indemnity may apply in the absence of a contract with express indemnity rights.⁵⁹

VIII. DAMAGES LIMITATIONS

A. Cost of Repair as General Measure of Damage, Absent Economic Waste

The measure of damage for nonconforming or defective work is the cost to repair or to bring the work into conformance with the contract, EXCEPT where such repair work would result in “economic waste” (i.e., the building would have to be substantially destroyed to completely remedy the defects), in which case, the measure of damage is the difference in market value of the building as designed, less the value as constructed.⁶⁰

B. Uniform Commercial Code Damages

The measure of damages for claims against a material supplier may be governed by the Arizona Uniform Commercial Code.⁶¹

C. Damages Based on Allocated Fault

In 1984, Arizona enacted a comparative fault regime as part of the Uniform Contribution Among Tort Feasors Act (“UCATA”). UCATA outlawed almost all forms of joint liability in favor of liability based on comparative fault. The jury is charged with finding percentages of fault among all of the parties, including plaintiff, and non-parties at fault.

Allocated fault under UCATA does not apply to breach of contract claims.⁶² UCATA’s allocation of fault was found to apply in a strict liability claim brought under Arizona’s product liability statutes, where an under-sink reverse osmosis water filtration system leaked.⁶³

An allocation of damages under the narrow form of indemnity must be based on the indemnitor’s relative fault as a cause of alleged damages.⁶⁴

D. Economic Loss Rule

Where there is contractual privity and the contract does not preserve tort remedies for economic losses, a claimant’s redress for economic loss is limited to an action on the contract.⁶⁵ This doctrine applies only where there is actual contract privity between the plaintiff and the defendant.⁶⁶

E. No Recovery for Damages That Could Have Been Mitigated

Damages that could have been mitigated by the claimant are not recoverable.⁶⁷ The claimant need only exercise reasonable care to mitigate and need not undertake measures that are possible, but extraordinary, or risky or not reasonable to attempt.⁶⁸

F. Contractors Not Liable For Defects in Plans

Arizona follows the “*Spearin* doctrine,” under which contractors are not liable for construction defects caused by following inadequate or defective plans.⁶⁹

G. Interest as a Component of Damage

Only liquidated claims accrue prejudgment interest.⁷⁰ A liquidated claim is one capable of ascertainment and calculation without resort to expert opinion.⁷¹ Accrual of prejudgment

interest on a liquidated claim begins only after the initial demand for claimant of the liquidated claim.⁷²

H. Punitive Damages

It would be a rare construction case where punitive damages would be recoverable, which require clear and convincing evidence of aggravated, outrageous, evil-minded conduct.⁷³

I. Emotional Distress Damages

Arizona does not have case law discussing whether emotional distress damages may be recovered in a construction defect case. However, Arizona case law in other areas holds that a tenant with a mold claim may pursue an emotional distress claim,⁷⁴ while a client with an attorney negligence claim may not recover for negligent infliction of emotional distress, absent harm in the nature of personal injury.⁷⁵ This case law suggests that only where defective construction has a physical impact on the claimant, would recovery for emotional distress be allowed.

J. Hazardous Substance Requiring Cessation of Work

An owner may not recover damages from a contractor where the contractor encounters hazardous substances requiring removal and causing interruption of the work.⁷⁶

K. Attorneys' Fees

The “successful party” on a claim arising out of contract is eligible for a discretionary award of attorneys’ fees.⁷⁷ Recovery of attorneys’ fees is mandatory where a contract between the parties provides for recovery of attorneys’ fees and costs.⁷⁸

¹ *Desert Mountain Properties L.P. v. Liberty Mutual Fire Ins. Co.*, 250 P.3d 196 (Ariz. 2011), *affirming* 236 P.3d 421 (Ariz. App. 2010) (strictly construing contractual liability exclusion provision in CGL policy to not include damages arising from developer’s contractual liability to its customers, based on actual language used, but leaving door open to enforcement of such a limitation if expressly stated in the contract); *Flagstaff Affordable Housing Ltd. P. v. Design Alliance, Inc.*, 223 P.3d 664 (Ariz. 2010) (held project owner’s claim against architect for damages in connection with FHA compliance costs was contractual in nature and, as such, economic loss rule precluded tort claim, where contract did not reserve tort remedies for purely economic losses); *1800 Ocotillo, LLC v. The WLB Group, Inc.*, 196 P.3d 222 (Ariz. 2008) (enforcing provision in contract between developer and engineering firm limiting damages resulting from survey errors to the amount of engineer’s fee). *Cf. North Peak Construction, LLC v. Architecture Plus, Ltd.*, 254 P.3d 404 (Ariz. App. 2011) (where contractor not in privity with architect, contractor could sue architect for damages caused by bad plans under implied warranty theory).

² *The Lofts at Fillmore Condominium Assoc. v. Reliance Commercial Constr. Inc.*, 190 P.3d 733 (Ariz. 2008).

³ Arizona’s mechanics’ lien statutes are found at Ariz. Rev. Stat. §§ 33-981 *et seq.*

⁴ A.R.S. §33-1003.

⁵ *See* A.R.S. §33-992.

⁶ A.R.S. §33-1002.B.

⁷ A.R.S. §§33-420 and 1006.

⁸ *See* A.R.S. §33-981.F. *Also see* A.R.S. §33-982, permitting lien rights by an assignee of a contract or account for materials, or labor.

⁹ A.R.S. §33-981.F. *Also see* contractor regulation statutes at A.R.S. §32-1101 *et seq.*

¹⁰ A.R.S. §§33-981.D and 992.01.B.
¹¹ See A.R.S. §33-1051, *et seq.*
¹² A.R.S. §33-1056.
¹³ A.R.S. §33-992.01.
¹⁴ A.R.S. §33-992.01.E.
¹⁵ A.R.S. §33-992.01.C.
¹⁶ A.R.S. §33-002.01.D.
¹⁷ A.R.S. §33-992.01.H.
¹⁸ A.R.S. §33.992.02.
¹⁹ A.R.S. §33-993.
²⁰ A.R.S. §33-1004.
²¹ A.R.S. §33-993.A.
²² A.R.S. §33-993.F.
²³ A.R.S. §33-998.
²⁴ A.R.S. §33-998.A.
²⁵ A.R.S. §33-995.
²⁶ A.R.S. §33-1008.D.
²⁷ A.R.S. §12-548.
²⁸ A.R.S. §12-542.
²⁹ See A.R.S. §47-2725.
³⁰ A.R.S. §12-552.
³¹ *Evans Withycombe, Inc. v. Western Innovations, Inc.*, 159 P.3d 547 (Ariz.App. 2006).
³² *Flagstaff Affordable Housing v. Design Alliance, Inc.*, 223 P.3d 664 (Ariz. 2010).
³³ A.R.S. §§12-1361.3 and 12-1362.
³⁴ A.R.S. §12-1366.A.
³⁵ A.R.S. §12-1363.A.
³⁶ A.R.S. §12-1363.B and C.
³⁷ A.R.S. §12-1363.E.
³⁸ *Id.*
³⁹ A.R.S. §12-1364.
⁴⁰ *E.g., Lennar Corp. v. Auto-Owners Ins. Co.*, 151 P.3d 538, 548 (App. 2007).
⁴¹ *Desert Mountain Properties, L.P. v. Liberty Mutual Fire Ins. Co.*, 250 P.3d 196 (Ariz. 2011, *affirming* 236 P.3d 421 (Ariz. App. 2010)).
⁴² *Id.*
⁴³ *Id.*
⁴⁴ *Id.* at 549.
⁴⁵ *Id.*
⁴⁶ A.R.S. §32-1159.
⁴⁷ A.R.S. §32-1159.C.
⁴⁸ See discussion of A.R.S. §32-1159 in *James v. Burlington Northern Santa Fe Railway Co.*, 2007 WL 2461682 (D. Ariz. 8/27/07). Also see Trisha Strode, *Comment: From The Bottom of the Food Chain Looking Up: Subcontractors Are Finding That Additional Insured Endorsements Are Given Them More Than They Bargained For*, 23 St. Louis U. Pub.L.Rev. 697 (2004) (cited in *James v. Burlington*, *supra*, at *5), which discusses the use of additional insured status as an end-run around the statutory prohibition on indemnity for the sole negligence of the indemnitee, and the deleterious economic impact this practice is having on some subcontractors.
⁴⁹ *1800 Ocotillo, LLC v. The WLB Group*, 196 P.3d 222, 225 (Ariz. 2008).
⁵⁰ *Grubb & Ellis Mgmt. Services, Inc. v. 407417 B.C. LLC*, 138 P.3d 1210 (Ariz.App. 2006).
⁵¹ *James v. Burlington Northern Santa Fe Railway Company*, 2007 WL 2461682 (D. Ariz. 8/27/07) (Judge Neil V. Wake) *5 (emphasis added and in original; internal citations omitted).
⁵² *MT Builders, L.L.C. v. Fisher Roofing, Inc.*, 197 P.3d 758 (Ariz. App. 2008) (construing indemnity provision in subcontract).
⁵³ *Regal Homes, Inc. v. CNA Insurance*, 171 P.3d 610, 615 (Ariz. App. 2007; internal citations omitted) (builder attempting to find coverage for owner's claims of water intrusion under concrete subcontractor's policy).
⁵⁴ *MT Builders*, *supra*.
⁵⁵ *Sprint Communications Co. v. Western Innovations, Inc.*, 640 F.Supp.2d 1122 (D. Ariz. 2009).

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- ⁵⁶ *E.g., Lofts at Fillmore v. Reliance*, 218 Ariz. 574, 575, 190 P.3d 733, 734 (2008).
- ⁵⁷ *Highland Village Partners v. Bradbury*, 219 Ariz. 147, 195 P.3d 184, 187 (App. 2008).
- ⁵⁸ *Yanni v. Tucker Plumbing*, 233 Ariz. 364, 312 P.3d 1130 (App. 2013) (owner may not sue subcontractor for breach of implied warranty).
- ⁵⁹ *Evans Withycombe v. Western Innovations, Inc.*, 215 Ariz. 237, 243, 159 P.3d 547, 553 (App. 2006).
- ⁶⁰ *Bleick v. School District No. 18 of Cochise County*, 406 P.2d 750 (Ariz.App. 1966); *County of Maricopa v. Walsh & Oberg Architects*, 494 P.2d 44, 46 (Ariz.App. 1972).
- ⁶¹ A.R.S. §47-2101, *et seq.*
- ⁶² *See Bowen Productions, Inc. v. French*, 231 Ariz. 424, 296 P.3d 87 (App. 2013) at Note 3.
- ⁶³ *State Farm Ins. Co. v. Premier Manufactured Systems, Inc.*, 142 P.3d 1232 (Ariz.App. 2006) (holding fault must be allocated between the system manufacturer and the distributor).
- ⁶⁴ *MT Builders, supra*, at 197 P.3d at 774, ¶55.
- ⁶⁵ *Flagstaff Affordable Housing Limited Partnership v. Design Alliance, Inc.*, 223 P.3d 664 (Ariz. 2010).
- ⁶⁶ *Sullivan v. Pulte Home Corp.*, 232 Ariz. 344, 306 P.3d 1 (2013).
- ⁶⁷ *Fairway Builders, Inc. v. Malouf Towers Rental Co., Inc.*, 603 P.2d 513, 526 (Ariz.App. 1979).
- ⁶⁸ *Id.*
- ⁶⁹ *U.S. v. Spearin*, 248 U.S. 132, 136 (1918); *Williamette Crushing Co. v. State*, 932 P.2d 1350 (Ariz. 1977).
- ⁷⁰ *E.g., Fairway Builders, Inc. v. Malouf Towers Rental Co., Inc.*, 603 P.2d 513, 535 (Ariz.App. 1979).
- ⁷¹ *Vigilant Insurance v. Sunbeam Corp.*, 231 F.R.D. 582, 596 (D. Ct. Ariz. 2005) (finding building repair costs not liquidated because of complexity and need for expert testimony).
- ⁷² *Id.*
- ⁷³ *E.g., Saucedo v. Salvation Army*, 24 P.3d 1274 (Ariz.App. 2001); *but see Custom Roofing Co., Inc. v. Alling*, 706 P.2d 400 (Ariz.App. 1985) (punitive damages permitted where roof insulation material seller apparently maliciously cancelled roofing contractor's order for insulation causing loss of contract on large school project).
- ⁷⁴ *Killian v. Equity Residential Trust*, 2004 WL 3558509 (D. Ariz. 2004).
- ⁷⁵ *Reed v. Mitchell & Timbanard*, 903 P.2d 621 (Ariz.App. 1995).
- ⁷⁶ A.R.S. §32-1129.03.
- ⁷⁷ A.R.S. §12-341.01.
- ⁷⁸ *E.g., Lisa v. Strom*, 183 Ariz. 415, 904 P.2d 1239 (App. 1995), at Note 2.

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I. MECHANIC'S LIEN BASICS

Ark. Code Ann. §§ 18-44-101 through 18-44-135 provides for and governs mechanic's and materialmen's liens on improvements to real property. Mechanic's liens provide a vehicle by which contractors, subcontractors and certain suppliers may obtain a security interest in improvements to real property for which they provided labor or materials, and ultimately compel the sale of the property in order to pay for the labor or materials they provided. The four basic steps to perfect a lien are:

A. Pre-Lien Notices. Prior to imposing a material supplier's lien on residential real estate containing four or fewer units, the contractor must provide the owner a statutorily-required notice of the possibility of a lien in the event a material supplier is not paid.¹ Alternatively, a material supplier or other potential lien claimant may provide the notice and the benefit of such notice will accrue to all material suppliers and other lien claimants from the time of the notice forward.² In either event, this notice must be provided before work is commenced or materials are supplied. A pre-construction notice given after work starts on the project secures only the work preformed and/or materials supplied after the effective date of the notice.³ There is a severe sanction for failure to give the required pre-construction. Specifically, if a residential contractor fails to give the pre-construction notice, that contractor is barred from suing to enforce any provision of the construction contract.⁴ The wording of the pre-construction notice was modified in 2009.

A supplier of material or labor for commercial real estate (including residential real estate containing more than four (4) units) must provide a statutorily-required notice to the property owner and contractor that a lien may be placed on the property unless bills for labor, services or materials are paid.⁵ This notice must be served before seventy-five (75) days have elapsed from the time labor was supplied or materials furnished.⁶ The wording of the notice was also modified in 2009.

At least ten (10) days prior to filing a lien, every claimant must provide notice of the claim to the owner of the building or improvement that is the subject of the lien.⁷ The notice may be served by an authorized process server, a competent witness, or by certified mail with return receipt

requested and delivery restricted to the addressee.⁸ Additionally, service by any “[m]eans that provides written, third-party verification of delivery at any place where the owner of the building or improvement maintains an office, conducts business, or resides” (i.e. Fed Ex, UPS, and other commercial delivery options) is authorized.⁹

B. Lien Statement. After notice, a lien account, verified by affidavit, must be filed and served within 120 days of the last date on which the labor or materials was supplied.¹⁰ The contractor's last day of work is defined as when the work reaches “substantial completion.” The statement must contain all of the information required by Ark. Code Ann. § 18-44-117, and must be filed with the clerk of the circuit court of the county in which the property to be attached is situated.¹¹ This is the actual lien. A mechanic’s lien not filed within the statutory period is void.¹² When filing a lien, the lien claimant now has to file an “affidavit of notice” attached to the lien itself. The “affidavit of notice” must contain: a sworn statement (affidavit) evidencing compliance with all of the pre-lien notice requirements; and a copy of each notice given. In other words, the lien claimant must now state under oath that all of the required pre-lien notices were done correctly.¹³

C. Foreclosure. All actions arising out of a lien, including foreclosure, must be commenced within fifteen months after filing the lien and must be prosecuted without unnecessary delay.¹⁴ Under Arkansas Law, a mechanic’s lien holder who successfully forecloses upon his lien is entitled to the recovery of attorney’s fees.¹⁵ A significant change, those seeking to challenge a lien are no longer required to post a bond of double the amount of the lien claim. Now, the bond need only be the amount of the lien claimed.¹⁶ Arkansas law authorizes an expedited summary procedure by which to protest the filing of a lien. The issues in such a protest action are limited to whether the lien was filed in proper form and whether the required notices were properly proved.¹⁷ The prevailing party in a lien contest is entitled to recover attorney’s fees.¹⁸

D. Sale. A sale of the property may be initiated following a successful foreclosure action. At the sale, the property will be sold and the proceeds used to pay off the interest holders in the property based upon priority of interest.

E. Note for Public Projects: Public policy forbids the attachment of liens on public buildings for labor and materials furnished for construction of public facilities.¹⁹ To protect laborers and material suppliers on public projects not subject to mechanic’s and materialmen’s liens, Arkansas law requires a contractor on a public project exceeding \$20,000 to furnish a bond in the contract amount to secure payment for labor and materials supplied for the project.²⁰ Claims against the bond must be brought against the surety within twelve months after the state approves final payment on the contract.²¹

II. STATUTES OF LIMITATION AND REPOSE

A. Statute of Limitations

Oral Contracts. The statute of limitation for oral contracts is three years from the date the cause of action accrues.²² The cause of action accrues when one party has, by words or conduct, indicated to the other that the agreement is being repudiated or breached.²³ Arkansas has

adopted a statute of repose that may shorten the three-year statute of limitation for an oral contract, but will not extend it.²⁴ See Section II.B. below.

Written Contracts. The statute of limitations for actions to enforce written contracts is five years after the cause of action accrues.²⁵ The date that a statute of limitations begins to run is a factual issue and, in contract actions, the statute of limitations begins to run upon occurrence of the last element essential to the cause of action.²⁶ The test for determining when a breach of contract action accrues is the point when the plaintiff could have first maintained the action to a successful conclusion.²⁷

Contribution. A three-year statute of limitations applies to all actions for contribution in Arkansas.²⁸

B. Statutes of Repose

No action in contract to recover damages caused by any “deficiency in the design, planning, supervision, or observation of construction or the construction and repair of any improvement to real property or for injury to real or personal property caused by such deficiency, shall be brought against any person performing or furnishing the design, planning, supervision, or observation of construction or the construction or repair of the improvement more than five (5) years after substantial completion of the improvement.”²⁹ Actions for personal injury or wrongful death as a result of defective construction must be brought within four years after substantial completion of the project.³⁰ These limitations do not apply in the event of fraudulent concealment of the defect.³¹

Parties to a construction contract are specifically precluded from extending a limitation period by agreement or otherwise.³² There is no prohibition on contractually shortening the period.³³ Parties “have the right to contract for something less than the statutory 5-year limitation period as long as the lesser filing period is reasonable” and as long as the shorter period is not “in contravention of public policy.”³⁴ The same rule applies whether the shorter contractual limitation is found in a private or public contract.³⁵

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

An injured party is entitled to recover the reasonable costs of repair for defects in materials or workmanship.³⁶ However, the injured party must have provided notice of the defects and allowed the opportunity for inspection by the party sued.³⁷ This notice does not have to list each and every objection; it is for the jury to determine whether the notice was sufficient and was given within a reasonable time.

IV. COVERAGE AND ALLOCATION ISSUES

A standard commercial general liability policy provides coverage for amounts that the insured becomes legally obligated to pay as damages because of bodily injury or property damages that (1) are caused by an occurrence that takes place in the coverage territory, and (2)

occur during the policy period. An “occurrence” is typically defined as “an accident, including continuous and repeated exposures to substantially the same general harmful conditions.”

There is a split in the jurisdictions over whether defective workmanship is an accident and therefore an "occurrence" that is covered under the terms of a particular insurance policy. Under Arkansas law, “defective workmanship standing alone -- resulting in damages only to the work product itself -- is not an occurrence[.]”³⁸ However, damage resulting from faulty workmanship is an occurrence.³⁹ Arkansas Act 604 of 2011, which took effect on July 8, 2011, responds to *Lexicon, Inc. v. Ace Am. Ins. Co.* by seeking to codify its holding. Under the new law, commercial general liability policies sold in Arkansas must contain a definition of “occurrence that includes accidents and also “[p]roperty damage or bodily injury resulting from faulty workmanship.”⁴⁰

In most cases, the insured has the burden of proving allocation of liability between insurance carriers, but that burden may be shifted to the insurer when it takes over the defense of the insured.⁴¹

There is no Arkansas case law on point involving insurance coverage and allocation on construction defect claims. With respect to construction of insurance policies in general, such policies are construed strictly against the insurer, and such matters are to be determined by the court rather than the jury, except when the meaning of the language depends upon disputed extrinsic evidence.⁴² In Arkansas, it is an established principle of insurance law that provisions contained in a policy of insurance must be construed most strongly against the insurance company that prepared it, and if a reasonable construction may be applied that would justify recovery, it is the court’s duty to do so.⁴³ If the policy language is ambiguous and open to two interpretations, one of which is favorable to the insured and the other of which is favorable to the insurer, the former will be adopted.⁴⁴

V. CONTRACTUAL INDEMNIFICATION

Currently, in a public or private construction contract, an obligation to defend, indemnify, or hold harmless another party from damages for “death,” “bodily injury,” or “property” arising from its sole negligence or the negligence of “its agent, representative, subcontractor or supplier” is unenforceable. Effective July 31, 2007, Arkansas adopted Act 874 of 2007 to prevent indemnification in public or private construction projects absent limited circumstances or conditions.⁴⁵ The Act declares unenforceable any clauses in a public or private construction contract requiring indemnity for death or bodily injury arising out of the sole negligence of the indemnitee. Nevertheless, the Act provides that the clause will be enforceable if:

- (1) The first party indemnifies, defends, or holds harmless the second party from the first party's negligence or fault or from the negligence or fault of the first party's agent, representative, subcontractor, or supplier;
- (2) The first party requires the second party to provide liability insurance coverage for the first party's negligence or fault if the construction contract or construction agreement requires the second party to obtain insurance and the construction contract or construction

agreement limits the second party's obligation to the cost of the required insurance;

(3) The first party requires the second party to provide liability insurance coverage for the first party's negligence or fault under a separate insurance contract with an insurance provider; or

(4) The first party requires the second party to name the first party as an additional insurer as part of the...construction agreement or...contract.”

Act 874 of 2007, Acts of the General Assembly of Arkansas.

Indemnity agreements are construed strictly against the party seeking indemnification.⁴⁶ The losses to be indemnified against must be clearly stated and the intent of the indemnitor to indemnify against them must be clear.⁴⁷ The intent to extend the obligation to losses from specific causes need not be in any particular language, but unless this intention is expressed in the plainest words it will not be deemed that the party undertook to indemnify against it.⁴⁸

VI. DAMAGES LIMITATIONS

A. Attorneys' Fees

At the court's discretion, reasonable attorneys' fees are recoverable in breach of contract actions, unless otherwise provided by law or the contract that is the subject matter of the action.⁴⁹ In addition, attorneys' fees are recoverable by the successful party in a civil action to enforce an unpaid lien claim.⁵⁰

B. Consequential Damages

Absent an independent tort, Arkansas adheres to the minority "tacit agreement" doctrine that precludes consequential damages not the direct result of breach of contract and not tacitly agreed upon.⁵¹

As a general rule, liquidated damages in lieu of actual damages are enforceable.⁵² The damages to be liquidated must (a) have been contemplated by the parties, (b) be indeterminate or difficult to ascertain, and (c) be reasonable in proportion to the damages being liquidated. They have been allowed only up to the date of substantial completion.⁵³ Where such damages are merely a penalty or punitive, they will not be allowed.⁵⁴ "A stipulated sum will be regarded as a penalty if the sum agreed to exceeds the measure of a just compensation and the actual damages sustained are capable of proof."⁵⁵

C. Delay and Disruption Damages

"No damages for delay" clauses are enforceable under Arkansas law; however, they are strictly construed. "Courts give only a restrained approval to 'no damage' clauses because of their harsh effect. While such clauses are not void as against public policy and will be enforced

so long as the basic requirements for a valid contract are met, the courts accord such clauses a strict construction.”⁵⁶ It is probable that an Arkansas court will treat this type of clause the same whether the contract in which the clause appears is public or private.⁵⁷ Usual delays are anticipated in construction contracts and should be taken into account in setting a completion date.⁵⁸

A contractor does not assume the business risks for costs associated with delay if the delay was caused by the owner. Generally, however, the owner’s act of interference must be willful or intentional before the courts will decline to assess the cost of delay against the contractor.⁵⁹ In one case, a contractor delayed by owner fault recovered extended job costs and a pro rata share of home office overhead,⁶⁰ and Arkansas courts would likely accept documented and expert proof of contractor-owned equipment, labor inefficiency, and total cost claims in appropriate circumstances. Additional interest paid by an owner on a construction loan is a compensable element of damages against the contractor.⁶¹

A contractor whose construction project is handled in such a way as to negligently obstruct traffic, thereby reducing the normal flow of customers to a retailer, can be held liable for the retailer’s lost profits.⁶²

D. Economic Loss Doctrine

Arkansas does not follow the "economic loss doctrine." The economic loss doctrine prohibits a tort action when there is no damage for personal injury or property damage, other than to the product itself.⁶³ Arkansas allows strict product liability claims for economic losses or damage to the product only. Arkansas also permits negligence claims for purely economic losses (Damages for loss of tomato crop after vendor negligently supplied the wrong seeds).⁶⁴ In the context of construction of residential property, first and subsequent purchasers of homes are permitted to bring suit against the builder vendor for construction defects if the construction defects are latent--not discoverable upon reasonable inspection-- and there is no substantial change or alteration in the condition of the building from the original sale.⁶⁵

The Arkansas Supreme Court has held that a new house is a “product” in the strict liability context, and allowed recovery for economic loss.⁶⁶

E. Interest

Previously, in the absence of an agreement to the contrary, the Arkansas Constitution fixed the pre-judgment simple interest rate at 6 percent per annum. Effective January 1, 2011, that constitutional provision is repealed. Prejudgment interest accrues from the time of loss to judgment and is allowed where the amount of damages is definitely ascertainable by mathematical computation, or if the evidence furnishes data that makes it possible to compute the amount without reliance on opinion or discretion.⁶⁷ If collectable, the injured party is entitled to prejudgment interest as a matter of law.⁶⁸

The post-judgment rate of interest is the rate agreed upon in the contract or 10% per annum, whichever is greater, but in no event more than the maximum lawful rate set forth in the Arkansas Constitution.⁶⁹

F. Punitive Damages

Punitive or exemplary damages are generally not recoverable in contract actions, but are recoverable in personal injury and wrongful death actions.⁷⁰ Punitive damages may be awarded by the jury or the trier of fact when the defendant knew or ought to have known that the conduct would naturally and probably result in injury and the actor continued such conduct with reckless disregard of the consequences for which malice may be inferred or with malice.⁷¹

G. Contractors Barred from Certain Actions

Contractors are now barred from bringing certain actions if they were not licensed at the time or if they were licensed but included false information in their license application.

In *Meyer v. CDI Contractors, LLC* 284 S.W.3d 530 (Ark. Ct. App. 2008) the Arkansas Court of Appeals held that a contractor's claims against a party for breach of contract were barred as a matter of law because he violated the Arkansas Contractors Licensing Act.

CDI and Meyer Excavators Contractors ("Meyer") were negotiating about work that Meyer could do for CDI at the Church at Rock Creek. CDI learned that Meyer was not a licensed contractor in the state of Arkansas. Under Arkansas law, unlicensed contractors are forbidden from performing any work in excess of \$20,000. The subject work would exceed that amount. CDI then postponed the bidding in order to allow Meyer to acquire the proper license. Meyer received his license in July 2001. As part of the application process, Meyer signed an affidavit that he was not currently performing any work valued at more than \$20,000.

Meyer entered into contract with CDI in September of 2001 for the dirt work at the Church at Rock Creek. In December of 2001, CDI attempted to cancel the contract in apparent violation of the Arkansas Contractors Licensing Act (the "Act"). Part of the Act, A.C.A. § 17-25-103(a), states, in short, that any unlicensed contractor who undertakes construction work of \$20,000 or more or who gives false evidence to the Contractors Licensing Board in obtaining a license will be guilty of a misdemeanor and may be fined \$200.00 per offense per day. A.C.A. § 17-25-103(d) (Repl.2001) states: "No action may be brought either at law or in equity to enforce any provision of any contract entered into in violation of this chapter. No action may be brought at law or in equity for quantum meruit by any contractor in violation of this chapter."

As proof of a violation, CDI had Meyer's 2001 license application, deposition excerpts, and most importantly records dated 2001 from "Berry Farm Project," which showed Meyer's work on that project was valued at over \$20,000. At the time of Meyer's application, he had billed more than \$84,000 for work on that project.

Meyer never refuted that he was working on projects in excess of \$20,000 at the time of his application. The court held that because Meyer had violated the Arkansas

Contractors Licensing Act, his claims against CDI based on the contract were barred as a matter of law under A.C.A. § 17-25-103 (2005).⁷²

Thus, contractors are now barred from bringing certain actions if they were not licensed at the time or if they were licensed but included false information in the license application.

VII. RECENT CASE LAW.

A. No Bid Contracts: *Gatzke v. Weiss*, 2008 WL 5191102 (Ark. Dec. 11, 2008)

A group of Arkansas taxpayers (“Appellants”) sued several public officials, including the Director of the Department of Finance and Administration (“DFA”), alleging that Act 961 of 1997 (codified at A.C.A. § 19-4-1413) and Act 1626 of 2001 (Ark. Code Ann. § 19-4-1415) (collectively the “Acts”) violated Article 19, Section 16 of the Arkansas Constitution because they permit the State to enter into construction contracts without engaging in competitive bidding. Appellants also contended that the construction contracts permitted under the Acts constituted illegal exactions under Article 16, Section 13 of the Arkansas Constitution. Appellants requested a declaratory judgment that the Acts were unconstitutional and that the contracts were illegal exactions. Additionally, appellants sought to enjoin the State from entering into any new contracts or continuing work under existing contracts.

The DFA moved to dismiss the suit, arguing that Article 19, Section 16 of the Arkansas Constitution applies only to county-funded contracts. Article 19, Section 16 provides that “All contracts for erecting or repairing public building or bridges in any county, or for materials therefore; or for providing for the care and keeping of paupers, where there are no alms-houses, shall be given to the lowest responsible bidder, under such regulations as may be provided by law.” The circuit court agreed with DFA and granted the motion to dismiss.

The provisions of the Arkansas Constitution apply to the *State* unless there is an explicit provision to the contrary. In *Gatzke*, however, the Arkansas Supreme Court concluded that Article 19, Section 16, applied only to county contracts, reasoning that the phrase “in any county” would lack significance unless the provision relating to public buildings and bridges was restricted to county-funded contracts. As further support for its holding, the Arkansas Supreme Court looked to the state contracts referenced in Article 19, Section 15 (since repealed), to demonstrate that the legislature purposely included the words “in any county” and thus intended to restrict Article 19, Section 16, to county contracts.

Therefore, no-bid construction contracts are permissible for state projects, but not for county projects.

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- ¹ ARK. CODE ANN. § 18-44-115.
- ² ARK. CODE ANN. § 18-44-115(a)(5)(A).
- ³ ARK. CODE ANN. § 18-44-115(a)(5)(B)(ii).
- ⁴ ARK. CODE ANN. § 18-44-115(a)(4).
- ⁵ ARK. CODE ANN. § 18-44-115.
- ⁶ ARK. CODE ANN. § 18-44-115(b)(5)(A).
- ⁷ ARK. CODE ANN. § 18-44-114.
- ⁸ ARK. CODE ANN. § 18-44-114(b)(1).
- ⁹ ARK. CODE ANN. § 18-44-114(b)(1)(D).
- ¹⁰ ARK. CODE ANN. § 18-44-117.
- ¹¹ ARK. CODE ANN. § 18-44-117.
- ¹² *Calton Properties, Inc. v. Ken's Discount Bldg. Materials, Inc.*, 282 Ark. 521, 523, 669 S.W.2d 469 (1984).
- ¹³ ARK. CODE ANN. § 18-44-117(a)(1).
- ¹⁴ ARK. CODE ANN. § 18-44-119(a).
- ¹⁵ ARK. CODE ANN. § 18-44-128.
- ¹⁶ ARK. CODE ANN. § 18-44-118(a)(1)(A).
- ¹⁷ ARK. CODE ANN. § 18-44-118(f).
- ¹⁸ ARK. CODE ANN. § 18-44-118(f)(6).
- ¹⁹ *Dow Chemical Co. v. Bruce-Rogers Co.*, 255 Ark. 448, 501 S.W.2d 235 (1973). However, a lien placed on a project when it is privately-owned relates back to the commencement of construction and is not destroyed by the subsequent purchase of the property by a public authority. *Rawick Mfg. Co. v. Talisman, Inc.*, 17 Ark. App. 202, 706 S.W.2d 194 (1986).
- ²⁰ ARK. CODE ANN. § 18-44-503.
- ²¹ *Id.*
- ²² ARK. CODE ANN. § 16-56-105.
- ²³ *Elder v. Security Bank of Harrison*, 68 Ark. App. 132, 138, 5 S.W.3d 78, 81 (1999).
- ²⁴ ARK. CODE ANN. § 16-56-112.
- ²⁵ ARK. CODE ANN. § 16-56-111.
- ²⁶ *Hunter v. Connelly*, 247 Ark. 486, 446 S.W.2d 654 (1969).
- ²⁷ *Zufari v. Architecture Plus*, 323 Ark. 411, 914 S.W.2d 756 (1996) (holding that date architect's plans were rejected was the date the statute of limitations began to run).
- ²⁸ ARK. CODE ANN. § 16-56-105(3); *Sublett v. Hips*, 330 Ark. 58, 952 S.W.2d 140 (1997).
- ²⁹ ARK. CODE ANN. § 16-56-112(a).
- ³⁰ ARK. CODE ANN. § 16-56-112(b)(1). However, in the case of personal injury or an injury causing wrongful death that occurs in the third year after substantial completion, such action must be brought within one year "after the date on which the injury occurred, irrespective of the date of death, but in no event shall such an action be brought more than five (5) years after the substantial completion of construction of such improvement." ARK. CODE ANN. § 16-56-112(b)(2).
- ³¹ ARK. CODE ANN. § 16-56-112(d).
- ³² ARK. CODE ANN. § 16-56-112(f).
- ³³ *See* ARK. CODE ANN. § 16-56-112 (Supp. 2001).
- ³⁴ *Hawkins v. Heritage Life Ins. Co.*, 63 Ark. App. 67, 973 S.W.2d 823 (1998).
- ³⁵ *Ferguson v. United Commercial Travelers of Am.*, 307 Ark. 452, 455, 821 S.W.2d 30, 32 (1991).
- ³⁶ *Daniel V. Quick*, 270 Ark. 528, 606 S.W.2d 81 (Ark. App. 1980); *Pack v. Hill*, 18 Ark. App. 104, 105, 710 S.W.2d 847 (1986).
- ³⁷ *Pennington v. Rhodes*, 55 Ark. App. 42, 49, 929 S.W.2d 169 (1996).
- ³⁸ *Essex Ins. Co. v. Holder*, 372 Ark. 535, 540, 261 S.W.3d 456 (2008).
- ³⁹ *Lexicon, Inc. v. Ace Am. Ins. Co.*, 634 F.3d 423, 427 (8th Cir. 2010).
- ⁴⁰ ARK. CODE ANN. § 23-79-155.
- ⁴¹ *MedMarc Cas. Ins. Co. v. Forest Healthcare, Inc.*, 359 Ark. 495, 199 S.W.3d 58 (2004).
- ⁴² *Smith v. Prudential Prop. & Cas. Ins.*, 340 Ark. 335, 10 S.W.3d 846 (2000).
- ⁴³ *Drummond Citizens Ins. v. Sergeant*, 266 Ark. 611, 588 S.W.2d 419 (1979).
- ⁴⁴ *Id.*

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- ⁴⁵ ARK. CODE ANN. § 22-9-214; Ark. Code Ann. § 4-56-104.
- ⁴⁶ *Id.*
- ⁴⁷ *Id.*
- ⁴⁸ *Id.*
- ⁴⁹ ARK. CODE ANN. § 16-22-308; *Burnette v. Perkins & Assocs.*, 343 Ark. 237, 33 S.W.3d 145 (2000).
- ⁵⁰ ARK. CODE ANN. § 18-44-128.
- ⁵¹ *Morrow v. First Nat'l Bank of Hot Springs*, 261 Ark. 568, 570, 550 S.W.2d 429, 430 (1977).
- ⁵² *Phillips v. Ben M. Hogan Co.*, 267 Ark. 1104, 594 S.W.2d 39 (Ark. App. 1980).
- ⁵³ *Id.*
- ⁵⁴ *Id.*
- ⁵⁵ *Id.*
- ⁵⁶ *Little Rock Wastewater Util. v. Larry Moyer Trucking, Inc.*, 321 Ark. 303, 311, 902 S.W.2d 760, 765 (1995).
- ⁵⁷ *Id.* (utility was a public entity).
- ⁵⁸ *Housing Authority of Little Rock v. Forcum-Lannom, Inc.*, 248 Ark. 750, 454 S.W.2d 101 (1970).
- ⁵⁹ *United States Steel Corp. v. Missouri Pac. R. Co.*, 668 F.2d 435 (8th Cir. 1982), *cert. denied*, 459 U.S. 836 (1982) (applying Arkansas law).
- ⁶⁰ *Texarkana Housing Authority v. Johnson Const. Co.*, 264 Ark. 523, 573 S.W.2d 316 (1978).
- ⁶¹ *Taylor v. Green Memorial Baptist Church*, 5 Ark. App. 101, 633 S.W.2d 48 (1982).
- ⁶² *Mine Creek Contractors Inc. v. Grandstaff*, 300 Ark. 516, 780 S.W.2d 543 (1989).
- ⁶³ *Farm Bureau Ins. Co. v. Case Corp.*, 317 Ark. 467, 878 S.W.2d 741 (1994).
- ⁶⁴ *Dessert Seed Co. v. Drew Farmers Supply, Inc.*, 248 Ark. 858, 454 S.W.2d 307 (1970).
- ⁶⁵ *Curry v. Thornsberry*, 354 Ark. 631, 642, 128 S.W.3d 438, 444 (Ark. 2003)
- ⁶⁶ *Blagg v. Fred Hunt Co.*, 272 Ark. 185, 190, 612 S.W.2d 321, 324 (1981).
- ⁶⁷ *Ozark Unltd. Resources Coop., Inc. v. Daniels*, 333 Ark. 214, 969 S.W.2d 169 (1998).
- ⁶⁸ *Id.*
- ⁶⁹ ARK. CODE ANN. § 16-65-114(a).
- ⁷⁰ *Wheeler Motor Co. v. Roth*, 315 Ark. 318, 867 S.W.2d 446 (1993).
- ⁷¹ *Stein v. Lukas*, 308 Ark. 74, 823 S.W.2d 832 (1992).
- ⁷² *Stein v. Lukas*, 308 Ark. 74, 823 S.W.2d 832 (1992).

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I. MECHANIC'S LIEN BASICS

California's mechanics lien law provides various rights and remedies to persons who provide labor, service, equipment, or material to real property. One such right is a mechanics lien, which is an involuntary encumbrance against the real property for the value of the items (labor, service, etc.) furnished. California's state constitution expressly provides that those contributing to a private work of improvement have rights to a mechanics liens. Cal. Const. art. XIV, § 3. The purpose is to afford security for those who enhance the property of others. Thus, when a contractor, subcontractor, material supplier, or equipment lessor is not paid for contributing to a private work of improvement, the principal statutory remedies for obtaining payment are mechanics liens, stop notices, and bond actions. See Civ. Code, §§ 8302, 8402; see also *Mechanical Wholesale Corp. v. Fuji Bank, Ltd.* (1996) 42 Cal.App.4th 1647, 1654.

California's mechanics lien laws were enacted to prevent unjust enrichment of a property owner at the expense of laborers or material suppliers. "The mechanics' lien is the only creditors' remedy stemming from constitutional command and our courts 'have uniformly classified the mechanics' lien laws as remedial legislation, to be liberally construed for the protection of laborers and materialmen.'" *Basic Modular Facilities, Inc. v. Ehsanipour* (1999) 70 Cal.App.4th 1480, 1483 (citation omitted).

A. Requirements

There are three basic steps required before a contractor can recover money through a mechanics lien: (1) notice to the owner, (2) recording the lien; and (3) lien foreclosure action.

California requires that the property owner be informed about the specific work being done before the property owner can be held responsible. Therefore, a "Preliminary Notice" must be served by most types of lien claimants at the outset of their work, to preserve their lien claim, payment bond, and stop notice rights. Civ. Code, § 8200. California's Legislature imposed the preliminary notice requirements in order to alert owners, contractors, and lenders that "the

property or funds involved might be subject to claims arising from contracts to which they were not parties and would otherwise have no knowledge.” *Romak Iron Works v. Prudential Ins. Co.* (1980) 104 Cal.App.3d 767, 778 (1980). The theory is that if the property owner knows who is working on his project, he can make an effort to see that they will be paid. Civil Code section 8202 provides the required language for the Preliminary Notice.

A claimant other than a general contractor must provide a Preliminary Notice to the owner, direct contractor, and construction lender within 20 days of first furnishing work or materials. A general contractor must provide the notice to the lender. Civ. Code, § 8200 et seq. Contractors in a direct contractual relationship with the project owner need only provide a Preliminary Notice to construction lenders and reputed construction lenders, if any. Civ. Code, § 8200, subd. (e)(2). An individual worker or laborer, however, has lien rights without giving notice. Civ. Code, § 8200, subd. (e)(1).

The claimant must timely record the lien in the county where the work of improvement is located. The deadline for recording a mechanics lien is generally triggered by the completion of a work of improvement. Civ. Code, § 8180. Owners must record notices of completion within a window of 15 days after actual completion of the project. Civ. Code, § 8182, subd. (a). Acts signifying completion include: actual completion of all work on the project, occupation or use coupled with cessation of labor, a cessation of labor for 60 continuous days (or for 30 days after recording of a notice of cessation, and acceptance by a public entity. Note that following the 2012 amendments to California's mechanics lien law, acceptance by the owner is no longer one of the circumstances deemed to constitute completion.

Civil Code section 8416 provides the specific requirements for a lien document. The lien must contain: (1) a statement of the demand; (2) the name of the owner or reputed owner; (3) a general statement of the services furnished; (4) the name of the party who hired the claimant; (5) a description of the jobsite; (6) claimant's address; (7) proof of service; and (8) a specific "Notice of Mechanic's Lien" statement. The claimant must then serve a copy of the mechanics lien upon the property owner contemporaneously with filing the lien itself in the Recorder's Office in the county where the project is located.

B. Enforcement and Foreclosure

A recorded mechanics lien is released by operation of law if the claimant does not bring a lien foreclosure action within 90 days after the lien is recorded. Civ. Code, § 8460. That is, once the lien is filed, it is only effective for a period of 90 days. After this 90 day period, if the lien is not foreclosed upon or extended, it will expire. Civ. Code, § 8412. If the owner files a valid notice of completion, a direct contractor must record its lien and mail a copy to the owner within 60 days after recording of the notice of completion, and any other claimant must records its lien and mail a copy to the owner within 30 days after the recording of the notice of completion. Civ. Code, § 8414.

A claimant generally must sue to enforce the stop payment notice no earlier than 10 days after the notice was given and no later than 90 days after expiration of the time within which stop payment notices must be given. Civ. Code, § 8550. The claimant must notify the persons to

whom the stop notice was given of the commencement of the action within 5 days of commencing it. Any person who can record a lien can give a stop payment notice, as long as a preliminary notice has been given. Civ. Code, §§ 8520, 8530, 9100.

The proper court in which to file a foreclosure action is the superior court in the county where the real property or some part of it is situated. Code Civ. Proc., § 392, subd. (a)(2); see also *Automatic Sprinkler Corp. v. Southern Cal. Edison Co.* (1989) 216 Cal.App.3d 627. A lien foreclosure action that is neither filed nor transferred to the proper county court within 90 days after the claim of lien is recorded is time barred under Civil Code section 8460. Moreover, the court has discretion to dismiss causes of action for both foreclosure of a mechanics lien and enforcement of a stop notice if the action is not brought to trial within two years after commencement. Civ. Code § 8462.

Although a judgment for foreclosure of a mechanics lien orders the sale of the affected property, like judicial foreclosure of a mortgage, actual sales rarely occur. However, when a sale does occur, the sheriff auctions the property pursuant to Code of Civil Procedure sections 716.010 et seq. A claimant who prevails on a lien foreclosure suit should record the actual judgment immediately, so that the lien will relate back to the commencement date of the work of improvement and the priorities among competing interests decreed by the court in the foreclosure action will bind the property accordingly.

C. Ability to Waive and Limitations on Lien Rights

In order to ensure that a "downstream" subcontractor has validly released its right to assert lien, stop notice, or payment bond rights, the law requires that specific waiver and release language be used. Civ. Code, § 8132 et seq. Any provision in a subcontractor's or material supplier's contract to the effect that the subcontractor or material supplier waives its future lien or other collateral rights is void "unless and until the claimant executes and delivers a waiver and release" under the statute. Civ. Code, § 8122. Thus, all lien releases must conform to the forms set forth in the statute to be enforceable. The statute provides required language to use depending on whether the waiver is conditional or unconditional, and whether it concerns progress or final payments. The form utilized for progress payments (as opposed to final payments) does not cover certain disputed or extra work items or claims based on breach of contract, so "upstream" parties may want to supplement the statutory form with additional releases.

Finally, note that if an owner desires to sell or refinance the property that is subject to a valid mechanics lien, the owner can "bond around" the lien by posting cash or a bond for 125 percent of the face amount of the loan. § 8424, subd. (b).

II. **STATUTES OF LIMITATION AND REPOSE**

A. **Statutes of Limitation and Limitations on Application of Statutes**

The following five statutes of limitation apply to California's construction contract litigation and run from the time when the plaintiff discovered, or should have discovered, the injury:

1. Four (4) year statute of limitation for breach of written contract under California Code of Civil Procedure section 337
2. Four (4) year statute of limitation for breach of contract of sale under California Uniform Commercial Code section 2725;
3. Three (3) year statute of limitation for injury to real or personal property under California Code of Civil Procedure section 338;
4. Three (3) year statute of limitation for actions under Porter-Cologne Water Quality Control Act or under specified statutory provisions on hazardous waste control under California Code of Civil Procedure section 338; and
5. Two (2) year statute of limitation for breach of oral agreement under California Code of Civil Procedure section 339.

B. **Statutes of Repose and Limitations on Application of Statutes**

The following two provisions are called "statutes of repose" because they run from the date the construction project is completed, rather than from the time the cause of action arises (i.e. when the defect is discovered). The statutes of repose cannot be used to revive causes of action that have expired under other applicable statutes of limitation. Thus, a claimant cannot rely on a statute of repose to save what would otherwise be a late claim under the statute of limitations. Additionally, with certain exceptions, the statutes of repose apply equally to numerous claim theories (i.e. breach of contract, negligence, strict liability), while the statutes of limitation are different for each particular theory of liability.

1. **Patent Defects**

Pursuant to California Code of Civil Procedure section 337.1, an action for injuries to persons or property arising from patent defects in the planning or construction of improvements to real property must be commenced within four (4) years after substantial completion of the work of improvement. A defect is patent if it is apparent/discoverable by reasonable inspection. Code Civ. Proc., § 337.1, subd. (e).

Section 337.1 does not apply to suits for defects in owner-occupied single unit residences. Moreover, the four-year period announced in section 337.1 not only applies to actions for damages caused by patent defects existing at the time of substantial completion of

construction, but also to actions that involve patent defects that arose after substantial completion. See *Tomko Woll Group Architects, Inc. v. Superior Court* (1996) 46 Cal.App.4th 1326 (holding the four-year statute of limitation period under § 337.1 applies to actions involving a patent deficiency, whether the patent deficiency existed at the time of, or after, substantial completion of construction).

Section 337.1 protects developers and contractors but not product manufacturers. *Robinson v. Chin & Hensolt* (2002) 98 Cal.App.4th 702 (concluding total absence of legislative intent to protect mere manufacturers of devices solely because they happen to be installed in real property).

2. Latent Defects

Pursuant to Code of Civil Procedure section 337.15, an action for injuries to persons or property arising from latent defects in the planning or construction of improvements to real property must be commenced within ten (10) years after substantial completion of the work of improvement. A defect is latent if the deficiency is not apparent/discoverable by reasonable inspection. Code Civ. Proc., § 337.15, subd. (b). Section 337.15 protects developers, design and engineering professionals, persons who perform construction, and the sureties of such persons. Code Civ. Proc. § 337.15.

Section 337.15 applies to actions based upon breach of contract and tort. *Moseley v. Abrams* (1985) 170 Cal.App.3d 355. However, the statute does not apply to the following actions: (1) Personal injury or wrongful death actions (*Martinez v. Traubner* (1982) 32 Cal.3d 755); (2) Nuisance actions under the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (*Angeles Chem. Co. v. Spencer & Jones* (1996) 44 Cal.App.4th 112); (3) Actions based upon willful misconduct or fraudulent concealment (*Felburg v. Don Wilson Builders* (1983) 142 Cal.App.3d 383); and (4) Certain product liability actions (*Sevilla v. Stearns-Roger, Inc.* (1980) 101 Cal.App.3d 608; see also *Chevron U.S.A., Inc. v. Superior Court* (1994) 44 Cal.App.4th 1009; *San Diego Unified School Dist. v. County of San Diego* (2009) 170 Cal.App.4th 288 ("When interpreting section 337.15, the courts do not determine when the particular construction defect claim accrued, but rather, the courts measure the timeliness of a cause of action by the date of substantial completion of the improvement. [citation] This approach is consistent with the authority of *Chevron* . . . in which the court characterized section 337.15 as a 'statute of repose created by the Legislature's fixed starting point and outer limit for latent construction defects'."))

Courts interpreting section 337.15 agree that an action must be filed within the shorter of the limitations and the repose periods. See *Lantzy v. Centex Homes* (2003) 31 Cal.4th 363, 369-370 (adopting two-step analysis that actions for latent defects based upon fraud or breach of written contract must be filed within three years (Code Civ. Proc. § 338) or four years (Code Civ. Proc. § 337) after discovery, but in any event within ten years (Code Civ. Proc. § 337.15) after substantial completion) (distinguished by *McDonald v. Antelope Valley Community College Dist.* (2008) 45 Cal.4th 88 (2008) (concluding there is neither an express limit on grounds for tolling, nor, as in *Lantzy*, a textual or legislative-intent-based rationale that would compel declining to

extend the usual rule to FEHA claims, so FEHA claims may be equitably tolled during the voluntary pursuit of alternate remedies).

Finally, SB 800 or California's Right to Repair Act (discussed in more detail, *infra*, Part III) creates a slightly more complex process for determining what statutes of limitation and what statutes of repose may apply to any particular construction defect. Civil Code section 941 provides that Code of Civil Procedure sections 337.1 and 337.15 (the four-year and ten-year status of repose for patent and latent defects, respectively) do not apply to actions under the Right to Repair Act. Instead, Civil Code section 941, subd. (a) establishes a new statute of repose that expires "10 years after substantial completion of the improvement but not later than the date of recordation of a valid notice of completion." Civ. Code § 941, subd.(a). Section 941, subd. (e) provides that the "time limitations established by this title do not apply to any action by a claimant for a contract or express contractual provision." Civ. Code § 941, subd. (e).

Moreover, although the Right to Repair Act maintains the 10-year limitation period for actions falling within the ambit of the Act, there are shorter time frames prescribed for certain types of defects. For example, plumbing systems must operate properly for up to four years after the close of escrow. Civ. Code, § 896(e). Irrigation and drainage claims shall operate properly so as not to damage landscaping or other external improvements for up to one year from close of escrow (Civ. Code, § 896, subd. (g)(7)), and painting shall be applied in a manner so as not to cause deteriorating of the building surfaces for up to five years from close of escrow (Civ. Code, § 896, subd. (g)(10)). There are also tolling rules that apply. The limitations period is tolled from the time of the original claim to, for example, 100 days from completion of repairs, or 45 days from response due of an unresponsive builder.

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

There are two statutes that establish procedures for pre-litigation notice of claims and the opportunity to cure. One such statute is the Right to Repair Act or SB 800, which applies to residential construction defect actions. Another is the Calderon Amendment to the Davis-Stirling Common Interest Development Act, which applies to a homeowners association's right to sue for construction defects.

Although the two statutes are analogous, there are some significant differences. For example, the pretrial process in the Calderon Amendments are mandatory and involve a minimum 180-day period of information exchange, whereas SB 800's pre-litigation process lasts for a minimum of 101 days and the builder can opt out by using its own non-adversarial contractual provision. SB 800 also contains an express provision excusing compliance with the Calderon Amendments where the requirements of the two statutes are substantially similar. Civ. Code, § 935.

SB 800 applies new procedures and remedies for the making and resolving of construction defect claims for new residential construction. It is codified at Civil Code section 895 et seq. SB 800 applies to all newly constructed residential property intended to be sold as an individual dwelling unit, where the purchase agreement was signed by the seller on or after

January 1, 2003.¹ Civ. Code, §§ 896, 938. These provisions are also binding on original purchasers' successors-in-interest. Civ. Code, § 945. The goal of SB 800 is to provide homeowners with a means to have construction defects addressed, while allowing builders the right to fix problems prior to litigation. Another purpose is to stop defect claims for technical code violations, such as improper nail patterns, and instead focus on whether a home functions as "a home," such that the inclusion of the phrase "materially comply" throughout is intended to indicate that minor technical code violations are no longer actionable. Hence the enactment of SB 800 was intended to improve the standards and procedures for early disposition of construction defect claims.

Civil Code sections 910 to 938 outline the pre-litigation procedures required under the Right to Repair Act. Section 910 provides that a claimant may not file an action against any party alleged to have contributed to a violation of a building standard until the claimant has initiated pre-litigation procedures by providing written notice to the builder. Civ. Code, § 910, subd. (a). If the homeowner does not file a written claim with the builder in advance of filing suit, SB 800 provides for a statutory bar to the action, and a court would have no authority to hear the case and would dismiss the case without prejudice (to be reinitiated after proper exhaustion of the SB 800 process). Civ. Code, § 930, subd. (b).

Note that until service of the notice, the builder has no obligation to respond to requests for documents pursuant to Civil Code section 912 (e.g., builder must provide copies of all relevant plans, specifications pertaining to residence, etc.). But within fourteen days of receipt of the notice, the builder must acknowledge the notice. If the builder does not acknowledge the notice, the pre-litigation procedures do not apply, thus enabling the claimant to file suit against the builder. Civ. Code, §§ 913, 915.

Where there is service of notice, the builder must provide copies of relevant plans and other documents within thirty days thereafter. If a builder fails to comply, then the homeowner may proceed with filing of an action without giving the builder an opportunity to fix the problem. When the builder is in compliance, however, the builder has the right to offer to repair the alleged violation within the timeframe for the repair set forth in the Act. Civ. Code, § 917. Upon receipt of the offer to repair, the homeowner then has thirty days to authorize the builder to proceed. If a builder has complied with the Act's requirements and has completed a repair prior to the filing of an action by a homeowner (and if there has been no previous mediation between the parties), the homeowner is then required to request mediation in writing.

The builder also has the right to inspect and test the alleged violations. Civ. Code, § 916. Within fourteen days after acknowledgement of receipt of the notice of the claim, builders can inspect the claimed unmet standards. Nothing that occurs during an inspection may be used or introduced as evidence to support a spoliation defense by any potential party in a subsequent litigation. Most significantly, if a builder intends to hold a subcontractor, design professional, individual product manufacturer, etc. responsible for its contribution, the builder shall provide notice to that person in advance to allow them to attend the initial inspection.

¹ For those properties where a purchase agreement was signed prior to January 1, 2003, the relevant law is codified at Code of Civil Procedure sections 337 and 337.15

In short, under the Right to Repair Act, if no offer to repair the alleged defect(s) is made by the builder, or if the builder otherwise fails to adhere strictly to the process, the homeowner may proceed by filing a lawsuit.

Similarly, the California Legislature has established procedural (i.e., meet and confer) prerequisites to a civil action by a homeowners association against a common interest development builder for damages from construction defects. Known as the Calderon Amendment (Civ. Code, § 6000 (previously Civ. Code § 1375)), these prerequisites were added to the Davis-Stirling Common Interest Development Act (Civ. Code §§ 4000-6150). The Calderon Amendment expands the breadth of the prefiling dispute resolution process by involving not only the developer and the owner, but also the general contractor, all subcontractors, design professionals, and insurers of all potentially responsible parties. The Amendment also provided for the appointment of a dispute resolution facilitator to hold prelitigation case management and settlement meetings.

Like SB 800, the underlying objective of the Calderon Amendment is to reduce litigation. The Amendment specifically was enacted to reduce the number of construction defect lawsuits by mandating a series of privileged information exchanges and scheduled meetings between potential litigants as a precondition of litigation, through which settlement may be facilitated.

As such, before a homeowners association may file a complaint for damages against a builder, developer, or general contractor based upon a claim for defects in the design or construction of a common interest development project, a dispute resolution process must be followed. Civ. Code, § 6000(a). Civil Code section 6000, subdivisions (b) through (o) mandate a series of notices which commence the 180-day dispute resolution period, information exchanges, physical discovery (inspection and testing), meetings, and privileged communications conducted under the auspices of a dispute resolution facilitator, and involving all potentially responsible parties and their insurers. The Calderon notice tolls all statutes of limitation and statutes of repose by and against all potentially responsible parties regardless of whether they are named in the notice. Civ. Code, § 6000, subd. (c). Moreover, the Calderon process allows the parties to select a neutral dispute resolution facilitator and requires that party representatives and insurance carriers participate with settlement authority in prelitigation negotiations.

The builder, developer, or general contractor may submit a written settlement offer and request a meeting with the association's board. Civ. Code, § 6000, subd. (k). However, if the offer is not timely submitted, the association is relieved of all further Calderon objections. Civ. Code, § 6000, subd. (k)(1)(B). The board must meet to discuss the offer and, if the board rejects the offer, must call a meeting for the association members to consider the offer. Civ. Code § 6000, subd. (k)(1)(D). The respondent must pay the expenses of the meeting, and all discussions are privileged. Finally, defect lists, demands, communications, negotiations, and offers are inadmissible at trial under Evidence Code sections 1119 through 1124. See Civ. Code § 6000, subds. (k)–(l).

On completion of the 180-day dispute resolution process (or possibly 360-day period if an extension of 180-days is granted), if the matter has not been settled, the association may file a complaint, which will be assigned for trial at the earliest possible date. See Civ. Code § 6000(c).

IV. INSURANCE COVERAGE AND ALLOCATION ISSUES

A. General Coverage Issues

General liability insurance (i.e. insurance that protects the insured against third party liability claims) is involved in practically every construction claim. General liability insurance typically provides defense and indemnity benefits. Commercial general liability (CGL) policies, formerly comprehensive general liability policies, provide broad coverage for liability arising out of property damage (i.e. “physical injury to or destruction of tangible property”) and bodily injury (i.e. “bodily injury, disease, or sickness sustained by a person”) to third parties. Insurers issuing this form of insurance are obligated to retain the attorneys and consultants necessary to defend the defendants.

To constitute property damage, the damage must be to tangible property. For example, because water intrusion nearly always causes physical injury to tangible property, satisfying the foregoing definition of “property damage” does not generally prove difficult. However, the definition of property damage does raise the question of whether incorporating defective material or workmanship into a building causes physical injury to the structure. See *Economy Lumber Co. v. Ins. Co. of North America* (1984) 157 Cal.App.3d 641 (examining the viability of the incorporation theory under the revised property damage definition and holding the diminution in value constituted property damage); cf., *St. Paul Fire & Marine Ins. Co. v. Coss* (1978) 80 Cal.App.3d 888 (holding that, under the definition of property damage, a building contractor’s incorporation of both defective workmanship and defective materials in a house was not considered physical injury to the residence).

In contrast to property damage claims, bodily injury claims occur less often in construction litigation and generally are limited to emotional distress claims associated with the alleged deficient work by the contractor or developer. Moreover, the California Supreme Court established an important limitation to bodily injury claims in *Waller v. Truck Ins. Exch.* (1995) 11 Cal.4th 1, 43 (holding that a CGL policy does not cover emotional distress damages that flow solely from uncovered economic damages).

The most critical exclusion in determining the availability of coverage for construction defect claims is the “work product” or “your work” exclusion, the purpose of which is to exclude coverage for the cost to repair defective work by the insured, generally the contractor. California courts have consistently found this exclusion to bar coverage for the cost to repair the insured’s defective work, reasoning that a contractor must be responsible for performing its work in a workmanlike manner. Thus, the contractor cannot be indemnified for its failure to fulfill its contractual obligation to construct the work in accordance with a project’s plans and specifications. See *Diamond Heights Homeowners Ass’n v. Nat’l Am. Ins. Co.* (1991) 227 Cal.App.3d 563 (observing that if a contractor were able to insure the costs of repairing deficient work, it would have less incentive to perform the work without defects in the first instance).

Another application of the work product exclusion occurs when the insured’s defective work damages satisfactory work performed by the insured. See *Western Employers Ins. Co. v. Arciero & Sons* (1983) 146 Cal.App.3d 1027 (affirming holding in carrier’s favor and observing

that plain language of contractor's insurance policy extended the work product exclusion to resulting damage not only to defective work but also to satisfactory work).

The work product exclusion covers only property damage to the completed work of others or completed work performed on the insured's behalf. Consequently, an insured seeking coverage for a construction defect claim must demonstrate that its alleged deficient work has caused damage to the work of other trades or to completed work performed on its behalf.

Moreover, the exclusion applies only to damage to the insured's work; thus, damage to the work of others even during the repair of the insured's work is exempt from exclusion. See *St. Paul Fire & Marine Ins. Co. v. Sears, Roebuck & Co.* (9th Cir. 1979) 603 F.2d 780, 784 (holding that coverage would be afforded for the damage to the work of others "when the Named Insured's product becomes so integrated into other tangible property such that a repair or replacement of that product would entail some injury to or replacement of a part of the existing property which did not originate from the Named Insured"); cf., *New Hampshire Ins. Co. v. Vieira* (9th Cir. 1991) 930 F.2d 696 (distinguishing *Sears* on the grounds that the repairing of defective installation required adding not removing the defective material). Thus, *Sears* and *Vieira*, when read together, provide that coverage exists when the removal of defective work damages the work of others, but the work product exclusion applies when damage to other work is unavoidable in installing the omitted work.

B. Trigger of Coverage

In addition to determining whether a claim involves damage sustained during the policy period, it must also be established that the property damage or bodily injury resulted from an occurrence. CGL policies defined "occurrence" as an "accident, including continuous or repeated exposure to substantially the same general harmful conditions."

An occurrence of property damage, not an occurrence of injury to the claimant, triggers coverage. See *Century Indem. Co. v. Hearrean* (2002) 98 Cal.App.4th 734 (2002) (holding coverage was not determined by the occurrence of injury to the particular claimant but by the continuous and progressive injury to the hotel property caused by defective design and construction because to hold otherwise would transform an occurrence-based policy into a "claims made" policy); see also *Baroco West, Inc. v. Scottsdale Ins. Co.*, 110 Cal.App.4th 96 (2003) (denying coverage because damage to property occurred during construction operations, which was excluded under the policy). Finally, California courts have concluded that claims for negligent and intentional misrepresentation do not involve an accident and thus are not covered under a standard CGL policy. See *Miller v. Western Gen. Agency, Inc.* (1996) 41 Cal.App.4th 1144 (1996).

Even if the damage and occurrence requirements are satisfied, courts must still determine whether the complaining party sustained damage during the policy period. This requirement is often referred to as the "trigger of coverage," i.e., the operative event that must occur during the policy period in order to invoke, or trigger, coverage. In most claims for property damage, including construction defect disputes, the timing of the damages is fairly clear. In some instances, however, the timing of the property damage is not so clear. This is because a latent

defect may cause damage that first manifests long after it occurred, or the nature of the property damage may implicate one or multiple policies. For example, a single event could result in progressively deteriorating injury, such as poorly installed windows allowing intermittent water intrusion and mold growth and resulting damage.

California courts have adopted the continuous trigger theory of coverage in progressive property damages cases. Liability coverage under a CGL policy for bodily injury and property damage is therefore established at the time the complaining party was actually damaged. Therefore, each insurer that issued a policy during the period that damage potentially occurred must defend the claim. See *Montrose Chem. Corp. Admiral Ins. Co.*, 10 Cal. 4th 645 (1995). That is, if the damage is progressively deteriorating over multiple policy periods, the property damage may trigger coverage under each policy in effect during that period. *Maryland Cas. Co. v. Nat'l Am. Ins. Co.* (1996) 48 Cal.App.4th 1822. *Pepperell v. Scottsdale Ins. Co.* (1998) 62 Cal.App.4th 1045 reaffirmed this and held that all covering policies effective during the period that damage potentially occurred must defend a construction defect claim.

The significance of *Montrose* and its progeny to construction defect litigation is that coverage is not limited to the policy in effect at the time when the precipitating event or condition occurred, or to the policy in effect when the property damage first manifested itself. Further, the policy's full limit may be exposed, even if the property damage continues after the policy is terminated. As the California Supreme Court later explained in *Aerojet-General Corp. v. Transport Indem. Co.* (1997) 17 Cal.4th 38, 56, "if specified harm is caused by an included occurrence and results, at least in part, within the policy period, it perdures to all points of time at which some such harm results thereafter."

C. Allocation Among Insurers

The duty to defend is broader than the duty to indemnify, because an insurer is obligated to defend its insured against claims that create a potential for coverage under the insured's policy. Thus, even though the allegations may be false or ultimately never proved at trial, they will trigger the insurer's defense obligation if they create a bare potential or possibility of coverage. See *Buss v. Superior Court* (1997) 16 Cal.4th 35; *Montrose Chem. Corp. v. Superior Court* (1993) 6 Cal.4th 287. Moreover, the duty to defend arises when the policy is ambiguous, and the insured would reasonably expect coverage. See also *La Jolla Beach & Tennis Club v. Indus. Indem. Co.* (1994) 9 Cal.4th 27. However, if the claim does not involve damages that possibly occurred during the policy's effective period, there is no defense obligation. See *Waller v. Truck Ins. Exch.* (1995) 11 Cal.4th 1.

The duty to defend arises when the insured tenders the defense. See *Montrose Chem. Corp.*, *supra*. Once the defense obligation attaches, it usually continues until the claim is resolved. An insurer's unreasonable refusal to defend an action can subject the insurer to bad faith liability. See *Campbell v. Superior Court* (1996) 44 Cal.App.4th 1308 (insurer's alleged failure to defend a general contractor that claimed to be an additional insured under a subcontractor's policy).

In 2008, the California Supreme Court issued its ruling in *Crawford et al. v. Weather Shield Mfg. Inc.* (2008) 44 Cal.4th 541. In its decision, the California Supreme Court dealt with the contractual duty to defend in a non-insurance context. The court summarized the issue as follows: "We consider whether, by their particular terms, the provisions of a pre-2006 residential construction subcontract obliged the subcontractor to defend its indemnitee — the developer-builder of the project — in lawsuits brought against both parties, insofar as the plaintiffs' complaints alleged construction defects arising from the subcontractor's negligence, even though (1) a jury ultimately found that the subcontractor was not negligent, and (2) the parties have accepted an interpretation of the subcontract that gave the builder no right of indemnity unless the subcontractor was negligent."

More specifically, the California Supreme Court posed this question: "Did a contract under which a subcontractor agreed 'to defend any suit or action' against a developer 'founded upon' any claim 'growing out of the execution of the work' require the subcontractor to provide a defense to a suit against the developer even if the subcontractor was not negligent." The California Supreme Court answered this question in the affirmative and ruled that the contractual defense obligation in an indemnity provision of a construction subcontract operates in the same manner as the defense obligation of a general liability policy. The contractual duty to defend is prospective or prophylactic in nature and arises on the tender of defense. Further, the duty to defend is triggered by allegations of damage embraced by the indemnity agreement, regardless of whether the subcontractor is ultimately found negligent.

For example, as noted above, a progressive damage construction defect case creates a unique situation where multiple policies can be triggered. Because California has adopted the continuous trigger theory of coverage, construction defect claims often trigger multiple policies to defend the claim. In *Aerojet-General Corp. v. Transport Indem. Co.*, *supra*, 17 Cal.4th 38, 70, the California Supreme Court established that each carrier has a duty to defend the insured that is "separate and independent" from the duty of other carriers. Moreover, the *Aerojet* court explained that if covered damages potentially occurred during the insurer's policy period, the insurer is obligated to defend claims of damage occurring outside that policy period if the potential damages relate to harm during that period. *Id.* at p. 73.

Other hotly contested issues include defense and indemnity between a general contractor and its subcontractors, i.e., allocation between direct coverage and additional insured coverage. Generally, additional insured issues arise because an owner may require the general contractor to name the owner as an additional insured on the contractor's policies. The contractor, in turn, generally instructs and requires the subcontractors to name the contractor and owner as additional insureds on the subcontractors' policies. The purpose of the additional insured endorsement is to receive additional insurance benefits for liability arising out of the work by the principal named as insured under the policy. While the insured has direct rights, a question of allocation occurs once the insured's defense and indemnity has been covered.

Assuming that the general contractor has direct primary insurance, contribution will apply, and the court will equitable distribute costs of defense and indemnity between the triggered policies. *Maryland Casualty Co. v. Nationwide Mutual Insurance Co.* (2000) 81

Cal.App.4th 1082. The court has wide discretion to do equity to allocate liability. *Axis Surplus Ins. Co. v. Glencoe Ins. Ltd.* (2012) 204 Cal.App.4th 1214, 1231.

V. **CONTRACTUAL INDEMNIFICATION**

Historically, California law permitted Type 1 indemnity provisions in construction contracts. A Type 1 provision requires a party to indemnify and defend another from any claim arising out of or related to the indemnitor's scope of work, including the active negligence or misconduct of the indemnified party.

Starting in 1967, the California Legislature restricted the ability to contract for Type 1 indemnity in construction contracts. Civ. Code, section 2782. Thus, subject to very limited exceptions, California's construction contract anti-indemnity statute (Civ. Code, § 2782) makes broad form indemnity provisions unenforceable by prohibiting a party from requiring indemnity against its own sole negligence or willful misconduct.² The practical effect of Civil Code section 2782 is that no one can be forced to indemnify another party for that other party's sole negligence or willful misconduct. A recent expansion of this law makes clear that indemnity for active negligence is also generally unenforceable for both public and private contracts entered into on or after January 1, 2013.

However, Civil Code section 2782 does not prevent a party to a construction contract and the owner from negotiating and expressly agreeing to allocate, liquidate, or limit liability between themselves for design defects or other liability arising from the contract. Civ. Code § 2782.5. Section 2782.5 provides: "Nothing contained in Section 2782 shall prevent a party to a construction contract and the owner or other party for whose account the construction contract is being performed from negotiating and expressly agreeing with respect to the allocation, release, liquidation, exclusion, or limitation as between the parties of any liability (a) for design defects, or (b) of the promisee to the promisor arising out of or relating to the construction contract."

The California Legislature enacted Civil Code section 2782 because of the increasing use of hold-harmless agreements in construction contracts. Such hold-harmless agreements attempted to shift, to general contractors, responsibility for liabilities not historically the general contractors, such as liability for latent defects in a building caused by negligence of the [owner's]

² Civil Code section 2782(a) provides as follows:

Except as provided in Sections 2782.1, 2782.2, 2782.5, and 2782.6, provisions, clauses, covenants, or agreements contained in, collateral to, or affecting any construction contract and that purport to indemnify the promisee against liability for damages for death or bodily injury to persons, injury to property, or any other loss, damage or expense arising from the sole negligence or willful misconduct of the promisee or the promisee's agents, servants, or independent contractors who are directly responsible to the promisee, or for defects in design furnished by those persons, are against public policy and are void and unenforceable; provided, however, that this section shall not affect the validity of any insurance contract, workers' compensation, or agreement issued by an admitted insurer as defined by the Insurance Code.

architect or engineer. Thus, while section 2782 was intended to eliminate indemnity agreements forced upon parties to construction contracts, and which required the promisor to indemnify the promisee for the promisee's sole negligence, section 2782.5 was enacted to permit parties to continue to negotiate and limit their respective liability to each other. *See Markborough California, Inc. v Superior Court*, 227 Cal App 3d 705 (1991).

Also of significance is Civil Code section 2782.05, which the California Legislature added in 2012. As explained above, section 2782 protects certain contractors, subcontractors, and suppliers from having to indemnify public or private owners for the owners' active negligence. The more recently enacted section 2782.05 expands the protections for subcontractors under new contracts. Section 2782.05 extends the provisions of section 2782 to any construction contract executed on or after January 1, 2013. The statute prohibits indemnity provisions that attempt to shift liability or defense obligations for the active negligence of the party to be indemnified. Although it is not applicable in a number of circumstances, including residential projects, section 2782.05 now prevents other participants from imposing certain indemnity, insurance, and defense duties on subcontractors.

Specifically, Civil Code section 2782.05 provides that construction subcontracts may not require a subcontractor to indemnify, defend, or insure a general contractor, construction manager or other subcontractor for: (1) claims of personal injury or property damage or other loss to the extent that the claims relate to the active negligence or willful misconduct of the indemnified parties; (2) claims that arise from any defects in designs provided by the indemnified parties; or (3) claims that do not arise out of the subcontractor's scope of work set forth in the subcontract. That is, general contractors, subcontractors and construction managers may not obtain indemnity for their own active negligence or willful misconduct, nor may they obtain a defense against allegations of their active negligence or willful misconduct. However, indemnity may still be required for the owner or general contractor's "passive negligence." In other words, the Legislature has provided that the parties may enter into certain types of agreements, as long as the indemnitee cannot avoid its obligations for its active negligence or willful misconduct. Passive negligence (such as failure to discover a dangerous condition) on the part of the general contractor is still subject to indemnity.

Note that the Legislature has placed the onus on the party seeking indemnification to notify the indemnitor of their demand to indemnify. Section 2728.05 provides that the subcontractor has no obligation to defend or indemnify the general contractor until the general contractor provides a written tender of the claim. Likewise, the new regime adds two further subcontractor protections. A subcontractor can no longer be forced to indemnify or insure a general contractor or another subcontractor (or their agents) for defects in the project's design provided by them to that subcontractor, or to the extent the claims at issue arise outside the scope of that subcontractor's work. Civil Code, § 2782.05, subd. (a).

In short, the California Legislature has taken big steps towards holding construction participants accountable for their own "active negligence" by not allowing them, in many circumstances, to foist their liability onto other participants. Additional protections have been added to protect a subcontractor from having to indemnify other participants for their active

negligence, for defects in the project's design, and for claims arising outside the scope of the subcontractor's work.

VI. **CONTINGENT PAYMENT AGREEMENTS**

A contingent payment clause is a contractual provision that makes payment contingent upon the happening of some event. In construction subcontracts, the typical contingent payment clause makes the subcontractor's payment contingent upon the payment of the contractor by the owner. Such clauses take on one of two forms in subcontract agreements. Some clauses link the timing of the subcontractor's payment to the time when payment is made by the owner ("pay-when-paid clauses"). Other clauses specify that the owner must pay the contractor in order for the subcontractor to ever receive payment ("pay-if-paid clauses").

A. **Enforceability**

In California, "pay-if-paid" clauses are unenforceable because they unlawfully inhibit subcontractor's mechanics lien rights. *William R. Clark Corp. v. Safeco Ins. Co.* (1997) 15 Cal.4th 882. Because Civil Code section 3262 prevents a waiver of lien rights, "pay-if-paid" provisions are prohibited for their indirect effect on lien rights. A pay-if-paid clause is, in essence, an indirect forfeiture of a subcontractor's constitutionally protected lien rights. As noted herein, a subcontractor may not waive its mechanics lien rights except under certain specific circumstances. Civil Code, § 3262.

As to pay-when-paid clauses, those are upheld as valid and enforceable, but the contractor may avoid payment for a reasonable period of time only. *Yamanishi v. Bleily & Collishaw, Inc.* (1972) 29 Cal.App.3d 457, 462; see also *William R. Clark Corp.*, *supra*, 15 Cal.4th at p. 885. As noted by the California Supreme Court: "[I]f reasonably possible, clauses in construction subcontracts stating that the subcontractor will be paid when the general contractor is paid will not be construed as establishing true conditions precedent, but rather as merely fixing the usual time for payment to the subcontractor, with the implied understanding that the subcontractor in any event has an unconditional right to payment within a reasonable time." *William R. Clark Corp.*, *supra*, 15 Cal.4th at p. 885.

B. **Requirements**

As noted above, only pay-when-paid clauses are enforceable. The contractor may avoid payment, but only for a reasonable amount of time. A pay-when-pay clause is valid and allows the general contractor to delay payment to the subcontractor for a reasonable time while awaiting payment from the owner.

The net effect of the *William R. Clark Corp.* Supreme Court decision is that the contractor must pay the subcontractor whether or not the owner pays the contractor and regardless of what is in the contract.

VII. **DAMAGES LIMITATION**

A. **Personal Injury Damages vs. Construction Defect Damages**

As stated herein, the Legislature enacted the Right to Repair Act, which overruled the California Supreme Court's holding in *Aas v. Superior Court* (2000) 24 Cal. 4th 627 that homeowners could not recover in negligence against defendant developers of a condominium project for prospective property damage from construction defects. The Right to Repair Act specifically provides that upon a showing of violation of an applicable standard, a homeowner may recover economic losses from a builder without having to show that the violation caused property damage or personal injury. In such an instance, the Act abrogates the economic loss rule, thus legislatively **superseding** *Aas*, and allows plaintiff homeowners to recover for prospective property damage in this circumstance.

That being said, Civil Code section 944 of Right to Repair Act provides a “limitation” on what damages are recoverable by a claimant, including but not limited to: reasonable value of repairing any violation of the standards, reasonable cost of repairing any damages caused by repair efforts, reasonable cost of repairing and rectifying any damages resulting from the failure of the home to meet the standards, and reasonable investigative costs for each established violation.

As to emotional distress damages, in *Erlich v. Menezes*, 21 Cal. 4th 543 (1999), the California Supreme Court held that homeowners cannot recover emotional distress damages for negligent construction of their homes when negligence directly causes only economic and property damage and no independent tort duty is breached. As such, the available damages for defective construction are limited to the cost of repairing the home or the diminution in value, whichever is less.

B. **Attorney's Fees Shifting and Limitations on Recovery**

California follows the American Rule whereby each party must pay his or her own attorney fees, except as specifically provided for by statute or agreement of the parties. Code Civ. Proc., § 1021. Civil Code section 1717 governs attorney fees awards for enforcing contracts that include fee-shifting clauses. Section 1717 awards attorney fees to the party prevailing on the contract in any action on a contract where the contract specifically provides for an award of attorney's fees and costs incurred to enforce the contract.

Specifically pursuant to California's mechanics lien law, the prevailing party is entitled to reasonable attorney fees in an action to enforce payment of the claim stated in a bonded stop payment notice. Civ. Code, § 8558. Previously, the prevailing party in an action to release a property from a mechanic's lien could only recover a maximum of \$2,000 in attorneys' fees. Recent amendments to the statute removed that cap and a prevailing party is now entitled to recover its reasonable attorney fees.

Finally, note that under Code of Civil Procedure section 1029.8, an unlicensed person who causes injury or damage as a result of providing goods or services for which a license is required may be liable for attorney fees in the discretion of the court, unless the person had a

good faith belief that he or she was licensed. Treble damages may also be recovered within the court's discretion.

C. Consequential Damages

Contractual provisions that mutually waive the rights of the owner and contractor to recover consequential damages are frequently used in construction contracts. Consequential damages are those that do not follow directly and immediately from breach of contract (direct damages), but follow instead from some of the consequences of the breach. The most common example in the construction context is lost profits.

When a party breaches a construction contract, the law requires the non-breaching party to be placed in the position that it would have been but for the breach. The non-breaching party can recover both direct/general damages or indirect/consequential damages. To be recoverable, however, consequential damages must be contemplated by the parties at the time of contracting. Parties to a contract are deemed to have expected the normal and usual risks in the absence of specific contractual language to the contrary. Accordingly, general or direct damages, which represent the normal and expected risks, are always recoverable. However, consequential damages, which represent additional risks due to unusual circumstances of the non-breaching party, are not awarded unless the non-breaching party can establish that the parties were aware of the special circumstances at the time they entered into the contract.

Waiver of consequential damages between sophisticated parties is generally enforceable. Cal. U. Com. Code § 2719(3). But courts will not enforce a waiver that is unconscionable, against public policy, or prohibited by statute. Some courts will enforce consequential damages waivers to narrow the issues to be resolved without a trial. Other courts find that it is a question of fact for a jury to decide whether certain categories of damages are consequential and thus barred. Thus, even where the parties have agreed to waive their right to recover all consequential damages, courts may still find that whether a particular damage is a consequential damage is a question of fact that should be decided by a jury. As such, owners and contractors should retain counsel to carefully draft consequential damages waivers to fit the particular type of construction project at issue to increase the odds that: (1) the parties will not dispute what types of damages are recoverable under the contract; and (2) if there is such a dispute, the waiver will be found to be enforceable.

In short, both owners and contractors should avoid general boilerplate or “catch-all” consequential damages waivers that do not define what the parties mean by consequential damages. Waivers should be project specific in that they should anticipate and define the potential types of damages that could arise with this project and ensure they are clearly waived.

D. Delay and Disruption Damages

Homeowners are entitled to damages for losses suffered because completion of the project was delayed beyond the completion date provided in the contract. The damages are based on a cause of action for a breach of the contract. The measure of damages is the rental value of the property, or other value of the loss of the use of the property, during the period of

delay. *Amerson v. Christman* (1968) 261 Cal.App.2d 811, 824–825. In addition, as noted herein, California courts also allow for any other losses that are foreseeable and naturally result from the damage caused to the owner's property, including lost profits during the period repairs are being performed. *Diamond Springs Lime Co. v. American River Constructors* (1971) 16 Cal.App.3d 581, 598–599.

E. **Economic Loss Doctrine**

The economic loss doctrine precludes tort recovery in the absence of personal injury or property damage. In *Aas*, the California Supreme Court explained that under the economic loss rule, “appreciable, nonspeculative, present injury is an essential element of a tort cause of action.” *Aas, supra* 24 Cal.4th at p. 646. As such, “Construction defects that have not ripened into property damage, or at least into involuntary out-of-pocket losses, do not comfortably fit the definition of ‘appreciable harm’—an essential element of a negligence claim.” *Ibid*.

Aas has since been superseded by the passage of the Right to Repair Act. The Right to Repair Act expressly superseded *Aas* by allowing claims where there is no resultant or consequential damage other than the defect itself. These causes of action, however, are based on statutory strict liability. Now, proof of actual damage to real property is not required for most of the stated actionable defects. If a claim for damages is made under SB 800, the homeowner is entitled to damages for the reasonable value of repairing any violation of the standards defined under the SB 800, the reasonable costs of repairing any damage caused by the repair efforts, the reasonable cost of repairing and rectifying any damages resulting from the failure to meet the standards, the reasonable cost of removing and replacing any improper repair by the builder, reasonable relocation and storage expenses, lost business income if the home was used as a principal

F. **Interest**

Under Civil Code section 3287, “A person who is entitled to recover damages certain, or capable of being made certain by calculation . . . is entitled also to recover interest thereon from that day . . .” Damages are deemed certain or capable of being made certain within the provisions of section 3287 where there is no dispute between the parties concerning the basis of computation of damages if any are recoverable but where their dispute centers on the issue of liability giving rise to damage.” *Esgro Central, Inc. v. General Ins. Co. of America* (1971) 20 Cal.App.3d 1054.

G. **Punitive Damages**

Punitive or exemplary damages are permitted in California in actions not arising from a contract where a defendant is guilty of oppression, fraud, or malice. Civ. Code, § 3294. As such, tort liability is a necessary predicate for punitive damages.

H. **Other Damage Limitations**

Expert costs incurred investigating how to repair construction defects (known as Stearman costs or fees) are recoverable as damages without any contractual provision. *Stearman v., Centex Homes* (2000) 78 Cal.App.4th 611, 625; see also Civil Code § 3333. Civil Code section 3333 provides that the measure of damages is the amount that will compensate for all the detriment proximately caused by the breach. The expenses incurred by a party in having professionals investigate construction deficiencies in order to formulate an appropriate repair plan are inclusive of the costs of remedying the defects and are recoverable as part of the cost of repair. *Stearman, supra*, at pp. 624-25.

The Right to Repair Act also specifically provides for recovery for investigative costs. Civil Code § 944. In contrast, expert costs incurred to prove up or defend a litigated case ordinarily are not recoverable as costs in the absence of an attorney's fees clause in a contract, or a statutory settlement offer. But contractual attorney fees provisions often support recovery of costs of experts incurred in litigation.

VII. CASE LAW AND LEGISLATION UPDATE

Update on SB 800

As noted herein, SB 800 was enacted to curb construction defect lawsuits by giving developers an opportunity to repair defects before being sued in court. Despite its intentions, many critics have noted that SB 800 will probably not result in an appreciable decrease in the amount of construction litigation in California. Indeed, several recent California decisions signify that SB 800 may actually cause additional litigation over the statute's meaning and intent. The exclusivity issue in particular has already been the subject of litigation, with courts concluding that the Right to Repair Act does not provide an exclusive remedy or limit common law claims of defects that have caused property damage.

The first decision to address the exclusivity issue was *Liberty Mutual Insurance Co. v. Brookfield Crystal Cove LLC* (Aug. 28, 2013) 219 Cal.App.4th 98 (*Liberty Mutual*). There, the court held that an insurer's subrogation claim was not time barred under SB 800 because the statute does not provide the exclusive remedy for construction defects involving "actual" property damage, as opposed to mere economic damages. The court explained that SB 800 was intended to change the law so that homeowners could file suit for construction defects even where the only damages are economic damages. But the court found that nothing in the statute supported a conclusion that SB 800 rewrote the law on common law claims arising from actual damages sustained as a result of construction defects.

In reaction to *Liberty Mutual*, a number of trade organizations petitioned the Supreme Court to review. They argued that the decision opened the floodgates to allowing homeowners to choose a remedy that avoids the statutes of repose contained in SB 800. They further argued that the decision affected the enforceability of insurance policies, CC&Rs, and purchase agreements that incorporated the Right to Repair law (i.e., for builders who "opted in" to the Act's pre-litigation "right to repair" provisions, those rights no longer exist in cases where there is actual physical damage). The critics contended that if SB 800 intended to preserve common law tort theories, then the Legislature would not have implemented the new functionality standards and specifically mention which standards required a showing of damage. Finally, they

argued that the decision eliminated a fundamental right of SB 800—the absolute right to repair. The Supreme Court, however, denied review on December 11, 2013.

Since then, the California appellate courts have decided two cases with ramifications under the Right to Repair Act. The first, *Burch v. Superior Court* (Feb. 19, 2014) 223 Cal.App.4th 1411, followed *Liberty Mutual* by holding that the Right to Repair Act does not provide the exclusive remedy for a homeowner seeking damages for construction defects that resulted in property damage. The *Burch* court concluded that the plaintiff's claims for negligence and breach of implied warranty alleged damages for construction defects, including defects allegedly resulting in property damage, which claims were not precluded by the Act. Separately, just two days later, the court in *KB Home Greater Los Angeles v. Superior Court* (Feb. 21, 2014) 223 Cal.App.4th 1471, confirmed that if a party does not follow the SB 800 procedures to precision, the case will be thrown out. The court held that failure to give timely notice and opportunity to inspect/offer to repair the construction defect excused liability for damages under the act.

In sum, *Liberty Mutual* and *Burch* effectively provide homeowners with a choice of remedies when actual damage has occurred: proceed via SB 800 or common law. But the Court's decision in *KB Home* makes clear that the former route must follow strictly SB 800's procedures. If the defect is time-barred under SB 800, homeowners will logically elect to proceed under common law, which provides a ten-year statute of limitations for all latent construction defects. Now that there is clear precedent on the issue, California could see an increase in construction defect litigation of claims that are now available under common law remedies.

COLORADO

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I. MECHANICS' LIEN BASICS

Mechanics' liens in Colorado are statutory, and courts construe the right to a mechanics' lien strictly.¹ Once the right is established, however, Colorado courts liberally construe mechanics' lien statutes in favor of mechanics and materialmen.²

A. Who May File a Mechanics' Lien?

Any person performing labor or furnishing material used in constructing, altering, improving, adding to, or repairing any structure or improvement upon land is entitled to file a mechanics' lien.³ This includes general contractors and subcontractors.⁴ The only parties without lien rights are those who merely supply materials to materialmen.

B. What Items are Liable?

Generally, the labor and materials of those entitled to file a mechanics' lien are lienable.⁵ Tools are lienable if they are consumed during construction; for example, sanding belts and certain saw blades.⁶ Services performed by a superintendent are lienable.⁷ Labor and materials for sidewalks, curbs, and gutters are lienable.⁸ Labor performed and materials used off-site, such as fabricated steel components, can likewise be lienable.⁹ Fixtures are also lienable.¹⁰

Work done by a lien claimant to correct his own errors is not lienable.¹¹ Attorneys' fees are not lienable.¹²

C. Mechanics' Lien Perfection.

The necessary steps for perfecting a mechanics' lien in Colorado are set forth in C.R.S. §§ 38-22-109 and 110.

First, a lien claimant must preserve the lien by serving upon the owner or reputed owner and the general contractor a notice of intent to file a lien statement. This notice must be served at least ten days before recording a lien statement.¹³

Second, not less than ten days after properly serving a notice of intent, the claimant must record a lien statement with the county clerk and recorder. The lien statement must be sworn and include an affidavit of service. Particular requirements of the lien statement are included in C.R.S. § 38-22-109. Laborers by day must file their lien statements after their last work and within two months of completing improvements upon the real property. All other claimants must file within four months.¹⁴

Third, a foreclosure action must be commenced within six months after the lien claimant completes its improvements or the date of project completion, whichever is later.¹⁵ When all work upon a project has been abandoned for three months, completion is deemed to have occurred.¹⁶

Fourth, once a judgment is entered in a foreclosure action, a sheriff's sale of the property may be initiated.¹⁷ After the sale is concluded, the highest bidder is issued a certificate of purchase.

II. STATUTES OF LIMITATION AND REPOSE

A. Statute of Limitations Against Construction Professionals.

The statute of limitations for claims against construction professionals is two years from the date that the claim accrues.¹⁸ A claim accrues on the date that the claimant or the claimant's predecessor-in-interest "discover[s] or in the exercise of reasonable diligence should have discovered the physical manifestations of a defect in the improvement which ultimately causes the injury."¹⁹

1. Tolling.

The statute of limitations can be tolled. If a notice of claim is sent before the filing of a lawsuit, the statute of limitations does not run until sixty days after the notice-of-claim process required by the Colorado Construction Defect Action Reform Act ("CDARA").²⁰

Colorado courts previously accepted the proposition that a statute of limitations should be tolled during the time a party attempts to make repairs to an improvement.²¹ In 2010, the Colorado Supreme Court in *Smith v. Executive Custom Homes, Inc.*, 230 P. 3d 1186 (2010), rejected "the repair doctrine" and held that repairs do not toll the statute of limitations because the CDARA notice-of-claim process already provides for tolling.²²

2. Reimbursement/Third-Party Claims.

Reimbursement claims may be brought against a third party within ninety days of entry of judgment or settlement of the principal claims.²³ However, reimbursement claims may also be asserted before settlement or judgment of the principal claims.²⁴

B. Statute of Repose.

The statute of repose for claims against construction professionals is six to eight years from the date of substantial completion of the improvement.²⁵ A cause of action cannot be brought more than six years after the date of substantial completion, unless the physical manifestation of a defect is discovered or should have been discovered within the fifth or sixth year, in which event the statute of repose is extended for another two years.

The statute of repose is also subject to sixty-day tolling for the CDARA notice-of-claim process.²⁶ However, the statute of repose is not tolled by the ninety-day statute of limitations for reimbursement claims. In other words, the statute of repose can bar reimbursement claims against third parties before settlement or judgment of the principal claims.²⁷

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

CDARA establishes a mandatory notice-of-claim process affording the construction professional a right of remedy before litigation. A claimant must send a written notice describing the defect “in reasonable detail . . . and any damages claimed to have been caused by the defect.”²⁸ The construction professional then has thirty days to inspect the property, after which the construction professional may offer to repair the defect or propose a monetary settlement of the claim within thirty days of the inspection.²⁹ The claimant can accept or reject the repair offer or money, but unless a claimant accepts an offer in writing within fifteen days, the offer is automatically rejected.³⁰

IV. COVERAGE AND ALLOCATION ISSUES

Commercial general liability (“CGL”) policies provide indemnification when three threshold inquiries are satisfied: (1) that the claim arises within the policy definitions, (2) that coverage is triggered by the type of damage and the policy’s effective dates, and (3) the basis of the claim is not specifically excluded by the policy.

In Colorado, there is a split of authority on whether property damage caused by a construction defect is an “occurrence.” Generally, damage for the insured's own faulty work is excluded under the “business risk doctrine.” However, if property damage to third parties results from faulty workmanship, CGL policies will often cover the loss, and Colorado appellate courts are trending towards finding coverage for construction defects as covered “occurrences.”³¹ The

wide breadth of these cases and their contradictory conclusions demonstrate that the particular facts of each case should be carefully examined.

In addition to qualifying as an “occurrence,” damage resulting from poor workmanship must also be “property damage.” CGL policies define “property damage” as “physical injury to tangible property, including all resulting loss of use thereof, or loss of use of tangible property which has not been physically injured.” Only third-party property damage is intended to be covered. Various exclusions preclude the insured’s own work from being considered covered “property damage,” and the insured’s own property is always excluded. Moreover, the definition of “property damage” does not include purely economic losses.³²

Colorado follows the rule that coverage is triggered when the claimant sustains actual damage, and not when the act or omission that caused such damage was committed.³³ The Supreme Court has held that a third party, other than the insured, must sustain actual damage within the policy period in order to recover under a CGL policy defining “occurrence” as an “accident.”³⁴ However, the Supreme Court also ruled that plaintiffs “must have some legally recognizable injury to their interests during the policy period in order to recover.”³⁵ Two recent decisions make it clear that a third party who did not own the property during the policy period may have a viable claim as long as some property damage occurred during the policy period.³⁶

Some cases involve continuous trigger, i.e., a coverage trigger that exists continuously over many policy periods. For example, gradual roof corrosion, leading to a total collapse of the roof, may continue through several policy periods.³⁷ Indemnity for judgments or settlements in such cases is to be allocated according to time-on-the-risk and degree of risk assumed.³⁸

Numerous CGL exclusions can preclude coverage for claims arising out of construction defects. These include: the contractual liability exclusion; the owned property exclusion; the “your work” exclusions; the “your product” exclusion; the products-completed operations exclusion; the impaired property exclusion; the recall exclusion; and the alienated premises exclusion. Colorado courts construe these exclusions very narrowly and have found coverage for construction defects in a wide range of circumstances.³⁹

V. CONTRACTUAL INDEMNIFICATION

A. Anti-Indemnification Statute.

Colorado no longer allows contractual provisions intended to protect parties from their own negligence in construction.⁴⁰ Colorado law voids any provision in a construction agreement that requires a person to indemnify, insure or defend in litigation another person against liability for damage arising out of death or bodily injury to persons or damage to property caused by the negligence or fault of the indemnitee or any third party under the indemnitee’s control or supervision.⁴¹ This anti-indemnification statute includes a number of qualifications.⁴² For example, it does not affect any provision in a construction agreement that requires a person to indemnify and insure another person for an amount which is no greater than the “degree or percentage of negligence or fault attributable to the indemnitor or the indemnitor’s agents, representatives, subcontractors or suppliers.”⁴³ Nor does it affect the doctrine of *respondeat*

superior, vicarious liability or other nondelegable duties, or affect the liability for the negligence of an at-fault party.⁴⁴ It also does not affect the exclusive remedy provided within the workers' compensation statute.⁴⁵

The statute does not void or prohibit provisions requiring additional insured insurance for the indemnitee to the extent it provides "coverage to the indemnitee for liability due to the acts or omissions of the indemnitor."⁴⁶ However, any provision that requires the purchase of additional insured insurance for damage not caused by the fault of the party providing such insurance is void.⁴⁷

B. Common Law Indemnification.

Common law indemnity is also recognized in many instances, but a duty to indemnify only arises when there is a pre-existing legal relationship,⁴⁸ and the indemnitee can establish that it is wholly without fault.⁴⁹ When there is a right to indemnification, a contribution claim by an indemnitee against an indemnitor is barred.⁵⁰ Indemnification and contribution claims are mutually exclusive.

C. Statute Of Limitations And Repose.

In construction cases, indemnitees are not required to commence a claim for indemnification or contribution until the claims against the primary defendants are "settled" or "final judgment is entered."⁵¹ Thereafter, indemnitees have ninety days to bring claims.⁵² The Supreme Court has clarified, however, that indemnitees need not wait until the underlying suit is resolved to bring claims for indemnity or contribution.⁵³

VI. CONTINGENT PAYMENT AGREEMENTS

Colorado recognizes pay-if-paid provisions in construction contracts. However, such provisions must unequivocally express the party's intent to establish a condition precedent to payment to be enforceable. A pay-when-paid clause is an unconditional promise by the general contractor to pay its subcontractor even if the owner becomes insolvent.⁵⁴

VII. DAMAGE LIMITATIONS

CDARA places limits on the categories and amounts of recoverable damages.⁵⁵ Generally, claimants in Colorado can recover no more than "actual damages."

"Actual damages" are *the lesser of*:

- 1) the fair market value of the property without the alleged defect; or,
- 2) the reasonable cost to repair the alleged defect; or
- 3) the replacement cost of the property.

together with:

- 4) relocation costs, if any;

- 5) economic costs related to loss of use (residential property only);
- 6) interest;
- 7) cost of suit; and,
- 8) attorney's fees (but only if provided by statute or contract).⁵⁶

Under this definition, if the fair market value of the property without the defect is \$500,000, the cost to replace the property is \$250,000, and the cost to repair the defect is \$750,000, the claimant's "actual damages" are \$250,000.

In most instances, a claimant will not be able to recover more than its "actual damages." However, CDARA contains an exception to the "actual damages" limit if two conditions are met. First, the claimant must prove a violation of the Colorado Consumer Protection Act ("CCPA"), which involves deceptive trade practices such as false advertising, representing that a warranty exists without disclosing its limitations, or representing that a service or product is of a certain grade or quality when it is not. Second, the value of the construction professional's offer to remedy or last offer of settlement must be less than eighty-five-percent of the amount awarded as actual damages.⁵⁷ In addition, if in violating the CCPA, the construction professional acted fraudulently, willfully, knowingly, or intentionally, the claimant may be awarded treble its actual damages and attorney fees, which are subject to a combined cap of \$250,000.⁵⁸

Further, if the construction professional does not substantially comply with the terms of an accepted offer to repair or an accepted cash offer, or if the construction professional fails to respond to a notice of claim, and the claimant proves a CCPA violation, the construction professional is likewise subject to the treble damages provision of section of the CCPA.⁵⁹

There are other types of construction-related litigation that may not involve defects, such as when delays result. "No damages for delay" clauses are valid and enforceable in Colorado, but they are to be strictly construed against the owner or contractee and numerous exceptions apply such as fraud, misrepresentation, bad faith and active interference.⁶⁰

The economic loss rule is a well-recognized legal doctrine which bars tort claims where the duty alleged to have been breached is contractual and the resulting damages are economic. "A party suffering economic loss from the breach of an express or implied contractual duty may not assert a tort claim for such a breach absent an independent duty of care under tort law."⁶¹ The economic loss rule is recognized in construction litigation and economic loss rule jurisprudence in Colorado is one of the more developed in the country.⁶² However, a significant exception to the economic loss rule may arise in residential construction.

Prejudgment interest is a matter of contract and statute. Parties are free to provide for prejudgment interest within their contracts and, generally speaking, the only limitation upon such provisions is that they avoid usury.⁶³ Where parties have not addressed prejudgment interest within their contract, prejudgment interest may still be recovered pursuant to statute.⁶⁴ In the context of construction defect actions, claimants cannot recover prejudgment interest on repairs that have not been undertaken.⁶⁵

VIII. CASE LAW UPDATE

A. *Colo. Pool Sys. v. Scottsdale Ins. Co.*⁶⁶

On October 25, 2012, the Court of Appeals released its opinion in *Colorado Pool Systems, Inc. v. Scottsdale Insurance Company*. The decision settled two open questions – one relating to whether C.R.S. 13-20-808 (2012) was unconstitutionally retrospective, and the second concerning the interpretation of CGL policies under the common law.

Section 13-20-808 was enacted in response to *General Security Indemnity Co. v. Mountain States Mutual Casualty Co.*⁶⁷ In that case, the Court of Appeals held that faulty workmanship, standing alone, is not an “accident.” In enacting the statute, the legislature declared that *General Security* “does not properly consider a construction professional’s reasonable expectation that an insurer would defend the construction professional against an action or notice of claim.”⁶⁸ The legislature created an interpretive presumption:

(3) In interpreting a liability insurance policy issued to a construction professional, a court shall presume that the work of a construction professional results in property damage, including damage to the work itself or other work, is an accident unless the property damage is intended and expected by the insured. Nothing in subsection (3):

(a) Requires coverage for damage to an insured’s own work unless otherwise provided in the insurance policy; or

(b) Creates insurance coverage that is not included in the insurance policy.⁶⁹

Having concluded that the statute was intended to apply retroactively, the *Colo. Pool* Court next analyzed whether the statute was unconstitutionally retrospective. The Colorado Constitution forbids any law that is “retrospective in its operation.”⁷⁰ A statute is unconstitutionally retrospective if it would impair vested rights or create a new obligation, impose a new duty, or attach a new disability to transactions that have already occurred.⁷¹

The Court determined that the statute would retroactively change coverage provided under the CGL policy and that change in turn would retroactively alter the reasonableness of the insurer’s actions in refusing to defend and indemnify their insured. Thus, this sort of change was unconstitutional.⁷²

In addressing the question of whether a builder is covered under a CGL policy for damages that arose from the builder’s own faulty workmanship, the Court held that for certain damages, unless the policy contains specific exclusions, the answer is “yes.” The Court agreed with the Tenth Circuit’s holding in *Greystone Construction*⁷³ that injuries flowing from faulty workmanship constitute an “occurrence” so long as the resulting damage is to nondefective property, and is caused without expectation or foresight. This rule applies whether the resulting damage is to the insured’s work or to a third party’s work.

B. *Mt. Hawley Ins. Co. v. Creek Side at Parker Homeowners Ass’n*⁷⁴

On January 8, 2013, the U.S. District Court for the District of Colorado released its opinion in *Mt. Hawley Insurance Company v. Creek-Side at Parker Homeowners Association, Inc.* The decision was significant as the Court held that exclusion j(6) of the standard “Commercial General Liability Coverage Form,” along with an endorsement, precluded coverage for construction defects.⁷⁵

Exclusion j(6) excludes coverage for property damage to:

(6) That particular part of any property that must be restored, repaired or replaced because “your work” was incorrectly performed on it.

...

Paragraph (6) of this exclusion does not apply to “property damage” included in the “products-completed operations hazard.”

Exclusion j(6) has been interpreted to “exclude ‘property damage’ that *directly or consequentially* occurs from the faulty workmanship of the insured and its contractors/subcontractors (i.e. work that ‘was incorrectly performed’) while the work is ongoing.”⁷⁶ That exclusion, as interpreted, broadly excludes all property damage that occurred while the work was ongoing and was the result of faulty workmanship.

However, exclusion j(6) contains an exception for property damage included in the “products-completed operations hazard.” The “products-completed operations hazard” is found in the definitions section of the standard form. It includes property damage arising from the insured’s or its subcontractors’ work except “work that has not been completed or abandoned.”⁷⁷ Thus, the express exception to exclusion j(6) allows an insured to recover consequential damages that arise out of his or her faulty workmanship after the completion of the work.

The Court noted that the Mt. Hawley policy contained an endorsement to the standard form that provided that “[t]his insurance does not apply to ‘bodily injury’ or ‘property damage’ included within the ‘products-completed operations hazard’.”⁷⁸ The Court then found that this endorsement negated the exception to exclusion j(6). As a result, the Court declared that the insurance policy did not provide coverage for faulty workmanship.

C. *Shaw Construction, LLC v. United Builder Services, Inc.*⁷⁹

On February 12, 2012, the Court of Appeals released its opinion in *Shaw Construction, LLC v. United Builder Services, Inc.* This matter involved the construction of a multi-phase condominium complex and the application of the statute of repose. In this interlocutory appeal, the Court decided two questions of first impression under the CDARA. The Court first concluded that C.R.S. § 13-20-805 tolls construction defect claims only against parties who receive a notice.⁸⁰

Next, in applying the statute of repose to a multi-phase project, an improvement may be considered a discrete component of the larger project, which can be substantially completed before the entire project.⁸¹ The Court said that when an improvement to real property achieves a degree of completion at which the owner can utilize the improvement for the purpose it was intended, substantial completion has occurred.⁸²

D. *Sterling Construction Management, LLC v. Steadfast Insurance Company*⁸³

On September 6, 2011, the U.S. District Court for the District of Colorado released its opinion in *Sterling Construction Management, LLC v. Steadfast Insurance Company*. A notable discussion is the Court's analysis of the anti-indemnification statute.

Steadfast argued that it would not cover Sterling's losses because Sterling was not "legally obligated" to indemnify Overland for claims against Overland by third parties, because the indemnification language in Sterling's contract with Overland was not enforceable under C.R.S. § 13-21-111.5(6).⁸⁴ The Court commented that construction businesses in recent years have begun to use contract provisions to shift the financial responsibility for their negligence to others, thereby circumventing the intent of tort law.

The relevant indemnification language between Sterling and Overland was:

- Sterling agrees to protect, indemnify, and hold harmless Overland and Willbros . . . from losses arising from negligent acts of Sterling, its agents, subcontractors, or employees. . . .
- Sterling further agrees that it shall . . . defend any suit or action brought against Overland or Willbros and shall pay all damages, costs and expenses . . . in connection therewith or any matter resulting for which it is legally liable hereunder.
- Notwithstanding the foregoing, Sterling shall not be required to protect or indemnify Overland or Willbros against any claims to the extent arising out of . . . negligent acts or omissions of Overland.⁸⁵

The Court stated that the first provision is not objectionable under C.R.S. § 13-21-111.5(6)(b). Steadfast contended that the language in the second provision has been held to require the indemnitor to indemnify the indemnitee for the indemnitee's own negligence, which is void as against public policy. The Court determined, however, that such a conclusion is not necessarily self-evident. The only way that the provision would be void is if Sterling was indemnifying Overland for Overland's own negligence. The Court determined that Steadfast did not carry its burden of showing that Sterling's payment to Overland was for Overland's own.⁸⁶ Moreover, the Court determined that even if the Court were inclined to invalidate the second provision of the indemnity clause, the third provision would remedy any problem.⁸⁷

ENDNOTES

¹ C.R.S. §§ 38-22-101 through 133.

² *Lindemann v. Belden Consol. Mining & Milling Co.*, 65 P. 403 (Colo. App. 1901); *People v. Adams*, 243 P.3d 256, 262 (Colo. 2010).

³ C.R.S. § 38-22-101.

⁴ *Am. Irrigation Co. v. Fadenrecht*, 489 P.2d 1060 (Colo. App. 1971); *3190 Corp. v. Gould*, 431 P.2d 466 (Colo. 1967).

⁵ C.R.S. § 38-22-101.

⁶ C.R.S. § 38-22-101.

⁷ *Fisher v. Hanna*, 47 P. 303 (Colo. App. 1896).

⁸ C.R.S. § 38-22-101.

⁹ *Kobayashi v. Meehleis Steel Co.*, 472 P.2d 724 (Colo. App. 1970).

¹⁰ *See, e.g., Strapp v. Carb-Ice Corp.*, 224 P.2d 935 (Colo. App. 1950); *See Schmidt Constr. Co. v. Fast*, 776 P.2d 1175 (Colo. App. 1989).

¹¹ *Tabor v. Armstrong*, 12 P. 157 (Colo. 1886).

¹² *Laurence J. Rich & Assocs. v. First Interstate Mortg. Co.*, 807 P.2d 1199 (Colo. App. 1990).

¹³ C.R.S. § 38-22-109(3).

¹⁴ C.R.S. § 38-22-109(4) to (5).

¹⁵ C.R.S. § 38-22-110.

¹⁶ C.R.S. § 38-22-109(7).

¹⁷ C.R.S. § 38-22-114(1).

¹⁸ C.R.S. §§ 13-80-102, 13-80-104(1)(a).

¹⁹ C.R.S. § 13-80-104(1)(b)(I); *Smith v. Executive Custom Homes, Inc.*, 230 P. 3d 1186, 1190-91 (Colo. 2010); *United Fire Group v. Powers Electric, Inc.*, 240 P. 3d 569, 571-72 (Colo. App. 2010) (accrual of claim begins when physical manifestation of a defect appears).

²⁰ C.R.S. §§ 13-20-803.5, 13-20-805.

²¹ *E.g., Curraugh Queensland Mining, Ltd. v. Dresser Industries, Inc.*, 55 P. 3d 235, 239-40 (Colo. App. 2002); *Highline Village Associates v. Hersh Cos.*, 996 P. 2d 250, 253 (Colo. App. 1999), *aff'd, in part, and rev'd, in part, on other grounds, Hersh Cos. v. Highline Village Associates*, 30 P. 3d 221 (Colo. 2001).

²² *Smith*, 230 P. 3d at 1192.

²³ C.R.S. § 13-80-104(b)(II)(B).

²⁴ *CLPF-Parkridge One, L.P. v. Harwell Investments, Inc.*, 105 P. 3d 658, 664 (Colo. 2005).

²⁵ C.R.S. § 13-80-104(1)(a).

²⁶ C.R.S. § 13-20-805.

²⁷ *Thermo Development, Inc. v. Central Masonry Corp.*, 195 P. 3d 1166, 1168-69 (Colo. App. 2008).

²⁸ C.R.S. §§ 13-20-802.5(5), 13-20-803.5(1).

²⁹ C.R.S. § 13-20-803.5(2).

³⁰ C.R.S. § 13-20-803.5(4).

³¹ *Colard v. Am. Family Mut. Ins. Co.*, 709 P.2d 11 (Colo. App. 1985); *Hoang v. Monterra Homes*, No. 99CV2425 (Jefferson County Dist. Ct., Colo. Nov. 13, 2002); *Hoang v. Assurance Co. of Am.*, 149 P.3d 798 (Colo. 2007).

³² *See, e.g., Lamar Truck Plaza, Inc. v. Sentry Ins.*, 757 P.2d 1143 (Colo. App. 1988), *partially overruled by, Hoang*, 149 P.3d 798.

³³ *See Samuelson v. Douhirt*, 529 P.2d 631 (Colo. 1974).

³⁴ *Browder v. U.S.F. & G.*, 893 P.2d 132 (Colo. 1995), *partially overruled on other grounds, Hoang*, 149 P.3d 798.

³⁵ *Id.*

³⁶ *Hoang*, 149 P.3d 798; *Travelers Cas. & Sur. Co. v. Village Homes of Colo.*, No. 06SC471, 155 P.3d 369, 2007 Colo. LEXIS 35 (Colo. Jan. 8, 2007).

³⁷ *Am. Employers Ins. Co. v. Pinkard Constr. Co.*, 806 P.2d 954 (Colo. App. 1990).

³⁸ *Pub. Serv. Co. v. Wallis & Cos.*, 986 P.2d 924 (Colo. 1999).

³⁹ *Gerrity Co., Inc. v. CIGNA Prop. Cas. Ins. Co.*, 860 P.2d 606 (Colo. App. 1993); *Weger v. United Fire & Cas. Co.*, 796 P.2d 72 (Colo. App. 1990); *Hoang*, No. 99CV2425 (Jefferson County Dist. Ct., Colo. Nov. 13, 2002); *Browder v. U.S.F. & G.*, 893 P.2d 132 (Colo. 1995); *1700 Lincoln Ltd. v. Denver Marble & Tile Co., Inc.*, 741 P.2d 1270 (Colo. App. 1987); *McGowan v. State Farm Fire & Cas. Co.*, 100 P.3d 521 (Colo. App. 2004); *Ohio Cas. Ins.*

Co. v. Imperial Contractors, Inc., 765 P.2d 1060 (Colo. App. 1988); *Hoang*, 149 P.3d 798; *Friedland v. Travelers*, 105 P.3d 639 (Colo. 2005).

⁴⁰ C.R.S. § 13-21-111.5(6).

⁴¹ C.R.S. § 13-21-111.5(6)(b).

⁴² C.R.S. § 13-21-111.5(6)(c)-(f).

⁴³ C.R.S. § 13-21-111.5(6)(c).

⁴⁴ C.R.S. § 13-21-111.5(6)(f)(I), (II).

⁴⁵ C.R.S. § 13-21-111.5(6)(f)(III). Further express exceptions include agreements concerning:

- builder's risk insurance (C.R.S. § 13-21-111.5(6)(d)(II));
- property owned or operated by railroad, sanitation district, water district, water and sanitation district, municipal water enterprise, water conservancy district, water conservation district or metropolitan sewage disposal district (C.R.S. § 13-21-111.5(6)(e)(II)(A)); and,
- property leased or rented (C.R.S. § 13-21-111.5(6)(e)(II)(B)).

⁴⁶ C.R.S. § 13-21-111.5(6)(d)(I).

⁴⁷ C.R.S. § 13-21-111.5(6)(d)(I).

⁴⁸ *Johnson Realty v. Bender*, 39 P. 3d 1215, 1218 (Colo. App. 2001).

⁴⁹ *Brochner v. Western Insurance Co.*, 724 P. 2d 1293, 1298, n.6 (Colo. 1986).

⁵⁰ C.R.S. § 13-50.5-102(6).

⁵¹ C.R.S. § 13-80-104(1)(b)(II)(A). The Colorado Court of Appeals has determined that this provision applies to either the resolution of a dispute which results in a final judgment or the settlement of an action or claim of liability which a third-party could or actually did commence against the claimant. *Richmond American Homes of Colorado, Inc. v. Steel Floors, LLC*, 187 P. 3d 1199, 1205 (2008).

⁵² C.R.S. § 13-80-104(1)(b)(II)(B).

⁵³ *CLPF-Parkridge One, L.P.*, 105 P. 3d at 664-65.

⁵⁴ *Main Elec., Ltd v. Printz Servs. Corp.*, 980 P.2d 522, 524 (Colo. 1999).

⁵⁵ C.R.S. § 13-20-806.

⁵⁶ C.R.S. § 13-20-802.5(2).

⁵⁷ C.R.S. § 13-20-806(1).

⁵⁸ C.R.S. §§ 6-1-113(2)(a)(III); 6-1-113(2)(b); 6-1-113(2.3); 13-20-806(3).

⁵⁹ C.R.S. § 13-20-806(2),(3), (4).

⁶⁰ *Tricon Kent Co. v. Lafarge North Am., Inc.*, 186 P.3d 155 (Colo. App. 2008).

⁶¹ *Town of Alma v. AZCO Construction, Inc.*, 10 P.3d 1256, 1264 (Colo. 2000); *Grynberg v. Agri Tech, Inc.*, 10 P.3d 1267, 1269 (Colo. 2000).

⁶² *Hermansen v. Tasulis*, 48 P.3d 235, 240 (Utah 2002); *Springfield Hydroelectric Co. v. Copp*, 799 A.2d 67 (Vt. 2001).

⁶³ C.R.S. § 5-12-103(1).

⁶⁴ C.R.S. § 5-12-102.

⁶⁵ *Goodyear Tire & Rubber Co. v. Holmes*, 193 P.3d 821, 828-30 (Colo. 2008).

⁶⁶ 317 P.3d 1262 (Colo. App. 2012).

⁶⁷ 205 P.3d 529 (Colo. App. 2009).

⁶⁸ § 13-20-808(1)(b)(III).

⁶⁹ § 13-20-808(3)(a)-(b).

⁷⁰ Colo. Const. art. II, § 11.

⁷¹ *DeWitt*, 54 P.3d at 854.

⁷² See *Landgraf v. USI Film Products*, 511 U.S. 244, 270, 114 S. Ct. 1483, 128 L. Ed. 2d 229 (1994) (a statute cannot be applied retroactively if it imposes “new legal consequences [on] events completed before its enactment”); *City of Golden v. Parker*, 138 P.3d 285, 290 (Colo. 2006) (retroactive application of a statute is prohibited where “the reasonable expectations and substantial reliance of a party vested prior to the enactment of the statute”).

⁷³ See *Greystone Constr., Inc. v. Nat’l Fire & Marine Ins. Co.*, 661 F.3d 1272 (10th Cir. 2011).

⁷⁴ 2013 U.S. Dist. LEXIS 3405 (D. Colo. Jan. 8, 2013).

⁷⁵ #38-1.

⁷⁶ *Advantage Homebuilding, LLC v. Maryland Cas. Co.*, 470 F.3d 1003, 1012 (10th Cir. 2006) (emphasis added).

⁷⁷ #38-1 at 16.

⁷⁸ #38-1 at 18.

⁷⁹ 296 P.3d 145 (Colo. App. 2012).

⁸⁰ 296 P.3d at 152.

⁸¹ 296 P.3d at 154.

⁸² 296 P.3d at 155.

⁸³ 2011 U.S. Dist. Lexis 99604 (D. Colo. September 6, 2011).

⁸⁴ 2011 U.S. Dist. Lexis 99604 * 22.

⁸⁵ 2011 U.S. Dist. Lexis 99604 * 23.

⁸⁶ 2011 U.S. Dist. Lexis 99604 * 30-31.

⁸⁷ 2011 U.S. Dist. Lexis 99604 * 31.

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I. MECHANICS' LIEN BASICS

Conn. Gen. Stat. § 49-33 et seq. provides for and governs mechanics' liens on private projects. A mechanics' lien is an encumbrance on the owner's interest in the property and payment may be obtained after a lien is foreclosed upon. The two types of lien claimants generally include a general contractor with a direct agreement or the consent of the owner of the land upon which the construction work is performed and subcontractors and others who have the consent of someone having authority from or rightfully acting on behalf of the owner in procuring the labor or materials.¹ The statutory procedural requirements must be strictly followed to perfect a lien right. The general considerations for mechanics' lien include:

A. Notice of Intent. The first step for a subcontractor or supplier without a direct contract with the owner of the property is to serve a notice of intent to file a mechanics' lien upon the owner of the property.² The notice must be served after commencing the work and within 90 days after ceasing to furnish materials or services for the subject property. The notice period begins after the completion of *substantial* work or materials and may begin before all work is completed. However, if after *substantial* completion, the owner requests to have additional substantial work performed, the 90 day period will begin to run from the date the requested work was last performed.³ The notice must state that the claimant has furnished materials or rendered services and intends to claim a lien on the building, lot, or plot of land. For parties contracting directly with the owner, there is no need to furnish a notice of intent.

B. Certificate of Lien. The Certificate of Lien is the document which is actually filed on the land records. It needs to set forth the basis under which the lien arises, and must contain: (1) a description of the premises, (2) the amount claimed in the lien, (3) name of the person/entity against whom the lien is filed, (4) date of commencement of performance, and (5) a statement that the amount claimed is justly due. Finally, the lien certificate must be signed and its contents sworn to by the claimant.⁴ The Certificate must then be recorded in the land records in the town where the project is located within 90 days from the date of the last day of providing services or labor to the project.⁵ A copy of the lien certificate must be served on all property owners not later than 30 days after recording the certificate.⁶

C. Amount of Lien. The amount of a lien may include the costs of materials furnished (including equipment and machinery that is rented or leased)⁷ and services rendered so long as the materials and services are actually used in the project. The lien also secures interest and attorney's fees.⁸ Lost profits on work not completed are not covered.⁹ A subcontractor's

right to file a mechanics' lien is based on the doctrine of subrogation. The amount of a subcontractor's recovery is limited to the amount of the unpaid contract debt owed by the owner to the general contractor.¹⁰

D. Foreclosure. Once the lienor has complied with the statutory notice, service and recording requirements, the lien will be considered perfected. An action to foreclose a mechanics' lien must be commenced within 1 year after the lien is filed with the town clerk where the property is situated¹¹. Also, a notice of lis pendens must be filed on the land records within one year from the date the lien was recorded or the claimant will be deprived of the right to foreclose the lien. Foreclosure is not the exclusive remedy available to a party that has filed a lien.¹²

E. Defenses. In determining the amount of lien fund to which any lien may attach, the owner shall be allowed payments made to original contractor if (1) made in good faith, (2) made before receiving written notice of any liens, and (3) the owner gives written notice to all known subcontractors at least 5 days before making payment in advance of the time set forth in the contract.¹³ If written notice of advance payment is not given, such payment is considered made in "bad faith" and not deducted from the lien fund.¹⁴ In addition, if a contractor abandons the project, an owner may deduct from the lien fund any reasonable amount that the owner had to pay to complete the project including damages. Owner of property subject to mechanic's lien must have consented to work being performed on property.¹⁵

F. Lien Waivers. Prospective lien rights on all private commercial and industrial projects cannot be waived but may be subordinated.¹⁶ However some lien waiver agreements may be effective without payment for residential and public construction projects.¹⁷

II. STATUTES OF REPOSE AND LIMITATIONS

A. Contract for Sale under UCC - Conn. Gen. Stat. §42a-2-725. Action must be commenced within four years after the cause of action has accrued, which is when the breach occurs, regardless of the aggrieved party's lack of knowledge of the breach. The statute of limitations under this section may not be extended by contract. A breach of warranty occurs when tender of delivery is made, except where the warranty extends to future performance.

B. Action to recover for personal injuries - Actions founded upon a tort shall be brought within three years from the date of the act or omission complained of. Conn. Gen. Stat. §52-577. An action to recover damages for injury to persons or property must be brought within two years from the date an injury is first sustained or discovered or reasonably should have been discovered, except that no action may be brought more than three years from the date of the act complained of. Conn. Gen. Stat. §52-584.

C. Contract Actions - Conn. Gen. Stat. § 52-576. Actions for account or on simple and implied contracts, or on any contract in writing, have a 6-year statute of limitations after the right of action accrues, except that any person legally incapable of bringing any such action at the time of the right of action may sue at any time within 3 years after becoming legally capable of bringing the action. A breach of contract action accrues as of the time the injury is inflicted.¹⁸

The statute of limitations in Connecticut's Little Miller Act (Conn. Gen. Stat. § 49-41, *et seq.*) for bond claims cannot be modified by contract.¹⁹ No statutes of limitations, statutes of repose, contractual limitations period or doctrine of laches apply against the State to bar it from asserting claims unless the statute under which the State is asserting its rights expressly provides otherwise.²⁰

D. Oral Contract - Conn. Gen. Stat. § 52-581. An action founded upon any express contract or agreement which is not reduced to writing, must be brought within three years after the right of action accrues.

E. Indemnification Action - Conn. Gen. Stat. § 52-598a. An action for indemnification may be brought within three years from the date of the determination of the action against the party which is seeking indemnification by either judgment or settlement. The limitation in Conn. Gen. Stat. § 52-598a applies to all actions for indemnity, even when the indemnity claim is contractual.²¹

F. Design Professionals - Conn. Gen. Stat. § 52-584a. An action whether in contract, tort, or otherwise, to recover damages for a deficiency in design, planning...or construction of an improvement to real property... which is brought as a result of any such claim for damages against any architect, professional engineer or land surveyor performing or furnishing the design, planning, supervision, observation of construction...shall not be brought more than seven years after substantial completion of such improvement.²² If an injury occurs in the seventh year after substantial completion, a tort claim to recover damages may be brought within one year of the injury, but in no event more than 8 years after substantial completion of an improvement.

G. New Home Construction - Conn. Gen. Stat. §§ 47-117 and 47-118. Express and implied warranties for new home construction terminate one year after the delivery of the deed to the purchaser or one year after the purchaser takes possession of the house, whichever occurs first; and in the case of an improvement not completed at the time of delivery of the deed to the purchaser, one year after the date of the completion or one year after taking of possession by the purchaser, whichever occurs first.

III. PRE-SUIT NOTICE OF CLAIM

There is no pre-suit notice requirement before a claim for breach of a statutory warranty may be brought in Connecticut.

IV. COVERAGE TRIGGERS AND ALLOCATION ISSUES

A standard general liability policy ("CGL") provides protection that the insurer "will pay those sums that the insured becomes legally obligated to pay as damages because of 'bodily injury' or 'property damage' that is 'caused by an occurrence', during the applicable policy period." An occurrence policy is triggered when the damage occurs during the policy period, regardless of when the claim is made.

The Connecticut Supreme Court recently concluded that unintended defective or faulty construction work by a subcontractor that damages non-defective property may constitute an “occurrence” resulting in “property damage” covered by a CGL policy under certain circumstances.²³ However, defective work alone or repairs to defective work do not constitute property damage.

Connecticut follows the “injury-in-fact” rule to determine which liability policies have been triggered.²⁴ The policy will not depend on the causative event and occurrence but will be based upon injuries or damages which result from such an event and which happened during the policy period.

To determine which policy or policies apply, the policies that were in effect when the injury or damage took place need to be identified. If the physical injury was continuous, such as in environmental contamination cases, and existed over multiple policy periods, the continuous trigger approach is used and all injury policies issued during the extended exposure period would be triggered for coverage.²⁵ The triggered policies are given a pro rata allocation and the damages are split.²⁶ The Second Circuit ruled that property damage occurs upon installation of asbestos products in a building; the damage does not continue thereafter. Therefore, a single trigger is applied and only the insurers on the risk when installation occurred have a duty to defend and indemnify the insured.²⁷ If insurance was unavailable for a period, the insured is liable for costs attributable to losses incurred during periods when it was uninsured.

Finally, Connecticut adopts the pro rata approach to the allocation of defense costs that trigger multiple insurance policies.²⁸ In addition, because the duty to defend arises solely under contract, if the duty to defend the insured occurs outside of the policy period, the insured is required to pay its fair share of the defense costs.²⁹

In the context of a construction contract it is lawful to spread risk to an insurer by requiring the inclusion of other parties involved in a construction project as additional insureds.³⁰

V. CONTRACTUAL INDEMNITY

Under Conn. Gen. Stat. §52-572k, any construction contract which purports to indemnify the promisee for injury to persons or damage to property caused by the negligence of the promisee, his agents or employees, is against public policy and void. This statute, however, does not affect the validity of any insurance contract, workers’ compensation agreement or other agreement issued by a licensed insurer.

A waiver of subrogation provision in a standard AIA contract coupled with a requirement to provide insurance is not a hold harmless or indemnification provision as these terms are used in the statute and does not violate § 52-572k.³¹ The statute prohibits clauses purporting to require subcontractors to indemnify and hold harmless general contractors for the general contractor’s negligence, but does not prohibit a general contractor from being included as an additional insured.³² A subcontractor’s contractual duty to defend a general contractor is separate and distinct from the duty to indemnify, and therefore is not impacted by §52-572k.³³ The Second Circuit recently held that Conn. Gen. Stat. § 52-572k was preempted by 49 U.S.C. §

28103(b), which allows Amtrak to allocate responsibility for claims, and enforced a contract provision that allowed Amtrak indemnification for its own negligence.³⁴

VI. CONTINGENT PAYMENT AGREEMENTS

There is no definitive appellate authority governing the enforcement of the typical pay-when-paid and pay-if paid clauses in construction contracts.³⁵ A majority of superior courts have held that these clauses do not excuse the payment obligation but set a reasonable time for payment to be made.³⁶ However, one superior court has upheld a pay-if-paid on a private construction project.³⁷ The stronger and more comprehensive the clause the more likely it will be enforced. The Connecticut Appellate Court recently confirmed a lower court decision enforcing a pay-if-paid contract clause in the context of a State DOT project.³⁸

Liquidating agreements on public projects where a general contractor attempts to pass through subcontractor claims against the State are not enforceable in Connecticut unless certain conditions are satisfied.³⁹ One recent superior court decision allowed a pass-through claim against the state once the general contractor proved it admitted unconditional liability to the subcontractor, liquidated its liability to the subcontractor to a sum certain, and had incorporated the subcontractor's claim into the general contractor's own claim against the state.⁴⁰

VII. DAMAGES LIMITATIONS

A. Attorney's Fees, Interest, and Punitive Damages - Pre-judgment interest may be recovered if provided for in a contract or under Conn. Gen. Stat. §37-3a which allows for 10% annually. Connecticut case law follows the general rule known as the "American Rule" where attorney's fees are not allowed to the prevailing party as an element of damages unless such recovery is allowed by statute or contract.⁴¹ Punitive damages are generally not recoverable for breach of contract claims.

A judgment on foreclosure of a mechanics' lien shall be allowed costs including reasonable attorney's fees.⁴² When making a claim on a statutory payment bond pursuant to the Little Miller Act, attorney's fees are available if the surety's denial of claim is without substantial basis in fact or law.⁴³ Under the Fairness Act, on a private construction project, no surety is obligated to reimburse a bond claimant for interest, costs penalties or attorney's fees unless the terms of the bond expressly reference such costs.⁴⁴ If requirements of prompt payment are not met under the Fairness Act, the Act provides for the award of interest, costs, penalties and attorney fees.⁴⁵ A violation of the Connecticut Unfair Trade Practices Act ("CUTPA") can result in an award of punitive damages and attorney fees.⁴⁶ A violation of any of the provisions of the New Home Construction Contractors Act (Conn. Gen. Stat. §§ 20-417a – 20-417j) shall be deemed an unfair or deceptive trade practice under CUTPA which may result in an award of attorney fees.⁴⁷ The failure to comply with the Home Improvement Act is also a violation of CUTPA which may result in an award of attorney's fees.⁴⁸

B. Direct and Consequential Damages - The general rule in breach of contract cases is that the award of damages is designed to place the injured party, so far as can be done by money, in the same position as that which he would have been in had the contract been

performed.⁴⁹ A party may collect for any loss that may fairly and reasonably be considered as arising naturally from the breach of contract or were foreseeable at the time of contract formation. Consequential damages can include lost profits, unless they are too speculative or remote. A contractor's recovery may be limited if the architect and owner waive consequential damages.⁵⁰ A pay-if-paid provision can be a valid defense to a payment bond claim on a private project.⁵¹ With a few exceptions a general contractor may delegate responsibility to subcontractors for the safety of (and for liability for personal injuries to) the subcontractor's employees.⁵²

The New Home Construction Contractors Act provides for a fund to pay consumers who successfully bring claims against contractors who lack the ability to pay a judgment. The consumer can recover actual damages and costs but not punitive damages. Recovery under the fund is capped at \$30,000.⁵³ The Home Improvement Act provides for a similar fund however, the consumer may recover up to \$15,000 from the fund.⁵⁴

C. Delay and Disruption Damages - Absent contractual limitation, a contractor's recovery for damages for delays caused by the owner may include damages such as increased wages and material costs, cost of overhead, damages due to disruption and escalation.⁵⁵ When an owner requires a contractor to accelerate his efforts to adhere to the original contract schedule, the contractor, so long as he was not the cause of delay, is entitled to extra compensation.⁵⁶ No damages for delay provisions are enforceable in Connecticut.⁵⁷

D. Economic Loss Doctrine - This is a judicially created principle which bars recovery in tort where the relationship between the parties is contractual and the only losses alleged are economic.⁵⁸ While not expressly holding that the economic loss doctrine has been adopted in Connecticut, the Supreme Court applied the doctrine in *Flagg Energy Dev. Corp. v. General Motors Corporation*,⁵⁹ a case involving product liability and the sale of goods. Since *Flagg*, no appellate authority has addressed whether the doctrine is recognized in Connecticut. Consequently, there is a split in superior court decisions as to whether a broad economic loss doctrine bars claims for economic loss in non-product liability cases in Connecticut.⁶⁰

¹ Conn. Gen. Stat. § 49-33.

² Conn. Gen. Stat. § 49-33; Conn. Gen. Stat. §49-35(a). The original contractor is also entitled to a notice of intent if he files with the town clerk within 15 days of commencing construction an affidavit stating the business name and address, and a description of the project.

³ See *Martin Tire & Rubber Co. v. Kelly Tire & Rubber Co.*, 99 Conn. 396, 399 (1923) Trivial services requested well after the date of substantial completion will not extend commencement of the 90 day period. This rule was discussed in *F.B. Mattson Company, Inc. v. Tarte*, 247 Conn. 234, 239 (1999).

⁴ *Red Rooster Construction Co. v. River Associates, Inc.*, 224 Conn. 563 (1993). (If oath is not taken, the lien will be held invalid); *Stone-Krete Construction, Inc. v. Eder*, 280 Conn. 672 (2006); *TMC Services, Inc. v. Haines*, 45 Conn. L. Rptr. 130 (2/6/08); *McDonough v. Collender*, 44 Conn. L. Rptr. 209 (8/8/07).

⁵ *Brennan v. Fairfield*, 225 Conn. 693 (2001)

⁶ Conn. Gen. Stat. §49-34(2). If the owner resides in the same town as the project, notice must be served by an indifferent person or state marshal by leaving a true and attested copy with the owner or at his usual place of abode. § 49-35(a). If the owner does not reside in the same town, but has an agent therein, notice may be served upon the agent or it may be served by any indifferent person, state marshal, or other proper officer by registered mail or certified mail to the owner's home. *Id.*

⁷ Conn. Gen. Stat. §49-33(a) and Conn. Gen. Stat. §49-42(c)

⁸ Conn. Gen. Stat. §§ 52-249 and 52-249a

⁹ *Arganese Properties, LLC v. Salce Contracting Associates, LLC*, (Conn. Super. 2001) 2001 WL 752717; *Szymborski v. The Phoenix Group*, (Conn. Super 1993) 1993 WL 266604

¹⁰ *Seaman v. Climate Control Corp.*, 181 Conn. 592, 601-602 (1980); *ProBuild East, LLC v. Poffenberger*, 136 Conn. App. 184 (2012)

¹¹ *Frank Lill & Son, Inc. v. O&G Industries*, 2012 WL 6582897

¹² *MD Drilling and Blasting, Inc. v. MLS Construction, LLC*, 96 Conn. App. 798 (2006)

¹³ Conn. Gen. Stat. §49-36(c).

¹⁴ *Rene Drywall v. Strawberry Hill Assoc.*, 182 Conn. 568 (1980); *Raymond's Building Supply, Inc. v. Mattson*, 42 Conn. L. Rptr. 563 (1/2/07).

¹⁵ Conn. Gen. Stat. § 49-33(a); *Waterview Site Services, Inc. v. Pay Day, Inc.*, 125 Conn. App. 708 (2010)

¹⁶ Conn. Gen. Stat. §42-158l.

¹⁷ Conn. Gen. Stat. §§ 42-158i and 42-158l.

¹⁸ *Kennedy v. Johns-Manville Sales Corp.*, 135 Conn. 176 (1948).

¹⁹ *North Haven Construction, Co. v. Banton Construction, Co.*, 46 Conn. L. Rptr. 221 (8/7/08); *Paradigm Contract Mgmt Co. v. St. Paul Fire and Marine Ins. Co.*, 293 Conn. 569 (2009)

²⁰ *State of Connecticut v. Lombardo Brothers Mason Contractors, Inc.*, 307 Conn. 412 (2013).

²¹ *Alfred Chiulli & Sons, Inc. v. Hanover Insur. Co.*, 2007 Conn. Super. LEXIS 3014

²² See also, *Bagg v. Town of Thompson*, 2008 Conn. Super. LEXIS 965; *Town of Beacon Falls v. Towers Golde, LLC*, 2010 Conn. Super. LEXIS 140 (Conn. Gen. Stat. § 52-598a, a three year statute of limitations for indemnification actions, supersedes the seven year limitation period found in Conn. Gen. Stat. § 52-584a)

²³ *Capstone Development Corp. v. American Motorists Insurance Co.*, 308 Conn. 760 (2013)

²⁴ *Aetna Casualty & Surety Co. v. Abbott Lab. Inc.*, 636 F. Supp. 546 (D. Conn. 1986).

²⁵ *Security Insurance Co. of Hartford v. Lumberman's Mutual Casualty Co.*, 264 Conn. 688 (2003).

²⁶ *Id.*

²⁷ *Maryland Cas. Co. v W.R.. Grace & Co.*, 23 F.3d 617, 628 (2d Cir 1994); *Stonewall Ins. Co. v Asbestos Claims Mgmt. Corp.*, 73 F.3d 1178, 1210 (2d Cir 1995).

²⁸ *Security Insurance Co. of Hartford v. Lumberman's Mutual Casualty Co.*, 264 Conn. 688, 826 A.2d 107 (2003).

²⁹ *Id.*

³⁰ *Royal Indemnity Co. v. Terra Firma, Inc.*, 50 Conn Supp. 563, *aff'd per curium*, 287 Conn. 183 (2008); *Town of Manchester v. Vermont Mutual Insurance Co*, 2006 Conn. Super LEXIS 13; *National Union Fire Ins. Co. v. Zurich American Ins. Co.*, 2005 Conn. Super LEXIS 3351.

³¹ *Best Friends Pet Care, Inc. v. Design Learned, Inc.*, 77 Conn. App. 167, 823 A.2d 329 (2003).

³² *Royal Indemnity Company v. Terra Firma*, 50 Conn. Supp. 563 (2006), *Aff'd*, 287 Conn. 183 (2008)

³³ *Rouleau v. Walter D. Sullivan Co., Inc.* 2006 WL 301915 at *2.

³⁴ *O&G Indus. v. Hartford Fire Ins., Co.*, 537 F.3d 153 (2d Cir. 2008)

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- ³⁵ *Blakeslee Arpaia Chapman, Inc. v. EI Constructors, Inc.*, 239 Conn. 708 (1997); *DeCarlo and Doll v. Dilozi*, 45 Conn. App. 633 (1997)
- ³⁶ *R&L Acoustics v. Liberty Mutual Insur. Co.*, 2001 WL 1249658 (Conn. Super. 2001); *Titan Mech. Contractors, Inc. v. Klewin Bldg. Co.*, 2007 WL 4105715 (Conn. Super. 2007); *Compare, Star Contracting Corp. v. Manway Construction Co., Inc.*, 32 Conn. Supp. 64 (1973)
- ³⁷ *Lindade Const., Inc. v. Continental Cas. Co.*, 47 Conn. L. Rptr. 323 (2009)
- ³⁸ *Suntech of Connecticut, Inc. v. Lawrence Brunoli, Inc.*, 143 Conn App. 581 (2013), *cert denied*, 310 Conn. 910 (2013)
- ³⁹ Conn. Gen. Stat. § 4-61; *Federal Deposit Insur. Corp. v. Peabody, N.E., Inc.*, 239 Conn. 93 (1996); *Wexler Construction Co. v. Housing Authority*, 149 Conn. 602 (1962).
- ⁴⁰ *Worth Construction Co. v. State of Connecticut Department of Public Works*, 2010 WL 4884266 (Conn. Super. Ct. Aug 10, 2010)
- ⁴¹ *Gagne v. Vaccaro*, 118 Conn. App. 367 (2009)
- ⁴² Conn. Gen. Stat. §§ 52-249 and 52-249a; *DuBaldo Elec., LLC v. Montagno Constr., Inc.*, 119 Conn. App. 423 (2010); *Clem Martone Construction, LLC v. DePino*, 145 Conn. App. 316 (2013).
- ⁴³ Conn. Gen. Stat. §49-42(a); *Barreira Landscaping & Masonry v. Frontier Ins. Co.*, 47 Conn. Supp. 99 (2000).
- ⁴⁴ Conn. Gen. Stat. § 42-158o.
- ⁴⁵ Conn. Gen. Stat. §§ 42-158j(4) and 42-158r.
- ⁴⁶ Conn. Gen. Stat. §42-110a et. seq.; *Taylor v. King*, 121 Conn. App. 105 (2010)
- ⁴⁷ Conn. Gen. Stat. §20-417g; *D'Angelo Development and Constr. Corp. v. Cordovano*, 121 Conn. App. 165 (2010).
- ⁴⁸ Conn. Gen. Stat. § 20-427(c); *Lucien v. McCormick Construction, LLC*, 122 Conn. App. 295 (2010).
- ⁴⁹ *Ambrogio v. Beaver Road Assoc.*, 267 Conn. 148, 155 (2003); *Naples v. Keystone Bldg and Dev. Corp.*, 295 Conn. 214 (2010)(measure of damages for defective and incomplete construction); *Centimark v. Village Manor Assoc. L.P.*, 113 Conn. App. 509 (2009); *Campagnone v. Clark*, 116 Conn. App. 622 (2009)(damages involving violations of the Home Improvement Act.).
- ⁵⁰ *City of Milford v. Coppola Constr. Co., Inc.*, 2004 Conn. Super. LEXIS 3502, *Aff'd*, 93 Conn. App. 704 (2005).
- ⁵¹ *Lindade Construction, Co. v. Continental Cas. Co.*, 2008 Conn. Super. LEXIS 3190
- ⁵² *Pelletier v. Sordoni / Skanska Construction, Co.*, 286 Conn 563 (2008); *Archambault v. Soneco/Northeastern, Inc.*, 287 Conn. 20 (2008)
- ⁵³ Conn. Gen. Stat. §20-417i(d).
- ⁵⁴ Conn. Gen. Stat. §20-432(k).
- ⁵⁵ *Walter Kidde Constructors, Inc.*, 37 Conn. Supp. 50, 82 (1981) citing *Southern New England Contracting Co. v. State of Connecticut*, 165 Conn. 644 (1974).
- ⁵⁶ *Southern New England Contracting Co. v. State of Connecticut*, 165 Conn. at 664.
- ⁵⁷ *White Oak Corp. v. Dept of Transportation*, 217 Conn. 281 (1991)
- ⁵⁸ *Riggs-Brewer Industries, Inc. v. Shelton Senior Housing, Inc.*, 2006 Conn. Super. LEXIS 1741.
- ⁵⁹ 244 Conn. 126, 153-54 (1998).
- ⁶⁰ *Tyson Roller Bearing, Inc. v. Accuride Corp.*, 2008 Conn. Super. LEXIS 1116; *ODP, LLC v. Shelterlogic*, 44 Conn. L. Rptr. 722 (12/21/07); *Town of New Canaan v. Brooks Laboratories, Inc.*, 44 Conn. L. Rptr. 501 (11/7/07); *United Steel, Inc. v. Spiegel, Zamecnik & Shah, Inc.*, 43 Conn. L. Rptr. 476 (3/27/07); *Diversified Technology Consultants v. Sentinel Equities Corp.*, 41 Conn. L. Rptr. 813 (10/9/06); *Loureiro Contractors, Inc. v. City of Danbury*, 2010 Conn. Super. LEXIS 2938; *County Squire I, Inc. v. RAW Construction, LLC*, 56 Conn.L.Rptr 591(7/30/13).

DELAWARE

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I. MECHANIC'S LIEN BASICS

The process and procedure for mechanic's liens in Delaware is governed by statute. *See 25 Del. C. § 2701 et. seq.* The statute allows for "any person having performed or furnished labor or material ... for the erection, alteration, or repair of any structure, in pursuance of any contract ... with the owners ... or with the agent of such owner ... to obtain a lien upon such structure and upon the ground upon which the same may be is situated."¹ "The general purpose of a mechanic's lien is to provide protection for contractors or other laborers who furnish labor or other services on a structure pursuant to a contract with its owners."² Under the mechanic's lien statute, "labor" includes both physical and supervisory labor.³

Because the right to a mechanic's lien derives solely from the statute, the rights and remedies are in derogation of the common law, and the statute is strictly construed.⁴ "Strict compliance with the statute is required as powerful relief is afforded that was unavailable at common law."⁵ Delaware courts have held that strict construction, however, "does not mean unreasonable or unwarranted construction."⁶ Delaware Courts have mandated that those individuals who file mechanic's liens be in "substantial compliance" with the statutory requirements.⁷ Delaware Courts have readily dismissed complaints for non-compliance with the statutory requirements.⁸

In personam claims, such as breach of contract, can be filed concurrently with a mechanic's lien claim.⁹

1. Pre-Lien Notice

There is no statutory requirement to provide notice prior to initiating an action under the mechanic's lien statute.

2. Mechanic's Lien Statement

The statute defines "structure" to "include[] a building or house."¹⁰ Mechanic's liens may also be obtained by those furnishing labor or materials for the construction of or improvements to mills, factories, bridges, wharves, piers, and docks.¹¹ In the absence of a contract between the contractor and landowner which has been signed by the landowner, as well as meeting other

enumerated requirements as contained in the statute, a lien may not attach to improvements which are made solely to the land alone, that is, those not made for the benefit of or improvement to any structure thereon.¹²

Complaints or statements of claims for mechanic's liens must be filed in the county where the structure is situated, and must include certain information as enumerated in the mechanic's lien statute.¹³ Delaware's mechanic's lien statute, at 25 Del. C. § 2712, sets forth "requirements of complaint and/or statement of claim."¹⁴ This section, however, is not an exhaustive list of all necessary pleading requirements for mechanics' lien claims.¹⁵

If claims for liens are made against multiple structures, the claimant must designate in the complaint the amount which is claimed due on each structure.¹⁶

Contractors who have contracted directly with the owner of a structure must file a statement of claim within 180 days after the completion of the structure.¹⁷ A claim made under the mechanic's lien statute is deemed timely if it is filed within 180 days of any of nine (9) enumerated events in the construction process.¹⁸ Those not having a contract directly with the owner have 120 days from the date labor or delivery of materials was completed, or from the date final payments were due or made to the contractor, to file a statement of claim.¹⁹ Including a finishing date in a Statement of Claim is "essential ... for the creation of any mechanics' lien' in part because it is necessary to determine the running of the statute of limitations."²⁰

3. Foreclosure

If the contractor obtains a judgment upon a claim made under the statute, a lien will attach to the structure at issue and the grounds upon which it sits.²¹ A claimant is required to proceed by writ of *levari facias* in order to execute on a Judgment obtained under the mechanic's lien statute.²²

4. Sale

A judgment lienholder may file a writ of *scire facias* commanding a sheriff's sale of the property in order to recover his lien interest.²³ The statute does not provide for the priority or preference of claims. If the proceeds of the sale are insufficient to satisfy all outstanding liens obtained pursuant to the statute, the proceeds are divided on a *pro rata* basis between those claimants proceeding under the statute.²⁴

II. STATUTES OF LIMITATION AND REPOSE

A. Statute of Limitations

Actions based upon a construction contract must be commenced within three (3) years from time of breach.²⁵ Delaware courts have extended the limitations period in construction defect claims where the construction defect was "inherently unknowable."²⁶

B. Statute of Repose

A six-year limitations period applies to claims for death or injury arising out of construction on real property.²⁷ Known as Delaware's "builder's statute," this statute of repose

provides a limitations period that runs from the earliest date of various events in the construction process, such as substantial completion and/or acceptance by the owner.²⁸ The statute also provides that to the extent that the previous statutes provide for a shorter time period, they shall control.²⁹ The statute does not apply to someone in actual control such as an owner or a tenant at the time when the undertaking of an improvement to property constitutes the proximate cause of injury or death.³⁰

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

In the construction context, there are no statutory requirements that a party provide pre-suit notice prior to initiating an action for breach of warranty. The courts, however, have dismissed a homeowner's claims for non-compliance with the notice provisions contained in their warranty.³¹ The courts will enforce contractual pre-suit notice provisions between parties.³²

Pre-suit notice of claims is required when the suit involves certain municipalities as defendants.³³ No claims for damages relating to physical injuries, death, or injury to property and alleging negligence against the City of Wilmington or any of its departments, officers, agents or employees may be brought, unless written notice is provided to the Mayor within one year of the date of such injury, denoting the time, place and manner of injuries sustained.³⁴

IV. COVERAGE AND ALLOCATION ISSUES

Standard commercial general liability ("CGL") policies provide policyholders with insurance against liability for all sums the insured becomes legally obligated to pay as damages because of bodily injury or property damage caused by an occurrence. Whether coverage is triggered under CGL policies depends on policy interpretation and application of the requirements that the bodily injury or property damage occur during the policy period, and that such injury or damage is caused by an occurrence.

Delaware courts have taken divergent positions in coverage and allocation cases. The courts have distinguished injuries-in-fact, that is, discrete physical injuries or damage to property, from injuries which result from continuous conduct which extends over a period of time. In determining when an "occurrence" happens under applicable policies of insurance, Delaware courts undertake a fact-specific analysis.

The Delaware Superior Court has applied a continuous trigger analysis to claims of pollution resulting from leaching from a landfill.³⁵

The Supreme Court has held that insuring agreement language providing for "indemni[ty] for 'all sums' which an insured is obligated to pay ... caused by an occurrence" is inconsistent with *pro rata* allocation based upon time on the risk.³⁶ The *Monsanto* court, applying Missouri law, held that, without an express proportional limitation in the applicable policy, an insurer would be liable for the entirety of damages, up to the limits of coverage for the applicable policy periods. But in the *E. I. du Pont de Nemours & Co.*, the Supreme Court imposed a *pro rata* allocation based on time on the risk on equitable grounds, stating: "it is illogical to compress all of this damage into one policy period and hold each insurer fully liable. The presumption of continuous damage logically and fairly requires the imposition of the modified *pro rata* allocation of damage."³⁷

V. CONTRACTUAL INDEMNIFICATION

Contractual provisions in construction contracts which purport to obtain indemnification for a party's own negligence are void as a matter of legislatively-defined public policy.³⁸ The Delaware Superior Court has held that when a construction contract contains a severability clause, 6 *Del. C.* §2704(a) may invalidate only the parts of the agreement that indemnify a party against that party's own conduct.³⁹ The extent to which indemnification clauses are severable, however, depends upon the express language of the indemnification provision.⁴⁰

Delaware courts have distinguished agreements to procure insurance from agreements to indemnify. The Supreme Court has held that liability insurance purchased for another remains enforceable when a party seeks coverage under that policy, despite the provisions of 6 *Del. C.* § 2704(a).⁴¹ Where a party fails to honor their contractual agreement to purchase insurance coverage for another, an enforceable cause of action for breach exists.⁴² The Delaware Supreme Court has held that certain terms in an additional insured clause are construed broadly under Delaware law.⁴³

The common law recognized the right to indemnity only if it was based upon contract, express or implied.⁴⁴ While indemnity ordinarily arises out of contract, it may also be based upon "equitable principles" and that term is equivalent to the term "principles of fairness or justice."⁴⁵

Generally, contract provisions must be crystal clear and unequivocal in requiring a contractor to assume all liability for damage claims, regardless of which party is guilty of negligence actually causing the injury.⁴⁶ Contracts relieving a party of its own negligence are not favored, are strictly construed, and will not be interpreted to provide indemnification unless the intent of the parties is so expressed in very clear terms.⁴⁷

In addition, where the contract is silent on indemnification, Delaware provides us with several circumstances which can give rise to an implied obligation to indemnify. The first arises from an implied duty of workmanlike performance. Others involve special relationships in which a party with superior expertise or knowledge of a danger or risk of danger may be held to indemnify another.

Typically, if an indemnity provision specifically addresses, and permits, indemnification in a situation where the negligence of the indemnitor and indemnitee combine and concurrently cause a loss, that provision will be enforced. Delaware courts permit parties, by contract, to provide that each party would bear the loss proportionate to its fault.⁴⁸

An employer is immune from contribution claims due to the exclusivity provisions of Delaware's worker's compensation statute.⁴⁹ However, the Supreme Court has held that contractual claims for indemnification based upon express contract terms may be maintained against a plaintiff's employer.⁵⁰ The Superior Court has held that even implied indemnification claims may survive in certain cases where no express indemnification provision exists on the face of the contract.⁵¹

VI. DAMAGES LIMITATIONS

Delaware courts have generally adhered to the Restatement of the Law in determining damages in construction defect cases: “[I]f a party to a construction contract fails to perform its obligations under the contract, the aggrieved party is entitled to damages measured by the amount required to remedy the defective performance unless it is not reasonable or practicable to do so.”⁵²

A. Attorney’s fees

Delaware follows the “American Rule,” whereby a prevailing party is expected to pay its own attorney’s fees and costs.⁵³ Generally, Delaware courts may not order the payment of attorney’s fees as part of costs to be paid by the non-prevailing party unless a statutory or contractual basis exists for the award of such fees.⁵⁴

B. Consequential Damages

In a contract action, a party may recover damages for those injuries which are reasonably foreseeable or anticipated to flow from the breach.⁵⁵ In a construction contract action, compensatory damages have been equated to a plaintiff’s “‘out-of-pocket’ actual loss.”⁵⁶

C. Delay and Disruption Damages

Delaware courts have allowed delay damages where a construction contract provided for same in a liquidated damages provision.⁵⁷

D. Economic Loss Doctrine

Under the Economic Loss Doctrine, a party may recover in tort only if damages include bodily injury or property damage.⁵⁸ Delaware courts have adopted an exception to this rule as set forth in the Restatement (Second) of Torts § 552, which provides a basis for recovery for economic losses against those supplying false information.⁵⁹ In order to successfully meet the exception in a negligent misrepresentation claim, a plaintiff must show that (1) defendant supplied the information to the plaintiff for use in business transactions with third parties, and (2) the defendant is in the business of supplying information.”⁶⁰

Delaware courts have allowed purely economic tort claims to extend to suppliers of information.⁶¹

E. Interest

A prevailing party in a contract action is entitled to pre- and post-judgment interest.⁶² Pre-judgment interest is awarded as a matter of right.⁶³ As a general rule, pre-judgment interest is computed from the date payment is due under the contract.⁶⁴ The legal rate of interest is defined as 5% over the Federal Reserve Discount Rate.⁶⁵

F. Punitive Damages

Punitive damages generally are not recoverable in a breach of contract action.⁶⁶ However, the Delaware Supreme Court has stated that punitive damages are recoverable where “the defendant’s conduct exhibits a wanton or willful disregard for the rights of [the] plaintiff.”⁶⁷ A finding of “ill-will, hatred or intent to cause injury” is required in order to support a claim for punitive damages in a contract action.⁶⁸

¹ 25 Del. C. § 2702(a).

² *Commonwealth Const. Co. v. Cornerstone Fellowship Baptist Church, Inc.*, 2006 WL 2567916, *16 (Del. Super.), citing *J.G. Justis Co. v. Spicer*, 95 A. 239 (Del. Super. 1915).

³ *See A.J. Bradbury v Adeleke*, 2008 WL 5048427, at *3 (Del. Super.), citing *Construction Resource Management v. Littleton*, 2008 WL 4117186, at *3 (Del. Super.).

⁴ *Wyoming Concrete Industries, Inc. v. Hickory Commons, LLC II*, 2007 WL 53805, at *2 (Del. Super.) citing *Dep’t of Cmty. Affairs & Econ. Dev. V.M. Davis & Sons, Inc.*, 412 A.2d 939, 942 (Del. 1980).

⁵ *C&J Paving, Inc. v. Hickory Commons, LLC*, 2006 WL 3898268, at *2 (Del. Super.) citing *J.O.B. Constr. Co. v. Jennings & Churella Servs., Inc.* 2001 WL 985106, at *2 (Del. Super.); see *King Construction, Inc. v. Plaza Four Realty, LLC*, 2008 WL 4382798 (Del. Super.), *aff’d* 976 A.2d 145 (Del. 2009), citing *E.J. Hollingsworth Co. v. Continental-Diamond Fiber Co.*, 175 A.2d 266, 268 (Del. 1934)) (There is no right to a mechanic’s lien unless the statement of claim complies all of the applicable statutory requirements).

⁶ *Rockland Builders, Inc. v. Endowment Management, LLC*, 2006 WL 2053418, *3 (Del. Super.) (quoting *Ceritano Brickwork, Inc. v. Kirkwood Indus., Inc.*, 276 A.2d 267, 268 (Del. 1971)).

⁷ *See Ewing v. Bice*, 2001 WL 880120, at *2 (Del. Super.); citing 25 Del. C. § 2712; also citing *Silverside Home Mart, Inc. v. Hall*, 345 A.2d 427, 429-30 (Del. Super. 1975); *Lakewood Builders, Inc. v. Vitelli*, 1987 WL 10533, at *2 (Del. Super.).

⁸ *See Wyoming Concrete Industries, Inc.; C&J Paving, Inc., supra.*

⁹ *See Commonwealth Const. Co. v. Cornerstone Fellowship Baptist Church, Inc.*, 2006 WL 2567916 (Del. Super.), citing *Neukranz v. Delaware Lumber & Millwork, Inc.*, 1998 WL 442847 (Del. Super.) (citing amendment to 12 Del. C. § 2712).

¹⁰ 25 Del. C. § 2701(3).

¹¹ 25 Del. C. § 2702(b).

¹² *See 25 Del. C. § 2703; See also Whittington v. Segal*, 193 A.2d 534 (Del. Super. 1963) (holding that provisions contained in a lease did not comport with the statutory requirement of a contract signed by the owner for the work performed); see also *C&J Paving*, 2006 WL 3898268, *2 (Del. Super.) (dismissing mechanic’s lien action for paving work that was not appurtenant to or did not service any structure on the land, where plaintiff failed to allege any specific structure benefited by the materials delivered or the work performed); *Cf. Jones v. Julian*, 195 A.2d 388, 390 (Del. 1963) (finding that mechanic’s lien law applied to paving work done by a subcontractor around a motel then under construction because the paving was a “component part of [the] motel,” rather than an improvement to land alone (not requiring the pleading of a written contract signed by the owner)).

¹³ *See 25 Del. C. § 2712; See also Commonwealth Const. Co. v. Cornerstone Fellowship Baptist Church, Inc.*, 2006 WL 2567916, at *16 (Del. Super.).

¹⁴ *See 25 Del. C. § 2712.*

¹⁵ *See, e.g., King Construction, Inc. v. Plaza Four Realty, LLC*, 2008 WL 4382798 (Del. Super.), *aff’d* 976 A.2d 145 (Del. 2009), citing 25 Del. C. § 2712 (dismissing mechanic’s claim for failure to plead lessor’s written consent for work performed for its tenant) (“Although not explicitly referenced in the pleading requirements of § 2712, the statutory requirement of prior written consent has long been construed by Delaware courts to impose a pleading requirement upon that ‘special class of mechanics’ liens for labors or supplies contracted for by the tenant.’”).

¹⁶ *See 25 Del. C. § 2713.*

¹⁷ *See 25 Del. C. § 2711(a) (1).*

¹⁸ *See 25 Del. C. § 2711(a) (2) (a-i).*

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- ¹⁹ See 25 Del. C. § 2711(b).
- ²⁰ *King Const., Inc. v. Plaza Four Realty, LLC*, 2008 WL 4382798 *3 (Del. Super.), *aff'd* 976 A.2d 145, (Del. 2009), *citing Poole v. Oak Lane Manor, Inc.*, 118 A.2d 925, 926 (Del. Super. 1955), *aff'd* 124 A.2d 925 (Del. 1956).
- ²¹ 25 Del. C. § 2718.
- ²² 25 Del. C. § 2719.
- ²³ 25 Del. C. §§2714, 2715.
- ²⁴ 25 Del. C. §2720.
- ²⁵ See 10 Del. C. § 8106; See also *Nardo v. Guido DeAscanis & Sons*, 254 A.2d 254, 256 (Del. Super. 1969).
- ²⁶ See *Descano v. Walters*, 1992 WL 9078, *3 (Del. Super.), *aff'd* 614 A.2d 1275 (Del. 1992) (TABLE).
- ²⁷ See 10 Del. C. § 8127.
- ²⁸ *Id.*; see, e.g., *McConaghie v. Wakefern Food Corp.*, 2004 WL 1195391 (Del. Super.) (six-year limitations period ran from the date the certificate of occupancy was issued).
- ²⁹ See 10 Del. C. § 8127.
- ³⁰ See *Id.*
- ³¹ See *Commercial Union Ins. Co. v. S&L Contractors, Inc.*, 2002 WL 31999352, *2 (Del. Com. Pl.).
- ³² *U.S. Bank Nat. Ass'n v. U.S. Timberlands Klamath Falls, L.L.C.*, 2004 WL 1699057, *3, (Del. Ch.), *citing Harper v. Del. Valley Broadcasters*, 743 F. Supp. 1076 (D. Del. 1990) *aff'd*, 932 F.2d 959 (3d Cir.1991).
- ³³ 10 Del. C. § 8124.
- ³⁴ See 10 Del. C. § 8124; See also *City of Wilmington v. Spencer*, 391 A.2d 199, 202 (Del. 1978); *Sadler v. New Castle County*, 524 A.2d 18, 26 (Del. Super. 1987).
- ³⁵ See *National Union Fire Insurance Co. v. Rhone-Poulenc Basic Chemicals Company*, 1992 WL 22690, at *18-19 (Del. Super.) (finding that “every policy from the start of the injurious process is triggered”) (*citing New Castle County v. Continental Casualty Co.*, 725 F. Supp. 800, 809-812 (D. Del. 1989) (*aff'd in part, rev'd in part, New Castle County v. Hartford Acc. and Indem. Co.*, 933 F.2d 1162 (C.A. 3 (Del.) 1991)); *but see Olde Colonial Village Condominium Council v. Millers Mut. Ins. Co.*, 2002 WL 122885, at *10 (Del. Super.) (rejecting the continuous trigger analysis, finding that an engineer’s recommendations to evacuate a building, coupled with the condemnation of the building equated to the “collapse” of the building: “a collapse provision’s trigger is the collapse itself, not what led to it”).
- ³⁶ See *Monsanto Co. v. C.E. Heath Compensation and Liability Company*, 652 A.2d 30, 34-35 (Del. 1994) (applying Missouri law); *cf. Hercules, Inc. v. AIU Insurance Co., et. al.* 784 A.2d 481, 489 (Del. 2001) (holding that “*pro rata* allocation is inconsistent with the ‘all sums’ provisions in the [applicable] policies”; finding that insurers who agreed to indemnify for “all sums” in policies covering the applicable period were jointly and severally liable).
- ³⁷ See *Id.* at FN 7; *but see E. I. du Pont de Nemours & Co. v. Admiral Ins. Co.*, 1995 WL 654020, at *15 (Del. Super.) (imposing *pro rata* allocation based on time on the risk on equitable grounds: “it is illogical to compress all of this damage into one policy period and hold each insurer fully liable. The presumption of continuous damage logically and fairly requires the imposition of the modified *pro rata* allocation of damage.”), *aff'd, Travelers Cas. and Sur. Co. v. E.I. DuPont de Nemours & Co.*, 933 A.2d 1250 (Del. 2007) (Table).
- ³⁸ See 6 Del. C. § 2704(a); *Alberici Const. Co. v. Mid-West Conveyor Co., Inc.*, 750 A.2d 518, 521 (Del. 2000); See also *Kempski v. Toll Bros., Inc.*, 582 F. Supp. 2d 636, 641 (D. Del. 2008) (“Under Delaware law ... ‘a contractual provision requiring one party to indemnify another party for the second party’s own negligence, whether sole or partial, is against public policy and is void and unenforceable.’”) (applying Delaware law).
- ³⁹ See *Handler Corp. v. State Drywall Co., Inc.* 2007 WL 3112466, at *3 (Del. Super.) (where an indemnification provision between a contractor and subcontractor expressly provided that the subcontractor was required to indemnify the contractor for the negligence of either party, and the contract contained a severability clause, the court voided only the language of the provision requiring the subcontractor to indemnify the contractor for its own negligence, and held that the rest of the indemnification provision, providing that subcontractor was required to indemnify the contractor for vicarious liability, was enforceable), *see also Menkes v. Saint Joseph Church*, 2011 WL 1235225, at *3 (Del. Super.); *Patton v. 24/7 Cable Co., LLC*, 2013 WL 1092147, at *4 (Del. Super.).
- ⁴⁰ See *Kempski v. Toll Bros., Inc.*, 582 F.Supp.2d 636, 641 (D. Del. 2008) (applying Delaware law) (granting Summary Judgment for the subcontractor, refusing to apply a severability clause to the indemnification provision, holding that “the duties to indemnify for the conduct of the [contractor] and the actions of [the subcontractor] were expressed together as a single obligation, and were “not severable ... distinct[,] or distinguishable.”), *citing Handler Corp.*, 2007 WL 3112466, at *3.
- ⁴¹ See *Chrysler Corporation v. Merrell & Garaguso, Inc.*, 796 A.2d 648 (Del. 2002); See also 6 Del. C. § 2704(b).

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- ⁴² *DaimlerChrysler Corporation v. Pennsylvania National Mut. Ins. Co.*, 2003 WL 1903766 (Del. Super.).
- ⁴³ See *Pacific Ins. Co. v. Liberty Mut. Ins. Co.*, 956 A.2d 1246, 1257 (Del. 2008) (holding that the term “‘arising out of’ is broadly construed to require some meaningful linkage between the two conditions imposed in the contract [i.e., the contractors’] operations and the [landowner’s] resulting liability”).
- ⁴⁴ *Insurance Company of North American v. Waterhouse*, 424 A.2d 675 (Del. 1980); *Allstate Investigation Security Agency, Inc. v. Turner Construction Co.*, 301 A.2d 273 (Del. 1972).
- ⁴⁵ *Clark v. Teeven Holding Co., Inc.*, 625 A.2d 869, 878 (Del. Ch. 1992).
- ⁴⁶ *State v. Interstate Amiesite Corp.*, 297 A.2d 41, 44 (Del. 1972).
- ⁴⁷ *Waller v. J.E. Brenneeman Co.*, 307 A.2d 550 (Del. Super. 1973).
- ⁴⁸ *Precision Air, Inc. v. Standard Chlorine of Delaware, Inc.*, 654 A.2d 403 (Del. 1995).
- ⁴⁹ See 19 Del. C. § 2304; See also *Precision Air, Inc. v. Standard Chlorine of Del., Inc.*, 654 A.2d 403, 407 (Del. 1995) (“Because the employer cannot be held liable as a joint tortfeasor, it is not obligated to provide contribution to the third party.”).
- ⁵⁰ See *Precision Air*, at 407.
- ⁵¹ See *Davis v. R.C. Peoples, Inc.*, 2003 WL 21733013 (Del. Super.), see also *Thompson v. Murta Wiedemann, Inc.*, 2010 WL 596504, at *2 (Del. Super.).
- ⁵² See *Council of Unit Owners v. Carl M. Freeman Associates, Inc.*, 564 A.2d 357, 361 (Del. Super. 1989), citing *Farny v. Bestfield Builders, Inc.*, 391 A.2d 212, 214 (Del. Super. 1978); *Carey v. McGinty*, 1988 WL 55336, at *6, (Del. Super.); See also Restatement, Contracts § 346 (1932).
- ⁵³ See *Montgomery Cellular Holding Co. v. Dobler*, 880 A.2d 206, 227 (Del. 2005).
- ⁵⁴ See *Casson v. Nationwide Ins. Co.*, 455 A.2d 361, 370 (Del. Super. 1982); but see *Dover Historical Soc., Inc. v. City of Dover Planning Com’n*, 902 A.2d 1084, 1091 (Del. 2006) (“The Superior Court does hear cases in which it is occasionally required to apply equitable principles. In such cases [, to control its own process,] the Superior Court has jurisdiction to award attorneys’ fees even if no contract or statute requires it.”), citing *Burge v. Fidelity Bond & Mortgage Co.*, 648 A.2d 414, 421-22 (Del. 1994) (upholding award of attorneys’ fees in a Superior Court action involving a mortgage foreclosure, which is inherently equitable).
- ⁵⁵ *Clemens v. Western Union Telegraph Co.*, 28 A.2d 889, 890 (Del. Super. 1942).
- ⁵⁶ *Hazlett v. Pompeo*, 2002 WL 32074651 (Del. Com. Pl. 2002), citing *Strassburger v. Earley*, 752 A.2d 557, 579 (Del. Ch. 2000).
- ⁵⁷ See *Joseph T. Dashiell Builders v. Andrews*, 2002 WL 31819895 (Del. Super. 2002).
- ⁵⁸ *Christiana Marine Service Corp. v. Texaco Fuel and Marine Marketing, Inc.*, 2002 WL 1335360, at *22 (Del. Super.).
- ⁵⁹ See *Guardian Construction Co. v. Tetra Tech Richardson*, 583 A.2d 1378, 1385-1386 (Del. Super. 1990).
- ⁶⁰ See *Christiana Marine Services Corp.*, 2002 WL 1335360, at *6, citing *Danforth v. Acorn Structures, Inc.*, 1991 WL 269956 (Del. Super.).
- ⁶¹ As to design engineers (See *Guardian*, 583 A.2d at 1385), as to accountants (see *Carello v. PricewaterhouseCoopers, LLP*, 2002 WL 1454111, at *7 (Del. Super.), as to financial advisors, *Outdoor Technologies Inc. v. AllFirst Financial Inc.*, 2000 WL 141275, at *5 (Del. Super.), as to title searchers (see *Ruger v. Funk*, 1996 WL 110072, at *10 (Del. Super.). But cf. *Millsboro Fire Co. v. Construction Management Services, Inc.*, 2006 WL 1867705, (Del. Super. 2006) (refusing to apply an exception to a subcontractor, finding that plans and design drawings provided by a subcontractor did not place them in the “business of supplying information”).
- ⁶² But see *Reserves Development LLC v. Severn Sav. Bank, FSB*, 961 A.2d 521, 525 (Del. 2008) (Denying Appellant’s argument that it was entitled to pre-judgment interest as a matter of right and denying request for pre-judgment interest as untimely in a quasi-contract claim for unjust enrichment; affirming the Chancery Court’s decision to deny pre-judgment interest, where Appellant requested interest in its Amended Complaint, but did not specifically request pre-judgment interest until including it in a proposed form of Order).
- ⁶³ *Citadel Holding Corp. v. Roven*, 603 A.2d 818, 826 (Del. 1982); but see *Reserves Development LLC v. Severn Sav. Bank, FSB*, *supra*, at FN 57.
- ⁶⁴ *Moskowitz v. Mayor & Council of Wilmington*, 391 A.2d 209, 210 (Del. 1978).
- ⁶⁵ 6 Del. C. §2301(a).
- ⁶⁶ *Horizon J.J. White, Inc. v. Metropolitan Merchandise Mart*, 107 A.2d 892 (Del. Super. 1954).
- ⁶⁷ *Cloroben Chemical Corp. v. Comegys*, 464 A.2d 887, 891 (Del. 1983), citing *Riegal v. Aastad*, 272 A.2d 715, 718 (Del. 1970), or “for willful or malicious breaches of contract.” *Jardel Co., Inc. v. Hughes*, 523 A.2d 518, 529 (Del. 1987); see also *Casson v. Nationwide Insurance Co.*, 455 A.2d 361 (Del Super. 1982), citing *McClain v. Faraone*, 369 A.2d 1090 (Del. Super. 1977).

⁶⁸ *See Casson*, 455 A.2d at 368.

DISTRICT OF COLUMBIA

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I. MECHANIC'S LIEN BASICS

A. Requirements

A contractor desiring to enforce a lien shall record in the land records (the property records maintained by the Office of the Recorder of Deeds of the District of Columbia) a notice of intent that identifies the property subject to the lien and states the amount due or to become due to the contractor.¹ The notice of intent shall be recorded within 90 days after the earlier of the completion or termination of the project.² If the notice of intent is not recorded in the land records within 90 days after the earlier of the completion or termination of the project, the contractor's lien shall terminate upon the expiration of the 90-day period.³

Any contractor who timely records a notice of intent must send to the owner, by certified mail to the current address (or the last known address) of the owner, a copy of the notice within 5 business days after the date of its recordation in the land records.⁴ If the certified mail is returned to the contractor unclaimed or undelivered, the contractor must post a copy of the recorded notice of intent at or on the affected real property in a location generally visible from some entry point to the real property.⁵

The notice of intent shall include, *inter alia*, the following: (1) the name and address of the contractor or the contractor's registered agent; (2) the name and address of the owner or the owner's registered agent; (3) the name of the party against whom interest a lien is claimed and the amount claimed, less any credit for payments received up to and including the date of the notice of intent; (4) a description of the work done, including the dates that work was commenced and completed; (5) a description of the material furnished, including the dates that material was first and last delivered; and (6) a legal description and, to the extent available, a street address of the real property.⁶ Additional requirements exist when the contractor is an entity organized under the laws of the District of Columbia or is doing business in the District of Columbia,⁷ or if the contractor is an individual or an entity organized under laws other than those of the District of Columbia, and is not doing business in the District of Columbia within the meaning of applicable District laws but is required to be licensed by a governmental entity.⁸

Subcontractor's liens similarly require the same notice as a contractor's lien, but with additional requirements.⁹ These additional requirements include serving notice upon the owner of the property.¹⁰

B. Enforcement and Foreclosure

The proceeding to enforce a mechanic's lien shall be a bill in equity, which shall contain a brief statement of the contract on which the claim is founded, the amount due thereon, the time when the notice was filed with the Recorder of Deeds, and a copy thereof served on the owner or his agent, if so served, and the time when the building or the work thereon was completed, with a description of the premises and other material facts; and shall pray that the owner's interest in the premises be sold and the proceeds of sale applied to the satisfaction of the lien.¹¹

If such suit be brought by any person entitled, other than the principal contractor, the latter shall be made a party defendant, as well as all other persons who may have filed notices of liens. All or any number of persons having liens on the same property may join in one suit, their respective claims being distinctively stated in separate paragraphs. If several suits are brought by different claimants and are pending at the same time, the court may order them to be consolidated.¹²

Any person with a lien and who has recorded a valid notice of intent shall only enforce the lien by:

- a) Filing suit under §40-303.08 to enforce the lien at anytime within 180 days after the date that the notice of intent is recorded in the land records;¹³ and
- b) Recording, within 10 days of filing suit, a notice of pendency of action in accordance with §42-1207(b) in the land records.¹⁴

Failure to file suit within the 180-day period or to file timely a notice of pendency of action shall terminate the lien.¹⁵

If the right of the complainant or of any of the parties to the suit to the lien is established, the court shall decree a sale of the land and premises or the estate and interest therein of the person who, as owner, contracted for the erection, repair, improvement of, or addition to the building.¹⁶

C. Ability to Waive and Limitations on Lien Rights

A contractor or subcontractor may waive its right to file a mechanic's lien by express agreement, even when it was bargained for after the original contract was made.¹⁷ The right to file a lien may also be waived by implication. In some cases, a waiver has been found by accepting real security for payment of work being done, as the contractor was clearly not relying

on his right to file a mechanic's lien.¹⁸ The right to file a mechanic's lien is individual to each contractor, and it may not be waived by a third party.¹⁹

If the original contractor and its subcontractors have filed notices of liens, the subcontractor will be satisfied first out of the proceeds of sale, but not in excess of the amount due him, and the balance, if any, of said amount shall be paid to the contractor.²⁰

If one, or some only, of the persons employed under the original contractor shall have served notice on the owner, before payments made by him to the original contractor, said party or parties shall be entitled to priority of satisfaction out of said proceeds to the amount of such payments; but, subject to this provision, if the proceeds of sale, after paying there out the costs of the suit, shall be insufficient to satisfy the liens of said parties employed under the original contractor, the said proceeds shall be distributed ratably among them to the extent of the payments accruing to the original contractor subsequently to the service of notice on the owner by said parties.²¹

II. STATUTES OF LIMITATION AND REPOSE

A. Statutes of Limitation and Limitations on Application of Statutes

1. Contract for sale under UCC - four years, but can be reduced by the terms of contract to not less than one year; cannot be extended by the contract.²²

2. Statute of limitations on a simple contract, expressed or implied - three years.²³

B. Statutes of Repose and Limitations on Application of Statutes

An action to recover damages resulting from the defective or unsafe condition of an improvement to real property, and for such contribution and indemnity, will be barred unless the injury occurs within the ten year period beginning on the date the improvement was substantially completed.²⁴ An improvement to real property is considered substantially completed when it is first used, or it is first available for use after having been completed in accordance with the contract or agreement covering the improvement, including any agreed changes to the contract or agreement, whichever occurs first.²⁵

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

There are no statutory requirements in the District of Columbia for a claimant to provide the opportunity to cure with respect to improvements to realty; however, such a requirement may be included in the contract itself. A thorough analysis of the contract documents should be performed in each case to determine whether a Claimant is required to provide the opportunity to cure.

IV. INSURANCE COVERAGE AND ALLOCATION ISSUES

A. General Coverage Issues

In the District of Columbia, insurance policies are construed according to contract principles.²⁶ As such, if the terms are unambiguous, no extrinsic evidence is necessary.²⁷ Since ambiguities in contracts are typically construed against the drafter, the insurer is assumed to have drafted the policy and any ambiguous terms will be construed against the insurer.²⁸

Under a typical liability policy, an insurer has a duty to both provide the insured with a defense and to indemnify the insured for a judgment up to policy limits.²⁹ The duty to defend depends on whether the alleged facts bring the claim within the insurance policy, and the duty to indemnify depends on the ultimate truth of those facts.³⁰

Generally, insurance policies do not cover the insured's economic loss stemming from contractual liability for defective workmanship.

B. Trigger of Coverage

The District of Columbia has adopted the manifestation trigger as a general rule, which states that property damage occurs at the time the damage is discovered or when it has manifested.³¹ The District of Columbia also recognizes an exception to this general rule when the damage to the property can be characterized as "continuous or progressive."³² In continuous and progressive situations the initial damage occurred (i.e., was evident during the policy period) and further damage occurred afterward.³³

C. Allocation Among Insurers

Where there are two applicable insurance policies, one policy containing a *pro rata* "other insurance" clause and the other an excess "other insurance" clause, provisions of each will be interpreted to give effect to the intent of the contracting parties.³⁴ The application of this rule will probably result in the excess clause being given full effect.³⁵ The insurance company including a *pro rata* clause in its policy will be required to shoulder the loss up to its policy limit.³⁶ In some instances, it may be impossible to reconcile the two clauses or to give effect to the intent of the contracting parties (e.g. where the applicable portions of the two "other insurance" clauses are identical excess clauses) and the court will almost always require the insurers to apportion the liability.³⁷

V. CONTRACTUAL INDEMNIFICATION

The District of Columbia has no statutory provision voiding indemnity contracts for construction. Such clauses have been upheld by the District of Columbia Court of Appeals on more than one occasion.³⁸

The general rule is that indemnity provisions are permissible; however, such provisions "should not be construed to permit an indemnitee to recover for his [or her] own negligence unless the court is firmly convinced that such an interpretation reflects the intention of the

parties."³⁹ This is a diversion from the usual rules of contract interpretation.⁴⁰ Although questions of ambiguity in contracts are usually handed to the jury for determination, ambiguity in an indemnifying clause which purports to indemnify the negligence of the indemnitee, is, as a matter of law, void.⁴¹

The District of Columbia Court of Appeals' decisions in this area turn on the Court's interpretation of the indemnity clause in the contract. In *W.M. Schlosser Co., Inc. v. Maryland Drywall Co., Inc.*, and in *Grunley Constr. Co., Inc. v. Conway Corp.*, the language stated, essentially, that the subcontractor shall indemnify the general contractor and owner from all liability arising out of the execution of the work in the contract.⁴² Although there was no reference specifically to whose liability was to be indemnified, the broad language was interpreted not to be ambiguous, but simply all encompassing.⁴³ Thus, the indemnitee's liability fell within the broad language and was subject to indemnification.⁴⁴

In *Rivers & Bryan, Inc. v. HBE Corp.*, the contractor brought a claim of indemnity against the subcontractor for injuries caused on the work site in relation to work being performed on the contract.⁴⁵ The indemnity clause stated that the subcontractor would hold the contractor harmless from all damages or loss resulting from the subcontractor's failure to observe OSHA requirements.⁴⁶ In a note following the indemnity clause, there was written "subcontractor is not responsible for others who are not in conformance with OSHA."⁴⁷ The Court found ambiguity in the addition to the printed language of the contract and found that it was unclear whether the word "others" applied to the contractor or referred only to other subcontractors.⁴⁸ Thus, the Court held that the clause could not be upheld.⁴⁹

In *District of Columbia v. Royal*, the Court held that the government was not entitled to indemnification from the contractor based on an indemnity clause.⁵⁰ The Court stated that before it could uphold an indemnity clause it must be "firmly convinced that such an interpretation reflects the intention of the parties."⁵¹ The Court held that the indemnity clause clearly covered the contractor's own negligence; however, it could not be stretched to encompass the government's negligence as well.⁵² Consequently it denied the government's claim for indemnity from the contractor.⁵³

VI. CONTINGENT PAYMENT AGREEMENTS

A. Enforceability

Under D.C. law, a "pay if paid" provision establishes a valid condition precedent, it will be enforced.⁵⁴ There has not yet been a D.C. case which defines the treatment of a "pay when paid" clause.

B. Requirements

A "pay if paid" provision will be enforced if it is phrased to show that it is intended to be a condition precedent to payment.⁵⁵ Even if the clause is explicit, it will not be enforced if a contractor voluntarily lessens the amount of payment he receives.⁵⁶ This will be considered a breach of the contract, and the subcontractor will nevertheless be owed the money payable under

the contract.⁵⁷ For example, in *Urban Masonry Corp. v. N & N Contractors, Inc.*, a subcontractor's contract contained a "pay if paid" clause.⁵⁸ The contractor settled with his client for a lesser amount than was owed under the contract.⁵⁹ The contractor argued the condition precedent—being paid—had not been completely fulfilled, and he was not required to pay the subcontractor.⁶⁰ The D.C. Court of Appeals disagreed; the contractor had been paid, even if it was a lesser amount that originally bargained for.⁶¹ The Court also noted that even if the settlement had not constituted payment, the contractor would have breached the contract by frustrating the fulfillment of the condition precedent.⁶²

VII. DAMAGES LIMITATIONS

A. Personal Injury Damages vs. Construction Defect Damages

Under D.C. Code §12-301, an action for the recovery of real or personal property must be brought within three years from the time the injury is discovered.⁶³ Under D.C. Code §16-2702, an action for the recovery of wrongful death must be brought within two years after the death.⁶⁴

In the context of construction defect damages the injured party must be placed in the same position as if there had been no breach.⁶⁵ If the construction is incomplete, the injured party is entitled to reasonable costs of completion as long as that does not create unreasonable economic waste.⁶⁶ Additionally, the injured party is entitled to the value of the loss of the use, if the building was being constructed for use.⁶⁷ However, the injured party cannot recover more than he would have paid or more than he was damaged.⁶⁸

B. Attorney's Fees Shifting and Limitations on Recovery

The District of Columbia follows the "American Rule" that attorney's fees are ordinarily not recoverable.⁶⁹ The District of Columbia also recognizes as an exception to the "American Rule" the wrongful involvement in litigation doctrine.⁷⁰

C. Consequential Damages

An injured party is entitled to compensation for losses, which are the natural consequence and proximate result of the defendant's tort or breach of contract.⁷¹ Tortious injuries, however, need only be within the risk created by the defendant's action, whereas contract damages must be foreseeable.⁷² Where there is a breach of contract before the contractor starts work, the contractor is entitled to recover his lost profits due to the breach, which are measured by the contract price less the cost he would have incurred had the contractual obligation been completed.⁷³

D. Delay and Disruption Damages

Delay damages are compensable either as part of lost profits or reimbursement for costs.⁷⁴

E. Economic Loss Doctrine

The District of Columbia has not specifically addressed the economic loss doctrine, however, the United States District Court for the District of Columbia has.⁷⁵ The District Court noted an exception to this doctrine holding, “[w]hile it is true that a plaintiff is typically barred from recovering in tort for purely economic loss, this doctrine does not apply where there is a special relationship between the parties.”⁷⁶

F. Interest

Both pre and post-judgment interest are allowed in the District of Columbia.⁷⁷ Pre-judgment interest is generally regarded as merely another element of damages.⁷⁸ Interest is not allowable as part of punitive damages except as additional punishment.⁷⁹

G. Punitive Damages

Punitive damages are available in the District of Columbia upon proof that the defendant's tortious act was aggravated by “evil motive, actual malice, deliberate violence or oppression.”⁸⁰ Punitive damages must be supported by clear and convincing evidence that the tortious act was accompanied by conduct and a state of mind evincing malice or its equivalent.⁸¹ Punitive damages may be awarded only if the evidence demonstrates that the tort committed by the defendant was aggravated by egregious conduct and a state of mind that justifies punitive damages.⁸² Notwithstanding the availability of punitive damages, they are disfavored under District of Columbia law.⁸³

VIII. CASE LAW AND LEGISLATION UPDATE

The District of Columbia has recently implemented significant change to its Construction Code, putting in place requirements aimed at conservation.

On March 28, 2014, the District of Columbia made effective the 2013 DC Construction Codes. In doing so, the District has adopted the 2012 edition of the International Green Construction Code (IgCC). According to the District, these codes reflect the most modern, sustainable, and energy- and water-efficient building practices. The Code adoption serves to replace the District’s 2008 Construction Codes which previously governed.

Included in this adoption was the 2013 DC Energy Conservation Code. According to Mayor Vincent Gray’s Press Release,⁸⁴ the 2013 Energy Conservation Code will require that new buildings perform as much as 30 percent more efficiently, and the District’s inaugural Green Construction Code will extend the building practices legislated by the DC Green Building Act of 2006 to most construction projects.

The new codes incorporate more than five hundred (500) local DC amendments to the ICC and NFPA Codes,⁸⁵ so contractors and advisors must educate themselves regarding both the environmental-friendly changes and local requirements.

¹ D.C. CODE § 40-301.02(a)(1).
² *Id.*
³ *Id.*
⁴ *Id.* at (a)(2).
⁵ *Id.*
⁶ *Id.* at (b)(1)–(6).
⁷ *Id.* at (b)(7)(A).
⁸ *Id.* at (b)(7)(B).
⁹ D.C. CODE § 40.303.01.
¹⁰ D.C. CODE § 40.303.03.
¹¹ D.C. CODE § 40.303.08.
¹² *Id.*
¹³ D.C. CODE § 40.303.13(a)(1)(A).
¹⁴ *Id.* at (a)(1)(B).
¹⁵ *Id.* at § (a)(2).
¹⁶ D.C. CODE § 40.303.09.
¹⁷ *Kidwell & Kidwell, Inc. v. W.T. Galliher & Bro., Inc.*, 282 A.2d 575, 578 (D.C. 1971).
¹⁸ *Grant v. Strong*, 85 U.S. 623, 625–26 (1973).
¹⁹ *Battista v. Horton, Myers & Raymond*, 128 F.2d 29, 31 (D.C. Cir. 1942).
²⁰ D.C. CODE § 40.303.10.
²¹ D.C. CODE § 40.303.11.
²² D.C. CODE § 28:2-725.
²³ D.C. CODE § 12-301(7).
²⁴ D.C. CODE § 12-310(a)(1)(B).
²⁵ *Id.* at (a)(2)(A)–(B). This limitation does not apply to actions based on expressed or implied contracts. *Id.* at (b)(1).
²⁶ *Stevens v. United Gen. Title Ins. Co.* 801 A.2d 61, 66 (D.C. 2002).
²⁷ *Id.*
²⁸ *Meade v. Prudential Ins. Co. of Am.*, 477 A.2d 726, 728 (D.C. 1984).
²⁹ *Salus Corp. v. Continental Cas. Co.*, 478 A.2d 1067, 1069–70 (D.C. 1984)
³⁰ *Id.*
³¹ *Wrecking Corp. of Am., Virginia, Inc. v. Insur. Co. of North Am.*, 574 A.2d 1348, 1350 (D.C. 1990).
³² *Id.*
³³ *Id.*
³⁴ *Jones v. Medox, Inc.*, 430 A.2d 488, 493–94 (D.C. 1981).
³⁵ *Id.*
³⁶ *Id.*
³⁷ *Id.*
³⁸ See *Grunley Constr. Co., Inc. v. Conway Corp.*, 676 A.2d 477, 478 (D.C. 1996); *W.M. Schlosser Co., Inc. v. Maryland Drywall Co., Inc.*, 673 A.2d 647, 653 (D.C. 1996). Although this appears to be a slight shift in the law from prior decisions. See *Rivers & Bryan, Inc. v. HBE Corp.*, 628 A.2d 631, 634 (D.C. 1993); *District of Columbia v. Royal*, 465 A.2d 367, 369 (D.C. 1983). The law in the District of Columbia has been interpreted to uphold such clauses in the past. *Gen. Heating Eng'g. Co. v. District of Columbia*, 301 F.2d 549, 551 (D.C. Cir. 1962).
³⁹ *Schlosser*, 673 A.2d at 653 (quoting *United States v. Seckinger*, 397 U.S. 203, 211 (1970)).
⁴⁰ *Rivers & Bryan*, 628 A.2d at 635.
⁴¹ *Id.*
⁴² *Schlosser*, 673 A.2d at 653; *Grunley*, 676 A.2d at 478.
⁴³ *Schlosser* 673 A.2d at 654; *Grunley* 676 A.2d at 478.
⁴⁴ *Id.*
⁴⁵ 628 A.2d 631 (D.C. 1993).
⁴⁶ *Id.* at 634.
⁴⁷ *Id.*
⁴⁸ *Id.* at 635.
⁴⁹ *Id.* at 636–37.
⁵⁰ 465 A.2d 367 (D.C. 1983).

⁵¹ *Id.* at 368.
⁵² *Id.* at 369–70.
⁵³ *Id.* at 370.
⁵⁴ *Urban Masonry Corp. v. N & N Contractors, Inc.*, 676 A.2d 26, 36 (D.C. 1996)
⁵⁵ *Id.*
⁵⁶ *Id.*
⁵⁷ *Id.*
⁵⁸ *Id.*
⁵⁹ *Id.*
⁶⁰ *Id.*
⁶¹ *Id.*
⁶² *Id.*
⁶³ D.C. CODE § 12-301 (2)–(3).
⁶⁴ D.C. CODE § 16-2702.
⁶⁵ *Fleming v. Twine*, 58 A.2d 498, 499–500 (D.C. 1948).
⁶⁶ *Id.*
⁶⁷ *Id.*
⁶⁸ *Id.*
⁶⁹ *Jung v. Jung*, 844 A.2d 1099, 1107 (D.C. 2004) (citing *In re Antioch Univ.*, 482 A.2d 133, 136 (D.C.1984)). However, attorney fees can be awarded in certain circumstances, such as where authorized by contract (*Urban Masonry Corp. v. N & N Contractors, Inc.*, 676 A.2d 26 (D.C. 1996)); where authorized by statute (D.C. CODE § 28-3901, et seq. (Consumer Protection Procedures Act)); or where permitted by rule for discovery violations (*Lowery v. Glassman*, 908 A.2d 30 (D.C. 2006)).
⁷⁰ *Taylor v. Tellez*, 610 A.2d 252, 255–56 (D.C. 1992) (citing *Dalo v. Kivitz*, 596 A.2d 35, 37 (D.C. 1991)) (where attorney's fees may be awarded to clients who have been forced into litigation by their attorney's malpractice).
⁷¹ *Boiseau v. Morrisette*, 78 A.2d 777, 780 (D.C. 1951); *Murphy v. O'Donnell*, 63 A.2d 340, 342 (D.C. 1948).
⁷² *Bay General Industries, Inc. v. Johnson*, 418 A.2d 1050, 1056 (D.C. 1980).
⁷³ *Bergman v. Parker*, 216 A.2d 581, 583–84 (D.C. 1966).
⁷⁴ *District Concrete Co., Inc. v. Bernstein Concrete Corp.*, 418 A.2d 1030, 1038 (D.C. 1980).
⁷⁵ *Jones v. Hartford Life and Acc. Ins. Co.*, 443 F. Supp. 2d 3 (D.D.C. 2006).
⁷⁶ *Id.* at 7 n.4.
⁷⁷ D.C. CODE §15-109 and *Schwartz v. Schwartz*, 723 A.2d 841, 844–45 (D.C. 1998).
⁷⁸ *Schwartz*, 723 A.2d at 844–45.
⁷⁹ *Id.*; see also *Riss & Co. v. Feldman*, 79 A.2d 566 (D.C. Mun. App. 1951).
⁸⁰ *Columbia First Bank v. Ferguson*, 665 A.2d 650, 657 (D.C. 1995).
⁸¹ *Fred A. Smith Management Co. v. Cerpe*, 957 A.2d 907, 914 (D.C. 2008).
⁸² *Railan v. Katyal*, 766 A.2d 998, 1012 (D.C. 2001).
⁸³ *Krippen v. Ford Motor Co.*, 546 F.2d 993, 1002 (D.C. Cir. 1976).
⁸⁴ <http://mayor.dc.gov/release/district-columbia-publish-new-construction-codes>
⁸⁵ *Id.*

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I. MECHANIC'S LIEN BASICS

Mechanic's Liens (now known formally as Construction Liens) are permitted in Florida under a detailed statutory scheme detailed in Chapter 713, Florida Statutes (2013).

A. Requirements

Florida affords a wide range of persons and entities involved in the improvement of real property with the statutory remedy of a construction lien to protect their rights to payment. Protected parties under the statutory construction lien provisions include contractors; subcontractors; sub-subcontractors; laborers; materialmen who contract with the owner, a contractor, a subcontractor, or a sub-subcontractor; architects; landscape architects; interior designers; engineers; and surveyors and mappers.¹ Of special note, unlicensed contractors are not permitted to enforce their contracts or to obtain the benefits of a construction lien.²

The first critical procedural step under the law is the posting on the job site and recordation in the public records of a Notice of Commencement by the Owner. The Notice of Commencement includes, *inter alia*, the name and address of the Owner and it provides all persons who furnish labor or materials of the information necessary to transmit their Notices to Owner.³

To acquire a construction lien, lienors must carefully follow the procedural provisions of the construction lien laws, including the timely filing and service of the required notices.⁴ Parties who are in privity with the owner (except for a laborer or materialman in privity) must furnish a Contractor's Final Payment Affidavit before they can enforce their lien.⁵ That affidavit must recite that all subcontractors, suppliers and laborer are paid in full, or, if not, it must detail all persons who remain unpaid and the amounts owed to each. Parties who are not in privity (other than laborers) must serve a timely Notice to Owner (within 45 days from the lienor's first work or delivery of materials at the site) as a prerequisite to perfection of a construction lien.⁶ Design professionals are exempt from the notice to owner requirement.⁷

The scope of the security for a construction lien is heavily dependent upon the nature of the ownership interest of the person contracting for the improvements. If the property is held in fee simple ownership, the entire interest of the property owner will be subject to the construction lien.⁸ When property is owned in joint ownership or as a leasehold, the scope of the lien is usually commensurate with the rights and interests of the party contracting for the improvements.

If a lessee contracts for improvements, the lessor's interest will not be subject to the lien if (a) the lease contains language that prohibits lien liability and (b) the landlord records either a copy of the lease, a short form memorandum of the lease, or a notice in the public records of the county in which the property is located.⁹ Property held in trust is also subject to a construction lien.¹⁰

Construction liens are filed in the public records for the county in which the subject property is located.¹¹

A party who wishes to file a claim of lien may do so at any time during the progress of their work or furnishing of materials on the subject project.¹² All claims of lien must be recorded within ninety (90) days of the last date upon which the lienor furnished labor, services or materials to the owner.¹³ This "last date" does not include or relate to punchlist or warranty work.¹⁴

B. Enforcement and Foreclosure

Actions to foreclose a construction lien must be brought by the lienor within one (1) year of the recording of the construction lien (unless the owner records a Notice of Contest of Lien, which reduces the time for filing to sixty (60) days from the date on which the Clerk of Court certifies service of the Notice of Contest on the lienor).¹⁵ A prevailing lienor is entitled to recover pre-judgment interest and attorneys' fees, in addition to the amount of the lien.¹⁶ A prevailing owner can also be awarded attorneys' fees. To determine which party is the "prevailing party;" the trial court must determine whether either party to the litigation succeeded on any significant issues in the litigation and thereby achieved some of the benefits that such party sought by bringing or defending the suit.¹⁷

C. Ability to Waive and Limitations on Lien Rights

The construction lien statute makes it clear that the right to claim a lien may not be waived in advance.¹⁸ When waivers are requested during a job, lien rights may only be waived to the extent of labor, services or materials that have already been furnished.¹⁹ Any attempt to waive a lien in advance is unenforceable by statute.²⁰

II. STATUTES OF LIMITATION AND REPOSE

A. Statutes of Limitation and Limitations on Application of Statutes

Under Florida law, the Statute of Limitations for an action founded on the design, planning, or construction of an improvement to real property is four (4) years.²¹ The time will begin to run from the date of actual possession by the owner, the date of issuance of a certificate of occupancy, the date of abandonment of construction if not completed, or the date of completion or termination of the contract between the professional engineer, registered architect, or licensed contractor and his or her employer, whichever date is latest.²² If the action concerns a latent defect, the time will begin to run on the date when the defect is first discovered, or should have been discovered with the exercise of due diligence.²³ In some rare circumstances, claims against design professionals filed by parties in privity with those professionals will need to be brought within the shorter two (2) year statute of limitations applicable to professional

liability claims.²⁴ This occurs in the unusual situation when the claim is not founded upon the “design, planning or construction of an improvement to real property.”²⁵

Also of particular note; legal or equitable actions on a written contract are subject to a five (5) year statute of limitations;²⁶ tort actions (including fraud and negligence) and actions founded on an oral or implied contract are subject to a four (4) year statute of limitations;²⁷ wrongful death actions are subject to a two (2) year statute of limitations;²⁸ and actions for specific performance or to enforce equitable liens relating to improvements to real estate are subject to a one (1) year statute of limitations.²⁹

B. Statutes of Repose and Limitations on Application of Statutes

All actions founded upon the design, planning or construction of improvements to real property must be commenced within ten (10) years following the date of actual possession by the owner, the date of the issuance of a certificate of occupancy, the date of abandonment of construction if not completed, or the date of completion or termination of the contract between the professional engineer, registered architect or licensed contractor and his or her employer, whichever date is latest.³⁰

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

Florida has enacted statutory requirements for pre-suit notice and opportunities to cure for all residential construction defect claims.³¹ These requirements are intended to reduce the amount of litigation involving construction defects and apply to claims against contractors, subcontractors, suppliers, and design professionals.

Claimants are not authorized to file a construction defect lawsuit in Florida without first providing notice and opportunity to repair. If a claimant does file an action alleging a construction defect without first complying with the statute, then upon timely motion by a party to the action, the court shall stay the action, without prejudice, and the action shall not proceed until the claimant has fully complied with the statute.³²

At least sixty (60) days before filing a lawsuit alleging construction defects (or at least one hundred twenty (120) days before filing an action involving an association that represents more than twenty (20) parcels), the claimant shall serve a written notice of the claim on the contractor, subcontractor, supplier or design professional.³³ This notice of claim must describe the claim in reasonable detail sufficient to determine the general nature of each alleged construction defect and a description of the damage or loss resulting from the defect, if known.³⁴ The claimants shall endeavor to serve the notice of claim within fifteen (15) days after discovery of the alleged defect, although the untimely service of such notice of claim will not bar the filing of the action.³⁵

Within thirty (30) days after receipt of the notice of claim (or within 50 days after service of the notice of claim involving an association that represents more than twenty (20) parcels), the party receiving the notice is entitled to perform a reasonable inspection of the property or of each unit subject to the claim to assess the alleged construction defects. This inspection may even include destructive testing by mutual agreement and pursuant to the terms of the statute.³⁶

Within ten (10) days of receipt of the notice of claim, the party receiving the claim may forward a copy of the notice of claim to each contractor, subcontractor, supplier, or design professional whom it reasonably believes is responsible for each defect specified in the notice of claim and shall note the specific defect for which it believes the parties served are responsible. The parties receiving these forwarded notices are also entitled to access and inspections. The parties receiving notices of claims have statutory time periods within which to serve their own written responses to the claimant.³⁷

The service of the notice by the claimant tolls the applicable statute of limitations for specific periods of time detailed in the statute.³⁸ Persons served with the notice are to serve a written response which either (a) offers to remedy the alleged construction defect at no cost to the claimant, (b) offers to compromise and settle the claim by monetary payment that will not obligate the person's insurer, (c) offers to compromise and settle with a combination of repairs and monetary payment that will not obligate the person's insurer; (d) disputes the claim and rejects a remedy, compromise or settlement, or (e) states that a monetary payment including insurance payments will be determined by the person's insurer.³⁹ Claimants are given forty-five (45) days in which to accept or reject a proposed settlement offer.⁴⁰

IV. INSURANCE COVERAGE AND ALLOCATION ISSUES

A. General Coverage Issues

In Florida, insurance contracts are to be "construed in accordance with the plain language as bargained for by the parties."⁴¹ Insuring clauses in policies "are construed in the broadest possible manner to affect the greatest extent of coverage."⁴²

Any "ambiguities are interpreted liberally in favor of the insured and strictly against the insurer who prepared the policy."⁴³

One critical coverage issue that has been pretty well analyzed by the courts is what property damages for construction defects are covered under comprehensive general liability ("CGL") policies. In 2007, the Florida Supreme Court issued its decision in *U.S. Fire Insurance Co. v. J.S.U.B., Inc.*⁴⁴ In *J.S.U.B.*, the court was called upon to determine "whether a post-1986 standard form commercial general liability policy with products-completed operations hazard coverage, issued to a general contractor, provides coverage when a claim is made against the contractor for damage to the completed project caused by a subcontractor's defective work."⁴⁵

The *J.S.U.B.* court first ruled that a subcontractor's faulty workmanship would constitute an "occurrence" under the policy. The court then ruled that "faulty workmanship or defective work that has damaged the completed project has caused 'physical injury to tangible property' within the plain meaning of the definition in the policy."⁴⁶ "[i]f there is no damage beyond the faulty workmanship of defective work, then there may be no resulting 'property damage'."⁴⁷

The Florida Supreme Court further interpreted and applied the ruling in *J.S.U.B.* in its subsequent decision in *Auto-Owners Insurance Company v. Pozzi Window Company*.⁴⁸

The *Pozzi* case involved claims that water intrusion was occurring due to either defective windows or defective installation of windows. The court could not determine the ultimate

outcome in the case because it did not have a sufficient factual basis to apply the legal principles that it stated. The court ruled that “if the claim in this case is for the repair or replacement of windows that were defective both prior to installation and as installed, then that is merely a claim to replace a ‘defective component’ in the project”⁴⁹ and it is not covered because there would be no “property damage” under the policies. In contrast, “if the claim is for repair or replacement of windows that were not initially defective but were damaged by the defective installation, then there is physical injury to tangible property”⁵⁰ and the claim is covered.

B. Trigger of Coverage

While no definitive ruling has been made by the Florida Supreme Court as to trigger of coverage issue, the District Courts of Appeal and the federal courts have generally followed the manifestation trigger. There has, however, been some debate, particularly among the federal courts, as to what constitutes a manifestation. Is it when property damage was actually discovered by the insured? Or is it when the property damage would have been visible upon a prudent engineering investigation that might have included removal of building components that may have masked the damage? The latter view appears to be gaining acceptance,⁵¹ although these decisions are not binding upon the state courts.

C. Allocation Among Insurers

Allocations among insurers are ordinarily determined by applying the explicit terms of the relevant insurance policies. Florida “courts will not rewrite insurance policies, nor add meaning that is not present, or otherwise reach results contrary to the intentions of the parties.”⁵² “Where two or more policies of insurance each contain similar “other insurance” clauses whereby the insurers attempt to limit their liability for an insured’s loss covered by these policies, proration according to the policy limit is the proper method of determining the liability of the respective insurers.”⁵³

V. CONTRACTUAL INDEMNIFICATION

Under Florida law, any portion of an agreement or contract for construction, alteration, repair or demolition of a building or structure that contains a clause under which a party promises to indemnify and hold harmless the other party to the agreement for liability for damages to persons or property caused in whole or in part by any act, omission or default of the indemnity arising from the contract or its performance is void and unenforceable unless the contract contains a monetary limitation on the extent of the indemnification that bears a reasonable commercial relationship to the contract and is part of the project specifications or bid documents, if any.⁵⁴ This provision relates to contracts between an owner of real property and an architect, engineer, general contractor, subcontractor, sub-subcontractor, materialmen or any combination thereof.⁵⁵ The monetary limitation on the extent of the indemnification provided to the owner of real property by any party in privity of contract with the owner shall not be less than one million (\$1,000,000.00) dollars per occurrence, unless otherwise agreed by the parties.⁵⁶

Notwithstanding these limitations, if a design professional provides professional services to or for a public agency, that agency may require a professional services contract under which

the professional indemnifies and holds harmless the agency, and its officers and employees from liabilities, damages, losses, and costs, including but not limited to reasonable attorneys' fees, to the extent caused by the negligence, recklessness, or intentionally wrongful conduct of the design professional and other persons employed or utilized by the design professional in the performance of the contract.⁵⁷

VI. CONTINGENT PAYMENT AGREEMENTS

A. Enforceability

General contractors in Florida are permitted to include "pay when paid" clauses in their contracts with subcontractors, however, the contracts must clearly and unambiguously express this intention.⁵⁸

B. Requirements

Careful drafting of "pay when paid" clauses is necessary. For example, the Florida Supreme Court found a clause that stated that final payment would be made to a subcontractor "within 30 days after the completion of the work included in this subcontract, written acceptance by the architect and full payment therefore by the owner" to be ambiguous and unenforceable.⁵⁹ Likewise, a District Court of Appeals found a "pay when paid" clause that stated "Payments will be made for the value of the work installed each week within seven (7) business days after receipt of payment from the owner" to be ambiguous and unenforceable.⁶⁰

VII. DAMAGE LIMITATIONS

A. Personal Injury Damages vs. Construction Defect Damages

Generally, the damages recoverable for construction defects are the reasonable cost of construction and completion under the terms of the contract, unless such an award would constitute unreasonable or economic waste.⁶¹ When there would be economic waste, the damages will be the value that the product contracted for would have had if properly constructed less the value of the product that was actually delivered.⁶²

By way of contrast and comparison, personal injury plaintiffs who have proven liability will be entitled to recover an amount that will fairly and adequately compensate them for their injuries. This may include compensation for injury, pain, disability, disfigurement, loss of capacity for enjoyment of life, medical expenses (past and future), lost earnings and lost earning capacity. Spouses can recover loss of consortium and services. Parents can recover damages for their care and treatment of their minor child, loss of their child's services, earnings and earning capacity and loss of filial consortium.⁶³

B. Attorney's Fees Shifting and Limitations on Recovery

In Florida, Attorneys' Fees are generally only recoverable if that right is provided for in the contract being litigated or by statute. Among the many statutes providing for attorneys' fees are the frivolous lawsuit statute⁶⁴ and the statute authorizing the use of offers of judgment.⁶⁵ Florida also has a statute that provides that "[i]f a contract contains a provision allowing

attorney's fees to a party when he or she is required to take any action to enforce the contract, the court may also allow reasonable attorneys' fees to the other party when that party prevails in any action.⁶⁶

C. Consequential Damages

Consequential damages are recoverable in Florida, subject to the traditional limitations related to causation, foreseeability and certainty.⁶⁷ Plaintiffs who are seeking consequential damages must specifically include a reference to same in their complaint.⁶⁸

D. Delay and Disruption Damages

A party who establishes that he has been damaged as a result of delay occurring in a construction setting is entitled to recover damages for that delay.⁶⁹ The delay is measured by determining the loss that naturally and proximately results from the breach or that may have been reasonably within the contemplation of the parties to the contract at the time it was executed.⁷⁰ While no damages for delay clauses are generally enforceable in the State of Florida, they will not be enforced if a party fails to act in good faith, fails to engage in fair dealing, actively interferes with the project or actively impedes the ability of a performing party to perform under the contract.⁷¹ Delay damages will generally not be awarded if an agreement merely contains or sets forth an estimated time for completion of the improvements, or if the contract does not contain a clause making time of the essence in the performance of the agreement.⁷²

E. Economic Loss Doctrine

In 2013, the Florida Supreme Court issued a decision⁷³ that most observers regard as a significant retreat in the scope of the economic loss rule. The court set aside decades of case law expressing limitations and exceptions to the rule, and dramatically simplified the rule by declaring that the economic loss rule should only apply in cases involving defective products. Such cases were the genesis of the rule in Florida, and the court turned the clock back to that early and more restricted scope. At present, it remains to be seen whether this will have a serious impact on construction litigation. At a minimum, it would appear likely to make many more claims subject to insurance with a duty to defend.

In addition, the economic loss rule did not apply to negligence by professionals. Architects, engineers and surveyors are regarded as professionals by the Florida courts, and claims against them for professional negligence will not be barred by application of the rule.⁷⁴

F. Interest

Plaintiffs in Florida are generally entitled to recover prejudgment interest on contract claims. In rare instances, plaintiffs will even be able to recover prejudgment interest for non-contract cases if there was an ascertainable loss that occurred at a specific time prior to the entry of judgment.⁷⁵

Most Florida judgments accrue interest at the statutory rate set determined on December 1st of each year for the following year by the Chief Financial Officer for the State of Florida.⁷⁶ The rate is computed by averaging the discount rate of the Federal Reserve Bank of New York

for the preceding year, then adding five hundred (500) basis points to the averaged federal discount rate.⁷⁷ For the past two years through the first half of 2014, the applicable statutory interest rate has been 4.75 percent per annum. This same rate is also used for computing prejudgment interest.

G. Punitive Damages

Like most states, Florida has adopted tort reform measures. Section 768.72, Florida Statutes, now governs claims for punitive damages.

Pursuant to this statute, parties seeking punitive damages are not permitted to do so until there has been a reasonable evidentiary showing by the claimant that would provide a reasonable basis for recovery of punitive damages.⁷⁸ Punitive damages are awardable only if there is clear and convincing evidence that the defendant was guilty of intentional misconduct or gross negligence.⁷⁹ Under the statute, “intentional misconduct” means that the defendant had actual knowledge of the wrongfulness of the conduct and the high probability that injury or damage to the claimant would result and, despite that knowledge, intentionally pursued that course of conduct, resulting in injury or damage.⁸⁰ “Gross negligence” means that the defendants were so reckless or wanting and care that it constituted a conscious disregard or indifference to the life, safety, or rights of persons exposed to such conduct.⁸¹

Employers, principals, corporations and other legal entities are only liable for punitive damages if “intentional misconduct” or “gross negligence” has been shown, and a) the employer, principal, corporation or other legal entity actively and knowingly participated in such conduct; b) the officers, directors, or managers of the employer, principal, corporation, or other legal entity knowingly condoned, ratified, or consented to such conduct; or c) the employer, principal, corporation, or other legal entity engaged in conduct that constituted gross negligence and contributed to the loss, damages, or injury suffered by the claimant.⁸²

Florida also has specific caps and limitations on punitive damages.⁸³

VIII. CASE LAW AND LEGISLATION UPDATE

The newest significant change in Florida Construction Law was the enactment in 2013 of a statute that protects design professionals (defined as architects, interior designers, landscape architects, engineers, surveyors, or geologists) from individual or personal liability so long as: they contracted with their client in the name of a business entity (i.e., did not contract individually); include an express and prominent disclaimer of liability in the contract; and if their business entity maintains professional liability insurance. It remains to be seen how widely used this exemption will be, and whether it will eventually be expanded to licensed contractors and other regulated professions.⁸⁴

¹ Lienors are generally defined and described in §713.01(18) Florida Statutes (2013). Professional lienors, including design professionals, are defined in and authorized to file construction liens under §713.03, Florida Statutes (2013).

2 Section 489.128, Florida Statutes (2013).
3 Section 713.13, Florida Statutes (2013).
4 The procedural requirements for persons in privity with the owner are generally described in §713.05,
Florida Statutes (2013). The procedural requirements for persons not in privity with the owner are
generally described in §713.06, Florida Statutes (2013).
5 Section 713.05, Florida Statutes (2013). The requirements for the contractor's affidavit are set forth in
Section 713.06(3)(d), Florida Statutes (2013).
6 Section 713.06(2), Florida Statutes (2013).
7 Section 713.03(3), Florida Statutes (2013).
8 Section 713.01, Florida Statutes (2013).
9 Section 713.10, Florida Statutes (2013), as modified by Chapter 2011-212.
10 *Chapman v. St. Stephens Protestant Episcopal Church*, 105 Fla. 683, 136 So. 238 (1931).
11 Section 713.08(5), Florida Statutes (2013).
12 Section 713.08(5), Florida Statutes (2013).
13 *Id.*
14 Section 713.01(13), Florida Statutes (2013).
15 Section 713.22(1), Florida Statutes (2013).
16 Attorneys' fees are recoverable pursuant to §713.29, Florida Statutes (2013). Section 59.46, Florida
Statutes (2010) extends the right to recover attorneys' fees to appeals. Prejudgment interest is also
recoverable pursuant to case law. *Argonaut Ins. Co. v. May Plumbing Co.*, 474 So.2d 212, 214 (Fla. 1985);
17 *Encompass, Inc. v. Alford*, 444 So.2d 1085, 1087 (Fla. 1st DCA), review denied, 453 So.2d 43 (Fla. 1984).
18 *Trytek v. Gale Industries, Inc.*, 3 So.3d 1194 (Fla. 2009).
19 Section 713.20(2), Florida Statutes (2013).
20 *Id.*
21 *Id.*
22 Section 95.11(3)(c), Florida Statutes (2013).
23 *Id.*
24 *Id.*
25 Section 95.11(4)(a), Florida Statutes (2013).
26 *Id.*
27 95.11 (2)(b), Florida Statutes (2013).
28 95.11(3) Florida Statutes (2013).
29 95.11 (4)(d), Florida Statutes (2013).
30 95.11(5)(a) and (b), Florida Statutes (2013).
31 Section 95.11(3)(c), Florida Statutes (2013).
32 Section 558.001, Florida Statutes, *et seq.* (2013).
33 Section 558.003, Florida Statutes (2013).
34 Section 558.004(1), Florida Statutes (2013).
35 *Id.*
36 *Id.*
37 Section 558.004(2), Florida Statutes (2013).
38 Section 558.004(3), Florida Statutes (2013).
39 Section 558.004(10), Florida Statutes (2013).
40 Section 558.004(5), Florida Statutes (2013).
41 Section 558.004(7), Florida Statutes (2013).
42 *Westmoreland v. Lumbermens Mutual Casualty Co.*, 704 So.2d 176, 179 (Fla. 4th DCA 1997).
43 *Id.*
44 *Id.*
45 *U.S. Fire Ins. Co. v. J.S.U.B., Inc.*, 979 So.2d 871 (Fla. 2007).
46 *Id.* at 877
47 *Id.* at 889.
48 *Id.*
49 984 So.2d 1241 (Fla. 2010).
50 *Id.* at 1248-49.
Id. at 1249.

51 *Mid-Continent Cas. Co. v. Frank Casserino Constr. Ins.*, 721 F.Supp.2d 1209 (M.D.Fla. 2010); *United*
52 *Naional Ins. Co. v. Best Truss Co.*, No. 09-22897-CIV, 2010 WL 5014012 (S.D. Fla. 2010).
53 *Gulf Insurance Corporation v. Continental Casualty Company*, 464 So.2d 207, 209 (Fla. 3rd DCA 1985).
54 *Id.* at 209, 210
55 Section 725.06, Florida Statutes (2013).
56 *Id.*
57 *Id.*
58 Section 725.08, Florida Statutes (2013).
59 *DEC Electric, Inc. v. Raphael Construction Corp.* 53So.2d 427 (Fla. 4th DCA 1989), *Aff'd* 558 So.2d 427
60 (Fla. 1990).
61 *Peacock Const. Co., Inc. v. Modern Air Conditioning, Inc.*, 353 So.2d 840 (Fla. 1977).
62 *G.E.L. Recycling, Inc. v. Atlantic Environmental, Inc.*, 821 So.2d 431 (Fla. 5th DCA 2002).
63 *Gory Associated Industries, Inc. v. Jupiter Roofing & Sheet Metal, Inc.*, 358 So.2d 93 (Fla. 4th DCA 1978).
64 *Hampton-Chrysler-Plymouth-Dodge, Inc. v. White*, 448 So.2d 87 (Fla. 1st DCA 1984).
65 Section 501.1 and 501.2, Florida Standard Jury Instructions - Civil (2010).
66 Section 57.105(1), Florida Statutes (2013).
67 Section 768.79, Florida Statutes (2013).
68 Section 57.105(7), Florida Statutes (2013).
69 *Air Caledonie Intern. V. AAR Parts Trading, Inc.*, 315 F.Supp.2d 1319 (S.D. Fla. 2004).
70 Rule 1.120(g), Florida Rules of Civil Procedure.
71 *Tuttle/White Constructors, Inc. v. Montgomery Elevator Co.*, 385 So.2d 98 (Fla. 5th DCA 1980).
72 *Id.*
73 *Metropolitan Dade County v. Frank J. Rooney, Inc.*, 627 So.2d 1248 (Fla. 3rd DCA 1993).
74 *Caronte Enterprises, Inc. v. Berlin*, 668 So.2d 233 (Fla. 3rd DCA 1996); *American Somax Ventures v.*
75 *Touma*, 547 So.2d 1266 (Fla. 4th DCA 1989).
76 *Tiara Condo. Ass'n v. Marsh & McLennan Companies, Inc.*, 110 So3d 399 (Fla. 2013).
77 New Cases – Professional & Economic loss rule. *Estate of Rocks v. McLaughlin Engineering Company*,
78 49 So.2d 823 (Fla. 4th DCA 2010).
79 *Watkins Motor Lines, Inc. v. Underwriters at Interest, at Lloyds*, 892 So.2d 1143 (Fla. 3rd DCA 2005).
80 Section 687.01, Florida Statutes (2013).
81 *Id.*
82 Section 768.72(1), Florida Statutes (2013).
83 Section 768.72(2), Florida Statutes (2013).
84 Section 768.72(2)(a), Florida Statutes (2013).
85 Section 768.72(2)(b), Florida Statutes (2013).
86 Section 768.72(3), Florida Statutes (2013).
87 Section 768.73, Florida Statutes (2013).
88 Section 558.0035, Florida Statutes (2013).

GEORGIA

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MECHANICS' AND MATERIALMENS' LIEN BASICS

Georgia follows the rule that lien statutes, being in derogation of the common law, are strictly construed in favor of property owners.¹ Therefore, Georgia's lien statutes must be strictly followed.

Lien Requirements

In Georgia, in order to "make good" a lien, a lien claimant must comply with the following:

1. **Substantial compliance with the contract under which the lien is being claimed;**²
2. File a claim of lien in the superior court of the county in which the property is located within 90 days after completing the work or furnishing the material for which the lien is claimed;³
3. The face of the lien must include the following statement regarding its expiration, in 12 point bold font:

This claim of lien expires and is void 395 days from the date of filing of the claim of lien if no notice of commencement of lien action is filed in that time period;⁴

4. The lien must also include a notice to the owner of the property on which the claim of lien is filed that such owner has the right to contest the lien;⁵
5. The claim of lien shall be in substance as follows:

A.B., a mechanic, contractor, subcontractor, materialman, machinist, manufacturer, registered architect, registered forester, registered land surveyor, registered professional engineer, or other person (as the case may be) claims a lien in the amount of (specify the amount claimed) on the house, factory, mill, machinery, or railroad (as the case may be) and the premises or real estate on which it is erected or built, of C.D. (describing the houses, premises, real estate, or railroad), for satisfaction of a claim which became due on (specify the date the claim was due,

which is the same as the last date the labor, services, or materials were supplied to the premises) for building, repairing, improving, or furnishing material (or whatever the claim may be);⁶

6. No later than two business days after the claim of lien is filed of record, send a true and accurate copy of the claim of lien by registered or certified mail or statutory overnight delivery to the owner of the property or, if the owner's address cannot be found, the contractor, as the agent of the owner; provided, however, if the property owner is an entity on file with the Secretary of State's Corporations Division, sending a copy of the claim of lien to the entity's address or the registered agent's address shall satisfy this requirement;⁷
7. In all cases in which a notice of commencement is filed with the clerk of the superior court, send a copy of the claim of lien by registered or certified mail or statutory overnight delivery to the contractor at the address shown on the notice of commencement;⁸
8. Commence a lien action⁹ for recovery of the amount of the claim within 365 days from the date the lien was filed;¹⁰

Amount of Lien

In 2012, the Georgia Court of Appeals held that (1) overhead and administrative costs were not lienable, and (2) interest on the amount owed was not lienable.¹¹ In response, the Georgia legislature passed amendments to the lien statutes. Effective July 1, 2013 (a) the amount of a lien shall "include the amount due and owing the lien claimant under the terms of its express or implied contract, subcontract, or purchase order"¹² subject to a limitation that the aggregate amount of liens cannot exceed the contract price of the improvements made or services performed,¹³ and (b) a lien "shall include interest on the principal amount due in accordance with Georgia Code section 7-4-2 (legal rate of interest) or Georgia code section 7-4-16 (rate of interest on commercial accounts)."¹⁴ With respect to interest, see Section VII.D, *supra*.

9. Within 30 days after commencing the lien action for recovery of the amount of the lien, file a notice with the clerk of the superior court where the lien was filed, which notice must:
 - a. contain a caption referring to the then owner of the property against which the lien was filed and referring to a deed or other recorded instrument in the chain of title of the affected property;
 - b. be executed, under oath, by the party claiming the lien or by their attorney of record;
 - c. identify the court or arbitration venue wherein the lien action is brought; the style and number, if any, of the lien action, including the names of all parties thereto; the date of the filing of the lien action; and the book and page number of the records of the county wherein the subject lien is recorded;¹⁵ and
10. Pay the required filing fee for the lien.¹⁶

Enforcement and Foreclosure

Liens are enforced by filing a lien action within 365 days after the date the lien was filed.¹⁷ If a claimant's contract is with the owner, the lien action must be filed against the owner, but if not, the lien action must be filed against the contractor or subcontractor with which the claimant contracted¹⁸ before a lien may be foreclosed against the owner,¹⁹ except in the following circumstances: 1) the contractor or subcontractor has absconded, died, or left the state during the time required for filing a lien action such that personal jurisdiction cannot be obtained over such entity, or if the contractor or subcontractor has been adjudicated as bankrupt; or 2) after filing a lien action, no final judgment can be obtained against the contractor or subcontractor for the value of labor or materials provided, because the contractor or subcontractor dies, is adjudicated as bankrupt, or the contract between the claimant and the contractor or subcontractor includes a provision preventing payment to the claimant until after the contractor or subcontractor has received payment.²⁰ If the circumstances identified in the previous sentence exist, the claimant is relieved of filing a lien action or obtaining judgment against the contractor or subcontractor as a prerequisite to enforcing the lien against the property improved by the contractor or subcontractor, and the claimant may enforce the lien directly against the property improved in a lien action against the owner, as long as the lien action against the owner is filed within 365 days after the date the lien was filed. A judgment in an action against the owner is limited to a judgment in rem against the property improved.²¹

Despite the requirement that a claimant without a contract with the owner file a lien action against the contractor or subcontractor before foreclosing a lien against the owner, such claimant may file a complaint concurrently against the contractor or subcontractor and the owner of the property (if venue and jurisdiction are proper), claiming breach of contract against the contractor or subcontractor and seeking to foreclose the lien against the property.²²

A successful claim to foreclose a lien results in the court's judgment awarding a special lien to the claimant on the property.²³ Execution to satisfy the lien is by sale of the property in accordance with the requirements for a sheriff's sale.²⁴

Notice of Contest of Lien

An owner (or its agent or attorney) or a contractor (or its agent or attorney) may shorten the time in which to commence a lien action by recording in the superior court clerk's office a Notice of Contest of Lien, which must be in the form set forth in the statute and in boldface capital letters in at least 12 point font, along with proof of delivery upon the lien claimant.²⁵ A copy of the Notice of Contest must be sent to the lien claimant at the address noted on the face of the lien by registered or certified mail or statutory overnight delivery within seven (7) days of filing the Notice of Contest.²⁶ If the lien claimant fails to commence a lien action within 90 days after the filing of the Notice of Contest of Lien, the lien is extinguished.²⁷

Lien Waivers

Forms for an Interim Waiver and Release Upon Payment and a Waiver and Release Upon Final Payment are included in the statutes.²⁸ The forms must be substantially followed, and must be in

at least 12 point font.²⁹ Note that in Georgia, liens cannot be waived before labor, services, or materials are provided, and any such attempted waiver will be deemed null and void.³⁰

STATUTES OF LIMITATION AND REPOSE

Statute of Limitations

The statute of limitations for breach of contract claims on “simple contracts in writing,” such as construction contracts (including warranties), is six years.³¹ Georgia courts also recognize a claim for negligent construction, independently from a claim for breach of contract. Claims for negligent construction arise “from breach of a duty implied by law to perform the work in accordance with industry standards.”³² The statute of limitations for a negligent construction claim is four years.³³ The statute of limitations on breach of contract, negligent construction, and implied warranties begins to run at substantial completion.³⁴ The statute of limitations for a breach of express warranty to repair or replace defective workmanship, however, begins to run “from the date that the landowner notific[e]s the contractor of the alleged defects in construction.”³⁵

The discovery rule, i.e., that a claim does not arise until the injury is discovered, or through reasonable diligence should have been discovered, does not apply to contract cases,³⁶ and does not apply to negligent construction cases where the only injury is property damage.³⁷ A statute passed in the year 2000 specifically applies the discovery rule to the manufacture, negligent design, or negligent installation of synthetic exterior siding.³⁸

Statutes of Repose

There is an eight year statute of repose for any deficiency in the construction of an improvement to real property, which begins at substantial completion of the improvement.³⁹ An exception for wrongful death claims may extend the statute of repose to ten years.⁴⁰

PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

In 2004, the Georgia General Assembly enacted a statute requiring that, before litigation or arbitration is initiated, anyone who claims a construction defect in “a single-family house, duplex, or multifamily unit designed for residential use in which title to each individual residential unit is transferred to the owner under a condominium or cooperative system” must give the contractor notice and an opportunity to cure the defect through an alternative dispute resolution process.⁴¹ Although the statute is mandatory, the statute does not provide a penalty for failure to engage in the alternative dispute resolution process. A contractor may, however, stay any litigation filed and require compliance with the alternative dispute resolution process.⁴² A contractor must give explicit statutory notice to the owner upon entering a contract for sale, construction, or improvement of one of the aforementioned dwellings.⁴³ Neither the legislature nor the courts have given any guidance as to whether a contractor's failure to give the notice required by the statute prohibits the contractor from using the provision allowing it to stay litigation and require alternative dispute resolution.

INSURANCE COVERAGE

General Coverage Issues

A commercial general liability policy protects an insured contractor from tort liability for injury to persons or property but does not protect the insured from economic loss due to the insured's failure to properly complete a construction contract.⁴⁴ Thus, for example, where an insured negligently built a golf course on federally protected wetlands, the insured's policy did not cover economic damages incurred by the insured due to its breach of the contract for construction of the golf course, but it did cover tort damages incurred by the developer due to the insured's negligence in damaging the wetlands.⁴⁵

Trigger of Coverage

In 2012, the United States Court of Appeals for the Eleventh Circuit certified the following to the Georgia Supreme Court:

1. Whether, for an “occurrence” to exist under a standard CGL policy, Georgia law requires there to be damage to “other property,” that is, property other than the insured's completed work itself.
2. If the answer to Question One (1) is in the negative, whether, for an “occurrence” to exist under a standard CGL policy, Georgia law requires that the claims being defended not be for breach of contract, fraud, or breach of warranty from the failure to disclose material information.⁴⁶

The policy at issue in the case was a standard CGL policy that provided insurance for “bodily injury” or “property damage” caused by an “occurrence.”⁴⁷ The plaintiffs in the case, a class of 400 homeowners, alleged that the concrete foundations of their homes were improperly constructed, resulting in “water intrusion, cracks in floors and driveways, and warped and buckled flooring.”⁴⁸ The homebuilder’s insurance company filed a declaratory judgment action in federal court, asking the court to declare that there was no coverage under the insurer’s standard CGL policy.⁴⁹ The district court granted summary judgment to the insurer, finding, among other things, that there was no “occurrence” because the only “property damage” was to the work of the insured, i.e. the homes constructed by the homebuilder.⁵⁰ The homebuilder appealed, resulting in the certification of the questions to the Georgia Supreme Court.

Recognizing its holding two years prior that “an occurrence can arise where faulty workmanship causes unforeseen or unexpected damage to other property,”⁵¹ the court turned to whether that holding applied where the only damage alleged was to work of the insured.⁵² The court found that the policy defined an “occurrence” as an “accident, including continuous or repeated exposure to substantially the same, general harmful conditions,” but the policy did not define “accident.”⁵³ Because the policy did not indicate that the term “accident” was used in an unusual and uncommon way, the court “attribute[d] to that term its usual and common meaning,” holding that in its usual and common usage, the term “conveys information about the extent to which a happening is intended or expected,” and not information “about the nature or extent of injuries worked by such a happening, much less the identity of the person whose interests are injured.”⁵⁴ Therefore, the court answered the first certified question in the negative, holding that

that an “occurrence” “does not require damage to the property or work of someone other than an insured.”⁵⁵

Finding that the litigation at issue did not involve a claim of breach of contract, the court limited its review of the second certified question to fraud and breach of warranty claims.⁵⁶ The court held that, under Georgia law, fraud requires intent, and it therefore cannot be an “accident” and it therefore cannot be an “occurrence,” with the result that fraud claims are not covered by CGL policies under Georgia law.⁵⁷ The court held that a breach of warranty could be a result of faulty workmanship, which the court had already found to constitute an “occurrence,” and therefore the court held that a breach of warranty claim could be covered by a CGL policy under Georgia law, depending on the circumstances.⁵⁸

CONTRACTUAL INDEMNIFICATION

An agreement, made in connection with a contract for construction of a building, which seeks to indemnify the promisee against liability for damages to persons or property based on the promisee's own sole negligence is void as against public policy.⁵⁹ This rule does not hold true, however, “[w]here an insurance clause shifts the risk of loss to the insurance company, notwithstanding which party may be at fault.”⁶⁰ Nor does the rule apply when the promisee does not seek indemnification for its own negligence.⁶¹

CONTINGENT PAYMENT AGREEMENTS

Under Georgia law, “a provision in a contract may make payment by the owner a condition precedent to a subcontractor's right to payment if ‘the contract between the general contractor and the subcontractor should contain an express condition clearly showing that to be the intention of the parties.’”⁶²

DAMAGES LIMITATIONS

Attorneys' Fees

“The general rule is that expenses of litigation, including attorney's fees, are not recoverable by a litigant against the opposite party except in those cases which are specifically provided for by contract or by statute.”⁶³ The most common statutory provision for attorney's fees allows for recovery of attorney's fees where a defendant acted in bad faith, has been stubbornly litigious, or has caused the plaintiff unnecessary trouble and expense.⁶⁴ For an award of attorney's fees based on a defendant's bad faith, the bad faith “must relate to the acts in the transaction itself prior to the litigation.”⁶⁵ Neither refusal to pay a just debt nor mere negligence rise to the level of moral obliquity required to justify an award of attorney's fees for bad faith.⁶⁶ Attorney's fees for stubborn litigiousness and unnecessary trouble and expense may only be awarded where there is no bona fide dispute as to defendant's liability.⁶⁷ In addition, Georgia has a Prompt Pay Act,⁶⁸ pursuant to which the prevailing party is entitled to an award of reasonable attorney's fees.⁶⁹

Consequential Damages

“Damages recoverable for a breach of contract are such as arise naturally and according to the usual course of things from such breach and such as the parties contemplated, when the contract was made, as the probable result of its breach.”⁷⁰ “[R]emote or consequential damages are not recoverable unless they can be traced solely to the breach of the contract or unless they are capable of exact computation, such as the profits which are the immediate fruit of the contract, and are independent of any collateral enterprise entered into in contemplation of the contract.”⁷¹ Contracting parties may agree to exclude consequential damages from an award for breach of contract.⁷²

Economic Loss Doctrine

“The economic loss rule generally provides that a contracting party who suffers purely economic losses must seek his remedy in contract and not in tort.”⁷³ The economic loss rule does not apply to claims for negligent construction,⁷⁴ as long as the breach of duty results in damage to or defects in property in which the plaintiff has an interest.⁷⁵

Interest

Prejudgment interest is 7% per annum, unless otherwise established by written contract.⁷⁶ Contractual interest rates are subject to usury laws. Post judgment interest is “equal to the prime rate as published by the Board of Governors of the Federal Reserve System, as published in statistical release H. 15 or any publication that may supersede it, on the day the judgment is entered plus 3 percent.”⁷⁷ In a suit on a commercial account, the interest rate is 1-1/2 percent per month from the date upon which the amount owed became due and payable.⁷⁸ Georgia’s Prompt Pay Act provides for interest at a rate of one percent per month.⁷⁹

Punitive Damages

Punitive damages may not be awarded on claims for breach of contract.⁸⁰

LICENSING

Effective July 1, 2008, residential and general contractors must be licensed by the Georgia State Licensing Board For Residential and General Contractors.⁸¹

¹ *Roofing Supply of Atlanta, Inc. v. Forrest Homes, Inc.*, 632 S.E.2d 161, 163 (Ga. App. 2006).

² Ga. Code Ann. § 44-14-361.1(a)(1).

³ Ga. Code Ann. § 44-14-361.1(a)(2).

⁴ Ga. Code Ann. § 44-14-361.1(a)(2); Ga. Code Ann. § 44-14-367 (as amended effective March 31, 2009)..

⁵ Ga. Code Ann. § 44-14-361.1(a)(2).

⁶ *Id.*

⁷ *Id.*

⁸ *Id.*

⁹ A lien action is defined as “a lawsuit, proof of claim in a bankruptcy case, or a binding arbitration.” Ga. Code Ann. § 44-14-360(2.1).

¹⁰ Ga. Code Ann. § 44-14-361.1(a)(3).

¹¹ 182 *Tenth, LLC v. Manhattan Const. Co.*, 730 S.E.2d 495, 499-500 (Ga. App. 2012)

¹² Ga. Code Ann. § 44-14-361(c).

¹³ Ga. Code Ann. § 44-14-361.1(e).

¹⁴ Ga. Code Ann. § 44-14-361(d).

¹⁵ Ga. Code Ann. § 44-14-361.1(a)(3).

¹⁶ Ga. Code Ann. § 44-14-361.1(f).

¹⁷ See notes 9 and 10 and accompanying text.

¹⁸ *Cent. Atlanta Tractor Sales, Inc. v. Athena Development, LLC*, 657 S.E.2d 290, 293 n.5 (Ga. App. 2008).

¹⁹ *McDonough Const. Co. v. McLendon Elec. Co.*, 250 S.E.2d 424, 427 (Ga. 1978).

²⁰ Ga. Code Ann. § 44-14-361.1(a)(4).

²¹ *Id.*

²² *West Lumber Co. v. Aderhold*, 82 S.E.2d 670, 671 (Ga. App. 1954).

²³ Ga. Code Ann. § 44-14-530(a).

²⁴ See *Trust Co. of New Jersey v. Atlanta Aluminum Co.*, 255 S.E.2d 82, 83 (Ga. App. 1979); Ga. Code Ann. § 9-13-161.

²⁵ Ga. Code Ann. § 44-14-368(a).

²⁶ Ga. Code Ann. § 44-14-368(b).

²⁷ Ga. Code Ann. § 44-14-368(c).

²⁸ Ga. Code Ann. § 44-14-366.

²⁹ *Id.*

³⁰ *Id.*

³¹ Ga. Code Ann. § 9-3-24; see also *Feinour v. Ricker Co.*, 566 S.E.2d 396, 397 (Ga. App. 2002) (“We have repeatedly held that the six-year statute of limitation set out in OCGA § 9-3-24 applies to contract claims (whether breach of implied warranty, breach of express warranty, or breach of sale/construction contract)”).

³² *Young v. Oak Leaf Builders, Inc.*, 626 S.E.2d 240, 244 (Ga. App. 2006).

³³ Ga. Code Ann. § 9-3-30(a). Note, however, that “[g]enerally, once a property developer or home builder has sold property to another, it is not liable for damages resulting from negligent construction that could have been discovered through reasonable inspection, even if the negligent construction violated building codes, unless the developer or builder fraudulently concealed the negligence.” *Brazier v. Phoenix Group Management*, 633 S.E.2d 354, 359 (Ga. App. 2006).

³⁴ “With regard to tort claims and claims for breach of implied warranty and breach of the sale/construction contract, we have held that the applicable statutes of limitation begin to run on the date of substantial completion”

Feinour, 566 S.E.2d at 397.

³⁵ *Feinour*, 566 S.E.2d at 398.

³⁶ “The discovery rule ha[s] no application to a case in which a breach of contract is alleged” *Owen v. Mobley Const. Co., Inc.*, 320 S.E.2d 255, 256 (Ga. App. 1984).

³⁷ “The discovery rule is confined to cases of bodily injury and does not apply to actions seeking recovery for property damage only.” *Stamschror v. Allstate Ins. Co.*, 600 S.E.2d 751, 752 (Ga. App. 2004).

³⁸ Ga. Code Ann. § 9-3-30(b).

³⁹ Ga. Code Ann. § 9-3-51.

⁴⁰ *Id.*

⁴¹ Ga. Code Ann. § 8-2-36. The statute contains a convoluted process of notice of claim, possible inspection, offers to settle, acceptance or rejection, and possible counteroffers.

⁴² Ga. Code Ann. § 8-2-37.

⁴³ Ga. Code Ann. § 8-2-41.

⁴⁴ While it may be true that the same neglectful craftsmanship can be the cause of both a business expense of repair and a loss represented by damage to persons and property, the two consequences are vastly different in relation to sharing the cost of such risks as a matter of insurance underwriting.... The coverage applicable under the CGL policy is for tort liability for injury to persons and damage to other property and not for contractual liability of the insured for economic loss because the product or completed work is not that for which the damaged person bargained. *McDonald Const. Co., Inc. v. Bituminous Cas. Corp.*, 632 S.E.2d 420, 423 (Ga. App. 2006).

⁴⁵ *Glens Falls Ins. Co. v. Donmac Golf Shaping Co., Inc.*, 417 S.E.2d 197, 198 (Ga. App. 1992).

⁴⁶ *Taylor Morrison Servs., Inc. v. HDI-Gerling America Ins. Co.*, 746 S.E.2d 587, 588 (Ga. 2013). As used in the case, the court considered a standard CGL policy to be one “on standard ISO form CG 00 01 10 93” or “another standard form that is identical in all material respects.” *Id.*

⁴⁷ *Id.* at 589.

⁴⁸ *Id.*

⁴⁹ *Id.*

⁵⁰ *Id.*

⁵¹ *Am. Empire Surplus Lines Ins. Co. v. Hathaway Dev. Co.*, 707 S.E.2d 369, 372 (Ga. 2011).

⁵² *Taylor Morrison Servs., Inc.*, 746 S.E.2d at 590.

⁵³ *Id.* at 590-91.

⁵⁴ *Id.* at 591.

⁵⁵ *Id.* at 590-91.

⁵⁶ *Id.* at 588 n. 2 and 594 n. 14.

⁵⁷ *Id.* at 594-95.

⁵⁸ *Id.* at 595.

⁵⁹ Ga. Code Ann. § 13-8-2.

⁶⁰ *Great Atlantic & Pacific Tea Co., Inc. v. F.S. Associates, L.P.*, 571 S.E.2d 527, 528 (Ga. App. 2002).

⁶¹ *Buffington v. Sasser*, 363 S.E.2d 2, 6 (Ga. App. 1988). In *Buffington*, the indemnitor contended “that the indemnity clause contained in the termination agreement contravenes public policy and is unenforceable,” relying on Ga. Code Ann. § 3-8-2(b). The court found that “the indemnity clause at issue” only purported to “indemnify and save harmless [indemnitee] from any and all liabilities and responsibility arising out of the subcontracts....,” and did “not expressly apply to damage caused by [indemnitee’s] own negligence”

⁶² *Sasser & Co. v. Griffin*, 210 S.E.2d 34, 39 (Ga. App. 1974); *St. Paul Fire & Marine Ins. Co. v. Georgia Interstate Elec. Co.*, 370 S.E.2d 829, 831 (Ga. App. 1988).

⁶³ *Arbor Station Homeowners Servs., Inc. v. Dorman*, 567 S.E.2d 102, 104 (Ga. App. 2002).

⁶⁴ Ga. Code Ann. § 13-6-11.

⁶⁵ *Lay Bros., Inc. v. Golden Pantry Food Stores, Inc.*, 616 S.E.2d 160, 166 (Ga. App. 2005).

⁶⁶ *Beacon Indus., Inc. v. Vanderbunt Concrete, Ltd.*, 323 S.E.2d 871, 874 (Ga. App. 1984) (“The mere failure of a defendant to pay a claim does not constitute bad faith.”); *Rapid Group, Inc. v. Yellow Cab of Columbus, Inc.*, 557 S.E.2d 420, 426 (Ga. App. 2001) (“Bad faith is not simply bad judgment or negligence, but it imports a dishonest purpose or some moral obliquity, and implies conscious doing of wrong, and means breach of known duty through some motive of interest or ill will.”) (citations and quotations omitted).

⁶⁷ *Steel Magnolias Realty, LLC v. Bleakley*, 622 S.E.2d 481, 483 (Ga. App. 2005) (“A recovery of attorney fees under OCGA § 13-6-11 for stubborn litigiousness or for causing the plaintiff unnecessary trouble and expense is authorized where the evidence reveals no bona fide controversy or dispute with regard to the defendant’s liability.”)

⁶⁸ Ga. Code Ann. §§ 13-11-1 through 13-11-11.

⁶⁹ Ga. Code Ann. § 13-11-8.

⁷⁰ Ga. Code Ann. § 13-6-2.

⁷¹ *Esprit Log and Timber Frame Homes, Inc. v. Wilcox*, 691 S.E.2d 344, 347 (Ga. App. 2010) (quoting Ga. Code Ann. § 13-6-8).

⁷² *Am. Car Rentals, Inc. v. Walden Leasing, Inc.*, 469 S.E.2d 431, 433 (Ga. App. 1996) (“A clause excluding the recovery for consequential damages is valid and enforceable, unless prohibited by statute or public policy.”)

⁷³ *General Elec. Co. v. Lowe’s Home Centers, Inc.*, 608 S.E.2d 636, 637 (Ga. 2005).

⁷⁴ *Rowe v. Akin & Flanders, Inc.*, 525 S.E.2d 123, 126 (Ga. App. 1999).

⁷⁵ *City of Atlanta v. Benator*, 714 S.E.2d 109, 116-17 (Ga. App. 2011).

⁷⁶ Ga. Code Ann. § 7-4-2.

⁷⁷ Ga. Code Ann. § 7-4-12.

⁷⁸ Ga. Code Ann. § 7-4-16.

⁷⁹ Ga. Code Ann. § 13-11-7.

⁸⁰ *Trust Co. Bank v. Citizens & Southern Trust Co.*, 390 S.E.2d 589, 592 (Ga. 1990) (citing O.C.G.A. §§ 13-6-10 & 51-12-5.1).

⁸¹ Ga. Code Ann. §§ 43-41-1 through 43-41-17.

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I. MECHANIC LIEN BASICS

A. Idaho Code § 45-501 *et seq.* -Liens of Mechanics and Materialmen

Essentially every person who provides professional services, labor, material, equipment or otherwise improves real property, or improvements situated thereon, may record a lien against the real property to secure due and owing payment. Idaho law provides lien rights regardless of the nature of the project; that is, commercial or residential. Idaho Code § 45-501 *et seq.* The well-established rule in Idaho is that materialman lien statutes are to be liberally construed so as to effect their objects and to promote justice. *Barber v. Honorof*, 116 Idaho 767, 768, 780 P.2d 89, 90 (1989). These liens are creatures of statute and as such, require *substantial* compliance with the statute. *Id.*

“Statutes such as the Idaho provision which permit a lien for materials furnished usually apply only to furnishing for building purposes, and do not include a furnishing for general or unknown purposes ... or on a general open account.’ The ‘open account defense’ is applicable ‘in situations when a person furnishing materials relies exclusively on the general credit of the purchaser, and does not look to the land, structure or building as additional security for the materials sold on credit.’ In such a case, the materialman is not entitled to a lien. In addition, the lien statutes do not apply to ‘a sale without any reference as to what shall be done with the material sold.’ So, to secure the protection of a mechanic’s lien law, ‘[m]aterials must be furnished with special reference to their use in a particular building.’ Therefore, ‘a mere furnishing for building purposes generally is not sufficient.’ As a result, ‘if a materialman sells his materials without any understanding as to their application the materialman can assert no lien upon the building upon which the materials may, in fact, be used.’ However, ‘[w]here materials are furnished for use in a particular building, the fact that the materialman looks first or primarily to the contractor for payment and only subsequently to the building for security, would not of itself defeat the lien.’

¹ The information set forth herein is not intended as legal advice and is not to be relied upon for any purpose other than reference to relevant law. An Idaho attorney should be consulted before providing or relying on any information set forth herein.

BMC West Corp. v. Horkley, 144 Idaho 890, 894, 174 P.3d 399, 403 (2007) (internal citations omitted).

B. Time to File Lien

Any party claiming a mechanics lien must file a claim of lien within ninety (90) days after "the completion of labor or services, or the furnishing of materials." *Id.* at § 45-507(2). Trivial work done, or materials furnished, after the contract was materially completed will not extend the time in which the lien must be filed. *Franklin Bldg. Supply Co. v. Sumpter*, 87 P.3d 955 (2004) (discussing numerous cases involving attempts to provide additional work and revive untimely lien).

C. Place of Filing

The claim for lien must be filed with the county recorder for the county in which the property, or some part it, is situated. I.C. § 45-507(1).

D. Claim of Lien Contents

The claim must contain:

- (a) A statement of his demand, after deducting all just credits and offsets;
- (b) The name of the owner, or reputed owner, if known;
- (c) The name of the person by whom he was employed or to whom he furnished the materials; and
- (d) A description of the property to be charged with the lien, sufficient for identification.

I.C. § 45-507(3)(a)-(d). The claim must also be verified by the oath of the claimant, his agent or attorney, that he or she believes the same to be just. I.C. § 45-507(4). Idaho Courts have held that the purpose of the requirement that a claim of mechanics lien be verified to the effect that the claimant believes the same to be just is a desire to frustrate the filing of frivolous claims. *See ParkWest Homes LLC v. Barnson*, 238 P.3d 203, (2010). Also, a builder's statement in claim of lien that "I have read said mechanics' lien and [know] the contents thereof," and that "the same is true to my knowledge," did not render mechanics' lien invalid for builder's failure to state that he believed claim to be "just". *Id.* at 149.

"A verification is a formal declaration made in the presence of an authorized officer, such as a notary public. An acknowledgement is not a verification by oath. Thus, for verification of a claim of lien to be valid, it must state that the person signing the lien was first sworn by a person authorized to administer oaths, such as a notary public. If the notary public or other person authorized to administer oaths does not specifically certify in the claim of lien that the claimant was first sworn before him or her, the lien fails to comply with the verification requirement of I.C. § 45-507(4) and is therefore void."

Allied General Fire and Sec., Inc. v. St. Luke's Regional Medical Center, 2014 WL 1778267 (Idaho Ct. App. 2014) (internal citations omitted).

E. Notice of Lien Claim

Within five (5) business days of the filing of the claim, the claimant must serve a true and correct copy of the claim of lien on the owner or reputed owner of the property. Service may be accomplished by personal service or by certified mail to the last known address. I.C. § 45-507(5).

F. Foreclosure of Lien

Within six (6) months of recording the lien, the claimant must initiate judicial proceedings to enforce the lien. I.C. § 45-510. Where payment on account is made or an extension of credit is given with an expiration date, the lien is valid six months (6) after the date of such payment or expiration of extension; provided that the payment to credit and expiration date is endorsed on the record of lien. *Id.*

G. Lien Priority

Idaho Code § 45–506 governs the priority between a mechanics lien and a mortgage. It provides:

The liens provided for in this chapter shall be on equal footing with those liens within the same class of liens, without reference to the date of the filing of the lien claim or claims and are preferred to any lien, mortgage or other encumbrance, which may have attached subsequent to the time when the building, improvement or structure was commenced, work done, equipment, materials or fixtures were rented or leased, or materials or professional services were commenced to be furnished; also to any lien, mortgage, or other encumbrance of which the lienholder had no notice, and which was unrecorded at the time the building, improvement or structure was commenced, work done, equipment, materials or fixtures were rented or leased, or materials or professional services were commenced to be furnished.

I.C. § 45–506. The Court has interpreted this provision to mean “that the lien claimant could be given priority when either the building, improvement or structure was commenced, some entity or individual began to work on the building, improvement or structure, or when the materials or professional services were first furnished.” *Ultrawall, Inc. v. Washington Mut. Bank, FSB*, 135 Idaho 832, 835, 25 P.3d 855, 858 (2001). In sum, “whichever of these events occurred first would determine the priority for all liens as against a mortgage lien holder.” *Id.*

A mechanic's lien generally “relates back to the date of commencement of the work or improvement of the commencement to furnish the material.” *White v. Const. Mining & Mill. Co.*, 56 Idaho 403, 420, 55 P.2d 152, 160 (1936). However, this rule is not without exception. In *Terra–West*, this Court explained that “[c]entral to our analysis [in *White*] was the fact that all of the work claimed under the mechanic's lien was completed pursuant to one continuous employment contract, and therefore, the lien attached at the time the work began and encompassed all work subsequently done under the contract.” *Terra–West*, 150 Idaho 393, 400, 247 P.3d 620, 627 (2010). This Court went on to hold: “so long as a lien is filed within ninety days after the

completion of the labor or services, the lien may encompass the entirety of the work performed under the contract.” *Id.*

Credit Suisse AG v. Teufel Nursery, Inc., 321 P.3d 739, 748-49 (2014)

II. STATUTES OF LIMITATION AND REPOSE

A statute of limitation bars plaintiff from bringing an already accrued claim after a specific period of time. A statute of repose terminates a right of action after a specific time, even if the injury has not yet occurred.

A. Statute of Repose

Idaho has a statute of repose:

Actions will be deemed to have accrued and the statute of limitations shall begin to run as to actions against any person by reason of his having performed or furnished the design, planning, supervision or construction of an improvement to real property, as follows:

(a) Tort actions, if not previously accrued, shall accrue and the applicable limitation statute shall begin to run six (6) years after the final completion of construction of such an improvement.

(b) Contract actions shall accrue and the applicable limitation statute shall begin to run at the time of final completion of construction of such an improvement.

I.C. § 5-241(a)-(b). The statute of repose ensures that risk of liability has an end: no longer than eight years for tort claims, no longer than 4 years for oral contract claims, and no longer than five years for written contract claims. There is no discovery rule that supercedes the statute of repose. The one exception is that equitable estoppel can toll the statute of repose or statute of limitation if the party seeking to use those statutory time limits is guilty of some form of deceit that prevents the injured party from learning of the breach or tortious conduct or bringing a lawsuit within the time limits. *See Twin Falls Clinic & Hospital Bldg. Corp. v. Hamill*, 103 Idaho 19, 644 P.2d 341 (1982).

B. Statutes of Limitation

1. Written and Oral Contracts

An action upon any contract, obligation or liability founded upon an instrument in writing must be commenced within five years. I.C. § 5-216. An action upon a contract, obligation or liability not founded upon an instrument of writing must be commenced within four years. I. C. § 5-217.

2. Uniform Commercial Code (Sales)

The Idaho version of Article 2 the UCC provides:

(1) An action for breach of any contract for sale must be commenced within four (4) years after the cause of action has accrued. By the original

agreement the parties may reduce the period of limitation to not less than one (1) year but may not extend it.

(2) A cause of action accrues when the breach occurs, regardless of the aggrieved party's lack of knowledge of the breach. A breach of warranty occurs when tender of delivery is made, except that where a warranty explicitly extends to future performance of the goods and discovery of the breach must await the time of such performance the cause of action accrues when the breach is or should have been discovered.

(3) Where an action commenced within the time limited by subsection (1) is so terminated as to leave available a remedy by another action for the same breach such other action may be commenced after the expiration of the time limited and within six (6) months after the termination of the first action unless the termination resulted from voluntary discontinuance or from dismissal for failure or neglect to prosecute.

(4) This section does not alter the law on tolling of the statute of limitations nor does it apply to causes of action which have accrued before this act becomes effective

Idaho Code§ 28-2-725.

3. Personal Injuries, Negligence, and Professional Malpractice

Generally, an action to recover damages for professional malpractice, or for an injury to the person, or for the death of one caused by the wrongful act or neglect of another, including any such action arising from breach of an implied warranty or implied covenant must be filed within two (2) years of the occurrence giving rise to the injury. I. C. § 5-219(4).

4. All Other Claims

To the extent the Idaho legislature has not identified a particular limitation period for an action for relief, such action must be commenced within four (4) years after the cause of shall have accrued. I.C. § 5-224

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

Idaho Code§ 6-2501 *et seq.* (Notice and Opportunity to Repair Act) requires a claimant to give the "construction professional" an opportunity to repair a construction defect before filing an "action". This section defines "action" as:

any civil lawsuit or action in contract or tort for damages or indemnity brought against a construction professional to assert a claim, whether by complaint, counterclaim or cross-claim, for damage or the loss of use of real or personal property caused by a defect in the construction of a residence or in the substantial remodel of a residence. "Action" does not include any civil action in tort alleging personal injury or wrongful death to a person or persons resulting from a construction defect.

I. C. § 6-2502(1). If a claimant files an action without giving notice and an opportunity to repair to the construction professional, then the statute allows the construction professional to dismiss, *without* prejudice, the claimant's suit. Idaho's Notice and Opportunity to Repair Act does not apply to commercial construction. Rather, this section applies only to "a homeowner or association that asserts a claim against a construction professional concerning a defect in the construction of a residence or in the substantial remodel of a residence." I.C. § 6-2502(3).

IV. INSURANCE COVERAGE AND ALLOCATION ISSUES

A. General Coverage Issues

Standard commercial general liability insurance policies may provide coverage for liability related to property damage that occurs during the applicable policy period. *See Millers Mut. Fire Ins. Co. of Texas v. Ed Bailey, Inc.*, 103 Idaho 377, 647 P.2d 1249 (1982).

B. Trigger of Coverage

To determine whether a particular claim for property damage arises under a particular policy, Idaho courts apply the rule that an "accident" or "occurrence," unless defined otherwise in the policy, is not the time the wrongful act was committed but the time the complaining party was actually damaged. *Id.*

C. Allocation Among Insurers

When losses are less than combined limits of all applicable policies, and in cases of concurrent coverage, losses should be allocated pro rate in proportion to amount of insurance provided by respective parties. *Empire Fire and Marine Ins. Co. v. North Pacific Ins. Co.* 127 Idaho 716 (1995) There is no repugnancy in arbitrarily selecting one insurer over the other for payment, so long as the rule is chosen and uniformly invoked the risk can be allocated actuarially by the insurance companies.

V. CONTRACTUAL INDEMNIFICATION

Any covenant, promise, agreement or related matter that is in connection with or collateral to, a contract or agreement that relates to construction, maintenance, or repair of a building, structure, highway or anything similar that purports to indemnify the promisee against liability for damages arising out of bodily injury to persons or property damage caused by or resulting from the sole negligence of the promisee, his agents or employees is against public policy and is void and unenforceable. I.C. § 29-114. However, if an indemnitor is seeking indemnity for other people's negligence, Idaho courts will likely uphold a contractual indemnification clause. In *Beitzel v. City of Couer d'Alene*², a telephone company was contracted with an asphalt company and a digging company after it was issued a permit to install underground phone lines by the city. The plaintiff, unrelated to the project, was seriously injured when his motorcycle fell into the unmarked ditch at night. The plaintiff was found to not be negligence, while the city (35%), telephone company (30%), contractor (25%), and asphalt company (10%) all shared varying degrees of liability. There was a

² *See Beitzel v. City of Couer d' Alene*, 121 Idaho 709, 827 P.2d 1160 (1992)

provision in the contract between the telephone company and the contractor which provided that the contractor would indemnify the telephone for any damages for personal injuries resulting from the project work or caused by his employees or agents, but precluded any indemnification for damages caused solely by the negligence of the telephone company. The Idaho Supreme Court held that this indemnification clause was valid and enforceable and required the contractor to indemnify the telephone company.

VI. CONTINGENT PAYMENT AGREEMENTS

Contingent payment agreements (“pay-if-paid” or “pay-when-paid”) have not been explicitly dealt with by Idaho Courts. The validity and enforceability of contingent payment clauses, while not addressed in Idaho, has been addressed in other states. *See, e.g., Evans, Mechwart, Hambleton & Tilton, Inc. v. Triad Architects, Ltd.*, 965 N.E.2d 1007, 1010-18 (Ohio Ct. App. 10 Dist. 2011) (containing extensive string-cites of cases discussing the issues)

How an Idaho Court would decide on such an issue is difficult to predict, but it is likely that if such a clause were drafted so as to preclude a right of recovery by a subcontractor who had actually performed work on a project and was indisputably entitled to compensation, the Idaho courts would not enforce such a provision. While Idaho would likely frown upon a "pay-if-paid" contingent payment agreement, a "pay-when-paid" contingent agreement would likely be followed in Idaho because it creates less risk of unconscionability or impermissible forfeiture. To be safe, the subcontractor and their counsel should seek to add provisions to their payment clauses that clarify that the general contractor is not relieved from the ultimate obligation of payment to the subcontractor, despite the owner's failure to remit payment to the contractor. The subcontractor should also require that a schedule of payment dues be included in the contract so that it is clear that it is entitled to payments on periodic dates consistent with the time within each stage of the subcontractor's work that is completed. *Id.*

VII. DAMAGES LIMITATIONS

A. Personal Injury Damages vs. Construction Defect Damages

Idaho has statutory limitations on damages that can be awarded when the injured party dies “from causes not related to the wrongful act or negligence”: “the damages that may be recovered in such action are expressly limited to those for: (i) medical expenses actually incurred, (ii) other out-of-pocket expenses actually incurred, and (iii) loss of earnings actually suffered, prior to the death of such injured person and as a result of the wrongful act or negligence.” I.C. § 5-327(2).

In Idaho, under the Notice and Opportunity to Repair Act that applies only to residential construction, the claimant may recover only the following damages proximately caused by a construction defect: (1) the reasonable cost of repairs necessary to cure any construction defect, including any reasonable and necessary engineering or consulting fees required to evaluate and cure the construction defect, that the contractor is responsible for repairing under this chapter; (2) the reasonable expenses of temporary housing reasonably necessary during the repair period; (3) the reduction in market value, if any, to the extent that the reduction is due to structural failure; and (4) reasonable and necessary attorney's fees. If no offer is made by the construction professional, the limitations on damages and defenses to liability provided by the Idaho Code does not apply. I. C. § 6-2504.

B. Attorney's Fees Shifting and Limitations on Recovery

Idaho adopts the "American Rule" that holds that an award of attorney fees to the prevailing party is not allowed unless made pursuant to a contract provision or statute. There are several statutes that may allow for attorney fees to be recovered by the prevailing party in construction litigation. *See, e.g.*, I.C. §§ 12-120(3) (litigation regarding a "commercial transaction"), 12-121 (frivolous claims or defenses), 45-513 (mechanic liens), 12-117 (lawsuits involving governmental entity).

C. Consequential Damages and Lost Profits

"In Idaho, consequential damages are not recoverable unless they were contemplated by the parties at the time of contracting." *Strate v. Cambridge Telephone Co., Inc.*, 795 P.2d 319, 322 (Idaho Ct. App. 1990); *see also Brown's Tie & Lumber Co. v. Chicago Title*, 115 Idaho 56, 764 P.2d 423 (1988) ("Consequential damages need not be precisely and specifically foreseen; but they must have been reasonably foreseeable, and within the contemplation of the parties, when the contract was made."). Lost profits are generally not recoverable in contract unless there is something in that contract that suggests that they were within the contemplation of the parties and are proved with reasonable certainty. *Silver Creek Computers, Inc. v. Petra, Inc.*, 136 Idaho 879, 884-85, 42 P.3d 672, 677-78 (Idaho, 2002).

D. Delay and Disruption Damages

A party may recover actual damages caused by delay. *See City of Idaho Falls v. Beco Const. Co., Inc.*, 123 Idaho 516, 521-22, 850 P.2d 165, 170-71 (1993). A general contractor may recover from a subcontractor for delay under a liquidated damages clause. However, "a general contractor cannot recover from its subcontractor for delay under a liquidated damages clause where the general contractor contributed to the delay by failing to perform a contractual duty, such as failing to provide adequate equipment." *Seubert Excavators, Inc. v. Eucon Corp.*, 871 P.2d 826, 831 (1994); *see also Beco Const.*, 123 Idaho 516, 850 P.2d 165. If liquidated damages for delay cannot be recovered, then actual damages from the delay can be recovered instead. *Id.*

E. Economic Loss Doctrine

The economic loss rule prohibits recovery of purely economic losses in negligence actions. *Blaht v. Smith, Inc.*, 108 P.3d 996, 1000 (2005). Generally, a plaintiff may not recover in tort where the sole allegation is that the defendant prevented the plaintiff from gaining a purely economic advantage. *Id.* However, damage to person or property when the property is not the subject of the transaction is recoverable under a negligence theory. *Aardema v. U.S. Dairy Systems, Inc.*, 147 Idaho 785, 790, 215 P.3d 505, 510 (2009). Economic loss includes costs of repair and replacement of defective property which is the subject of the transaction, as well as commercial loss for inadequate value and consequent loss of profits for use. *See Salmon Rivers Sportsman Camps, Inc. v. Cessna Aircraft Co.*, 544 P.2d 305, 309 (1975). A party may recover "property damage" so long as the damage is not the subject of the transaction. It is the subject of the transaction that determines whether a loss is property damage or economic loss, not the status of the party being sued. *See Stapleton v. Jack Cushman Drilling and Pump Co. Inc.*, 153 Idaho 735, 742-43, 291 P.3d 418, 425-26 (2012)

F. Interest

Post-judgment interest: “The legal rate of interest on money due on the judgment of any competent court or tribunal shall be the rate of five percent (5%) plus the base rate in effect at the time of entry of the judgment. . . . The legal rate of interest as announced by the treasurer on July 1 of each year shall operate as the rate applying for the succeeding twelve (12) months to all judgments declared during such succeeding twelve (12) month period.” I. C. § 28-22-104 (2).

Pre-judgment interest: Is 12% “when there is no express contract in writing fixing a different rate of interest” and when the damages are liquidated or certain. I. C. § 28-22-104 (1).

G. Punitive Damages

Idaho Code § 6-1604 allows for punitive damages so long as a plaintiff can prove, “by clear and convincing evidence, oppressive, fraudulent, malicious or outrageous conduct by the party against whom the claim for punitive damages is asserted.” Punitive damages cannot be pled in initial complaint but must be added through motion to amend. *Id.* Award of punitive damages depends on whether the plaintiff is able to establish the requisite intersection of two factors: a bad act and a bad state of mind. *See, e.g., Hall v. Farmers Alliance Mut. Ins. Co.*, 145 Idaho 313, 319, 179 P.3d 276, 282 (Idaho,2008).

As amended in 2003, “no judgment for punitive damages shall exceed the greater of two hundred fifty thousand dollars (\$250,000) or an amount which is three (3) times the compensatory damages contained in such judgment.” I.C. § 6-1604(3). The limitations on non-economic damages are not applicable to punitive damages. *Id.*

Punitive damages are not available if a wrongdoer has died: “Causes of action arising out of injury to the person or property, or death, caused by the wrongful act or negligence of another, . . . shall not abate upon the death of the wrongdoer, and each injured person . . . shall have a cause of action against the personal representative of the wrongdoer; provided, however, the punitive damages or exemplary damages shall not be awarded nor penalties adjudged in any such action.” I.C. § 5-327(1).

H. Non-Economic Damages

Idaho Code § 6-1603 provides that “in no action seeking damages for personal injury, including death, shall a judgment for noneconomic damages be entered for a claimant exceeding the maximum amount of two hundred fifty thousand dollars (\$250,000).” *See also Carrillo v. Boise Tire Co., Inc.*, 152 Idaho 741, 751-52, 274 P.3d 1256, 1266-67 (2012). The cap adjusts annually and is currently approximately \$300,000. *Id.* This cap applies to “the sum of: (a) noneconomic damages sustained by a claimant who incurred personal injury or who is asserting a wrongful death; (b) noneconomic damages sustained by a claimant, regardless of the number of persons responsible for the damages or the number of actions filed.” The non-economic damage cap does not apply to “(a) Causes of action arising out of willful or reckless misconduct, (b) Causes of action arising out of an act or acts which the trier of fact finds beyond a reasonable doubt would constitute a felony under state or federal law.” *Id.*

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I. MECHANIC'S LIEN BASICS

The object and purpose of the Mechanics' Lien Act ("Act") is to protect those who, in good faith, furnish material or labor for the improvement of real property. The theory underlying the Act is that the owner is benefited by the improvements made to their property and should pay for that benefit when it has been induced or encouraged by the owners act. The Act permits a contractor to place a lien on property when the owner has received a benefit, and the furnishing of labor and materials have increased the value or improved the condition of the property.¹ The Act attempts to balance the rights and duties of owners, contractors, subcontractors, and material providers. The burden of proving that each requisite of the Act has been satisfied is on the party seeking to enforce the lien.²

The rights granted by the Mechanics Lien Act are creations of statute, not common law. A lien holder must therefore prove compliance with the Act's provisions to establish his right to the statutory remedy and cannot claim surprise when a defendant attempts to defeat his claim by proof of noncompliance.³ However, once the contractor or subcontractor has strictly complied with the requirements and the lien has properly attached, then the Act should be liberally construed to accomplish its remedial purpose.⁴

Illinois Compiled Statutes 770 ILCS 60/1 governs Mechanic's Liens. Section 1 of the Act allows, anyone who contracts with the owner or with one whom the owner has authorized or knowingly permitted to contract for purposes of improving the land, to file a lien. It also permits the filing of a lien by those who contract to manage a structure under construction. Others who constitute a contractor capable of filing and enforcing a lien under the Act include general contractors, architects, engineers, land surveyors, structural engineers, professional engineers and project managers. In *LaSalle Bank National Association v. Cypress Creek*, 242 Ill.2d 231 (2011), the Illinois Supreme Court treated LaSalle Bank, a lender, as a lien holder by effectively subrogating it to the value of improvements made to the subject property which were funded by LaSalle's construction loan to the owner. The Illinois legislature, however, effectively nullified that ruling and passed House Bill 3636 which amended Section 16 of the Act. The amendment

to Section 16, which became effective on February 11, 2013, impacts the distribution of sale proceeds when they are insufficient to satisfy the claims of both previous encumbrancers and lien creditors. The significant portion of the Amendment reads that “When the proceeds of a sale are insufficient to satisfy the claims of both previous encumbrancers and lien creditors, the proceeds of the sale shall be distributed as follows: (i) any previous encumbrancers shall have a paramount lien in the portion of the proceeds attributable to the value of the land at the time of making of the contract for improvements; and (ii) any lien creditors shall have a paramount lien in the portion of the proceeds attributable to the value of all subsequent improvements to the property.”⁵

The Contractors. *Original Contractor* – An original contractor has a contract with the owner or with one whom the owner has authorized or knowingly permitted to contract to improve the property. *Subcontractor* – A subcontractor is one who contracts with the original contractor.⁶

The Lien. There are four prerequisites for bringing a contractor's lien claim: (1) a valid contract; (2) with the owner of the property or his agent or someone who is knowingly permitted by the owner to contract for improvements; (3) for the furnishing of services or materials; and (4) performance of the contract or a valid excuse for nonperformance. A contractor who has met these prerequisites for bringing a claim for lien has merely acquired an inchoate right to a lien which must then be perfected in accordance with the requirements prescribed in the Mechanics Lien Act. A properly perfected mechanic's lien claim relates back to the date of the contract.

A. Requirements of Lien Claim

A claim for lien must: (1) be verified by the affidavit of the claimant, or his or her agent or employee;⁷ (2) shall consist of a brief statement of the claimant's contract, the balance due after allowing all credits; and (3) a sufficiently correct description of the lot, lots or tracts of land to identify the same.⁸ Such claim for lien may be filed at any time after the claimant's contract is made, and as to the owner may be filed at any time after the contract is made and within 2 years after the completion of the contract, and as to such owner may be amended at any time before the final judgment.⁹

B. Enforcement and Foreclosure

Contractors must record a claim for lien within 4 months of completion of the contract or within 4 months after furnishing any extra work or material thereunder. Contractors must also file suit to enforce the lien within 2 years after completion of the contract or within 2 years after furnishing any extra work or material thereunder.¹⁰ Contractors also have the option of filing suit within 4 months of contract completion. In order to have a valid lien, a contractor must have completed the lienable work within three years from the commencement of said work as to residential property; and within 5 years from the commencement of said work in the case of work done as to any other type of property.¹¹

Subcontractors must serve a written notice, on the owner – or its agent and on any mortgagees of record, notifying it of any work performed or to be performed on the property and the amount due or to become due thereunder, within 90 days after completion of the work. The

subcontractor must also file a claim for lien within four months of the last date of work performed and file suit within 2 years of that same date. Service of the 90-day notice is a condition precedent to the creation of the lien, so that no lien attaches when the owner does not receive timely written notice.¹²

a. 60 day Exception for Single Family Residence. The exception to this for *subcontractors* comes into play when work is being performed on an existing owner occupied single family residence. In that instance, notice must be given to the occupant within 60 days from the time that it first furnishes labor. The notice shall contain the name and address of the subcontractor or material man, the date he started to work or to deliver materials, the type of work done and to be done or the type of materials delivered and to be delivered, and the name of the contractor requesting the work. The notice shall also contain the following warning in at least 10 point bold face type:

“NOTICE TO OWNER - The subcontractor providing this notice has performed work for or delivered material to your home improvement contractor. These services or materials are being used in the improvements to your residence and entitle the subcontractor to file a lien against your residence if the services or materials are not paid for by your home improvement contractor. A lien waiver will be provided to your contractor when the subcontractor is paid, and you are urged to request this waiver from your contractor when paying for your home improvements.”

Such warning shall be by certified mail and will be considered served at the time of its mailing.

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Lien Foreclosure. If payment is not made to the contractor having a lien by virtue of this Act of any amount when it becomes due, then the contractor may bring suit to enforce his lien in the circuit court in the county where the property is located, as long as he does so within 2 years after contract completion. Any two or more persons having liens on the same property may join in bringing a suit, setting forth their respective rights in their complaint.

Notice of Foreclosure. A notice of foreclosure, whether the foreclosure is initiated by complaint or counterclaim, made in accordance with The Act and recorded in the county in which the mortgaged real estate is located shall be constructive notice of the pendency of the foreclosure to every person claiming an interest in or lien on the mortgaged real estate, whose interest or lien has not been recorded prior to the recording of such notice of foreclosure. (*Lis Pendens*).

Liens Against Public Funds. Any person who shall furnish labor, services, material, fixtures, apparatus or machinery, forms or form work to any contractor having a contract for public improvement for any county, township, school district, city, municipality, municipal corporation, or any other unit of local government in this State, shall have a lien for the value thereof on the money, bonds, or warrants due or to become due the contractor having a contract.¹⁴ No person shall have a lien as provided herein unless such person shall, before payment or delivery thereof is made to such contractor, notify the clerk or secretary, as the case may be, of the public entity by written notice of the claim for lien.¹⁵ The notice must contain a sworn statement identifying the claimant's contract, describing the work done by the claimant,

and stating the total amount due and unpaid as of the date of the notice for the work and furnish a copy of said notice at once to said contractor.¹⁶ Upon written demand from the contractor, the lien holder shall, within 30 days, notify the clerk or secretary of the public entity of his claim for a lien in the same manner provided for above. Failure to do so will result in forfeiture of the lien.¹⁷

The person claiming the lien against the public entity shall, within 90 days after serving such notice, commence proceedings by complaint for an accounting.¹⁸ In filing such a suit, the claimant must name, as a party defendant, the contractor who had a contract with the unit of local government and the contractor to whom such services and material was furnished.¹⁹ Within ten days after filing the complaint, the claimant must notify the clerk or secretary of the public entity of the commencement of such suit by delivering to him or them a copy of the complaint filed.²⁰ Failure to abide by these guidelines shall terminate the lien and result in forfeiture thereof.²¹

C. Ability to Waive and Limitation on Lien Rights

Owner's Ability to Limit Liability. Section 34 and 35 of The Act provide a procedure by which the owner of land can demand commencement of suit within 30 days. If a suit to enforce the lien is not commenced by the lien holder within 30 days, and the lien is not released upon subsequent demand, an owner can file suit to extinguish the lien. Failure to commence suit and/or release the lien after demand by the owner could subject the lien holder to financial liability of \$2,500 plus fees.²² When an owner of real estate sends a written demand pursuant to Section 34 of the Act, the owner making the demand is required to include the following language in at least 10 point bold face type: "Failure to respond to this notice within 30 days after receipt, as required by Section 34 of the Mechanics Lien Act 770 ILCS 60/34, shall result in the forfeiture of the referenced lien."

As an owner of property, you should never pay a contractor for services rendered thereon prior to receiving a sworn statement pursuant to section 5 of the Act. Section 5 of The Act requires Contractors to issue a sworn statement to the owner listing names and addresses of all parties furnishing materials and labor and the amounts due or to become due to each.²³

II. STATUTES OF LIMITATION AND REPOSE

The Illinois Code of Civil Procedure contains both a statute of limitations and a statute of repose for construction claims.²⁴ A construction claim includes actions based upon tort, contract or otherwise for an act or omission in the design, planning, supervision, observation or management of construction. An action must be commenced within 4 years from the time the plaintiff knew or should reasonably have known of the act or omission. No action can be brought after ten years from the act or omission. However, if discovery of the act or omission is made within 10 years from the date of the act or omission, the plaintiff shall in no event have less than 4 years to bring the action from the date of discovery. The statute also contains exceptions for minors, plaintiffs with disabilities, and cases involving fraudulent misrepresentation or concealment.

Actions against property owners premised on defendants' capacity as a property owner rather than a party engaged in construction related activity fall outside the scope of the construction statute of repose.²⁵ Furthermore even though a party receives the protection of a statute of repose for activity that falls within the purview of the statute, it does not receive protection for other activities outside of that purview.²⁶

The discovery rule requires the injured party to make further inquiry into the injury and its causes to determine whether actionable conduct is involved. Where there are both actionable and non-actionable explanations for an injury, the determination of whether the information available to the claimant was sufficient to meet the knowledge requirement is left to the trier of fact.²⁷

Personal injuries related to construction are subject to the four-year statute of limitations for construction claims rather than the general two-year statute of limitations for personal injuries.²⁸ But a claim for contribution or indemnity must be filed within two years after the party seeking such relief knew or should have known of the act or omission giving rise to the action for contribution or indemnity, but in no event later than two years after the party seeking such relief has been served with process in the underlying action.²⁹

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

The legal rights of the parties involved in a construction dispute are determined primarily by the terms of the contract into which they have entered. Two areas of contention that often arise are whether one party's breach of the contract discharges the other party from performing its own contractual obligations and under what circumstances an owner may rightfully terminate the contractor.

While a party may subject itself to liability by failing to perform its contractual duties, only a material breach of the contract's terms will serve to excuse the other party from performing its own obligations under the contract.³⁰ The determination of materiality is a question of fact involving an inquiry into the intent of the parties with respect to the disputed provisions as well as the equitable factors and circumstances surrounding the alleged breach.

Termination of a contractor must also be predicated on a material breach of the contract. The grounds and procedure for termination are dictated by the contract. The American Institute of Architects publishes the most widely used set of construction contracts in the industry.³¹ Pursuant to the AIA documents, two steps are required to justify termination under the contract. First, the architect must certify to the owner that sufficient cause exists to justify termination under the contract. Second, the owner may be required to serve several written notices of termination on the contractor and the surety.³² The contractor then must be given the opportunity to cure the defect within the time period specified in the contract, and the owner cannot obstruct, interfere, or otherwise impair the contractor's ability to correct the defect.³³ The compliance or violations of the notice and cure provisions will then determine the rights and obligations of the respective parties.

The growing national trend towards expansion of construction defect litigation has prompted some states to pass some version of a “right to repair” or “notice and opportunity” law. While these statutes vary from state to state, they typically allow for dismissal of a homeowner’s action if the homeowner has not provided the contractor with notice of the alleged defect, an opportunity to inspect the premises, and an opportunity to correct the defect or settle the claim. The American Legislative Exchange Council (ALEC) has drafted model legislation in this area.

Over the years similar legislation has been proposed in Illinois, but has not been enacted into law. House Bill 4873 which would have created the “Notice and Opportunity to Repair Act” was introduced in the 94th General Assembly (2005/2006), but was not enacted. More recently House Bill 1114, which would have created the “Notice and Opportunity to Repair Act,” was introduced in the 95th General Assembly (2007/2008), given a first reading and assigned to the Illinois House Judiciary I-Civil Law Committee and twice to the Rules Committee for further hearings, but was ultimately not enacted. The status of any proposed legislation may be monitored on the General Assembly website.³⁴ Should this, or similar legislation be re-introduced and become law, Illinois would require notice to the construction professional of a complained of defect in the construction by the homeowner prior to the commencement of a construction defect lawsuit.³⁵ The construction professional would then be given a period of time to inspect the alleged defect and/or dispute the claim or make an offer of repair or settlement.³⁶ The satisfaction or violation of this provision and others would then dictate the respective rights and obligations of the parties to the dispute.

At this time there is no similar legislation pending in the 97th (2011-2012) Illinois General Assembly.

IV. COVERAGE AND ALLOCATION ISSUES

A standard Commercial General Liability (“CGL”) policy typically provides coverage for those sums that the insured becomes legally obligated to pay as damages because of “bodily injury” or “property damage” to which the insurance applies. The insurance typically applies to “bodily injury” and “property damage” if: (1) the “bodily injury” or “property damage” is caused by an “occurrence” that takes place within the covered territory; and (2) the “bodily injury” or “property damage” occurs during the policy period.

Further, typical policy exclusions exclude from property damage coverage, damage to your “product” or damage to “your work.” Your work includes “work or operations performed by you or on your behalf and materials, parts or equipment furnished in connection with such work and operations.”

A. Key Cases in Property Damage, Construction Defect Cases. Under Illinois law, the aforementioned exclusions have been interpreted to indicate that GL policies are not intended to provide protection against the insured’s own faulty workmanship or product, which are normal risks associated with the conduct of the insured’s business.³⁷ A liability insurance policy is not intended to become a warranty or converted into a performance bond.³⁸

In addition, the use of the term "occurrence" instead of "accident" in insurance policies broadens coverage and eliminates the need to find an exact cause of the damages, so long as the damages are neither expected nor intended (that is, are accidental) from the standpoint of the insured.³⁹ An accident under Illinois law is defined as "an unforeseen occurrence, usually of an untoward or disastrous character, or a sudden or unexpected event of an inflictive or unfortunate character."⁴⁰ Property damage to a building caused by a contractor's defective construction of the building is not an accident and does not, therefore, constitute an occurrence under the CGL policy at issue.⁴¹

Accordingly, when a property damage case arises, it is imperative that a determination be made as to whether there has been an occurrence and whether there is property damage covered under the subject policy.

B. Insurance Coverage for Personal Injury Actions and Additional Insured Endorsements. Under the case of *John Burns Construction Co. v. Indiana Ins. Co.*,⁴² the Illinois Supreme Court recognized that an insured who is named as an additional insured on multiple insurance policies can select which policy or policies they wish to invoke coverage under to the exclusion of other policies on which they are named as an insured, thus allowing a "targeted tender." Accordingly, a contractor can tender the defense and insurance obligation to another contractor's insurance company if said contractor has been named as an additional insured. That insurer is then required to pick up the defense exclusively, and is not allowed to invoke any of the contractor's own insurance coverage to defend or indemnify the contractor in litigation.

Further, under what has been termed the "horizontal exhaustion rule," a contractor named as an additional insured on multiple policies has the right to stack the primary policies of coverage in the order it deems appropriate.⁴³ However, Illinois does not allow a contractor with multiple primary and excess policies to target an excess policy to respond prior to all primary policies being exhausted.⁴⁴

In the case of *North River Ins. Co. v. Grinnell Mutual Reinsurance Co.*,⁴⁵ the Illinois Appellate Court recognized that one that has multiple excess policies can target tender those excess policies and dictate the order of response after all applicable primary policies have been exhausted.⁴⁶

V. CONTRACTUAL INDEMNIFICATION

Illinois courts do not recognize indemnity agreements in construction contracts. Attempts at indemnification as among parties set forth in contracts for construction work are void in violation of the Illinois Construction Contract for Negligence Act, more commonly known as the Illinois Anti-Indemnity Act.⁴⁷ However, at the present time, having contract provisions that agree to provide *insurance coverage* for another party are acceptable and enforceable. See above.

Because almost all construction contracts, including AIA contracts, continue to contain indemnity provisions, Illinois courts have stated that these clauses were intended to bind the parties to unlimited contribution as among one another, and to act as a waiver on any potential cap on damages that might be afforded an employer by way of the Illinois Worker's

Compensation Act and *Kotecki v. Cyclops Welding Corp.*⁴⁸ The seminal Illinois Supreme Court cases on this topic are *Braye v. Archer-Daniel-Midland Co.* and *Liccardi v. Stolt Terminals*.⁴⁹

Thus, the indemnity language in a typical construction contract can expose an employer to unlimited contribution to the full extent that an employer is responsible for causing or contributing to cause an accident to his employee, without regard to the amount of money it is paid in worker's compensation benefits to that employee. These provisions have also been interpreted as valid agreements to provide defenses for parties in litigation. These indemnity agreements are often looked to in cases where an insurer has failed to assume a defense pursuant to a tender of defense, or to provide adequate coverage for protection of a named defendant. Accordingly, when a subcontractor employee sues another contractor, that contractor often files a contribution claim against the employer for unlimited contribution therein seeking to have the indemnification agreement contained within their contract interpreted as an express agreement to waive any limitation on the right of contribution against the employer.

Illinois courts have struggled to determine what insurance policy if any covers the employer's exposure over and above its workers compensation lien in situations where the employer waives its cap on contribution through an indemnity provision. In *Virginia Surety v. Northern Insurance Co.*, the Illinois Supreme Court interpreted a standard commercial general liability policy as well as a standard indemnity provision and held that the employer's CGL carrier did not owe a duty to defend or indemnify the employer for its exposure above its workers compensation lien.⁵⁰

VI. DAMAGES LIMITATIONS

A. Personal Injury Damages v. Construction Defect Damages

Where a contract has been breached, recoverable damages are those which (1) naturally result from the breach, or (2) are the consequence of special or unusual circumstances which were within the reasonable contemplation of the parties when making the contract.⁵¹

Most construction contracts today contain liability limiting provisions which would apply to various circumstances. For example, a Time-Is-Of-The-Essence Clause, a Damages-For-Delay-Clause, or a No-Damages-For Delay Clause operates to protect a party in the event of nonperformance, such as unforeseen circumstances or impractical occurrences. These provisions are strictly construed, and Illinois courts may recognize exceptions to them where the contractee is not acting in good faith, the delay is not within the contemplation of the parties, the delay is of unreasonable duration, or the delay is attributable to inexcusable ignorance or incompetence.⁵²

Costs or Diminution of Value. When a construction error or defect creates a need to repair or replace a portion or all of a constructed project, courts typically apply the "cost rule," which seeks to put the owner in the position that he would have occupied but for the error by compensating him for the cost of repair or replacement.⁵³ However, if the cost to repair or replace is disproportionate to the value of the building or otherwise excessive, the measure of damages will likely be the diminution in value of the property as a whole which was caused by the defect.⁵⁴

B. Attorney's Fees

Attorneys' fees are not recoverable unless specifically authorized by statute or contract.⁵⁵ Provisions for attorneys' fees are enforced at the discretion of the trial court, and the party requesting the fees bears the burden of providing evidence from which the circuit court can make a decision regarding the reasonableness of the fees.⁵⁶ The court is required to strictly construe a contractual provision for attorney fees.⁵⁷ If the contract does not specifically state the term "attorneys' fees" within it by name, the court will not allow recovery therefor.⁵⁸

C. Consequential Damages

Consequential damages may be recoverable in claims for a construction defect if they were within the contemplation of the parties at the time that the contract was entered into.⁵⁹ These may include excess costs, loss of use, costs to settle with owner for subcontractor's breach, or even lost profits or market share if proved with reasonable certainty.

D. Delay Damages. A contractor or subcontractor may recover delay damages where the owner or contractor fails to prepare the property for work in a timely manner. The plaintiff must prove with reasonable certainty that its loss was caused by the delay and the amount of damages suffered.⁶⁰

A contractor may recover increased-cost-of-performance damages resulting from delay caused by the contractee in the absence of a contractual provision to the contrary.⁶¹ Depending on the facts of the case, the court may apply the "total cost" method, which compares the total cost of performing the work with the amount the contractor originally estimated would be required for the project, or the "discrete" method, which considers at the damages due to the delay of specific items of work or periods of low work productivity.⁶²

E. Economic Loss Doctrine

The economic loss doctrine in Illinois precludes an owner from recovering on a negligence theory in its construction claim unless personal injury or damage to property not contemplated by the construction contract occurred as a result of the negligence alleged.⁶³

F. Interest

Under Illinois law, prejudgment interest is only recoverable on the basis of a contract or statute.⁶⁴ The Illinois Interest Act provides for prejudgment interest in eight different circumstances: for money after it becomes due on any (1) bond, (2) bill, (3) promissory note, or (4) other instrument of writing; (5) on money lent or advanced for the use of another; (6) on money due on the settlement of an account from the day of liquidating accounts between the parties and ascertaining the balance; (7) on money received to the use of another and retained without the owner's knowledge; and (8) on money withheld by unreasonable and vexatious delay of payment.⁶⁵ Parties may also contract for prejudgment interest in the event of a breach. This

interest provision must be reasonable, and the court will evaluate the provision to ensure it is compensatory and not punitive.⁶⁶

Post-judgment interest is more universally available; it will accrue on most judgments at nine percent per annum.⁶⁷ However, when the judgment debtor is a unit of local government, a school district, a community college district, or any other government entity, post-judgment interest will only accrue at six percent per annum.⁶⁸

G. Punitive Damages

Punitive damages are generally not recoverable for breach of contract unless the breach amounts to an independent tort which involves the requisite allegations and proof of malice, wantonness, or oppression.⁶⁹

VII. CONTINGENT PAYMENT AGREEMENTS

Contingent Payment Agreements, also known as “Pay-When-Paid” Agreements, are enforceable in Illinois.⁷⁰ However, they are the type of condition precedent Courts frown upon, and therefore will be looked at with scrutiny when challenged.

A. Enforceability

As indicated above, Illinois courts do recognize Pay-When-Paid provisions. Paid-When-Paid provisions are interpreted like all contract provisions in Illinois, and in determining the meaning of the contract, especially with respect to Pay-When-Paid provisions, a court must make every effort to effectuate the intentions of the parties.⁷¹ A court must arrive at meaning from language used in the contracts and if language in the contracts is clear and unambiguous no evidence outside of the contract itself may be considered in determining the contract’s meaning.⁷²

Construction of contractual terms is a pure question of law, and one need only look to the principles of construction and the contract itself to resolve disputes.⁷³

However, it is also well documented under Illinois law that conditions precedent in contracts are not favored by the courts, and contracts will not be construed as having condition precedents unless required to do so by plain, unambiguous language.⁷⁴

B. Requirements

Although Pay-When-Paid clauses are enforceable, and particularly, will be enforced if clear and unambiguous, it is equally true that the performance of a condition precedent is excused if the party for whose benefit the condition is created prevents the condition from occurring.⁷⁵ For example, where a contractor by its own fault has lost the right to payment from the owner, a subcontractor is entitled to compensation from that contractor. Further, the party for whose benefit a condition precedent runs must “use reasonable efforts to have it occur.”⁷⁶ In the *Marino* case, Marino entered into a contract with a local Village whereby Marino agreed to

construct a 4,000,000 gallon water storage reservoir. Marino hired Preload as a subcontractor. Preload agreed to furnish the pre-stressed concrete. Preload completed its work and submitted requests for payment. Marino refused to pay contending that it had not yet been paid by the Village. However, the Village's refusal to pay Marino was based upon the Village suing Marino for breach of contract. Further, the contract between the Village and Marino authorized the Village to recover liquidated damage for said breach and to refuse payment where it was entitled to a set off.⁷⁷ Wherefore, the United States District Court for the Northern District of Illinois, Eastern Division, held that Marino could not refuse payment to Preload based upon the "Pay-When-Paid" provision in its contract, where Marino itself had caused the failure of the Village to pay it.

The case of *Brown and Kerr, Incorporated v. St. Paul Fire & Marine Ins. Co.*,⁷⁸ cautioned that a surety cannot rely upon a subcontract agreement Pay-When-Paid clause to refuse payment on the surety bond, where the surety agreement does not incorporate the payment terms of the subcontract, nor include its own condition precedent to payment. The bond agreement and the subcontract agreement are two separate agreements and will be determined separately.⁷⁹

Finally, the case of *DeGraff Bros. Inc. v. Mellon Stuart Co.*,⁸⁰ the court found a Pay-When-Paid clause ambiguous and unenforceable, where the terms of the Pay-When-Paid clause did not dictate whether payment to subcontractors would come from the first installment payment it received, or only after the last, or based upon a *pro rata* share of the payments received.

In the *DeGraff* case, DeGraff brought an action against Mellon Stuart based upon a contract to perform work as a subcontractor to Mellon Stuart, the general. Mellon Stuart argued that it was not allocated to pay DeGraff's balance out of the first installment it received from the owner, but rather, because it had not received full payment for all of the work performed by its subcontractors, Mellon Stuart argued that the only equitable method for dividing the payments it received among its subcontractors was on a *pro rata* basis.

The *DeGraff* court found that the subcontract was ambiguous as to whether DeGraff was to receive its final payment out of the first installment, or to receive partial payments out of each installment and was unable to find any contingency provision within the contract to cover this situation. They, therefore, held that the contract was ambiguous, and reserved that question to be determined at trial.⁸¹

C. Conclusion

Although Pay-When-Paid clauses are enforceable, they are not favored, and as such, must be clear and unambiguous in order to assure enforcement of the terms intended.

VIII. SIGNIFICANT CASE LAW

Under Illinois law, litigation against construction companies is typically brought as a general negligence claim. However, under ordinary negligence, one who entrusts work to an

independent contractor is typically not responsible for the acts or omissions of that independent contractor when those acts or omissions result in injury or damages. Therefore, plaintiff's attorneys look to the Restatement Second of Torts Section 414 to circumvent that general rule and to impose liability upstream on the construction project to expose general contractors, owners and developers alike, to liability for acts of independent contractors. Section 414 of the Restatement Second of Torts states that:

“one who entrusts work to an independent contractor, but who retains the control of any part of the work, is subject to liability for physical harm to others or who's safety the employer owes a duty to exercise reasonable care, which is caused by its failure to exercise its control with reasonable care.”

Therefore, if the employer of the independent contractor retains any control over the operative details of any part of the independent contractor's work, the entity that employed that contractor is subject to liability as the master would be under the principles of agency. If the employer retains only supervisory control, i.e. the power to direct the order in which the work shall be done or to forbid that it be done in an improper or unsafe manner then the employer can be liable under Section 414 only if he fails to exercise his supervisory control with reasonable care so as to prevent the work which he has ordered to be done from causing injury to others.

One recent Illinois case, *Oshana v. FCL Builders*⁸², has found that where a fabricator contracted to fabricate and erect certain ironwork and subcontracted the ironwork erection portion to plaintiff's employer, the fabricator, who was never on site except to supply material to the job, had not exercised sufficient control over the safety of the erector's work so as to impose liability upon them under the 414 theory. Oshana was an employee of the steel erector who was allegedly injured when he fell while erecting steel. A plain reading of the contract between the fabricator and the employer steel erector indicated that the fabricator had the authority to delegate the erection of the work and all of its attendant supervisory and safety responsibilities to the erector. Therefore, the employer erector became responsible for all of the means, manners, and methods of the work, and all of the safety responsibilities for the steel erection, and was required to provide all of the tools and competent workers to complete the work safely and in accordance with all of the OSHA regulations and requirements. The fabricators never visited the site, never supervised the work, and never provided any direction to the ironworkers as to how they were to complete that work. They simply sent the material out and provided some oversight as to the sequencing of the work consistent with the material that was sent to the job.

However, the fabricator never retained control over the erectors work and the erection of the steel sufficiently to have exposure for failing to control the activities of its contractor. In fact, the *Oshana* case supported a long line of cases in Illinois that now seem to corroborate the fact that a typical fabricator, who does not have any on-site presence, will not be held responsible for any injuries that are caused as a result of the methods or processes undertaken by the erector they have hired to perform the work.

A second significant new case stemming from the 414 line of reasoning is *Calloway v. Bovis Lend Lease, Inc.*⁸³ In this case, the court expanded what it means to “entrust” work to an independent contractor and imposed liability upon a construction manager that had no direct

contract with the employer of the injured plaintiff. Typically, the contract dictated the entrustment of work as between an employer and an independent contractor. As indicated above, it was the “employer” of the independent contractor who was held responsible for failure to exercise control over the entity that it employed. The court, looking at a recent federal court decision from the Northern District of Illinois, *Henderson v. Bovis Lend Lease, Inc.*,⁸⁴ stated that the lack of a formal contractual relationship standing alone should not preclude a finding of “entrustment” insofar as the general contractor and an owner could conceivably evade liability by drafting contracts to avoid responsibility of entrustment to subcontractors such that both parties could refuse responsibility for the work of the subcontractor. The court envisioned a possible scenario in which both the owner and general contractor would avoid 414 exposure, and they frowned upon the concept that a general contractor could “skirt the entrustment requirement in this manner.”

Therefore, the court found that the control requirement of the Restatement Second of Torts 414 can be met with respect to a construction manager where evidence of the construction manager’s actions demonstrate that it retained sufficient control over the activities of the independent contractor such that entrustment was essentially assumed, although not contractually created. The *Calloway* court found that entrustment can be satisfied when the totality of the circumstances of an individual case demonstrate that the construction manager in fact “entrusted” work to a subcontractor even though it did not actually sign an agreement with that subcontractor.

In the *Calloway* case, the construction manager had a significant on-site presence, was present when the accident occurred, and had given direction as to the means and methods of the work to be performed by the independent contractor. When the accident occurred, and plaintiff’s were injured, the injured employees of the independent contractor sued the construction manager. The construction manager contended it could not be found liable under the Restatement of Torts 414 as it had not contract with the employer. As indicated above, the court found that the construction manager could be held responsible for that accident because of their negligence in exercising control over the work of the independent contractor.

A new significant case of note in Illinois is *Indiana Ins. Co. v. Power Screen of Chicago*⁸⁵ which stems from insurance coverage issues that arise on construction cases. In this case a renter of equipment to a construction company claimed additional insured status on the rentee’s insurance pursuant to the rental agreement. The relevant terms of the insurance policy at issued defined an additional insured as any person or organization which the named insured of the policy had agreed in writing to be added as an additional insured. Coverage would be provided to the additional insured for any liability that arose out of the named insured’s on-going operations performed for that person or organization. The carrier argued that once the equipment was rented to its named insured, there were no on-going operations being performed. The court, however, disagreed with that contention and held that while the equipment was in use, and while it was under the direct control of the contractor, and while the contractor was bound to return the equipment in satisfactory condition, and to maintain it while it was in its possession, the rental equipment was on-going and continuing in use, i.e., on-going operations, and therefore the rental company was entitled to the coverage afforded by the insurer as an additional insured. Further in that case, because the carrier had initially denied coverage, and the rental company had to have

its own insurance company protected in the litigation, while the DJ was determined, the rental company's own insurer was entitled to full reimbursement to all defense fees incurred from date of tender to the date of case resolution.

In another significant new case, *Pekin Ins. Co. v. United Contractor Midwest*⁸⁶ Pekin Insurance Company filed a declaratory action in response to negligence suits filed by a Mr. Hill, an employee, of Pekin's named insured, against the general contractor that hired Pekin's named insured to perform certain work for it. The contract between the employer and the general contractor required that the employer procure insurance providing additional insured coverage to the general contractor. The policy language indicated that an additional insured would include any person or organization for whom the employer was performing operations when its insured and had agreed in a written contract executed prior to the bodily injury or property damage for which coverage is sought, be added as an additional insured on a policy. The policy however limited coverage to an additional insured by stating that the additional insured would be covered "only with respect to vicarious liability for bodily injury or property damage imputed from you to the additional insured as a proximate result of your on-going operations for that additional insured, or for your work performed for that additional insured during the policy and provided for completed operations coverage." The additional insured endorsement also excluded liability in any way attributable to the claimed negligence or statutory violation of the additional insured other than vicarious liability which is imputed to the additional insured solely by virtue of the acts of the named insured.

In Illinois, plaintiffs cannot sue an employer directly. Their sole remedy is to pursue remedy through worker's compensation. Therefore, when the employee or Pekin's named insured was hurt, Mr. Hill filed a complaint against the general contractor and in it he alleged the general contractor was negligent. The *Pekin* court, in comparing the allegations of the complaint to the language of the policy, indicated that there were no allegations in the plaintiff's complaint against the general contractor for vicarious liability *per se*, nor were there any allegations of fault against the employer *per se*. The general contractor, however had filed a third party complaint against the employer, and in it alleged that all of the acts and omissions that caused this accident were the sole negligent conduct of the employer. The court, considering the third party complaint, determined that it could not be used to create coverage, and specifically found that because the third party complaint had been filed after the declaratory judgment was filed, that the attempt to supply the "missing allegations from the original complaint in an attempt to gain coverage as an additional insured under the policy" could not be relied upon. As such, the court concluded that because the underlying complaint did not contain any facts alleging negligence of the employer, Pekin had no duty to the additional insured. There was a strong dissent written that objected to the opinion of the court, and felt that because the plaintiff was hurt in the course of his conduct for the employer, that that fact coupled with the allegations of the third party complaint were sufficient to create a duty to defend.

Finally, in *Mt. Hawley Ins. v. Robinette*⁸⁷ a dispute arose over insurance coverage pursuant to an on-going subcontract agreement in which a subcontractor was required to obtain insurance covering the general contractor and others as additional insureds. The policy had a notice provision contained in it. Although the named insured was familiar with the fact that an accident occurred, the named insured did not notify the carrier concerning the incident. The

general contractor, however, when sued by an injured employee, quickly tendered the litigation to the carrier of its subcontractor. The carrier disputed a duty to defend on the basis that the named insured had breached the policy notice provision. The primary court sided with the carrier and found that as a result of the named insured's breach, Mt. Hawley did not owe a duty to defend any of the defendants in the underlying suit. On appeal, however, the court reversed that decision. The Illinois Appellate Court, after reviewing the policy and the circumstances, noted specifically that while the named insured was under a duty to notify Mt. Hawley of the accident, only the employer had a duty to do so. There was nothing contained within the language of the policy itself that indicated that the general contractor or additional insureds had a duty to notify the carrier of the occurrence. Rather, they put notice to Mt. Hawley immediately upon being sued. Although it was several years after the incident had occurred, it was promptly after they were exposed and, therefore, the court held that Mt. Hawley could not refuse to defend the general contractor based upon the named insured's failure to provide notice.

Further, expanding coverage even further, certain entities who had no direct contract with the employer, but who were referenced in a purchase order and certificate of insurance, also sought coverage from Mt. Hawley. Mt. Hawley maintained that the certificate of insurance did not constitute a written contract as required by the policy. Further on its face the certificate of insurance expressly disclaimed that the certificate conveyed any benefit to the persons named on it. The court held that when all read together the certificate of insurance "does provide an additional writing which supports a finding that the written agreement between the employer and the general contractor contemplated that additional entities would be named as additional insureds." Relying upon the totality of documents, therefore, they felt that the contract requirement was met, and for all of the foregoing reasons, found that the additional insureds, including those not specifically named in the contract, were entitled to coverage as additional insureds under the policy. This too is met with a strong dissent that indicated that the entities that were not specifically identified in the contract could not have coverage created pursuant to the additional documents, to wit, separate purchase order or the certificate itself.

¹ *Weather-Tite, Inc. v. Univ. of St. Francis*, 233 Ill. 2d 385; 909 N.E.2d 830 (2009).

² *Mostardi-Platt Assocs. v. Czerniejewski*, 399 Ill. App. 3d 1205, 929 N.E.2d 94 (5th Dist. 2010).

³ *Cordeck Sales, Inc. v. Constr. Sys.*, 394 Ill. App. 3d 870; 917 N.E.2d 536 (1st Dist. 2009).

⁴ *Id.*

⁵ 770 ILCS 60/16.

⁶ 770 ILCS 60/1; 770 ILCS 60/21

⁷ In *Weydert Homes, Inc. v. Kammes*, 395 Ill. App. 3d 512; 917 N.E.2d 64; (2nd Dist. 2009), the Illinois Appellate Court rejected the validity of a lien because the contractor failed to have it notarized.

⁸ *Cordeck Sales, Inc. v. Constr. Sys.*, 394 Ill. App. 3d 870; 917 N.E.2d 536 (1st Dist. 2009).

⁹ 770 ILCS 60/7.

¹⁰ *Id.*

¹¹ 770 ILCS 60/6.

¹² Section 24 does not, however, require a subcontractor to serve notice of its claim on the owner when the sworn statement of the contractor or subcontractor provided for herein shall serve to give notice of the amount due and to whom due. 770 ILCS 60/24 (2004); *Weather-Tite, Inc. v. Univ. of St. Francis*, 233 Ill. 2d 385; 909 N.E.2d 830 (2009).

¹³ 770 ILCS 60/21(c).

¹⁴ 770 ILCS 60/23(b).

¹⁵ *Id.*

¹⁶ *Id.*

¹⁷ 770 ILCS 60/23(b)(2).

¹⁸ 770 ILCS 60/23(b)(4).

¹⁹ *Id.*

²⁰ *Id.*

²¹ 770 ILCS 60/23(b)(5).

²² 770 ILCS 60/34-35.

²³ 770 ILCS 60/5.

²⁴ 735 ILCS 5/13-214.

²⁵ *Ambrosia Land v. Peabody Coal Co.*, 521 F.3d 778 (7th Cir. 2008).

²⁶ *Ryan v. Commonwealth Edison*, 381 Ill. App.3d 877, 885 N.E.2d 544 (1st Dist. 2008).

²⁷ *County of DuPage v. Graham, Anderson, Probst & White, Inc.*, 109 Ill. 2d 143, 485 N.E.2d 1076 (1985).

²⁸ 735 ILCS 5/13-202; *Hernon v. E.W. Corrigan Construction Co.*, 149 Ill. 2d 190, 595 N.E.2d 561 (1992).

²⁹ 735 ILCS 5/13-204.

³⁰ *Quality Components Corp. v. Kel-Keef Enterprises, Inc.*, 316 Ill. App.3d 998, 738 N.E.2d 524 (1st Dist. 2000).

³¹ See, e.g. AIA Document A101-1997, Standard Form of Agreement between Owner and Contractor, and AIA Document A201-1997, General Conditions of the Contract for Construction.

³² *Id.*

³³ *Id.*

³⁴ See Bill Status at <http://www.ilga.gov/legislation/>.

³⁵ Illinois HB 1114, 95th General Assembly.

³⁶ *Id.*

³⁷ *Travelers Ins. Co. v. Eljer Mfg.*, 197 Ill. 2d 278, 757 N.E.2d 481 (2001)

³⁸ *Qualls v. Country Mutual Ins. Co.*, 123 Ill. App. 3d 831, 462 N.E.2d 1288 (1984). See also *Viking Construction Management, Inc. v. Liberty Mutual Ins. Co.*, 358 Ill. App. 3d 34, 831 N.E.2d 1 (2005), for the proposition that a CGL policy does not cover defective work or construction damages.

³⁹ *Bituminous Casualty Corp. v. Gust K. Newburg Const.*, 218 Ill. App. 3d 956, 578 N.E.2d 1003 (1991).

⁴⁰ *State Farm Ins. & Casualty Co. v. Tillerson*, 334 Ill. App. 3d 404, 777 N.E.2d 986 (2002); *State Farm Ins. & Casualty Co. v. Watters*, 268 Ill. App. 3d 501, 644 N.E.2d 492 (1994).

⁴¹ *Monticello v. Wil-Fred's Construction*, 277 Ill. App. 3d 697, 661 N.E.2d 451 (1996). See also, *Stoneridge Development Company, Inc. v. Essex Ins. Co.*, 382 Ill. App. 3d 731, 888 N.E.2d 633 (2008) where the court held that cracks that developed in a home were not an occurrence, because the damage was the natural and ordinary consequence of improper construction methods and would not fall within the coverage of the CGL policy.

⁴² *John Burns Construction Co. v. Indiana Ins. Co.*, 189 Ill. 2d 570, 727 N.E.2d 211 (2000) and *Kajima Construction Services, Inc. v. St. Paul Fire & Marine Ins. Co.*, 227 Ill. 2d 102, 879 N.E.2d 305 (2007).

⁴³ See *Kajima Construction Services, Inc. v. St. Paul Fire & Marine Ins. Co.*, 227 Ill. 2d 102, 879 N.E.2d 305 (2007) (where the Illinois Supreme Court again held that an insured with multiple insurance policies covering any given loss has the right to select and/or deselect those policies that it wants to provide coverage under a factual scenario).

⁴⁴ *Id.*

⁴⁵ *North River Ins. Co. v. Grinnell Mutual Reinsurance Co.*, 369 Ill. App. 3d 563, 860 N.E.2d 460 (2006).

⁴⁶ See also, *Legion Ins. Co. v. Empire Fire & Marine Ins. Co.*, 354 Ill. App. 3d 699, 822 N.E.2d 1 (2004) for a discussion and explanation of the select or target tender.

⁴⁷ 740 ILCS 35/1.

⁴⁸ *Kotecki v. Cyclops Welding Corp.*, 146 Ill. 2d 155, 585 N.E.2d 1023 (1991).

⁴⁹ *Braye v. Archer-Daniel-Midland Co.*, 175 Ill. 2d 201, 676 N.E.2d 1295 (1997) and *Liccardi v. Stolt Terminals*, 178 Ill. 2d 540, 687 N.E.2d 968 (1997).

⁵⁰ *Virginia Surety v. Northern Insurance Co.*, 224 Ill. 2d 550, 866 N.E.2d 149 (IL 2007).

⁵¹ *Edward E. Gillen Co. v. City of Lake Forest*, 221 Ill. App. 3d 5, 581 N.E.2d 739 (2nd Dist. 1991).

⁵² *J & B Steel Contractors, Inc. v. C. Iber & Sons, Inc.*, 162 Ill. 2d 265, 642 N.E.2d 1215 (1994); *Batteast Const. Co., Inc. v. Public Bldg Comm. of Chicago*, 195 F. Supp.2d 1045 (N.D.IL 2001).

⁵³ *Fieldcrest Builders, Inc. v. Antonucci*, 311 Ill. App. 3d 597, 724 N.E.2d 49 (1st Dist. 1999).

⁵⁴ *Arch of Illinois, Inc. v. S.K. George Painting Contractors, Inc.*, 288 Ill. App. 3d 1080, 681 N.E.2d 1049 (5th Dist. 1997).

⁵⁵ *Fontana v. TLD Builders, Inc.*, 362 Ill. App. 3d 491, 840 N.E.2d 767 (2nd Dist. 2005).

⁵⁶ *Mirar Development, Inc. v. Kroner*, 308 Ill. App. 3d 403, 720 N.E.2d 270 (3rd Dist. 1999).

⁵⁷ *Bjork v. Draper*, 381 Ill. App. 3d 528, 886 N.E.2d 563 (2nd Dist. 2008).

⁵⁸ *Hous. Auth. v. Lyles*, 395 Ill. App. 3d 1036 (4th Dist. 2009).

⁵⁹ *Edward E. Gillen* (supra), 221 Ill. App.3d 5.

⁶⁰ *Pathman Const. Co. v. Hi-way Elec. Co.*, 65 Ill. App. 3d 480, 382 N.E.2d 453 (1st Dist. 1978).

⁶¹ *Amp-Rite Electric Co. v. Wheaton Sanitary Dist.*, 220 Ill. App. 3d 130, 580 N.E.2d 622 (2nd Dist. 1991).

⁶² *Id.*

⁶³ *Mars, Inc. v. Heritage Builders of Evingham, Inc.*, 327 Ill. App. 3d 346, 763 N.E.2d 428 (4th Dist. 2002).

⁶⁴ *First Arlington National Bank v. Stathis*, 115 Ill.App.3d 403, 450 N.E.2d 833. (1st Dist. 1983).

⁶⁵ 815 ILCS 205/2.

⁶⁶ See, e.g., *Weidner v Szostek*, [245 Ill App 3d 487, 490, 614 NE2d 879, 881 \(2nd Dist 1993\)](#); *Chemical Bank v American Natl Bank & Trust Co.*, [180 Ill App 3d 219, 229-30, 535 NE2d 940, 946 \(1st Dist. 1989\)](#).

⁶⁷ 735 ILCS 5/2-303.

⁶⁸ *Id.*

⁶⁹ *Morrow v. L.A. Goldschmidt Assoc., Inc.*, 112 Ill. 2d 87, 492 N.E.2d 181 (1986).

⁷⁰ *A. A. Conte, Inc. v. Campbell-Lowrie-Lautermilch Corp.*, 132 Ill. App. 3d 325, 477 N.E.2d 30 (1st Dist. 1985).

⁷¹ *Id.* citing *National Aircraft Policing Ltd. v. American Airlines, Inc.*, 74 Ill. App. 3d 1014, 1020, 394 N.E.2d 470, 475 (1979).

⁷² *Id.* citing *National Aircraft Policing Ltd. v. American Airlines, Inc.*, 74 Ill. App. 3d 1014, 1020, 394 N.E.2d 470, 475 (1979).

⁷³ *Vigilante v. National Bank*, 106 Ill. App. 3d 820, 436 N.E.2d 652 (1982).

⁷⁴ *A. A. Conte, Inc. v. Campbell-Lowrie-Lautermilch Corp.*, 132 Ill. App. 3d 325, 477 N.E.2d 30 (1st Dist. 1985) (dissenting opinion).

⁷⁵ *Preload, Inc. v. Marino Construction Company*, 1991 U.S. Dist. Court LEXIS 13710 (USDC Northern District of Illinois, Eastern Division) (1991).

⁷⁶ *Id.* citing *Dodson v. Nink*, 72 Ill. App. 3d 51, 390 N.E.2d 546 (2nd Dist. 1979).

⁷⁷ *Id.*

⁷⁸ *Brown and Kerr, Incorporated v. St. Paul Fire & Marine Ins. Co.*, 940 F. Supp. 1245 (USDC Northern District of Illinois 1996).

⁷⁹ *Id.*

⁸⁰ *DeGraf Bros. Inc. v. Mellon Stuart Co.*, 1991 U.S. District LEXIS 14594 (USDC Northern District of Illinois, Eastern Division 1991).

⁸¹ *Id.*

⁸² *Oshana v. FCL Builders*, 964 N.E.2d 748 (2012).

⁸³ *Calloway v. Bovis Lend Lease, Inc.*, 995 N.E.2d 381 (2013).

⁸⁴ *Henderson v. Bovis Lend Lease, Inc.*, 848 F. Supp. 2d 847 (N.D. Ill. 2012).

⁸⁵ *Indiana Ins. Co. v. Power Screen of Chicago*, 975 N.E.2d 141 (2012).

⁸⁶ *Pekin Ins. Co. v. United Contractor Midwest*, 997 N.E.2d 235 (2013).

⁸⁷ *Mt. Hawley Ins. v. Robinette*, 994 N.E.2d 973 (2013).

INDIANA

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I. MECHANIC'S LIEN BASICS

Indiana permits mechanics liens for nearly all types of work. The Mechanic's Lien Act is found at I.C. 32-28-3-1 *et seq.* The notice requirements for Indiana's Mechanic's Lien run from the last date work or equipment is provided.

A. Requirements

Indiana Code 32-28-3-3 requires that a person seeking a Mechanic's Lien must file a Notice of Intention to Hold a Lien in the Recorder's office for the county for the amount of the claim.

The Notice must provide the following:

- The amount claimed;
- The name and address of the claimant;
- The owner's name and address;
- The legal description and street number of the property; and
- Must be filed within ninety (90) days of the last date of work or furnishing of materials or equipment.

B. Enforcement and Foreclosure

There is no requirement to perfect a Mechanic's Lien in Indiana. Suit may be filed to foreclose on the lien in a circuit or superior court. Indiana Code 32-28-3-12 requires that suit be filed within one year after the Notice of Intention is filed.

C. Ability to Waive and Limitations on Lien Rights

A failure to file suit to foreclose upon a Mechanic's Lien within one year of the filing of the Notice of Intention to Hold a Mechanic's Lien operates as a waiver of the lien.¹

II. STATUTES OF LIMITATION AND REPOSE

A. Statutes of Limitation and Limitations on Application of Statutes

The statute of limitations for personal injury, property damage or wrongful death claims in Indiana for adults is 2 years.² The statute of limitations for claims based upon a written contract is 10 years.³

B. Statutes of Repose and Limitations on Application of Statutes

An action to recover damages for personal injury, property damage or wrongful death based upon improvements to real property may be brought within the earlier of 10 years after substantial completion or 12 years after the completion and submission of plans to the owner if the action is for a design defect.⁴ If personal injury or wrongful death occurs during the 9th or 10th years after substantial completion, then the action may be brought within 2 years after date of injury; however, the action may not be brought more than 12 years after substantial completion, or 14 years after the completion and submission of plans to the owner if the action is for design defect.⁵

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

When one party repudiates a contract, the injured party has the option of pursuing one of three remedies: 1) he may treat the contract as rescinded and recover upon *quantum meruit*; 2) he may keep the contract alive for the benefit of both parties, being at all time ready and able to perform, and at the end of the time specified in the contract for performance, sue to recover under the contract; or 3) he may treat the repudiation as putting an end to the contract and sue to recover the damages caused by refusing to carry out the contract.⁶ When the injured party treats the other's breach or repudiation as putting an end to the contract for all purposes of performance, the injured party is not bound to give further notice of its election before a suit is brought and is not bound to show it has been ready, willing and able to perform its part of the repudiated contract.⁷ If the injured party was not at fault at the time of the repudiation and was adhering to contract when repudiated by the other party, it has discharged its obligations.⁸

However, when a party deviates from strict performance called for by the contract, the former cannot suddenly declare the deviation a breach of contract.⁹ Notice must be given to the other party that strict performance will be required in the future, then, if the party continues to deviate, a default can be declared.¹⁰ Similarly, when both parties to a contract acquiesce to a delay, neither side can suddenly declare the contract rescinded and simply walk away. Notice must be given to the other party along with an opportunity to perform within a reasonable time.¹¹

IV. INSURANCE COVERAGE AND ALLOCATION ISSUES

A. General Coverage Issues

Standard CGL policies provide coverage for those sums that the insured becomes legally obligated to pay due to "bodily injury" or "property damage". The coverage applies to "bodily injury" or "property damage" if the bodily injury or property damage is the result of an occurrence resulting during the policy period. Coverage is excluded if the damages result to "your work" which is generally defined to be the scope of work described by the construction agreement.

B. Trigger of Coverage

In order to trigger coverage, there must be a claim for “bodily injury” or “property damage” as a result of an “occurrence.” For many years, Indiana case law held that coverage was not afforded to damages to the work of the insured based upon the reasoning that there was no “occurrence” under the policy. However, recently, the Indiana Supreme Court has reversed that line of cases. In *Sheehan Constr. Co. v. Cont’l Cas. Co.*,¹² the Indiana Supreme Court held that the “your work” exception, created the presumption that an occurrence as defined under the standard CGL policy included faulty workmanship. Thus, the Court held that claims for faulty workmanship would trigger coverage under the policy along with any other event constituting an “occurrence.”

C. Allocation Among Insurers

In Indiana, there must be more than a casual connection between the insured’s operations and a loss in order for the coverage of the insured to extend to other operations. For claims involving multiple coverages, liability for the insurer will be afforded according to the reading of the “other insurance” clauses in the policies. In the event of a conflict, coverage will be afforded on a pro-rata basis. Indiana has no so-called “targeted tender” doctrine as the same has not yet been addressed by Indiana appellate courts.

V. CONTRACTUAL INDEMNIFICATION

In Indiana, contractual indemnification provisions are not *per se* invalid although they are frowned upon and, as such, they are strictly construed by Indiana courts. Accordingly, a party may contract to indemnify the other party for the other party’s own negligence.¹³ However, this may only be done if the indemnitor knowingly and willingly agrees to such indemnification.¹⁴ Such clauses indemnifying the indemnitee’s own negligence are strictly construed and will not be held to provide indemnification unless the obligation is stated in clear and unequivocal terms. Indiana courts disfavor these indemnity clauses because “to obligate one party to pay for the negligence of another is a harsh burden that no party would likely accept.”¹⁵

Indiana statutory law renders as void and unenforceable any construction contract which purports to indemnify the indemnitee against liability for personal injury or property damage arising from its own “sole negligence” or “willful misconduct.”¹⁶ State highway contracts are exempted from this provision.

VI. CONTINGENT PAYMENT AGREEMENTS

No Indiana appellate court has addressed the matter of contingent payment or so-called “pay-when-paid” agreements. Unless the provision can be demonstrated to be unconscionable, an Indiana court will likely enforce such a provision. The Seventh Circuit Court of Appeals has predicted that Indiana would enforce a “pay-when-paid” provision and enforced the same in litigation arising in Indiana in *BMD Contractors, Inc. v. Fidelity and Deposit Co. of Maryland*.¹⁷

VII. DAMAGE LIMITATIONS

A. Personal Injury Damages vs. Construction Defect Damages

There is no statutory limitation on compensatory damages in Indiana.

B. Attorney's Fees Shifting and Limitations on Recovery

Indiana has adopted a Qualified Settlement Offer Statute. That statute is found at Indiana Code 34-50-1-1 *et seq.* and allows a party to extend an offer of settlement at least 30 days before trial. If the offer is not accepted and the trial result is more favorable to the offeror, that party may recover attorney's fees and litigation expenses. The attorney's fees recoverable are limited to \$1,000.00, however.

C. Consequential Damages

Consequential Damages are recoverable under Indiana damage law. Limitations on consequential damages are enforceable so long as they are not construed as being unconscionable. However, the Indiana Commercial Code may provide limitations on consequential damages depending on the nature of the claim being made.

D. Delay and Disruption Damages

Delay and Disruption damages are recoverable in Indiana.

E. Economic Loss Doctrine

Damage from a defective product or service may be recoverable under a tort theory if the defect causes personal injury or damage to other property, but contract law governs damage to the product or service itself and purely economic loss arising from the failure of the product or service to perform as expected. In this respect, Indiana law is consistent with admiralty law, and the law of most other states. "Economic losses" occur when there is no personal injury and no physical harm to other property. Rather these losses are viewed as disappointed contractual or commercial expectations.¹⁸

F. Interest

Pre Judgment interest may be recoverable in Indiana pursuant to I.C. 34-51-4-1 between 6 and 10%; post judgment interest accrues on all judgments at 8%.¹⁹

G. Punitive Damages

Punitive Damages are recoverable in Indiana for personal injury claims but not for wrongful death or contract claims. Punitive damages are recoverable for claims of insurance bad faith. Punitive damages must be established by clear and convincing evidence.²⁰ However, a statutory cap on punitive damages of three times compensatory damages or \$50,000.00, whichever is greater, is imposed by I.C. 34-51-3-4. Additionally, 75% of any punitive damages recovered must be paid to the Indiana Violent Crimes Victims Compensation Fund.²¹

VII. CASE LAW AND LEGISLATION UPDATE

The Indiana Court of Appeals has recently given an expansive reading to the AIA waiver of subrogation provision holding that the provision bars all claims, both insured and uninsured, in the event of a fire loss.²² In this case, the Court of Appeals adopted the so-called “majority approach” rejecting the “work vs. non-work” distinction in applying the waiver-of-subrogation provision. The Court’s opinion conflicts with a prior decision of another panel of the Indiana Court of Appeals which expressly adopted and applied the “work vs. non-work” approach in limiting the waiver provision to “the work” called for under the contract. This conflict will likely be resolved by the Indiana Supreme Court in the near future.

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- 1 I.C. 32-28-3-12.
 - 2 I.C. 34-11-2-4.
 - 3 I.C. 34-11-2-9.
 - 4 I.C. 32-30-1-5.
 - 5 I.C. 32-30-1-6.
 - 6 *Indianapolis v. Twin Lakes Enterprises*, 568 N.E.2d 1073 (Ind. Ct. App. 1991) trans. denied.
 - 7 *Twin Lakes*, 568 N.E.2d at 1080.
 - 8 *Id.*
 - 9 *Pierce v. Yochum*, 330 N.E.2d 102, 112, (Ind. Ct. App. 1975) trans. denied.
 - 10 *Id.*
 - 11 *Keliher v. Cure*, 534 N.E.2d 1133, 1137 (Ind. Ct. App. 1989).
 - 12 *Sheehan Constr. Co. v. Cont’l Cas. Co.*, 935 N.E.2d 160 (Ind. 2010).
 - 13 *Moore Heating & Plumbing, Inc. v. Huber Hunt & Nichols*, 583 N.E.2d 142, 145 (Ind. Ct. App. 1991).
 - 14 *Weaver v. American Oil Company*, 276 N.E.2d 144 (Ind. 1971).
 - 15 *Henthorne v. Legacy Healthcare, Inc.*, 764 N.E.2d 751, 757 (Ind. Ct. App. 2002).
 - 16 I.C. 26-2-5-1.
 - 17 *BMD Contractors, Inc. v. Fidelity and Deposit Co. of Maryland*, 679 F.3d 643 (7th Cir., 2012).
 - 18 *KB Home Ind., Inc. v. Rockville TBD Corp.*, 928 N.E.2d 297 (Ind. Ct. App. 2010).
 - 19 I.C. 24-4.6-1-101.
 - 20 I.C. 34-51-3-2.
 - 21 I.C. 34-51-3-6.
 - 22 *Bd. of Comr’s of Jefferson v. Teton Corporation*, 72A04-1302-CT-55 (Ind. Ct. App. 2014).

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I. MECHANIC'S LIEN BASICS

The Iowa legislature significantly changed the structure of the Iowa mechanic's lien statute in 2013. The major changes, which will be discussed in more detail below, include the following. First, all mechanics' lien filings on or after January 1, 2013 were to be filed with the Iowa Secretary of State, rather than with the Clerk of District Court in the County in which the improvement was made. The law implemented a new online registry, called the "Mechanic's Notice and Lien Registry," ("MNLN") which is used for filing (1) residential and commercial mechanic's liens; (2) residential notices; and (3) all other lien documents. Further, for all residential construction, the contractor is required to submit a notice within 10 days of starting the job. Contractors not filing the notice are not able to get a mechanics' lien. A subcontractor on residential construction must also post a "Preliminary Notice" to be entitled to a mechanics' lien.

A. Requirements

1. Important Dates

Under Iowa Code Chapter 572, general contractors and subcontractors (suppliers are included within the statutory definition of "subcontractor"¹ have 90 days from the date of furnishing the last labor or materials to the property in which to file a statement of lien.² The last labor performed or the last material furnished must be something other than a minor visit to the site merely made to resurrect the time period for filing the lien. In other words, there must be something significant done for the project at the time of the last visit.³

A mechanic's lien filed beyond the 90-day period may still be enforced. However, the priority of the lien may be lost. For example, a purchaser of a lien property who acquires the property

after the 90-day filing period, but before the actual filing of the mechanic's lien, will overcome the mechanic's lien of a contractor or subcontractor.⁴

The filing deadline is particularly critical to a subcontractor or supplier. A subcontractor or supplier can file a lien after the expiration of the 90-day period but the lien amount will not exceed the balance due from the owner to the contractor at the time the notice of the late-filed lien is served upon the owner.⁵ This makes it extremely important for subcontractors and suppliers to closely monitor their records of payment from general contractors.

A suit to foreclose the lien must be brought within two years and 90 days from the date that materials were last furnished or labor was last performed on the property.⁶ In many cases, the value of the owner's equity in the project will not be sufficient to pay all unpaid contractors, suppliers or subcontractors. This is because, in most instances, the mortgagee has priority over all other lien claimants. If there is some equity remaining to be distributed among the lien claimants, the mechanic's liens shall have priority over each other in the order of filing.⁷

2. Where and How to File a Mechanic's Lien

After the recent change in legislation, mechanic's liens are perfected by filing the actual mechanic's lien statement with the Secretary of State's office, which administers the MNLR System.⁸ The mechanic's lien form must be verified (notarized) and must contain a statement of the amount due the mechanic's lien claimant after allowing any credits. The mechanic's lien statement must also set out the date when material was first furnished or labor first performed, the date when the last material was furnished or labor was last performed, the legal description of the property to be charged with the lien, the name and last known mailing address of the owner of the property, the address of the property or a description of the location of the property if there is no address, and the tax parcel identification number of the parcel. After the lien is filed, the Administrator of the MNLR will mail a copy of the lien to the owner.⁹

However, if the lien is filed by a subcontractor or supplier after the expiration of the 90-day period, the subcontractor or supplier must cause the notice of the lien to be served on the owner of the property.¹⁰

3. Special Lien Provisions Pertaining to "Residential Construction" Properties

While lien laws are generally designed to protect unpaid contractors or subcontractors, the Iowa legislature amended the mechanic's lien statute to incorporate protections for "Residential Construction" properties (in other words to protect owners of single-family residential properties). Most of the provisions are designed to insure the homeowner is aware subcontractors or suppliers may have mechanic's lien rights despite the fact that the homeowner fully paid the general contractor with the expectation that the subcontractors would be paid by the general contractor.

Section 572.13 pertains to general contractors, who must provide the owner with the following notice, which must be in "boldface type" and a minimum size of ten points:

Persons or companies furnishing labor or materials for the improvement of real property may enforce a lien upon the improved property if they are not paid for their contributions, even if the parties have no direct contractual relationship with the owner. The mechanics'

notice and lien registry provides a listing of all persons or companies furnishing labor or materials who have posted a lien or who may post a lien upon the improved property.¹¹

A general contractor failing to provide the notice will not be entitled to a lien.

Section 572.13A pertains to a general contractor or owner builder, who must post a “Notice of Commencement” of work to the MNLR no later than 10 days after the commencement of work on the property. The notice of commencement will be effective only to labor, service, equipment, and material furnished to the property subsequent to the posting of the notice.¹² The Notice of Commencement must include the name and address of the owner; the name, address, and telephone number of the general contractor or owner-builder; the address or general description of the property; the legal description; the date the work was commenced; and the tax parcel ID number.¹³ A failure to post the Notice of Commencement while eliminate the general contractor or owner-builder’s ability to file a lien on the project.

Section 572.14 and 572.13B pertain primarily to subcontractors (including suppliers). These sections provide that a subcontractor may lose his lien rights unless he provides a “Preliminary Notice” to the owner in the form specified by the statute.¹⁴ The notice is to be posted before the balance due is paid to the general contractor. The notice must contain the name of the owner; the MNLR number; the name, address, and telephone number of the subcontractor furnishing the labor, service, equipment, or material; the name and address of the person who contracted with the claiming subcontractor; the address of the property or general description if it has none; the legal description of the property; the date the material or materials were first furnished or labor was performed; and the tax parcel ID number.

The subcontractor or supplier is well advised to provide notice beyond what the administrator provides, which can be made by certified mail, personal service, or a signed receive of notice from the owner.¹⁵ This is so because, in the event of a dispute, the subcontractor bears the burden of demonstrating receipt of the Preliminary Notice. If the subcontractor or supplier fails to provide such a notice, the subcontractor or supplier may be deprived of his lien rights if the owner has already paid the general contractor.

B. Enforcement and Foreclosure of the Lien

A petition to foreclose a mechanic’s lien must be filed in the district court where the lien was filed within two years and 90 days of the last day that labor was performed or materials were furnished. If the suit is not filed within that time period, the lien will no longer be enforceable. At the foreclosure action, the court may establish priority among all other lien claimants for any equity available in the property for the payment of all the claims. In addition, certain lien claimants may be entitled to recovery of attorney’s fees expended to foreclose their mechanic’s lien rights.

The Code provides that the plaintiff (lien claimant) in a foreclosure action, if successful, may be awarded reasonable attorney’s fees.¹⁶ A prevailing owner also may in certain situations recover attorney fees.¹⁷ If an owner of a residential construction property, in resisting a mechanic’s lien foreclosure, prevails then such owner may be awarded attorney fees. Additionally, if the lien was filed in bad faith or the supporting affidavit was materially false then the court shall award to the owner \$500 or the amount of the lien, whichever is less.

C. Lien Rights of Second-Tier Subcontractors – Commercial Construction

Iowa Code Section 572.33 deals with notice requirements for persons furnishing labor or material to a subcontractor, but only for commercial construction projects (also known as second-tier subcontractors because they are not in privity of contract with the principal contractor). The one-time notice must be furnished to the general contractor or owner-builder within thirty days of first furnishing materials or labor. The notice requires the name, mailing address, and telephone number of the person furnishing the materials or labor, and the name of the subcontractor to whom the materials or labor were furnished. The notice covers additional material or labor furnished by the same person to the same subcontractor for use in the same construction project. If the deadline for providing notice is not met then all lien rights of the second-tier subcontractor are lost.

The same section also provides that the general contractor or owner-builder has the right to request information from a person furnishing materials or labor to a subcontractor regarding payments made or to be made by the subcontractor.

D. No Mechanic's Liens on Public Projects

The principle of sovereign immunity -- "one cannot sue the king" -- prohibits the enforcement of lien remedies against property owned by the government or its various subdivisions. However, the federal government and all states have enacted statutes which provide lien-like remedies for those who perform work on or provide materials for public property. Most of these statutes, however, serve to protect subcontractors and suppliers rather than the general contractors. General contractors are usually left with their contract remedies in the case of work performed on public property. In Iowa, the applicable statute is Iowa Code Chapter 573. It addresses the procedure for making claims for labor performed and materials supplied on public improvement projects.

II. STATUTES OF LIMITATION AND REPOSE

A. Statute of Limitations

Under Iowa Code Section 614.1(4), actions generally founded on "injuries to property" and fraud are to be brought within five years. Under Section 614.1(5), actions founded on written contracts must be brought within ten years.

It is well settled in Iowa that no cause of action accrues until the wrongful act produces loss or damage to the claimant.¹⁸ Under the discovery rule, "a cause of action based on negligence does not accrue until plaintiff has in fact discovered that he has suffered injury or by exercise of reasonable diligence should have discovered it."¹⁹ The discovery rule has been applied to cases involving negligence²⁰ and express and implied warranty.²¹

B. Statute of Repose

Statutes of repose are different from statutes of limitation. A statute of limitation "bars, after a certain period of time, the right to prosecute an accrued cause of action."²² A statute of repose, by contrast, "terminates any right of action after a specified time has elapsed, regardless of whether or not there has as yet been an injury."²³

Despite the fact that Iowa Code Chapter 614 is titled “Limitations of Actions,” Section 614.1(11) is in all actuality a statute of repose. It states that “[i]n addition to limitations contained elsewhere in this section, an action arising out of the unsafe or defective condition of an improvement to real property based on tort and implied warranty . . . and founded on injury to property, real or personal . . . shall not be brought more than fifteen years after the date on which occurred the act or omission of the defendant alleged in the action to have been the cause of the injury.” The section also expressly excludes claims against a “person” solely “in the person’s capacity as an owner, occupant, or operator of an improvement to real property.”²⁴

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

Iowa law requires that, in order to maintain an action for breach of warranty, notice of an alleged breach of the warranty must be given within a reasonable time after the claimant discovered, or should have discovered, the breach.²⁵

IV. INSURANCE COVERAGE AND ALLOCATION ISSUES

Standard CGL policies provide coverage for amounts the insured is liable to pay because of property damage occurring during the policy period. When a contractor makes an insurance claim for property damage on a construction project, there is often a dispute over which policy applies and whether or not the damage is covered.

Generally, no coverage for defective construction work is afforded to contractors if the only damage is to the work product itself.²⁶

V. CONTRACTUAL INDEMNIFICATION

Under a contract for indemnification, “one party (the indemnitor) promises to hold another party (the indemnitee) harmless for loss or damage of some kind.”²⁷ Iowa courts have maintained that “indemnifying agreements will be enforced according to their terms, as in any other contract case.”²⁸

There are, however, some “unique rules” in the indemnity context. First, “where an indemnification is not given by one in the insurance business but is given incident to a contract whose main purpose is not indemnification, the indemnity provision must be construed strictly in favor of the indemnitor.”²⁹ Furthermore, “an indemnity contract is strictly construed against the drafter.”³⁰ Second, a party can receive indemnity for its own negligence only if the indemnity provides for it in “clear and unequivocal language.”³¹ “Broad and general language” will not suffice to “shift the burden of liability, particularly when the damage is caused by the indemnitee’s sole negligence.”³²

When interpreting and construing an indemnity problem, the Iowa courts frame the issue with reference to two questions: “(1) for whose negligent acts causing damage is indemnity promised? and (2) what is the scope of the area in which indemnity is available?”³³

VI. CONTINGENT PAYMENT AGREEMENTS

There is no per se legal prohibition against contingent payment clauses in Iowa. The enforceability and requirements of contingent payment agreements depend whether the project is private or public.

A. Private Projects

Under Iowa Code Section 572.30, a contractor who engages a subcontractor or supplier to provide labor or materials on an owner-occupied dwelling must pay the subcontractor for labor and materials within 30 days after the contractor receives full payment from the owner. If the contractor fails to pay the subcontractor as required, the unpaid subcontractor or supplier may sue the contractor and recover in addition to the actual damages, “exemplary damages” against the contractor in an amount not less than one percent and not exceeding 15 percent of the amount due the subcontractor.

Prior to instituting such an action, however, the subcontractor or supplier must give written notice to the contractor of nonpayment indicating the amount of payment due and a description of the real estate improved.

The general contractor can avoid the exemplary damages penalties under the statute if he or she does one or both of the following:

1. Establishes that all proceeds received from the person making the payment have been applied to the cost of labor or material furnished for the improvement.
2. Within fifteen days after receiving notice of nonpayment the principal contractor gives a bond or makes a deposit with the clerk of the district court, in an amount not less than the amount necessary to satisfy the nonpayment for which notice has been given under this section, and in a form approved by a judge of the district court, to hold harmless the owner or person having the improvement made from any claim for payment of anyone furnishing labor or material for the improvement, other than the principal contractor.³⁴

B. Public Projects

Under Iowa Code Section 573.12, the public corporation must make prompt payment to the principal contractor. Further, the principal contractor must pay subcontractors no later than either 1) seven days after receipt of payment for the subcontractor’s work or 2) a reasonable time after the prime contractor could have received payment for the subcontractor’s work, if nonpayment isn’t the subcontractor’s fault. This last clause could trump contrary pay-if-paid or pay-when-paid clauses.

VII. DAMAGES LIMITATIONS

A. Personal Injury Damages v. Construction Defect Damages

The damages that a plaintiff may recover arising from a construction project include both personal injury damages and construction defect damages depending on the circumstances. Unlike other states, the legislature has not recently enacted a statute that affects this issue. Thus, basic contract and tort principles apply.

B. Attorneys' Fees

The general rule is that parties may recover attorney fees only pursuant to a statute or contract. Iowa courts have recognized a limited exception to this rule “when the losing party has acted in bad faith, vexatiously, wantonly, or for oppressive reasons.”³⁵ To be entitled to an award under this common law rule, the injured party must demonstrate that the offending party’s actions “rise to the level of oppression or connivance to harass or injure another.”³⁶

C. Consequential Damages

A contractor may recover “consequential damages,” which includes damages foreseeable at the time the parties entered the contract, or damages naturally flowing from the contract’s breach.³⁷

D. Delay and Disruption Damages

Generally, delay and disruption damages, if shown to be consequential, are recoverable. A plaintiff seeking such damages must “establish the amount of claimed damages with some reasonable degree of certainty [but] mathematical precision is not required.”³⁸

E. Economic Loss Doctrine

The general rule in Iowa is that a plaintiff “cannot maintain a claim for purely economic damages arising out of [a] defendant’s alleged negligence.”³⁹ In the construction project context, the Iowa Supreme Court has made the following remarks concerning the economic loss doctrine: (T)he line to be drawn is one between tort and contract rather than between physical harm and economic loss. . . . When, as here, the loss relates to a consumer or user’s disappointed expectations due to deterioration, internal breakdown or non-accidental cause, the remedy lies in contract.

Tort theory, on the other hand, is generally appropriate when the harm is a sudden or dangerous occurrence, frequently involving some violence or collision with external objects, resulting from a genuine hazard in the nature of the product defect.⁴⁰

Note, however, that an exception to the Economic Loss Doctrine has been carved out for licensed professionals such as architects and engineers.⁴¹

F. Interest

Interest is permitted, in pertinent part, on all money due on judgments and decrees of courts at a rate calculated under Iowa Code Section 668.13.⁴² Additionally, in construction cases, Iowa courts have held that a nonbreaching party may recover interest payments made to third parties if “reasonably foreseeable and proximately caused by the defaulting party’s breach.”⁴³

Additionally, contractors may recover interest on an open account (i.e. “finance charges”), provided the formalities of Iowa Code Section 535.11 are adhered to.

G. Punitive Damages

Unless provided for by statute, punitive damages will not be awarded for breach of contract. A narrow exception, however, has been recognized in Iowa when the breach “also constitutes an intentional tort, or other illegal or wrongful act, if committed maliciously.”⁴⁴

While the intentional tort or illegal/wrongful act may occur at the time of and/or in connection with the breach, such a “wrongful act” is not committed by the breaching of the contract, even if intentional.⁴⁵

VII. CASE LAW AND LEGISLATION UPDATE

In 2008, the Iowa Supreme Court held that the implied warranty of workmanlike construction runs to the benefit of subsequent purchasers of a home.⁴⁶ The Court further held that the implied warranty is a judicially created warranty that is independent of the construction contract. Builder-vendors, according to the Court, should be liable to subsequent purchasers for breach of the implied warranty of workmanlike construction because builder-vendors are in a superior position as a result of their expertise in construction.

In 2011, the Iowa legislature passed SF 396 and thereby banned “broad-form” indemnification in most construction contracts. The new law will be codified at Iowa Code Section 573A.5.

In 2011, the Iowa legislature passed HF 646 in an effort to reduce (post bid submittal) bid-shopping. The amended law (Iowa Code Section 8A.311) will require general contractors on State construction projects to identify their subcontractors 48 hours after the published date for which bids must be submitted, obtain approval from the State before changing subcontractors, and disclose the change in subcontract price caused by a change in subcontractor.

In 2012, the Iowa Court of Appeals declined to extend the implied warranty of workmanlike construction to subcontractors, even where general contractors had become insolvent, and subcontractors had performed the allegedly defective work.⁴⁷ As discussed herein, in 2013 the Iowa Mechanic’s Lien Law was substantially changed by the introduction of the MNLR and attendant provisions discussed in the section concerning mechanic’s liens.

Early in 2014, the Iowa Court of Appeals again refused to extend the implied warranty of workmanlike construction this time, based on a request to extend it to multi-unit residential dwellings and to protect consumer lenders providing funds to build a multi-unit dwelling for occupancy as a residence.⁴⁸

¹ Iowa Code § 572.1 (2013).

² *Id.* §§ 572.9, 572.11.

³ *Skemp v. Olansky*, 85 N.W.2d 580 (Iowa 1957).

⁴ Iowa Code § 572.18.

⁵ *Id.* § 572.11.

⁶ *Id.* § 572.27.

⁷ *Id.* § 572.17.

⁸ *Id.* § 572.8.

⁹ *Id.*

¹⁰ *Id.* § 572.10.

¹¹ *Id.* § 572.13(1).

¹² *Id.* § 572.13A(1).

¹³ *Id.* § 572.13A(1)(a)-(g).

¹⁴ *Id.* § 572.13B(1).

¹⁵ *Id.* § 572.13B(3)(b).

¹⁶ *Id.* § 572.32.

¹⁷ *Id.* § 572.32.

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- ¹⁸ *Bob McKiness Excavating & Grading, Inc. v. Morton Buildings, Inc.*, 507 N.W.2d 405, 408 (Iowa 1993).
- ¹⁹ *Id.* (citing *Chrischilles v. Griswold*, 150 N.W.2d 94, 100 (Iowa 1967)).
- ²⁰ *Id.*
- ²¹ *Brown v. Ellison*, 304 N.W.2d 197, 201 (Iowa 1981).
- ²² *Bob McKiness v. Morton*, 507 N.W.2d at 408.
- ²³ *Id.* (citing *Hanson v. Williams County*, 389 N.W.2d 319, 321 (Iowa 1984)).
- ²⁴ Iowa Code § 614.1(11).
- ²⁵ *Kirk v. Ridgway*, 373 N.W.2d 491, 496 (Iowa 1985).
- ²⁶ *Cont'l Western Ins. Co. v. Jerry's Homes, Inc.*, 2006 Iowa App. LEXIS 122 (Iowa Ct. App. Feb. 1, 2006)
- ²⁷ *McNally & Nimergood v. Neumann-Kiewit Constructors, Inc.*, 648 N.W.2d 564, 570 (Iowa 2002) (citing II E. Allan Farnsworth, *Farnsworth on Contracts* § 6.3, at 108 (2d ed. 1998)).
- ²⁸ *Pugh v. Prairie Constr. Co.*, 602 N.W.2d 805, 808 (Iowa 1999).
- ²⁹ *Id.* at 808.
- ³⁰ *Id.*
- ³¹ *McNally & Nimergood v. Neumann-Kiewit Constructors, Inc.*, 648 N.W.2d 564, 571 (Iowa 2002).
- ³² *Herter v. Ringland-Johnson-Crowley Co.*, 492 N.W.2d 672, 674 (Iowa 1992)
- ³³ Roger Stone, *Indemnity in Iowa Construction Law*, 54 Drake L. Rev. 125, 133 (2005) (citing *Modern Piping, Inc. v. Blackhawk Automatic Sprinklers, Inc.*, 581 N.W.2d 616, 624 (Iowa 1998) (internal citations omitted)).
- ³⁴ Iowa Code § 572.30.
- ³⁵ Roger Stone, *Construction Damages in Iowa*, 52 Drake L. Rev. 449, 460 (2004) (citing *Remer v. Bd. Of Med. Exam'rs*, 576 N.W.2d 598, 603 (Iowa 1998) (internal quotation omitted)).
- ³⁶ *Id.* (citing *Hockenberg Equip. Co. v. Hockenberg's Equip. & Supply Co.*, 510 N.W.2d 153, 159-160 (Iowa 1993)).
- ³⁷ *Metropolitan Transfer Station, Inc. v. Design Structures, Inc.*, 328 N.W.2d 532, 536 (Iowa Ct. App. 1982) (citing *Mihills Manufacturing Co. v. Day Brothers*, 50 Iowa 250, 252 (1878)).
- ³⁸ *Mills v. Guthrie County Rural Electric Coop. Ass'n*, 454 N.W.2d 846, 851 (Iowa 1990) (citing *Bushman v. Cuckler Building Systems*, 421 N.W.2d 145, 148 (Iowa App. 1988)).
- ³⁹ *Nebraska Innkeepers, Inc. v. Pittsburgh-Des Moines Corp.*, 345 N.W.2d 124 (Iowa 1984).
- ⁴⁰ *Determan v. Johnson*, 613 N.W.2d 259, 262 (Iowa 2000) (citing *Nelson v. Todd's Ltd.*, 426 N.W.2d 120, 125 (Iowa 1988)).
- ⁴¹ *Kemin Indus. v. KPMG Peat Marwick LLP*, 578 N.W.2d 212, 221 (Iowa 1998); *Burns Philp, Inc. v. Cox, Kliewer & Co., P.C.*, 2000 U.S. Dist. LEXIS 21653 (S.D. Iowa Nov. 2, 2000)
- ⁴² Iowa Code § 535.3.
- ⁴³ Roger Stone, *Construction Damages in Iowa*, 52 Drake L. Rev. 449, 458 (2004) (citing *Metro Transfer Station, Inc. v. Design Structures, Inc.*, 328 N.W.2d 532, 536 (Iowa Ct. App. 1982)).
- ⁴⁴ *Muchmore Equipment, Inc. v. Grover*, 315 N.W.2d 92, 100 (Iowa 1982) (citing *Pogge v. Fullerton Lumber Co.*, 277 N.W.2d 916, 919-20 (Iowa 1979)).
- ⁴⁵ *Id.*
- ⁴⁶ *Kemin Indus. v. KPMG Peat Marwick LLP*, 578 N.W.2d 212, 221 (Iowa 1998); *Burns Philp, Inc. v. Cox, Kliewer & Co., P.C.*, 2000 U.S. Dist. LEXIS 21653 (S.D. Iowa Nov. 2, 2000)
- ⁴⁷ *Village at White Birch Town Homeowners Association v. Goodman Associates, Inc.*, 2012 WL 5356045 (Iowa Ct. App. Oct. 31, 2012).
- ⁴⁸ *Luana Sav. Bank v. Pro-Build Holdings, Inc.*, 843 N.W.2d 477 (Iowa Ct. App. 2014)

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I. MECHANIC'S LIEN BASICS

The mechanic's lien in Kansas was created by statute and did not exist at common law. The Kansas mechanic's lien statute is located at K.S.A. § 60-1101 *et seq.*, which provides "[a]ny person furnishing labor, equipment, material, or supplies used or consumed for the improvement of real property, under a contract with the owner or with the trustee, agent or spouse of the owner, shall have a lien upon the property for the labor, equipment, material or supplies furnished at the site of the property subject to the lien, and for the cost of transporting the same." K.S.A. § 60-1101. As such, there are four (4) lienable items under the statute: (1) labor, (2) equipment, (3) materials, and (4) supplies. *Id.* The cost of transporting such items may also be included in the lien. *Id.* These items must be used or consumed for the purpose of improving the real property at issue. *Id.*

A. Who May Obtain a Mechanic's Lien

The most obvious party that may obtain a mechanic's lien is the general contractor. K.S.A. § 60-1103. However, the statute also provides that a subcontractor or supplier may obtain a mechanic's lien in certain circumstances as well. K.S.A. § 60-1103; *J.W. Thompson Co. v. Welles Prods. Corp.*, 243 Kan. 503, 758 P.2d 738 (1988); *Wichita Sheet Metal Supply, Inc. v. Dahlstrom and Ferrell Const. Co.*, 246 Kan. 557, 792 P.2d 1043 (Kan. 1990).

A contractor's lien is generally governed by K.S.A. § 60-1101 and 60-1102. The obvious difference between a contractor and a subcontractor is the contractor has direct contractual privity with the owner of the property. K.S.A. § 60-1101. A contractor is one who furnishes labor or materials under a contract directly with the owner for the improvement of the property. *See Stewart v. Cunningham*, 219 Kan. 374, 377, 548 P.2d 740 (1976).

A subcontractor's or supplier's lien is governed by K.S.A. § 60-1103. Such parties must be performing under an agreement with a contractor, subcontractor or "owner contractor." *Id.* In other words, there must be contractual privity with some entity that is in privity with the owner. K.S.A. § 60-1103a and 60-1103b provide additional requirements for subcontractors and suppliers for residential properties. For example, on a pre-existing residential property, a subcontractor or supplier is required to provide a warning statement, as provided in the statute, to the property owner. K.S.A. § 60-1103a. On a new residential property, the subcontractor or

supplier is required to furnish a notice of intent to perform prior to the recording of the deed effecting passage of title to the new residential property. K.S.A. § 60-1103b. The notice must be filed in the office of the clerk of the district court of the county where the property is located. *Id.* The subcontractor or supplier is required to file a release once paid in full and, irrespective, the notice of intent expires 18 months after it is filed, unless the party has perfected a lien under the statute. *Id.*

B, Creation and Perfection of a Mechanic's lien

1. Timing

A contractor has four (4) months after the date upon which the last material, equipment, or supplies were furnished or the last labor was performed under the contract in which to file its mechanic's lien. K.S.A. § 60-1102. A subcontractor, supplier, or other person furnishing labor, equipment, material or supplies, used or consumed at the site of the property subject to the lien, has three (3) months to file its mechanic's lien. K.S.A. § 60-1103. The time begins to run after the date the materials, equipment, or supplies were last furnished or the labor was last performed by the claimant. *Id.* The test to determine when the piece of work is completed and the time period for filing a mechanic's lien commences is whether the unfinished work was part of the work necessary to be performed under the terms of the original contract to complete the job. *Manhattan Mall Co. v. Shult*, 254 Kan. 253, 259, 864 P.2d 1136, [1141](#) (1993). For purposes of determining the timeliness of a mechanics' lien, it is not fatal to the lien for the lien statement to have an erroneous date for the time materials or labor were provided, so long as the filing date is within the time specified by the applicable statute from the actual date materials or labor were last supplied by the claimant. *Alliance Steel, Inc. v. Piland*, 39 Kan. App. 2d 972, 187 P.3d 111 (2008).

2. Procedure

The initial step to creating and perfecting a mechanic's lien is creating the lien statement. The lien statement must include (1) the name of the owner; (2) name and address sufficient for service of process of the claimant; (3) a description of the real property; and (4) a reasonably itemized statement of the amount of the claim. K.S.A. § 60-1102(a). The lien statement must also be verified. *Id.* The lien statement must then be filed with the clerk of the district court where the property is located. *Id.* The statute is silent on whether a contractor is required to serve the owner of the property with the filed lien statement. A subcontractor or supplier must file its lien as provided for by a contractor. However, the subcontractor or supplier must also provide a warning statement when necessary under K.S.A. § 60-1103(a), file a notice of intent when required under K.S.A. § 60-1103(a), and must also serve the statement upon the owner. K.S.A. § 60-1103. The manner of service is described in K.S.A. § 60-1103(c).

3. Enforcement

Once filed, the claimant will be required to foreclose on the lien in order to enforce its rights. The burden of proof is on the claimant in any foreclosure action. *See Kopp's Rug Co. v. Talbot*, 5 Kan. App. 2d 565, 620 P.2d 1167 (1980). Typically, the claimant will also file other claims with its foreclosure action, like breach of contract and/or unjust enrichment claims. The

foreclosure action must be filed within one (1) year of filing the lien statement (K.S.A. § 60-1105(a)) and all other lien holders and other encumbrances of record must be made a party to the action (K.S.A. § 60-1106).

C. Miscellaneous Matters

Perfection of a mechanic's lien requires that the statutory requirements be strictly met. *Walters Constr. Co. v. Greystone S. P'ship, L.P.*, 15 Kan. App. 2d 689, 691-92, 817 P.2d 201 (1991). The Kansas Court of Appeals recently reaffirmed the need for strict compliance. *See, e.g.*, *National Restoration Co. v. Merit General Contractors, Inc.*, 208 P.3d 755, 762, 41 Kan. App.2d 1010, 1019 (Kan. App. 2009)(refusing to uphold supplier's lien where supplier failed to identify general contractor); *Buchanan v. Overlay*, 39 Kan. App. 2d. 171, 176-77, 178 P.3d 58 (2008)(refusing to uphold a mechanic's lien where the contractor failed to verify his address as required by K.S.A. § 1102). Those claiming a mechanic's lien have the burden of bringing themselves clearly within the provisions of the statute. *Sec. Benefit Life Ins. Corp. v. Fleming Cos., Inc.*, 21 Kan. App. 2d 833, 838, 908 P.2d 1315 (1995). Finally, while a mechanic's lien may be filed against public property, all liens are discharged when a public works bond is filed. K.S.A. § 60-1111(b). The statute requires a bond to be filed for contracts exceeding \$100,000.00. K.S.A. § 60-1111(a).

II. STATUTES OF LIMITATION AND REPOSE

The statutes of limitation and the repose periods applicable to construction defect claims are contained in K.S.A. § 60-501 *et seq.* This section provides a brief overview of the statutes and highlights some of the important case law interpreting these provisions.

A. Statute of Limitations

1. Tort Claims

Tort or negligence claims are generally governed by the two (2) year statute of limitations. K.S.A. § 60-513(a). However, the discovery rule applies to cases falling under the umbrella of this section. K.S.A. § 60-513(b). One potential limitation on tort claims is the economic loss doctrine, which will be discussed below. Furthermore, Kansas courts have held that tort claims cannot be maintained between parties in a contractual relationship to impose tort duties concerning matters the parties have already allocated themselves by contract. *See, e.g.*, *Beeson v. Erickson*, 22 Kan. App. 2d 452, 461, 917 P.2d 901, *pet. for review denied*, 260 Kan. 991 (1996); *Ford Motor Credit Co. v. Suburban Ford*, 237 Kan. 195, 202-04, 699 P.2d 992 (1985).

2. Written Contract Claims

A claim for breach of a written agreement carries a five (5) year statute of limitations. K.S.A. § 60-511(1). The statute of limitations begins to run at the time the cause of action accrues. K.S.A. § 60-510. In general, "a cause of action accrues, so as to start the running of the statute of limitations, as soon as the right to maintain a legal action arises. The true test to determine when an action accrues is that point in time at which the plaintiff could have filed and prosecuted his action to a successful conclusion." *Kraemer & Sons, Inc. v. City of Overland*

Park, 19 Kan. App. 2d 1087, 1090, 880 P.2d 789 (1994). More specifically, “[a] cause of action in contract accrues at the time of the breach or failure to do the thing agreed to, irrespective of any knowledge on the part of the plaintiff or of any actual injury it has occasioned him, and he would be entitled to recover nominal damages if nothing more.” *Crabb v. Swindler*, 184 Kan. 501, Syl. ¶ 4, 337 P.2d 986 (1959) (holding that a claim for improper installation of plumbing fixtures, based on an implied contract theory, accrued when the installation was completed). There is no discovery rule for this type of cause of action as is provided for in K.S.A. § 60-513(b); *see also* *Ware v. Christenberry*, 7 Kan. App. 2d 1, 637 P.2d 452 (1981). Whether plaintiffs knew of or could have discovered the alleged breaches is not important to the analysis under K.S.A. § 60-511(1).

3. Implied Warranties

Under Kansas law, implied warranties may be brought in either contract or tort. *Ware v. Christenberry*, 7 Kan. App. 2d 1, Syl. ¶ 4, 637 P.2d 452 (1981). This decision is made at the election of the claimant, and the decision may be made at anytime before the matter is submitted to the trier of fact. *Id.* at 6. As such, the claimant can essentially choose his or her statute of limitations. If the implied warranty claim is brought in tort, it will be a two (2) year statute of limitations, but the discovery rule will apply. It is important to remember that there are other potential barriers to a tort claim, like the economic loss doctrine. If the implied warranty claim is brought in contract, a three (3) year statute of limitations will apply, but there will be no discovery rule. K.S.A. § 60-512(1). In the case of the implied warranty contract claim, “the time begins to run with the breach of the contract regardless of whether the injured party is aware of the breach.” *Ware*, 7 Kan. App. 2d at 4.

4. Kansas Consumer Protection Act

The Kansas Consumer Protection Act (“KCPA”) is a statutory creation, designed to protect consumers from deceptive or unconscionable acts and practices. The statute of limitations for any action upon a liability created by a statute, other than a penalty or forfeiture, is three (3) years. K.S.A. § 60-512. The Kansas Supreme Court has specifically acknowledged that the three-year statute of limitations applies to the KCPA where the claim seeks damages and civil penalties. *Alexander v. Certified Master Builders Corp.*, 268 Kan. 812, 824, 1 P.3d 899 (2000). There is no express discovery rule found in the statute, and the Kansas Court of Appeals has recently held that the discovery rule applicable to common-law fraud actions is not applicable to the KCPA. *Four Seasons Apartments, Ltd., v. AAA Glass Serv., Inc.*, 37 Kan. App. 2d 248, 250-51, 152 P.3d 101 (2007).

5. U.C.C.

Contracts for the sale of goods under the U.C.C. have a four (4) year statute of limitations. K.S.A. § 84-2-725. However, by agreement, the parties may reduce the period of limitation to not less than one year but may not extend it. *Id.*

B. Statutes of Repose

Kansas law sets forth a ten-year statute of repose for tort actions. K.S.A. § 60-513(b). The ten (10) years is an outside limit, meaning that no tort action can be maintained more than ten (10) years from the date of the action giving rise to the cause of action, irrespective of when or if the injury is discovered. In the products liability realm, K.S.A. § 60-3303 sets forth a ten-year statute of repose as a presumption of the useful life of a product. However, if warranted by seller, the statute of repose extends to the time warranted by the seller. *Id.*

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

The Kansas Legislature has passed the Residential Construction Defect Act (“RCDA”), which went into effect on July 1, 2003. K.S.A. § 60-4701 *et seq.* The primary purpose of the RCDA is to require a construction defect claimant to provide pre-suit notice of the claim upon the contractor. A “claimant” is defined as a “homeowner, including a subsequent purchaser, or association who asserts a claim against a contractor concerning a defect in the construction or in the remodel of a dwelling.” K.S.A. § 60-4701(c). A “contractor” is defined as “any person, firm, partnership, corporation, association or other organization that is engaged in the business of constructing dwellings.” K.S.A. § 60-4701(e). A “dwelling” includes a single family residence, a duplex, or multifamily unit designed for residential use. K.S.A. § 60-4701(f).

A. Notice Issues

As stated above, the claimant must serve written notice of a claim on the contractor prior to filing a lawsuit. The initial notice of claim shall state that the claimant asserts a construction defect claim and the notice of claim shall describe the claim or claims in detail sufficient to determine the general nature of any alleged construction defects. K.S.A. § 60-4704(a). If a claimant files an action against a contractor without service of notice under the RCDA, the action will be dismissed without prejudice upon motion of the contractor filed within sixty (60) days of service of process. K.S.A. § 60-4702(a). An action against a contractor cannot be re-filed until the parties have complied with the provisions of this act. *Id.*

After receipt of the notice, the contractor is required to serve a copy of the notice upon each subcontractor who may be responsible for a defect specified in the notice. K.S.A. § 60-4704(b). This must be done within fifteen (15) days after being served. *Id.* The notice must include the specific defect for which the contractor believes the subcontractor may be responsible. *Id.*

Within thirty (30) days after service of the notice of claim, each contractor that has received such notice shall serve a written response on the claimant. K.S.A. § 60-4704(c). The written response shall, (1) propose to inspect the subject dwelling, (2) offer to remedy the alleged defect at no cost to the claimant, (3) offer to settle the claim for a monetary amount, or (4) state that the contractor disputes the claim and will neither remedy the alleged construction defect nor compromise and settle the claim. *Id.*

If the contractor refuses service of the notice of claim, disputes the claim, does not respond to the claimant's notice of claim within the time stated above, does not commence or complete the work on the alleged construction defect on the date specified or does not make the payment in the time specified, the claimant may bring an action against the contractor without further notice. K.S.A. § 60-4704(d).

Absent good cause, the contractor's failure to respond in good faith to the claimant's notice of claim shall preclude the contractor from asserting that the claimant did not comply with the provisions of this act. K.S.A. § 60-4704(m).

B. Remedy Proposal

Any claimant accepting the offer of the contractor to remedy the construction defects shall do so by serving the contractor with a written notice of acceptance no later than thirty (30) days after receipt of the offer. K.S.A. § 60-4704(k).

If a claimant accepts a contractor's offer to repair a defect described in a notice of claim, the claimant shall provide the contractor and its agents reasonable access to the claimant's dwelling during normal working hours to perform and complete the construction by the timetable stated in the offer. K.S.A. § 60-4704(l).

C. Rejection of Contractor's Proposal

If the claimant rejects the inspection proposal or the settlement offer made by the contractor, the claimant shall serve written notice of the claimant's rejection on the contractor. K.S.A. § 60-4704(e). After service of the rejection, the claimant may bring an action against the contractor without further notice or elect an arbitration process under K.S.A. § 5-201 *et seq.* *Id.* A failure to give the notice of rejection will not require the dismissal of the action under K.S.A. § 60-4702(a). *Id.*

D. Inspection Proposal

If the claimant elects to allow the contractor to inspect the dwelling, the claimant must notify the contractor and provide the contractor with access to the dwelling during normal working hours. K.S.A. § 60-4704(f). The inspection must occur within thirty (30) days of notification to the contractor. *Id.* Within thirty (30) days following the inspection, the contractor must respond to the claimant in writing and either offer to remedy the construction defect, offer to settle the matter through monetary payment, or state that the contractor will not proceed further to remedy the defect. K.S.A. § 60-4704(g). As stated above, if an agreement cannot be reached, the claimant can proceed with bringing a lawsuit. K.S.A. § 60-4704(g), (h), (i) and (j). However, if the claimant is rejecting a contractor's proposed offer he must serve notice of rejection before proceeding with litigation. K.S.A. § 60-4704(j).

E. Miscellaneous Issues

The statute also requires the contractor to provide certain notices to the owner of the dwelling. For example, when constructing a new dwelling or remodeling the dwelling, the contractor must provide the owner notice of the requirements under this Act. K.S.A. § 60-4706. Furthermore, purchasers of newly constructed dwellings must be provided a list of subcontractors and a notification of the requirements under this Act. K.S.A. § 60-4707.

IV. COVERAGE AND ALLOCATION ISSUES

Many types of insurance coverage protect contractors and subcontractors in the construction industry. For example, a builder's risk policy typically provides coverage during a

construction project for property damage that occurs during the course of construction. The coverage will typically extend to the construction materials, equipment, and labor that are used in constructing a building. Concerning construction defect litigation, the most likely coverage is to come from a commercial general liability (“CGL”) policy.

Not surprisingly, the most likely issue that will arise in litigation is whether the CGL policy covers or protects the insured from the alleged loss. The interpretation of an insurance contract is a question of law that is determined by the court. *Lee Builders, Inc. v. Farm Bureau Mut. Ins. Co.*, 281 Kan. 844, Syl. ¶ 1, 137 P.3d 486 (2006). Like other contracts, an insurance contract is to be construed based on the intent of the parties. *Brumley v. Lee*, 265 Kan. 810, 963 P.2d 1224 (1998). Where there is an ambiguity in the insurance contract, it will be interpreted to provide coverage for the insured. *Lee Builders*, 281 Kan. at Syl. ¶ 3. Under Kansas law, the insurance company’s duty to defend and duty to indemnify are treated differently. For example, even where there is a remote possibility of coverage under the policy, the insurance company’s duty to defend will apply. *Johnson v. Studyvin*, 839 F. Supp. 1490, 1495 (D. Kan. 1993); *Patrons Mut. Ins. Assn. v. Harmon*, 240 Kan. 707, 710, 732 P.2d 741 (1987). The duty to defend is determined by the allegations of the underlying complaint and by the facts discoverable by the insurer at the time the complaint is made. *United Wats, Inc. v. Cincinnati Ins. Co.*, 971 F. Supp. 1375, 1382 (D. Kan. 1997); *Spruill Motors, Inc. v. Universal Underwriters Ins. Co.*, 212 Kan. 681, 686, 512 P.2d 403 (1973). The duty to indemnify is much narrower and is determined by the actual facts established in the case. *Cas. Reciprocal Exch. v. Thomas*, 7 Kan. App. 2d 718, 720, 647 P.2d 1361 (1982).

The typical CGL policy contains the following coverage language: “We will pay those sums that the insured becomes legally obligated to pay as damages because of ‘bodily injury’ or ‘property damage’ to which this insurance applies. We will have the right and duty to defend any ‘suit’ seeking those damages. We may, at our discretion investigate any ‘occurrence’ and settle any claim or ‘suit’ that may result.” See, e.g., *Lee Builders*, 281 Kan. at 850. The CGL policy typically provides coverage for “property damage” only if it is caused by an “occurrence” that occurs during the policy period. *Id.* An “occurrence” is typically defined as “[a]n accident, including continuous or repeated exposure to substantially the same general harmful conditions.” *Id.* “Accident” is not typically defined by the policy. *Id.*

In *Lee Builders, Inc. v. Farm Bureau Mutual Insurance Company*, the Court was asked to determine whether a CGL policy, with the above policy language, provided coverage for liability arising from the construction of a residential dwelling. 281 Kan. 844, 137 P.3d 486 (2006). Specifically, the issue raised on appeal was whether moisture leakage over time, which was allegedly caused by defective materials or workmanship and led to structural damage within a constructed home, was an “occurrence” under the CGL policy. *Id.* at 846. The Kansas Supreme Court noted that using clear distinctions in the policy is the obligation of the policy drafter, and furthermore, “[u]nclear and obscure clauses in a policy of insurance should not be allowed to defeat the coverage reasonably to be expected by the insured.” *Id.* at 857-58 (quoting *Sturdy v. Allied Mutual Ins. Co.*, 203 Kan. 783, 792, 457 P.2d 34 (1969)). “An insured would reasonably expect to have insurance coverage under an “occurrence” not only for the damage caused to the passerby by the falling wall described in the dissent, but also for the damage to the falling wall itself.” *Id.* at 858. The court concluded, “The damage in the present case is an occurrence . . . because faulty materials and workmanship provided by Lee’s subcontractors caused continuous

exposure of the Steinberger home to moisture. The moisture in turn caused damage that was both unforeseen and unintended.” *Id.* at 859. In reaching this conclusion, the court relied in part on *Fidelity & Deposit of Maryland v. Hartford Cas. Ins. Co.*, 189 F. Supp. 2d 1212 (D. Kan. 2002), where the Federal District Court held that faulty or negligent workmanship can constitute an “occurrence” so long as the insured did not intend for the damage to occur. *Id.* at 851-54.

Finally, it is important to keep in mind that there are fee shifting provisions found under K.S.A. § 40-908 and K.S.A. § 40-256 that may be applicable in insurance coverage disputes. *Lee Builders*, 281 Kan. at 859-62; *Johnson v. Westhoff Sand Co.*, 281 Kan. 930, 135 P.3d 1127 (2006).

For additional discussion of risk allocation and additional insured endorsements, see the discussion below under Section V concerning contractual indemnification and the application of K.S.A. 16-121.

V. CONTRACTUAL INDEMNIFICATION

Kansas has previously recognized contractual indemnification in building and construction contracts. *See, e.g., Sw. Nat’l Bank v. Simpson and Son, Inc.*, 14 Kan. App. 2d 763, 799 P.2d 512 (1991). The two most typical areas where one would likely see the use of contractual indemnification are (1) to protect a general contractor from contractual liability based on or arising out of the negligence of a subcontractor, or (2) to protect a party from injuries occurring on a construction site.

Indemnity is generally defined as “an obligation resting on a party to make good any loss another has incurred while acting at his request or for his benefit” *Missouri Pac. Ry. Co. v. City of Topeka*, 213 Kan. 658, 662, 518 P.2d 372 (1974). As with other contracts, in construing and determining the rights and liabilities of the parties, the intention of the parties must be determined and effect should be given to those intentions if it is legally possible. *Id.*; *Bartlett v. Davis Corp.*, 219 Kan. 148, 156, 547 P.2d 800 (1976); *Sw. Nat’l Bank v. Simpson and Son, Inc.*, 14 Kan. App. 2d 763, 772, 799 P.2d 512 (1990). All ambiguities are to be resolved against the party who prepared the contract at issue. *Sw. Nat’l Bank*, 14 Kan. App. 2d at 771. While the indemnification agreement will be interpreted according to its terms, an obligation of good faith is implied within those terms. *Hartford v. Tanner*, 22 Kan. App. 2d 64, 73, 910 P.2d 872 (1996); *Estate of Draper v. Bank of America*, 288 Kan. 510, 525, 205 P.3d 698, 710 (2009).

It is also important to note that a cause of action for indemnitee does not accrue until the indemnitee suffers actual loss or damage. *Leiker v. Gafford*, 249 Kan. 554, 558-59, 819 P.2d 655 (1991) *overruled on other grounds by Martindale v. Tenny*, 250 Kan. 651, 829 P.2d 561 (1992). “Simply because one has been found liable for an obligation of another, it does not necessarily follow that one is entitled to indemnification. A condition precedent to indemnification is that the indemnitee must actually have paid on the obligation for which he seeks indemnification.” *Id.* (discussing indemnity in the context of vicarious liability).

It should also be noted that absent express language in the contract, attorney’s fees are not recoverable in a lawsuit to enforce the indemnity agreement. *Chetopa State Bancshares, Inc. v. Fox*, 6 Kan. App. 2d 326, 333-34, 628 P.2d 249 (1981). The flip side, obviously, is where the contract provides for attorney’s fees, such a provision is enforceable. *Id.*

Before 2004, the legal authority related to indemnification provisions in construction contracts was governed by case law in Kansas. In 2004, the Kansas Legislature enacted K.S.A. 16-121, severely limiting the common-law rule allowing one party to secure indemnity from another party for the first party's negligence, as occurred and was previously approved in *Southwest*, 14 Kan. App. 2d at 763.

The 2004 statute was limited to apply strictly to "construction contracts", defined as agreements for the "design, construction, alteration, renovation, repair or maintenance of a building, structure, highway, road, bridge, water line, sewer line, oil line, gas line, appurtenance or other improvement to real property, including any moving, demolition or excavation". K.S.A. 2004 Supp. 16-121(a). The 2004 statute provided that "[a]n indemnification provision in a contract which requires the promisor to indemnify the promisee for the promisee's negligence or intentional acts or omissions is against public policy and is void and unenforceable." K.S.A. 2004 Supp. 16-121(b). The 2004 statute expressly stated it was not to be construed to "affect or impair the contractual obligation of a contractor or owner to provide railroad protective insurance or general liability insurance." K.S.A. 2004 Supp. 16-121(c).

In 2008, the Kansas Legislature substantially amended K.S.A. 16-121. First, the type of contracts to which the statute applies was expanded beyond "construction contracts" to include any defined "dealership agreement", "franchise agreement" or "motor carrier transportation contract." Second, the 2008 amended statute conclusively closed a perceived loophole which arguably allowed the indemnitee to require the indemnitor to provide liability insurance to the indemnitee as an "additional insured" under the indemnitor's liability insurance policy, a common practice in the construction and service industries. In this regard, the 2008 amended statute added subsection (c), which provides that any provision which requires a "party to provide liability coverage to another party, as an additional insured, for such other party's own negligence or intentional acts or omissions is against public policy and is void and unenforceable." As discussed below, there are two exceptions to subsection (c), being (d)(6)(A) and (d)(6)(B).

At first blush, the 2008 amended statute would seem to have been enacted to strengthen the announced "public policy" of the 2004 statute prohibiting "express indemnity" clauses which make one party responsible for another party's negligence or fault. But the 2008 amended statute created three exceptions to the prohibition on the "indemnification provision" described in subsection (b), which are found in subsections (d)(5), (d)(6)(A) and (d)(6)(B), respectively.

The exception set out in subsection (d)(5) is difficult to comprehend on its face. It provides that a "separately negotiated" indemnity clause whereby the parties "mutually agree to a reasonable allocation of risk" based on "generally accepted industry loss experience" and "supported by adequate consideration" is not prohibited. The most problematic, and mysterious, language in (d)(5) is the phrase "generally accepted industry loss experience." What does this phrase mean? Depending on how (d)(5) is interpreted by the appeals courts, and reconciled with the overall prohibition on indemnity clauses which make one party liable for the negligence of another, it could be a large or small exception to the general prohibition.

Subsection (d)(6)(A) provides that an agreement for a "mutual indemnity obligation" which is "supported by liability insurance coverage to be furnished by the promisor" is not

prohibited. A “mutual indemnity obligation” is defined as one where each party agrees to indemnify the “other and each other’s contractors and their employees” against “bodily injury, death or damage to property of the respective employees, contractors or their employees, and invitees of each party arising out of or resulting from the performance of the agreement.” K.S.A. 2008 Supp. 16-121(a)(8).

Subsection (d)(6)(B) of the 2008 provides that an agreement for a “unilateral indemnity obligation” which is “supported by liability insurance coverage to be furnished by the promisor” is not prohibited. A “unilateral indemnity obligation” is defined as an agreement whereby one party agrees to indemnify another party “with respect to claims for personal injury or death to the promisor’s employees or agents or the employees or agents of the promisor’s contractors but in which the promisee does not make a reciprocal indemnity promise to the promisor.” K.S.A. 2008 Supp. 16-121(a)(10)

Importantly, the substantive indemnity obligations permitted under (d)(6)(A) and (d)(6)(B) of the 2008 amended statute are strictly limited to the amount of liability coverage “supporting” the indemnity promise and ends when such “supporting” liability insurance is exhausted. While the legislature dislikes indemnity clauses which foist responsibility for the negligence of one party onto another, it does not dislike them so much it will prohibit the permitted “mutual indemnity obligation” and “unilateral indemnity obligation”, provided such types of “obligations” become the financial responsibility of a liability insurance company willing to assume the risk.

Again, the “mutual indemnity obligation” exception created by (d)(6)(A), which must be “supported” by liability insurance and is only valid to the extent it is “supported” by liability insurance, is limited to specific types of damage suffered by specific types of persons or entities—“loss, liability or damages arising in connection with bodily injury, death and damage to property of the respective employees, contractors or their employees and invitees of each party” to the contract. Thus, the permitted “mutual indemnity obligation”, and the corresponding “supporting” liability insurance, cannot extend to bodily injury sustained by some other third-person not listed, *e.g.*, a motorist or pedestrian struck by one of the party’s vehicles while out on a public street while in the performance of the contract, or a pedestrian walking past the job site on a public sidewalk, or property damage sustained by persons not on the job site who are not connected to the work as an employee of one of the parties or their contractors, or as one of their invitees, etc.

Similarly, the “unilateral indemnity obligation” exception created by (d)(6)(B), which must be “supported” by liability insurance and is only valid to the extent it is “supported” by liability insurance, is limited to specific types of damage suffered by specific types of persons (but not entities)—“claims for personal injury or death to the promisor’s employees or agents or to the employees or agents of the promisor’s contractors”.

With respect to the exceptions created by (d)(6)(A) and (d)(6)(B), the promisor can obtain liability insurance to make good such express indemnity provisions. On the other hand, the statute does not make any similar provision for an indemnitor (promisor) to purchase insurance to back up his indemnity promise to an indemnitee (promisee) with respect to an

indemnity agreement allowed by subsection (d)(5). In this connection, with the specific exceptions of (d)(6)(A) and (d)(6)(B), subsection (c) clearly prohibits the purchase of liability insurance which has as its goal one party indemnifying a second party for such second party's negligence.

While a promisor could argue that so long as a "supporting" insurance policy did not name the indemnitee as an "additional insured" then such liability policy is not prohibited, it is more likely that an appeals court will look to enforce the true intent of subsection (c), which, again, is to prohibit one party from being compelled, contractually, to buy liability insurance for a second party to protect such second party from damages caused by its own negligence or other fault.

VI. CONTINGENT PAYMENT AGREEMENTS

Kansas case law has provided little guidance regarding the enforceability of contingent payment agreements, or as they are often referred to "pay when paid" or "pay if paid" clauses. The Kansas Supreme Court has found that a "pay when paid" clause can modify the prevailing industry standard for payment of a subcontractor. *See Havens v. Safeway Stores*, 235 Kan. 226, 231, 678 P.2d 625 (1984). Kansas courts have not held, however, that contingent payment agreements create a valid condition precedent to payment.

In addition, the passage of the Kansas Fairness in Private Construction Act in 2005 has called the effectiveness of contingent payment agreements into greater question. The Act provides that a contract provision purporting to make payment to a contractor or subcontractor contingent on receipt of payment from another private party is not a defense to the enforcement of a mechanic's lien or bond to secure payment. K.S.A. § 16-1803(c). Consequently, even if a "pay if paid" clause were in place, a subcontractor could still attempt to obtain payment via a mechanic's lien pursuant to K.S.A. § 60-1101 *et seq.* It should be noted, however, that the Kansas Fairness in Private Construction Act is inapplicable to construction contracts concerning single family residential housing or residential housing consisting of four units or less. K.S.A. § 16-1807. Therefore, the enforceability of a contingent payment agreement in regards to residential housing remains undetermined.

VII. DAMAGES LIMITATIONS

A. Attorneys' Fees

In the construction context, attorney's fees are generally available in two contexts. *See, e.g., Chetopa State Bancshares, Inc. v. Fox*, 6 Kan. App. 2d 326, 333, 628 P.2d 249 (1981) ("As in Kansas, most states have a postulate that attorney fees are recoverable only if provided by statute or contract."). First, attorney's fees are available if the construction contract provides for the same. *Id.* Second, the Kansas Consumer Protection Act provides, "[T]he court may award to the prevailing party reasonable attorney fees, including those on appeal, limited to the work reasonably performed if: (1) The consumer complaining of the act or practice that violates this act has brought or maintained an action the consumer knew to be groundless and the prevailing party is the supplier; or a supplier has committed an act or practice that violates this act and the prevailing party is the consumer; and (2) an action under this section has been terminated by a judgment, or settled." K.S.A. § 50-634(e). Interestingly, this section is a "prevailing party"

provision, meaning that the supplier may be entitled to attorney's fees if it is determined that the consumer knew the action to be groundless.

B. Contract Damages

"The basic principle of contract damages is to make a party whole by putting it in as good a position as the party would have been had the contract been performed." *Stovall v. Reliance Ins. Co.*, 278 Kan. 777, 789, 107 P.3d 1219 (2005). Under Kansas law, "[b]reach of contract damages are limited to those damages which may fairly be considered as arising in the usual course of things, from the breach itself, or as may reasonably be assumed to have been within the contemplation of both parties as the probable result of the breach." *Enlow v. Sears, Roebuck and Co.*, 249 Kan. 732, Syl. ¶ 4, 822 P.2d 617 (1991). Such damages would include consequential damages, where foreseeable. *Jackson Trak Group, Inc. v. Mid States Port Auth.*, 242 Kan. 683, 694, 751 P.2d 122 (1988).

"The 'cost of repair' rule is recognized in [Kansas] for computation of damages from a breach of a construction contract." *English Village Properties, Inc. v. Boettcher & Lieurance Constr. Co.* 7 Kan.App.2d 307, 316, 640 P.2d 1282 (1982). "When a building contract has been so far performed that the building is occupied and used by the owner for the purposes contemplated by the contracting parties and where correction or completion would not involve unreasonable destruction of the work done by the contractor[,], evidence of the cost of correcting the defects and completing the omissions will, as a general rule, be a fair measure of the damages." *Id.* (quoting *Mahoney, Inc. v. Galokee Corp.*, 214 Kan. 754, 757, 522 P.2d 428 (1974)).

C. Delay and Disruption Damages

There are no Kansas cases directly on point related to delay and disruption damages in the construction context. However, it is assumed that traditional breach of contract rules would apply to allow delay and disruption damages where foreseeable. Furthermore, where the parties have contractually agreed, liquidated damages may be an appropriate substitute to compensate for damages resulting from delay or disruption in the work, but only to the extent the damages provision does not amount to a penalty, as discussed below.

D. Economic Loss Doctrine

In 2004, the Kansas Court of Appeals recognized the application of the economic loss doctrine in the construction context. See *Prendiville v. Contemporary Homes, Inc.*, 32 Kan.App.2d 435, 83 P.3d 1257, *pet. for rev. denied* (2004). *Prendiville* involved a residential construction project.

In 2011, the Kansas Supreme Court overturned *Prendiville* in the residential construction context. *David v. Hett*, 293 Kan. 679, 270 P.3d 1102 (2011). The Court held that the economic loss doctrine would not bar claims by homeowners seeking to recover economic damages resulting from negligently performed residential construction services. Thus, a homeowner's claim against a residential contractor may be asserted in tort, contract, or both, depending on the nature of the duty giving rise to the claim. In so ruling, the Court discussed the fact that residential construction contracts rarely involve sophisticated parties with equal bargaining positions. Thus, it is unclear whether the ruling in *Hett* would also apply in the commercial

construction setting. See, e.g., *Ran Const. Co. v. Dearborn Mid-West Conveyor Co.*, 944 F. Supp. 2d 1042 (D. Kan. 2013) (recognizing the narrow holding of the *Hett* court).

See also *Rinehart v. Morton Blds., Inc.*, 297 Kan. 926, 305 P.3d 622 (2013) (holding that negligent misrepresentation claims are not subject to the economic loss doctrine because the duty underlying such claims arises by operation of law and the doctrine's purposes would not be furthered by extending it to such claims).

E. Liquidated Damages

“It is well settled that parties to a contract may stipulate to the amount of damages for breach of the contract, if the stipulation is determined to be a liquidated damages clause rather than a penalty. A stipulation for damages upon a future breach of contract is valid as a liquidated damages clause if the set amount is determined to be reasonable and the amount of damages is difficult to ascertain.” *U.S.D. No. 315 v. DeWerff*, 6 Kan. App. 2d 77, 78, 626 P.2d 1206 (1981) (citing *White Lakes Shopping Center, Inc. v. Jefferson Standard Life Ins. Co.*, 208 Kan. 121, 126-28, 490 P.2d 609 (1971)). “The distinction between a provision for liquidated damages and one for a penalty is that a penalty is to secure performance, while a liquidated damages provision is for payment of a sum in lieu of performance.” *Id.* at 79.

In determining whether contractual agreements are to be treated as penalties or as liquidated damages, courts look behind the words used by the contracting parties to the facts and the nature of the transaction. The use of the terms “penalty” or “liquidated damages” in the instrument is of evidentiary value only. It is given weight and is ordinarily accepted as controlling unless the facts and circumstances impel a contrary holding. (Citations Omitted). The instrument must be considered as a whole, and the situation of the parties, the nature of the subject matter and the circumstances surrounding its execution taken into account. There are two considerations which are given special weight in support of a holding that a contractual provision is for liquidated damages rather than a penalty – the first is that the amount stipulated is conscionable, that it is reasonable in view of the value of the subject matter of the contract and of the probable or presumptive loss in case of breach; and the second is that the nature of the transaction is such that the amount of actual damage resulting from default would not be easily and readily determinable.

Beck v. Megli, 153 Kan. 721, 726, 114 P.2d 305 (1941); See also *Carrothers Const. Co., L.L.C. v. City of South Hutchinson*, 288 Kan. 743, 755, 207 P.3d 231, 241 (Kan., 2009). Retrospective analysis is unnecessary in determining whether a liquidated damages clause is a penalty. Reasonableness of a liquidated damages clause is determined as of the time the contract was executed, not with the benefit of hindsight. *Carrothers Const. Co., L.L.C. v. City of South Hutchinson*, 288 Kan. 743, 755, 207 P.3d 231, 241 (2009).

F. Interest

Post judgment interest in Kansas is set by statute and can change annually. K.S.A. § 16-204. Concerning prejudgment interest, Kansas follows the traditional approach, which recognizes a distinction between liquidated and unliquidated damages. In general, Kansas only allows prejudgment interest on liquidated claims. See, e.g., *Varney Bus. Servs, Inc. v. Pottroff*, 275 Kan. 20, 43, 59 P.3d 1003 (2002). A claim becomes liquidated when the amount due and

the date it is due are “fixed and certain or when the same become definitely ascertainable by mathematical calculation.” *Hamilton v. State Farm Fire & Cas. Co.*, 263 Kan. 875, 883, 953 P.2d 1027 (1998). Based on these factors, tort claims are unlikely to collect prejudgment interest. Concerning the amount of prejudgment interest, “[c]reditors shall be allowed to receive interest at the rate of ten percent per annum, when no other rate of interest is agreed upon, for any money after it becomes due.” K.S.A. § 16-201. However, the maximum allowable agreed interest rate (on loans, notes, etc.) is 15% per annum. K.S.A. § 16-207(a).

G. Punitive Damages

Punitive damages are not allowed in breach of contract claims, standing alone, even if the breach is intentional and unjustified, but such damages are allowable if there is some independent tort present. *Farrell v. General Motors Corp.*, 249 Kan. 231, 247, 815 P.2d 538 (1991). “This exception to the rule of unavailability of punitive damages in breach of contract actions is recognized when some independent tort or wrong results in additional injury which justifies the assessment of punitive damages by way of punishment of the wrongdoer. In such a case the proof of the independent tort must indicate the presence of malice, fraud or wanton disregard for the rights of others.” *Guar. Abstract & Title Co. v Interstate Fire and Cas. Co.*, 232 Kan. 76, 78-79, 652 P.2d 665 (1982).

VII. CASE LAW AND LEGISLATION UPDATE

Since 2011, there have been no legislative changes that will substantially affect the construction industry. The most significant case law update, discussed above, was the Kansas Supreme Court’s holding that the economic loss doctrine was inapplicable in the residential construction context. Below are a couple of additional interesting cases:

1. *Hewitt v. Kirk’s Remodeling and Custom Homes, Inc.*, 49 Kan. App. 2d 506, 310 P.3d 436 (2013) (“For purposes of K.S.A. 60-511(1), a cause of action based upon a builder’s express warranty to repair or replace construction defects in a newly built house must be brought within 5 years of the date the builder breached the warranty by refusing or failing to repair or replace the defects).

2. *Coker v. Siler*, 48 Kan. App. 2d 910, 304 P.3d 689 (2013) (holding that breach of implied warranty claim against the construction company’s president (individually) failed as a matter of law where there was no underlying agreement between the plaintiff and the company president).

KENTUCKY

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I. MECHANICS' LIEN BASICS

Kentucky lien law makes a distinction between mechanics' liens asserted against publicly owned property and those asserted against privately held property. A party providing materials or services for the improvement of privately owned real estate has a lien upon the real estate itself. KRS 376.010. A party providing materials or services for the improvement of land owned by the Commonwealth or a governmental subdivision has a lien against the proceeds due from the governmental entity. KRS 376.210. The procedure for securing payment through a lien for work performed or materials provided differs substantially between public and private jobs.

A. Requirements

1. *Public Property Lien.* A contractor, subcontractor or supplier owed money for improvements to public property must file a lien statement in the county clerk's office in the county in which the project is located within 60 days of the end of the last month on which materials or services are provided by the claimant or by the date of substantial completion of the project, whichever date is later. KRS 376.230. KRS 376.210(2) contemplates filing a preliminary statement of the intention to perform work or supply materials, but case law interpreting predecessor statutes strongly suggests that such a statement is not required. *Grigsbey v. Lexington & E.R. Co.*, 150 S.W. 687, 1912 Ky. LEXIS 945 (Ky. 1912).

To perfect the lien, a claimant must (1) file a lien statement; (2) deliver to the public authority making the contract an attested copy of the lien statement and (3) file with the public authority a copy of a letter (registered or certified with return receipt requested) sent to the contractor or subcontractor indebted to the claimant showing that a copy of the lien was sent to the contractor or subcontractor. KRS 376.240.

After receipt of the lien statement, the public authority must withhold the claim amount from the money due from the public authority to the contractor or subcontractor owing the claimant. After receipt of the lien statement, the contractor or subcontractor owing the money to the claimant must, within 30 days, file a protest to the lien, or the public authority may release the withheld funds to the claimant. KRS 376.250.

2. *Private Lien.* A party who performed work or supplied materials for the improvement of private real estate pursuant to a contract with someone other than the owner of

the property must, before filing a lien statement, send to the owner notice of an intent to file a lien. For owner-occupied single or double family residential jobs and for commercial jobs less than \$1,000, the claimant must send the notice within 75 days of last work. For commercial jobs more than \$1,000, the claimant must send the notice within 120 days. Regardless of whether pre-lien statement notice is required, the lien statement must be filed within six months of last work. KRS 376.080(1). Within 7 days of filing the lien statement the claimant must send a copy of the lien statement to the owner of the property. *Id.* The required contents of the lien statement are set forth in KRS 376.080.

B. Enforcement and Foreclosure

1. *Public Lien.* If the contractor or subcontractor whom the claimant alleges owes it for the work or materials provided files a protest with the public authority within 30 days of receiving the claim, the authority must send the protest by certified mail to the claimant. The claimant must initiate an action in the circuit court in the county in which the project is located within 30 days after the protest is mailed to the claimant by the public authority. KRS 376.250.

2. *Private Lien.* Within 12 months of filing the lien statement, the claimant must file an action to enforce the lien in the circuit court for the county in which the property is located. KRS 376.090. The action must name all lienholders of record as defendants and the matter may be referred for resolution to the master commissioner for the county in which the action is filed. KRS 376.110. The party filing the petition to enforce the lien should also file a *lis pendens* notice of the claim, thus shifting the burden to any subsequent lien holder to join in the action or risk losing such lien rights.

C. Ability to Waive and Limitations on Lien Rights

Any contract for construction entered after July 1, 2007 is now governed by the Kentucky Fairness in Construction Act, KRS 371.400 *et seq.* That Act provides that any provision in a construction contract requiring a party to waive, release or extinguish lien rights shall be against public policy, and a party may effectively waive lien rights only with respect to services or materials for which that party has actually been paid. KRS 371.405.

II. STATUTES OF LIMITATION AND RESPOSE

A. Statutes of Limitation

The following statutes of limitation may have application in a construction context:

1. *Sale of Goods.* A claim to enforce a contract for the sale of goods (such as materials and equipment for an HVAC system) must be brought within four years of the date of breach. Pursuant to the contract the parties can shorten the statute of limitations to not less than one year. The parties cannot extend the statute of limitations beyond the four year period. KRS 355.2-725.

2. *Professional Negligence.* An action for professional negligence (such as a claim against an architect for a design defect) shall be brought within one year from the date of the occurrence or the date when the cause of action was, or reasonably should have been, discovered by the party injured. KRS 413.245.

3. *Written Contract.* Action on a written contract not governed by a specific statute of limitation must be brought within 15 years. KRS 413.090.

4. *Oral Contract.* Actions to enforce an oral contract must be brought within 5 years. KRS 413.120.

5. *Building Code Violation.* Any party damaged as a result of a violation of KRS Chapter 198B or of the Uniform State Building Code must bring a cause of action within one year of the date of the damage being discovered and within 10 years of the date of the first occupation or settlement, whichever is sooner. KRS 198B.130(2).

B. Statutes of Repose

The Kentucky Supreme Court has repeatedly declared unconstitutional statutes of repose, which seek to “cut[] off an action before it exists.” *Coomer v. CSX Transp., Inc.*, 319 S.W.3d 366, 373 (Ky. 2010). Nonetheless, the Kentucky legislature has enacted and maintained two such statutes for the benefit of members of the construction industry, notwithstanding the judicial hostility.

KRS 413.135 provides, “No action to recover damages, whether based upon contract or sounding, resulting from or arising out of any deficiency in the construction components, design, planning, supervision, inspection or construction of any improvements to real property, or for any injury to the property, either real or personal, arising out of such deficiency, or for injury to the person or for wrongful death arising out of any such deficiency, shall be brought against any person after the expiration of seven (7) years following the substantial completion of such improvement.” Similarly, KRS 413.120(14) provides that an action against a builder for personal injuries suffered by any person must be brought within five (5) years and further states, “This cause of action shall be deemed to accrue at the time of original occupancy of the improvements which the builder caused to be erected.” *Id.*

As noted above, such statutes are not likely to withstand judicial scrutiny. In *Tabler v. Wallace*, 204 S.W.2d 179 (Ky. 1985), the Court struck down the prior incarnation of KRS 413.135 on the basis that it constituted “special legislation” forbidden by Section 59 of the Kentucky Constitution. The Court in *Tabler* soundly rebuked the legislature for favoring those in a particular industry:

The only apparent basis for the present legislation is that a special class, builders, architects and engineers involved in construction, faced with a growing exposure to litigation, lobbied for a statute limiting their liability. There is no social or economic basis presented to justify a special class, only their own self-interest. Other groups similarly situated do not share in

their legislative windfall. Their subjective reasons will not withstand public policy analysis.

Id. at 187.

Although KRS 413.135 was subsequently amended, and the appellate courts have not addressed directly the constitutionality of KRS 413.120(14), the analysis in *Tabler* remains the law of the Commonwealth, and defenses predicated on those statutes are unlikely to prevail.

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

Kentucky has enacted a statute requiring pre-suit notice of a construction defect claim although the legislation carries no real penalty for those who fail to comply with the mandate. KRS 411.258(1) requires a claimant in a construction defect case to serve written notice of the claim on the construction professional.” The statute then requires that the construction professional must respond to the claim with a proposal for resolution within twenty-one (21) days. KRS 411.258(2). If the construction professional fails to respond or if the claimant rejects the response, the claimant may then bring a claim. KRS 411.258(3). The statute provides that if a claimant files a complaint, counterclaim or crossclaim prior to meeting the requirements of this section, the court may issue an order holding the action in abeyance until the parties comply with this action. Accordingly, the “right to cure” statute may delay a party in moving forward with a civil action, but it will not prevent the filing of the complaint or provide the grounds for a dismissal.

IV. INSURANCE COVERAGE AND ALLOCATION ISSUES

A. General Coverage Issues

In the construction context, coverage under a commercial general liability (CGL) policy often depends on two related yet independent issues: (1) whether the construction activity causing the damage constitutes an “occurrence” and (2) whether the damage for which the claim seeks to recover constituted “property damage” allowed by the operative policy. A typical CGL policy would provide coverage only if the construction activities causing the damage constituted an “occurrence.” And the typical CGL policy excludes recovery for the cost of actually repairing the defective work.¹ The recent Kentucky Supreme Court decisions of *Bituminous Cas. Corp. v. Kenway Contracting, Inc.*, 240 S.W.3d 633 (Ky. 2007) and *Cincinnati Ins. Co. v. Motorists Mutual Ins. Co.*, 306 S.W.3d 69 (Ky. 2010), provide substantial guidance as to how Kentucky courts will resolve these issues in the future.

¹ The policies at issue in *Bituminous Cas. Corp. v. Kenway Contracting, Inc.*, 240 S.W.3d 633 (Ky. 2007), addressed below, precluded recovery for property damage to the “particular part of the real estate on which [the contractors] are performing operations” and “that particular part of any property that must be restored, repaired, or replaced because ‘your work’ was incorrectly performed on it” These exclusions are often referred to as the “business risk exclusions” and are “intended to distinguish between contract liability and tort liability.” *Id.* at 640.

In *Bituminous Cas.*, the Kentucky Supreme Court reviewed a case in which a contractor had been retained to convert a residence for commercial use. Part of that work required the demolition of a carport attached to the residence. As a result of communication problems between its employees, the contractor destroyed not only the carport but also a substantial part of the residential structure before recognizing the error.

The result in *Bituminous Cas.*, against the insurance company, reflects the rule that Kentucky law generally favors the insured in matters of insurance contract (i.e. policy) construction where there is any ambiguity. See *Dowell v. Safe Auto Ins. Co.* 208 S.W.3d 872, 877 (Ky. 2006) (“[I]t is a fundamental rule in the construction of insurance contracts that the contract should be liberally construed and any doubts resolved in favor of the insured.”) In *Bituminous Cas.* the Court held that the destruction of the residential structure constituted an “occurrence” and that the so called “business risk exclusions” were sufficiently ambiguous so as to be construed against the insurer.

In *Cincinnati Mutual*, the plaintiff attempted to recover damages associated with rebuilding a house that had allegedly been so poorly built it had to be razed five years after its initial construction. Notwithstanding the tendency to construe policy language against an insurer, in that case the Kentucky Supreme Court recently joined with the majority of jurisdictions in holding that faulty construction, “standing alone” does not constitute an “occurrence” for purposes of a CGL policy. The Court opined that to hold otherwise would “convert a policy for insurance into a performance bond.” *Id.* 75.

Future coverage determinations will likely turn on whether the insured can point to a specific action by the construction professional, beyond faulty construction “standing alone,” that caused the damage at issue. Moreover, to satisfy the typical CGL policy, the recovery sought will have to encompass more than the cost of the repair of the contractor’s own work.

B. Trigger of Coverage

Typically, insurance policies come in two standard forms. One is known as an “occurrence policy,” in which the event triggering coverage is the “occurrence” leading to the damage for which recovery is sought. An “occurrence” is typically defined as “an accident, including continuous or repeated exposure to substantially the same general harmful condition.” *Cincinnati Mutual*, S.W.3d at 73. The second type of policy is a “claims made policy” in which the trigger for coverage is the actual assertion of the claim by a third party for indemnification by the insured to a third party. The policy language will control what constitutes a “claim,” and such language is generally broadly worded to include not just the filing of a formal complaint or demand for arbitration but also a written notice of the intent to seek compensation for some negligent act or omission of the insured. Professional errors and omissions policies are typically “claims made” policies, while CGL policies are typically “occurrence” policies.

C. Allocation Among Insurers

Kentucky courts have struggled with the “policy clause drafting battle”² in which insurers attempt to craft language in their policies that will secure their position as the excess or secondary carrier rather than the primary insurer. Typically, such clauses take the form of “excess clauses” or “escape” clauses. In *Government Employees Ins. Co. v. Globe Indem. Co.*, 415 S.W. 2d 581 (Ky. 1967), Kentucky’s then highest court set out the pecking order in determining priorities among excess clauses, standard escape clauses, pro rata clauses and non-standard escape clauses. That determination looks closely at the specific language involved. Where it is found to be “indistinguishable in meaning and intent, [and] one cannot rationally choose between them [they are held] mutually repugnant and must be disregarded.” *Kentucky Farm Bureau Mut. Ins. Co. v. Shelter Mut. Ins. Co.*, 326 S.W.3d 803, 807 (Ky. 2010) (citations omitted).

In *Kentucky Farm Bureau*, the Kentucky Supreme Court addressed the inherent difficulty in reconciling two policies, each of which claimed to be secondary where there was any other coverage available. The Court noted that, previous decisions have focused on the specific language in the “excess” and “escape” clauses but rejected that approach. Kentucky’s highest court attempted a “simpler is better” approach, and, at least in the context of the case where a covered permissive driver was involved in an accident in a vehicle he did not own, found that the owner’s policy was always primary. *Id.* Unfortunately, the result in *Kentucky Farm Bureau* is unlikely to bring significant clarity in the construction context although it may indicate an intention of the appellate courts to focus on the relative positions of the insurers and the expectations of the insureds rather than merely the policy language itself in resolving allocation issues in the future.

V. CONTRACTUAL INDEMNIFICATION

Kentucky law generally recognizes a freedom to contract, and courts have generally held that indemnification provisions are enforceable so long as the intention of the parties is expressed in unequivocal terms. *Employers Mutual Liability Ins. Co. of Wis. v. Griffin Construction Co.*, 280 S.W.2d 179 (Ky. 1955). Where the bargaining positions of the parties are unequal, however, especially where one party seeks indemnity for its own negligence, courts are far less likely to enforce such provisions. *See Speedway v. Erwin*, 250 S.W.3d 339 (Ky. App. 2008).

Moreover, in the construction context, enforcement of any indemnification for one’s own negligence is expressly precluded by Kentucky’s Fairness in Construction Act: “Any provision contained in any construction services contract purporting to indemnify or hold harmless a contractor from that contractor’s own negligence or from the negligence of his or her agents, or employees is void and wholly unenforceable.” KRS 371.180(2).

²*Kentucky Farm Bureau Mut. Ins. Co. v. Shelter Mut. Ins. Co.*, 326 S.W.3d 803, 808 n. 4 (Ky. 2010).

VI. CONTINGENT PAYMENT AGREEMENTS

General contractors often seek to transfer the risk of being paid by the owner down to the subcontractors through so-called “pay when paid” or “pay if paid” clauses. Kentucky appellate courts have not yet addressed the enforceability of such provisions under Kentucky law³, and it is difficult to predict how courts will treat these attempts at pushing the risk of payment down stream to subcontractors or suppliers. On one hand, absent guidance from the appellate level, a trial court might very well be hesitant to declare unenforceable an agreed upon clause making payment to a subcontractor contingent on the receipt of payment by the general contractor from the owner. On the other hand, Kentucky’s Fairness in Construction Act provides that any contract for construction which requires a party to waive lien rights under KRS Chapter 376 is deemed unenforceable as contrary to public policy. Arguably, a contractual provision that precludes action by the subcontractor unless the general contractor has been paid by the owner for the subcontractor’s work would run afoul of those lien rights and thus be deemed unenforceable in the Commonwealth.

VII. DAMAGE LIMITATIONS

A. Personal Injury Damages v. Construction Defect Damages

Kentucky courts have struggled with the distinction between personal injury damages and the purely economic loss typical to construction defect claims. The Commonwealth’s courts have recognized that a contractor is protected by traditional privity requirements from liability for purely economic damages related to construction defects. *See Real Estate Marketing, Inc. v. Franz*, 885 S.W.2d 921 (Ky. 1994). In *Franz* the plaintiffs had purchased a home from the original owner, who had contracted with the builder. The Kentucky Supreme Court ruled that the subsequent purchases had no warranty or negligence claim against the builder arising from alleged structural defects with the home. The Court dismissed the warranty claim for lack of privity and dismissed the negligence claim because there was no “damaging event” upon which the claim could be based. The Court did, however, rule that claims based on a violation of the building code did extend to subsequent purchasers by virtue of KRS 198B.130, which expressly provided for a cause of action “to any person or party, . . . damages as a result of a violation of the [building code].” *Id.* at 927.

Where the alleged negligence of the builder has led to a personal injury, the limitations and protections of the privity requirement do not apply. In *Saylor v. Hall*, 497 S.W.2d 218 (Ky. 1973), Kentucky’s high court recognized that tenants could recover for the injury to their two children when a negligently constructed fireplace and mantle collapsed. The *Franz* court distinguished *Saylor* on the basis that the loss presented to it did not involve a “damaging event” as was present in *Saylor*. More logically, as discussed below, subsequent decisions have adopted

³ The closest any Kentucky Court has come to addressing the enforceability of “pay if paid” clauses was in *Dimension Serv. Corp. v. Don Jacobs Imps.*, 2014 Ky. App. Unpub. LEXIS 26. In that case, the court applied Ohio law and cited an Ohio case dealing with a “pay if paid” provision to address the issue of what constituted a condition precedent. In the context of that case, the court concluded there was no unsatisfied condition precedent so as to preclude enforcement of the contract.

the economic loss rule to maintain the distinction between the loss afforded by a purely economic loss as opposed to physical damage suffered to person or property.

B. Attorney's Fees Shifting and Limitations on Recovery

Under Kentucky law, attorney's fees are shifted only when provided for by statute or by contract. The chapter of the Kentucky Revised Statutes addressing housing, building and construction (KRS 198B.010 *et seq.*) provides for the recovery of fees in any action to recover for damages suffered as a result of violations of that Chapter or the Uniform State building Code. KRS 198B.130. Absent a contractual fee shifting provision, typical construction claims, including claims to enforce liens, do not allow for the recovery of fees.

C. Consequential Damages

Kentucky allows for the recovery of consequential damages in a claim for breach of contract. *Lawson v. Menefee*, 132 S.W.3d 890 (Ky. App. 2004). Parties to a contract may, however, limit recoverable damages to exclude consequential damages in certain commercial situations. KRS 355.2-219. Kentucky also allows the recovery of consequential damages in tort situations as well "when they can be accurately estimated, but to reject them, as too remote or speculative for judicial ascertainment, whenever they are incapable of accurate estimation." *Nucor Corp. v. General Electric Co.*, 812 S.W.2d 136, 142 (Ky. 1991) (citations omitted).

D. Delay and Disruption Damages

Delay and disruption damages are recoverable under Kentucky law. In fact, the Kentucky Fairness in Construction Act provides that any provision within a contract for construction that "purports to waive, release or extinguish the right of a contractor or subcontractor to recover costs, additional time, or damages, or obtain an equitable adjustment of the contract, for delays in performing the contract that are, in whole or in part, with the control of the [owner]" shall be unenforceable as contrary to public policy. KRS 371.405(2)(c).

E. Economic Loss Doctrine

The Kentucky Supreme Court has only recently, "charted a course in . . . the 'choppy waters' of the economic loss rule." *Giddings & Lewis, Inc. v. Industrial Risk Insurers, Inc.*, 348 S.W.3d 720 (Ky. 2011). In *Giddings* the Court addressed a case in which the manufacturer of an industrial lathe was protected from claims in negligence, strict liability and negligent misrepresentation by virtue of the economic loss rule (the "Rule"). The plaintiff had also asserted contract, warranty and fraud claims, which were dismissed for reasons unrelated to the Rule. The Kentucky Supreme Court set forth the justification for, and the parameters of, the Rule as follows:

Like the United States Supreme Court, we believe the parties' allocation of risk by contract should control without disturbance by the courts via product liability theories borne of a public policy interest in protecting people and their property from a dangerous

product. Thus, costs for repair or replacement of the product itself, lost profits and similar economic losses cannot be recovered pursuant to negligence or strict liability theories but are recoverable only under the parties' contract, including any express or implied warranties.

Id. at 17.

Giddings resolved any doubt as to whether Kentucky has officially adopted the Rule as the law in products liability cases where the sole damage was to the allegedly defective product itself. The Kentucky Court of Appeals has recently applied the Rule in the construction context in an unpublished opinion. *Cincinnati Ins. Co. v. Staggs & Fisher Consulting Engineers, Inc.*, 2013 Ky. App. Unpub. LEXIS 227. In *Staggs* an electrical contractor's insurer had paid the owner on a claim for "damage that was attributed to [the contractor's] electrical work" performed in connection with the new construction of the owner's building. *Id.* pp. 1-2. After paying the claim, the insurer sued another contractor, who had contracted with the owner, claiming that the damage had actually been caused by that third party's "negligent installation of a faulty transformer" as part of the same new construction. *Id.* p. 2. The Court of Appeals noted that because there had been no "personal injury or property damage to 'other property'" and because there had been no privity of contract, the economic loss doctrine applied.

In addition to citing the *Giddings*'s decision, the Court of Appeals in *Staggs* also quoted extensively from the concurrence in *Presnell Construction Managers, Inc. v. EH Construction*, 134 S.W.3d 575 (Ky. 2004), which had advocated for the adoption of the Rule in the context of a Construction dispute.

In *Presnell* a general contractor sued a construction manager. Both had contracted with the owner but not with one another. The general contractor alleged that the construction manager had failed to properly coordinate certain trades and had made misrepresentations upon which the general contractor had relied. The majority opinion rejected contractual and related claims because of lack of privity but adopted the *Restatement (Second) of Torts* § 552, recognizing a claim for negligent misrepresentation. The Court allowed that claim to go forward notwithstanding the lack of privity. The concurring opinion reached the same result, but urged for the adoption of the Rule and opined that the general contractor's negligence claim against the construction manager was barred by the Rule. The concurrence also found that the negligent misrepresentation claim could go forward but did so by reasoning that a negligent misrepresentation claim was a recognized exception to the Rule, relying on the decision of the Colorado Supreme Court in *Town of Alma v. Azco Const., Inc.* 10 P.3d 1256 (Colo. 2000).

Although it expressly adopted the Rule, *Giddings* took issue with the concurrence in *Presnell* and rejected the negligent misrepresentation exception where the Rule was implicated. *Giddings*, 348 S.W.3d at 746. In discussing *Presnell*, the *Giddings* opinion further noted, The *Presnell Construction* majority never mentioned the economic loss rule, perhaps because the absence of a contraction between the litigants, or the absence of a "product" or both of these facts, underscored its inapplicability." *Giddings* pp. 737-8. This distinction is important and

may signal the Supreme Court's view that the Rule should simply have no application between parties who have not contracted with one another.

Ultimately, however, the Court in *Giddings* did not expressly state that the concurrence in *Presnell* was simply wrong in applying the Rule to a claim between parties not in privity, and the Court of Appeals in *Staggs* applied the rule to dismiss a case between parties who had not contracted with one another. Where this ultimately leaves us is uncertain, except that it appears plain that Kentucky Courts will apply the Rule in the construction context and well as in matters asserting products liability.

F. Interest

Kentucky law provides that pre-judgment interest is available for liquidated amounts at the rate of 8% per annum. KRS 360.010. The determination as to the amount, if any, of interest is at the discretion of the trial judge and not the jury. *Nucor Corp. v. General Electric Co.*, 812 S.W.2d 136 (Ky. 2005).

The Kentucky Fairness in Construction Act provides that if a contractor holds money due a subcontractor for 15 days after receipt by the contractor, the subcontractor is entitled to recover interest at 12% per annum for any undisputed amounts. KRS 371.405(9).

G. Punitive Damages

The Kentucky legislature attempted to limit the award of punitive damages "only upon proving, by clear and convincing evidence, that the defendant from whom such damages are sought acted toward the plaintiff with oppression, fraud or malice." KRS 411.184(2). "Malice" is defined as conduct "which is specifically intended by the defendant to cause tangible or intangible injury to the plaintiff or conduct that is carried out by the defendant both with a flagrant indifference to the rights of the plaintiff and with a subjective awareness that such conduct will result in human death or bodily harm." KRS 411.184(1)(c). The limitation within the statute, implicitly precluding the award of punitive damages in cases of gross negligence, was declared unconstitutional under Kentucky's jural rights doctrine in the matter of *Williams v. Wilson*, 972 S.W.2d 260 (Ky. 1988).

On the other side of the punitive damages coin, the Kentucky Supreme Court has recognized the constitutional protection enunciated in *BMW of North America, Inc. v. Gore*, 517 U.S. 559 (1996) and that award must comport with due process standards and take into account, "the degree of reprehensibility . . .; the disparity between the harm or potential harm suffered by [plaintiffs] and [their] punitive damages award; and the difference between this remedy and the civil penalties authorized or imposed in comparable cases." *Craig & Bishop, Inc. v. Piles*, 247 S.W.3d 897 (Ky. 2008).

VIII. CASE LAW AND LEGISLATION UPDATE

In addition to *Cincinnati Insurance Company v. Motorists Mutual Insurance Company*, 306 S.W.3d 69 (Ky. 2010), *Giddings & Lewis, Inc. v. Industrial Risk Insurers, Inc.*, 2009-SC-

485, 2011 Ky. LEXIS 90 (Ky. June 16, 2011) and *Cincinnati Ins. Co. v. Staggs & Fisher Consulting Engineers, Inc.*, 2013 Ky. App. Unpub. LEXIS 227, discussed at length above in Sections IV A and VII E respectively, recent significant Kentucky cases addressing construction law issues include the following:

McBride v. Acuity, 2013 U.S. App. LEXIS 622(6th Cir.). After homeowners sued their contractor for negligent construction of their home, the contractor sought to compel its insurer to provide coverage for the claim. The U.S. District Court for the Western District of Kentucky and the Sixth Circuit Court of Appeals, sitting in diversity, in an unpublished opinion relied on the Kentucky Supreme Court's decision in *Cincinnati Insurance* to deny coverage on the grounds that faulty construction did not constitute an "occurrence" so as to trigger coverage under the commercial general liability policy. The District Court and the Sixth Circuit also rejected the argument that Kentucky would apply the "subcontractor's exception" to the general rule that a CGL policy did not cover loss suffered to the contractor's work when the cause was faulty construction.

Ryan v. Acuity, 2012 Ky. App. Unpub. LEXIS 514 A homeowner was sued by his contractor for non-payment and counterclaimed based on faulty construction. The homeowners also sued the contractor's insurer. The homeowner claimed that faulty grading work had led to damage to the foundation and excessive moisture in the basement. Kentucky Court of Appeals rejected the claim against the insurer relying on *Cincinnati Ins. Co. v. Motorists Mutual*. The homeowner attempted to distinguish his case from that at issue in *Cincinnati Ins.* on the basis that the grading work was a separate component of the construction apart from the foundation work that had been damaged. In rejecting that argument, the Court of Appeals noted that the insured contractor "had control of and contracted to construct the entire home." *Id.* p. 9

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I. MECHANIC'S LIEN BASICS

A. Private Projects.

The perfection of a mechanic's lien for private work is addressed at La. R.S. 9:4801, *et seq.* To perfect such a lien,

1. Pursuant to 9:4811, written notice of a contract between the general contractor and an owner must be filed as provided in R.S. 9:4831 before the contractor begins work on the immovable. The notice: (1) shall be signed by the owner and contractor; (2) shall contain the legal property description of the immovable upon which the work is to be performed and the name of the project; (3) shall identify the parties and give their mailing addresses; (4) shall state the price of the work or, if no price is fixed, describe the method by which the price is to be calculated and give an estimate of it; (5) shall state when payment of the price is to be made; (6) shall describe in general terms the work to be done.

2. Under 9:4831, the filing of a notice of contract, notice of termination, or statement of a claim or privilege is accomplished when it is filed for registry with the recorder of mortgages in the parish in which the work is to be performed. Each filing made with the recorder of mortgages which contains a reference to immovable property shall contain a description of the property sufficient to clearly and permanently identify the property. A description which includes the lot and/or square and/or subdivision or township and range is sufficient, but naming the street or mailing address without more is not sufficient.

3. Under 9:4820, the lien and/or privilege is effective as to third parties when: (1) notice of the contract is filed as required by R.S. 9:4811; or (2) the work is begun by placing materials at the site of the immovable to be used in the work or conducting other work at the site of the immovable the effect of which is visible from a simple inspection and reasonably indicates that the work has begun. Certain activities, such as surveying/ engineering work, the driving of test pilings, cutting or removal of trees and debris, placing of fill dirt, demolition of existing structures, the leveling of the land, or the placing of materials on the immovable having an aggregate price of less than \$100.00, shall not be considered as "work begun." If the work is for the addition, modification, or repair of an existing building or other construction, that part of the work performed before a third person's rights become effective shall, for the purposes of R.S. 9:4821, be considered a distinct work from the work performed after such rights become

effective if the cost of the work done, in labor and materials, is less than one hundred dollars during the thirty-day period immediately preceding the time such third person's rights become effective as to third persons.¹

4. Pursuant to 9:4822, if a notice of contract is properly and timely filed in the manner provided by 9:4811, the persons to whom a claim or privilege is granted by 9:4802 (subcontractors, laborers or employees of the contractor or a subcontractor, sellers, etc.) must within **30 days** after the filing of a notice of termination of the work: (1) file a statement of their claims or privilege; (2) deliver to the owner a copy of the statement of claim or privilege. A general contractor to whom a privilege has been preserved must file a statement of his privilege within **60 days** after the filing of the notice of termination or substantial completion of the work.

Finally, any party granted a claim and privilege by 9:4802 for work arising out of a general contract, **notice of which is not filed**, and other persons granted a privilege under 9:4801 or a claim and privilege under 9:4802 must file a statement of their respective claims and privileges within **60 days after**: (1) the filing of a notice of termination of the work; or (2) the substantial completion or abandonment of the work, if a notice of termination is not filed.

5. The effect of recordation of the statement of claim ceases as to third persons if no **lis pendens** is filed **within one year** of filing of the Statement of Claim with the respective mortgage office.²

B. Public Projects.

The perfection of a mechanic's lien for public work is addressed at La. R.S. 38:2241, *et seq.* To perfect such a lien,

1. Pursuant to 38:2241.1, whenever a public entity enters into a contract for the construction, alteration, or repair of any public works, the official representative of the public entity must record in the office of recorder of mortgages, in the parish where the work has been done, an acceptance of the work or of any specified area thereof upon substantial completion of the work. Those public entities which do not file such recordation shall require the contractor to file such recordation.

2. Under 38:2242(B), any claimant may, after the maturity of his claim and within 45 days after the recordation of acceptance of the work or of notice of default of the contractor or subcontractor, file a sworn statement of the amount due him with the governing authority having the work done and recorded in the office of the recorder of mortgages for the parish in which the work was done. Under 38:2242(E), if an architect or engineer has not been employed by the contractor or subcontractor, he has no claim to or privilege on the funds due the contractor or subcontractor.

3. Pursuant to 38:2242.1(F), the effect of filing for recordation of a statement of claim or privilege and the privilege preserved by it shall cease as to third persons unless a notice of *lis pendens* identifying the suit is filed within one year after the date of filing the claim or privilege.

4. If at the expiration of the 45 days any filed and recorded claims are unpaid, the public entity shall file a petition in the proper court of the parish where the work was done, citing all claimants and the contractor, subcontractor, and surety on the bond and asserting any claims it has against any of them, and shall require the claimants to assert their claims. If the governing authority fails to file the proceeding, any claimant may do so.³

II. STATUTES OF LIMITATION AND REPOSE

A. Statute of Limitations (“Prescription”)

1. Contract for Sale.

Redhibitory actions against a seller who did not know the existence of a defect in the thing sold prescribes four years from the day of delivery or one year from the day the defect was discovered, whichever occurs first.⁴ However, when the defect is of residential or commercial immovable property, an action for redhibition against a seller who did not know of the existence of the defect prescribes in one year from the day delivery of the property was made. Nevertheless, if the seller knew, or is presumed to have known, of the existence of a defect, the action prescribes one year from the day the defect was discovered by the buyer.⁵

2. Contract action to recover for personal injuries.

The statute of limitation for a contract action to recover for personal injuries is one year.⁶

3. Contract actions.

An action against a contractor or an architect on account of defects of construction, renovation, or repair of buildings and other works is subject to a liberative prescription of ten years.⁷

4. Enforcement of a Privilege/ Lien against the Owner/Contractor.

Under the Private Works Act, an action on a privilege, or a claim against the owner/contractor must be brought one year from the date the lien was filed.⁸

Under the Public Works Act, action against the surety or the contractor (or both) must be made within one year from the registry of acceptance of the work or of notice of default of the contractor;

Additionally, under the Public Works Act, before any claimant having a direct contractual relationship with a subcontractor but **no contractual relationship with the contractor** shall have a right of action against the contractor or the surety on the bond furnished by the contractor, he shall in addition to the notice and recordation required in R.S. 38:2242(B) **give written notice to said contractor within forty-five days from the recordation of the notice of acceptance** by the owner of the work or notice by the owner of default, stating 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 or service was done or performed.⁹

5. Public Works.

Actions against the contractor on the contract or on the bond, or against the contractor or the surety or both on the bond furnished by the contractor, all in connection with the construction, alteration, or repair of any public works let by the state or any of its agencies, boards or subdivisions prescribes five years from the substantial completion or acceptance of such work, whichever occurs first, or of notice of default of the contractor.¹⁰

Actions by the contractor on the contract or on the bond, or by the contractor or the surety or both on the bond furnished by the contractor, against the state, or any of its agencies, boards or subdivisions, all in connection with the construction, alteration, or repair of any public works prescribes five years from the completion, substantial completion or acceptance of such work, whichever occurs first, or of notice of default of the contractor or other termination of the contract.¹¹ La. R.S. 38:2189.1.

B. Statute of Repose (“Peremption”)

La. R.S. 9:2772(A) provides, in pertinent part, that "no action, whether ex contractu, ex delicto, or otherwise, ... shall be brought against any person performing or furnishing ... the construction of an improvement to immovable property (1) more than 5 years after the date of registry in the mortgage office of acceptance of the work by owner; or (2) if no such acceptance is recorded within six months from the date the owner has occupied or taken possession of the improvement, in whole or in part, more than 5 years after the improvement has been thus occupied by the owner ..."

The statute does not encompass allegedly deliberate fraudulent planning and building.¹²

The phrase "construction of an improvement to immovable property" as used in the statute for actions arising out of such improvements refers to renovations as well as to new construction.¹³

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

Under the Private Works Act, sellers of movables, or materialmen, are required to:

[T]he **seller of movables** shall deliver a notice of nonpayment to the owner at least ten days before filing a statement of his claim and privilege. The notice shall be served by registered or certified mail, return receipt requested, and shall contain the name and address of the seller of movables, a general description of the materials provided, a description sufficient to identify the immovable property against which a lien may be claimed, and a written statement of the seller's lien rights for the total amount owed, plus interest and recordation fees.¹⁴

Similarly, the notice required for materialmen under the Public Works Act is as follows:

[I]f the materialman has not been paid by the subcontractor and has not sent notice of nonpayment to the general contractor and the

owner, then the materialman shall lose his right to file a privilege or lien on the immovable property. The return receipt indicating that certified mail was properly addressed to the last known address of the general contractor and the owner and deposited in the U.S. mail on or before seventy-five days from the last day of the month in which the material was delivered, regardless of whether the certified mail was actually delivered, refused, or unclaimed satisfies the notice provision hereof or no later than the statutory lien period, whichever comes first.¹⁵

Lastly, lessors of movables are also required to provide notice prior to filing a lien on the project, the specifics of which are addressed in Section VIII below.

IV. INSURANCE COVERAGE AND ALLOCATION ISSUES

A. General Coverage Issues

Louisiana accepts as normative standard commercial general liabilities (“CGLs”) policies, as well as builder’s risk workers’ compensation and professional liability policies.

Typically, general liability policies exclude coverage for professional acts or services, all of which should be defined by the policy itself. In *North American Treatment Systems, Inc. v. Scottsdale Ins. Co.*, the court found “professional services” to typically mean “services performed by one in the ordinary course of the practice of his profession, on behalf of another, pursuant to some agreement, express or implied, and for which it could reasonably be expected compensation would be due.”¹⁶ Whether professional judgment are required of a particular skill or special training, or whether the act could be done by an unskilled person are also considered.

B. Trigger of Coverage

Generally, coverage begins on the effective date of the policy. Coverage ends when the contract expires. Furthermore, most policies are classified as either “occurrence” based or “claims-made” based. An “occurrence” based policy provides coverage for acts or event that occurred during the policy period, regardless of when the claim is actually made. As such, coverage attaches when the occurrence takes place even though a claim has not been made yet.¹⁷ On the other hand, a “claims made” policy provides coverage for claims made during the policy’s effective dates.

C. Additional Insurance Issues

Determining who an additional insured is under the policy is just one of many important insurance related issues on construction projects. Louisiana jurisprudence has held that interpretations of additional insured endorsements are questions of law.¹⁸ Previously, courts generally held that an insurance company’s liability only extended coverage to an additional insured when the additional insured’s liability was derivative of the named insured. However, in *Jones v. Capital Enterprises*, the court looked to the policy and held that the insurance company

“failed to include language in its policy clearly reflecting the intent that coverage extended only to the named insured’s wrongs.”

V. CONTRACTUAL INDEMNIFICATION

Louisiana statutory law only limits the enforceability of indemnity provisions in public construction contracts. La. R.S. 38:2216(G) states that:

[A]ny provision contained in a public contract, other than a contract of insurance, providing for a hold harmless or indemnity agreement, or both,

(1) from the contractor to the public body for damages arising out of injuries or property damage to third parties caused by the negligence of the public body, its employees, or agents, or,

(2) from the contractor to any architect, landscape architect, engineer, or land surveyor engaged by the public body for such damages caused by the negligence of such architect, landscape architect, engineer or land surveyor is contrary to the policy of the state, and any and all such provisions in any and all contracts are null and void.

However, the statute merely bars a contractor from indemnifying a public body for damages to third parties caused by the public body's negligence. It does not bar indemnity due to claims of strict liability or claims of damages because of defective work performed by the contractor.¹⁹

With respect to private construction contracts, indemnity provisions are generally valid. Interpretation of such a contract requires an application of the general rules governing the interpretation of other contracts.²⁰ Consequently, "[t]he contract of indemnity forms the law between the parties and must be interpreted according to its own terms and conditions."²¹ "Interpretation of the contract is the determination of the common intent of the parties and when the words of the contract are clear and explicit and lead to no absurd consequences, no further interpretation may be made in search of the parties' intent."²² Moreover, "[t]he determination of the intention of the parties is the foremost requirement in the interpretation and construction of a contract."²³ However, when an indemnity contract contains anything doubtful, the court must ascertain the common intention of the parties, rather than adhere to the literal meaning of its terms.²⁴ Notwithstanding an important caveat: a contract indemnifying an indemnitee against his own negligence must be strictly construed, and the contract will not be enforceable unless such an intention was expressed in unequivocal terms.²⁵

VI. CONTINGENT PAYMENT AGREEMENTS

Contingent payment agreements are typically recognized in Louisiana jurisprudence as “pay-when-paid” or “pay-if-paid” provisions and are generally enforceable based on the fundamental notion of contractual freedom.²⁶ Such agreements commonly appear within construction subcontracts. While some courts have used the phrases “pay-when-paid” and “pay-if-paid” clauses interchangeably, Louisiana courts construe “pay-when-paid” clauses differently

than “pay-if-paid” provisions. In Louisiana, “pay-if-paid” provisions are construed as transferring the risk of owner nonpayment to the subcontractor whereas “pay-when-paid” provisions are interpreted as simply delaying payment to a subcontractor until the owner pays the general contractor.²⁷

The Louisiana Supreme court has expressly enforced “pay-when-paid” provisions and interpreted them not as suspensive conditions, but rather as provisions creating terms for payment relating “to the time when [the] contractor must pay, and not the fact or certainty of such payment.”²⁸ Under these payment agreements, a contractor’s obligation to pay the subcontractor arises upon the receipt of payment by the owner. Louisiana jurisprudence generally construes these payment provisions to mean that the contractor’s obligation to make payment is suspended for a reasonable amount of time for the contractor to receive payment from the owner.²⁹ Accordingly, such agreements have been viewed by Louisiana courts as creating a timing mechanism only and not as imposing a condition precedent to the obligation to ever make payment.³⁰ Thus, Louisiana courts do not interpret these provisions as shifting the risk of nonpayment by the owner to the subcontractor.

Louisiana law does recognize that contingent payment provisions can be very burdensome for the subcontractor, particularly in situations where payments are withheld from the general contractor for a prolonged period of time typically arising in the event of an owner-general contractor dispute, or where the owner becomes financially unable to make any further payments to the general contractor. Thus, even when a “pay-when-paid” provision appears within a contract, Louisiana courts will typically require payment to the subcontractor by the general contractor within a reasonable period of time.

Additionally, in 1987, La. R.S. 9:2784 was amended to provide that if a contractor or subcontractor, without reasonable cause, fails to make any payment to the subcontractors or suppliers within fourteen consecutive days of the receipt of payment from the owner for improvements to an immovable, the contractor or subcontractor shall pay to the subcontractors and suppliers, in addition to the payment, a penalty in the amount of one-half of one percent of the amount due, per day, not to exceed 15% of the outstanding balance, together with reasonable attorneys’ fees.³¹ Further, under La. R.S. 14:202, a contractor may face criminal penalty including jail and fines for misappropriation of funds. If a contractor only receives partial payment from the owner, to escape criminal and civil liability, the contractor must still apply all funds to the payment of subcontractors, laborers, and materials, even if the amount paid is not adequate to pay all of the outstanding bills.³²

The Louisiana Supreme Court has yet to directly address the enforceability of “pay-if-paid” provisions, however, Louisiana appellate courts have upheld such provisions as creating a valid suspensive condition.³³ Louisiana Civil Code article 1767 provides that an obligation subject to a suspensive condition depends upon the occurrence of an uncertain event. Accordingly, under Louisiana law, if a “pay-if-paid” provision appears within a construction subcontract, a general contractor’s obligation to pay the subcontractor arises if, and only if, he is paid by the owner.

However, because “pay-if-paid” provisions create a possibility that there may be an utter and complete failure of any payment to the subcontractor, Louisiana jurisprudence requires parties to use explicit language to indicate that payment by the owner is not contemplated by the parties as a reasonably certain event.³⁴ Further, as a general rule of contractual interpretation, Louisiana jurisprudence holds that contractual provisions should be construed as *not* to be suspensive conditions whenever possible.³⁵

VII. DAMAGE LIMITATIONS

A. Private Projects

For private works, “[a]ny seller ... whose claims have not been settled may file any action for the amount due, including reasonable attorney fees and court costs.”³⁶ In cases of fraud, where the amount misapplied is one thousand dollars or less, the civil penalties shall be not less than two hundred fifty dollars nor more than seven hundred fifty dollars. Where misapplied funds total \$1,000.00 or greater, civil penalties shall be assessed at a rate between \$500.00 and \$1,000.00 per \$1,000.00 misapplied.³⁷

B. Public Projects

For public works, La. R.S. 38:2246(A) provides that:

After amicable demand for payment has been made on the principal and surety and thirty days have elapsed without payment being made, any claimant recovering the full amount of his timely and properly recorded or sworn claim ... shall be allowed ten percent attorney's fees which shall be taxed in the judgment on the amount recovered.

C. Louisiana Unfair Trade Practices Act

The Louisiana Unfair Trade Practices Act (“LUTPA”) codified in La. R.S. 51:1401 *et seq.* dictates that persons subject to unfair and/or deceptive business practices have a civil action and can recover treble damages and attorney’s fees against the opposing party. The wording of the statute is extremely broad and undoubtedly encompasses conduct on construction projects.

D. Interest

Louisiana allows for the collection of legal interest in any contracts dispute.³⁸

VIII. CASE LAW AND LEGISLATION UPDATE

There have been a few noteworthy legislative or jurisprudential changes in the domain of construction law in Louisiana since the publication of the 2011 Construction Law Compendium, some of which are as follows:

A. Peremption Cases

In *Ebinger, et ux. v. Venus Construction Corp., et al.*, the Louisiana Supreme Court addressed the commencement of the peremptive period under New Home Warranty Act. In *Ebinger*, the homeowners brought an action against a contractor under New Home Warranty Act, alleging that defects in the home's foundation had caused cracks in the drywall, tile, brick walls, and floor. The contractor then filed a third-party demand seeking indemnification from engineer and subcontractor that supplied foundation. The Louisiana Supreme Court construed La. R.S. 9:2772, which establishes a peremptive period for actions against residential building **contractors**, to determine whether the construction company's third-party demand against a subcontractor was time-barred. The court held that the five year peremptive period under the Act began to run when the certificate of occupancy was issued for the house and not when homeowner discovered cracks in brick veneer of the foundation. The court concluded that the contractor's claim against the subcontractor was perempted before its cause of action arose because the peremptive period began when the Ebingers occupied the residence in 1997.³⁹

In *Bossier Parish School Bd. v. LeBlanc*, the court held that the five-year preemptive period of the Public Works Act applied to **all** claims, sounding in contract and tort, against the public works **contractor**, noting that, while there are different categories of actions, when the suit is between a public entity and a **contractor** and arises out of performance of a public work contract, **all claims** are subject to the time limitation set forth in the Public Works Act.⁴⁰

B. Lien Notice Changes for Lessors

In August, 2013, La. R.S. 9:4802(G) was amended to change the notice provision for lessors wishing to file a lien. Historically, lessors merely had to provide a copy of the full lease to the owner (and general contractor if items were leased to a subcontractor) within ten (10) days after the leased items were placed at the worksite. The change in the law eliminates the delivery of lease and requires "notice" to be sent (under the same 10 day period) by the lessor containing the following information: 1. Address of the lessor; 2. Address of the lessee; 3. A description "sufficient to identify the movable property placed at the site of the immovable" for use in the work; 4. Terms of the rental and terms of payment; and 5. The notice must be signed by the lessor and lessee.

Without question, the last requirement is the biggest change to the statute. So, we recommend lessor to have a form pre-drafted and require that form be signed by the lessee along with the lease itself.

Also, it should be noted that the similar provision in the Public Works Act, La R.S. 38:2242 (C)(1) was not amended and still requires lessors provide a full copy of the lease in order to preserve their rights against the statutory payment bond.

C. Lien Enforcement Period Shortened Under Private Works Act

Effective August 1, 2013, lien claimants must file suit to enforce their Private Works Act liens within one year following the date the lien was filed. Previously, the Act allowed suits to

enforce liens to be filed no later than one year from the expiration of the relevant deadline for filing liens.⁴¹

¹ La. R.S. 9:4820(B).

² La. R.S. 9:4833(F).

³ La. R.S. 38:2243.

⁴ A defect is redhibitory when it renders the thing useless, or its use so inconvenient that it must be presumed that a buyer would not have bought the thing had he known of the defect. The existence of such a defect gives the buyer the right to obtain rescission of the sale. A defect is redhibitory also when, without rendering the thing totally useless, it diminishes its usefulness or its value so that it must be presumed that a buyer would still have bought it but for a lesser price. The existence of such a defect limits the right of a buyer to a reduction of the price. La. C.C. art. 2520.

⁵ La. C.C. art. 2534.

⁶ La. C.C. art. 3492.

⁷ La. C.C. art. 3500.

⁸ La. R.S. 9:4823.

⁹ La. R.S. 38:2247.

¹⁰ La. R.S. 38:2189.

¹¹ La. R.S. 38:2189.1.

¹² *Academy Park Improvement Assoc. v. City of New Orleans*, 469 So.2d 2, 4 (La.App. 4th Cir. 1985).

¹³ *Dugas v. Cacioppo*, 583 So.2d 26, 27 (La.App. 5th Cir. 1991).

¹⁴ La. R.S. 9:4802(G)2.

¹⁵ La. R.S. 38:2242(F).

¹⁶ 943 So. 2d 429 (La. App. 1 Cir. 2006)

¹⁷ *Guthrie v. Louisiana Medical Mut. Ins. Co.*, 975 So.2d 804 (La. App. 2008)

¹⁸ *Jones v. Capital Enterprises, Inc.*, 89 So.3d 474 (La. App. 4 Cir. 2012)

¹⁹ *Roberts v. State, through DOTD*, 576 So.2d 85, 90 (La.App. 2nd Cir. 1991); *Recotta Trucking Co. v. State*, 573 So.2d 526, 527 (La.App. 4th Cir. 1990).

²⁰ *Yocum v. City of Minden*, 566 So.2d 1082, 1086 (La.App. 2nd Cir. 1990).

²¹ *Id.*

²² *Id.*

²³ *Id.*

²⁴ *Polozola v. Garlock, Inc.*, 343 So.2d 1000, 1003 (La. 1977).

²⁵ *Id.*

²⁶ See *Southern States Masonry, Inc. v. J.A. Jones Const. Co.*, 507 So.2d 198, 204 (La. 1987). *Imagine Const., Inc. v. Centex Landis Const. Co., Inc.*, 707 So.2d 500, 502 (La.App. 4 Cir. 1998). *Vector Elect. & Controls, Inc. v. JE Merit Constr., Inc.*, 2006 WL 3208462, at *4 (La.App. 1 Cir. 2006). Louisiana Civil Code article 1971 states, “[P]arties are free to contract for any object that is lawful, possible, and determined or determinable.”

²⁷ *Imagine Const., Inc.*, 707 So.2d at 502.

²⁸ *Southern States Masonry, Inc.*, 507 So.2d 198, 204. The Louisiana Supreme Court has recognized that the common law term “condition precedent” is analogous to the civilian term “suspensive condition.” *Id.* at 204 n. 15.

²⁹ *Id.* at 204.

³⁰ *Id.* See also *Chartres Corp. v. Charles Carter & Co., Inc.*, 346 So.2d 796 (La.App. 1 Cir. 1977); *Pelican Const. Co. v. Sewerage and Water Bd. of New Orleans*, 240 So.2d 556 (La.App. 4 Cir. 1970).

³¹ La. R.S. 9:2784(C). However, in the event the claimant loses he is obligated to pay all costs and attorneys' fees of the defendant. *Id.*

³² *State v. Weems*, 595 So.2d 358 (La. App. 2 Cir. 1992); *State v. Marshall*, 808 So.2d 376 (La.App. 1 Cir. 2000)

³³ *Imagine Const., Inc.*, 707 So.2d at 502; see also *Vector Elect. & Controls, Inc.*, 2006 WL 3208462, at *4.

³⁴ *C Bel for Awnings, Inc. v. Blaine-Hays Const. Co.*, 532 So.2d 830 (La.App. 4 Cir. 1988). See also *Artificial Lift, Inc. v. Production Specialties, Inc.*, 626 So.2d 859 (La.App. 3d Cir. 1993).

³⁵ *Southern States Masonry, Inc.*, 507 So.2d at 204.

³⁶ La. R.S. 9:4814(A).

³⁷ La. R.S. 9:4814.

³⁸ La. R.S. 9:3500.

³⁹ *Ebinger, et ux. v. Venus Construction Corp., et al.*, 2010–C–2516 (La. 01/07/11).

⁴⁰ *Bossier Parish School Bd. v. LeBlanc*, 48 So.3d 35545, 632 (La.App. 2 Cir. 9/22/10).

⁴¹ La. R.S. 9:4823.

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I. MECHANIC'S LIEN BASICS

Mechanics' liens provide a vehicle by which contractors, subcontractors, suppliers, surveyors, architects, engineers, real estate agents, and others can obtain a security interest in real property they improve or that benefit from their services. In Maine, such mechanic's liens are governed by the archaic, entangled provisions of 10 Maine Revised Statutes Annotated ("M.R.S.A.") §3251 *et seq.* Landscape gardeners have their own additional lien provisions, 10 M.R.S.A. §3501, as do laborers who work with or furnish lime, limerock, granite, and slate, 10 M.R.S.A. §3651, and those who provide monuments, tablets, headstones, vaults, posts, curbing, and other monumental work or materials, 10 M.R.S.A. §3701.

A. Pre-Lien Notice

There is no notice required pre-lien. The lien is created as soon as the claimant provides the labor, furnishes the materials, or performs the services. 10 M.R.S.A. §3251. However, as discussed below, notice is required in certain circumstances in connection with the enforcement of the lien.

B. Mechanic's Lien Statement

If the claimant is not under contract with the owner, 10 M.R.S.A. §3253(2), the lien granted by Section 3251 is dissolved unless the claimant, within 90 days after ceasing to provide labor, to furnish materials, or to perform services, 10 M.R.S.A. §3253(1), files in the office of the register of deeds in the county or registry district in which the property is situated a sworn statement of the net amount due the claimant, together with a description of the property subject to the lien that is sufficient to identify the property and the owner. 10 M.R.S.A. §3253(1)(A). A copy of the statement must be mailed to the owner by ordinary mail. 10 M.R.S.A. §3253(1)(B).

C. Foreclosure

The lien is preserved and enforced by filing an action against the debtor, the owner of the property, and all other interested parties within 120 days after the last of the labor, materials, or services were furnished. 10 M.R.S.A. §3255(1). This period is extended under limited

circumstances, *id.*, such as when the owner dies, is adjudicated bankrupt, etc., 10 M.R.S.A. §3256. *Bona fide* purchasers for value have certain protections under the statute. 10 M.R.S.A. §3255(2).

With regard to construction intended for or used, in whole or in part, for residential purposes, the lien may be enforced only against the property affected to the extent of the balance due to the person with whom the owner has directly contracted. This defense is available where payment by the owner to the person with whom he directly contracted was made prior to (1) commencement of the action to enforce the lien by the person performing or furnishing labor, materials, or services without a contract with the owner or (2) a written notice to the owner stating that a lien may be claimed and containing a specific warning at the top of the notice about paying twice. 10 M.R.S.A. §3255(3). The total amount due from the owner to those with whom he did not contract shall not exceed the balance due from the owner to the person with whom he directly contracted. *Id.*

D. Sale

The court may decree that the property liened shall be sold at a particular place and time and under specific conditions and order an adjournment from time to time. A deed of the officer of the court recorded in the registry of deeds where the land lies within 3 months after the sale shall convey all the title of the debtor and the owner in the property ordered to be sold. 10 M.R.S.A. §3259. For just cause, the owner may be granted a right to redeem the property from such sale. If the court determines that the whole of the land on which the lien exists is not necessary to satisfy the lien, it will describe in the order of sale a suitable portion, and only that portion shall be sold. 10 M.R.S.A. §3259.

In addition to the sale remedy provided, liens can be enforced by attachment obtained by filing an action. The attachment must be made within 180 days after the last of the labor, materials, or services were performed or furnished. 10 M.R.S.A. §3262.

E. Note for Public Projects

Payment and performance bonds are required for the full amount of the contract on projects costing more than \$125,000. 14 M.R.S.A. §871. An exception applies for situations when the public body advertises for sealed proposals but no proposals are received from qualified, bonded contractors. In that case, contracts may be awarded to non-bonded contractors. 5 M.R.S.A. §1745.

II. STATUTES OF LIMITATION AND REPOSE

The statutes of limitation and repose applicable to construction or design defect claims are contained in several statutes, depending on the party against whom the claim is asserted and the tort, contract, or warranty nature of the claim.

A. Statutes of Limitation and Limitations on Application of Statutes

Breach of Contract and Tort: All civil actions for breach of contract and unintentional torts shall be commenced within six (6) years after the cause of action accrues, in general. 14 M.R.S.A. §752.

Actions for equitable contribution and indemnification are governed by this statute as well, unless asserted against design professionals protected by the statute of repose, 14 M.R.S.A. §752-A. The cause of action accrues for contribution or indemnification when a judgment or settlement has been paid by the indemnitee or when the indemnitee is subject to some harm, such as liability to injury accompanied by inconvenience or damage.¹

Sale of Goods: Under the Uniform Commercial Code (“U.C.C.”), an action for breach of a contract for the sale of construction materials that are “goods” is four (4) years after the cause of action accrues. 11 M.R.S.A. §2-725. The parties to a contract may agree to a shorter period of limitation not less than one (1) year, however.

To the extent one material fails and damages another part of the construction, the claim is one for a product’s damage to itself. Such claims are governed by the breach of warranty statute of limitations of the Uniform Commercial Code, which is four (4) years.² Arguments that the defective materials installed within the structure of a building damaged other parts of the building and, therefore, damaged “other property” so as to trigger tort liability in hopes of gaining the benefit of the longer, six-year statute of limitations provided in 14 M.R.S.A. §752 have failed.³

B. Statute of Repose and Limitations on Application of Statutes

All civil actions for malpractice or professional negligence against architects or engineers duly licensed or registered shall be commenced within four (4) years after such malpractice or negligence is discovered, but in no event shall any such action be commenced more than ten (10) years after the substantial completion of the construction contract or the substantial completion of the services provided, if a construction contract is not involved. 14 M.R.S.A. §752-A. The parties may change this limitations period by a valid contract.

There is no comparable statute of repose available to builders, and the discovery rule does not apply to parties who are not design professionals.⁴

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

There is no Maine case law requiring notice and an opportunity to cure as a prerequisite to pursuing an action against a contractor for defective construction or a designer for design defects. Maine courts are likely to follow the notice requirements of the contract and the case law of any other jurisdiction they find most persuasive on the issue.

The notice requirements of the Uniform Commercial Code apply to claims for defective goods such as construction materials. The buyer must notify the seller of the breach within a reasonable time after he discovers, or should have discovered, the deficiency in the materials, or else be barred from any remedy. 11 M.R.S.A. 2-607(3)(a).

A breach of the Home Construction Contract Act (“HCCA”), 10 M.R.S.A. §1486 *et seq.*, is deemed a *prima facie* breach of the Unfair Trade Practices Act (“UTPA”), 10 M.R.S.A. §1490(1). A homeowner proving such breach is entitled to attorney’s fees, 5 M.R.S.A. §213(2), and penalties, 10 M.R.S.A. §1490(2). At least 30 days prior to the filing of an action for damages based on a breach of the Home Construction Contract Act or another unfair trade practice, a written demand for relief must be mailed or delivered to any prospective respondent at the respondent’s last known address identifying the claimant and reasonably describing the unfair and deceptive act or practice relied upon and the injuries suffered. 5 M.R.S.A. §213 (1-A). A person receiving a demand for relief may make a written tender of settlement or, if a court action has been filed, an offer of judgment. If the judgment obtained in court by a claimant is not more favorable than any rejected tender of settlement or offer of judgment, the claimant may not recover attorney’s fees or costs incurred after the more favorable tender of settlement or offer of judgment. *Id.* If a notice is not sent according to the UTPA, then the action still may be maintained, but the homeowner probably does not recover attorney’s fees or costs.⁵

IV. INSURANCE COVERAGE AND ALLOCATION ISSUES

A standard commercial general liability (“CGL”) policy provides coverage for those amounts that the insured is legally liable to pay because of bodily injury or property damage that occurs during the applicable policy period.

A. General Coverage Issues

Under Maine law, exclusions and exceptions in CGL insurance policies are disfavored and are construed strictly against the insurer. Any ambiguity in an insurance policy must be resolved against the insurer and in favor of coverage. An insurance contract is ambiguous if it is reasonably susceptible to different interpretations.⁶

The duty to defend an insured under a CGL policy in Maine is broader than the duty to indemnify. It is determined using the “comparison test,” whereby the allegations in the complaint are compared with the terms of the insurance policy. All evidence extrinsic to the allegations pleaded within the four corners of the complaint is ignored even if the evidence is agreed upon and undisputed by the insured, the third-party claimant, or the insurer.⁷ The duty to defend is triggered if the complaint reveals any potential that the facts ultimately proved may come within coverage.⁸ In other words, the Court will not uphold an insurer’s denial of a defense to its insured unless the allegations in the complaint give rise to no set of facts that would establish coverage.⁹

B. Trigger of Coverage

Maine has not taken a position on which of the various triggers, e.g., manifestation, injury-in-fact, exposure, or continuous, determine which liability policy must answer for the claim. Assuming multiple policies apply to the same claim, Maine courts give effect to the “other insurance” clauses of the policies where possible. Logically inconsistent clauses are to be disregarded as repugnant to one another, and each policy is deemed to provide primary

coverage.¹⁰ An example is when multiple policies contain excess insurance clauses. In such situations Maine has adopted the minority rule requiring each insurer to contribute equally up to the limits of the lower policy, with any remaining portion of the loss then being paid from the larger policy up to its limits.¹¹

V. CONTRACTUAL INDEMNIFICATION

Maine common law and statutory law have left the area of contractual indemnification in construction contracts largely unmolested. The parties generally get what the contract states, so long as it is stated clearly and unambiguously. However, indemnification for one's own negligence is disfavored in Maine. Courts will scrutinize such provisions and construe them strictly against indemnification if they are not expressly, specifically, and clearly worded to achieve that result.¹²

Similarly, insurance procurement clauses are enforceable based on the intent of the parties as evidenced by the written contract. However, the strict scrutiny applicable to indemnity clauses for one's own negligence applies equally to agreements to procure insurance for another party.¹³

Interestingly, Maine courts employ more lenient rules of interpretation for insurance procurement clauses when those clauses operate to waive subrogation rights. In that context, insurance procurement clauses intended to cover a party for its own negligence are not held to the strict scrutiny applicable to indemnification agreements. Contractual allocations of risk to insurers by way of insurance procurement clauses are favored under the law.¹⁴

VI. CONTINGENT PAYMENT AGREEMENTS

The Maine prompt payment statute provides a tool that a contractor or a subcontractor can use to collect unpaid bills.¹ The statute allows enhanced interest and recovery of attorney's fees for the "substantially prevailing party." A contractor, or subcontractor, seeking payment must prove by way of a breach of a contract claim or a *quantum meruit* claim that he is entitled to payment. Then, in order for a contractor or subcontractor to recover the additional penalties and fees under the statute, it must prove that the owner did not pay in accordance with the payment terms in the contract. Absent a contract an owner must pay within twenty days. Absent a contract a subcontractor must prove: 1. the services were performed in accordance with the agreement between the parties, 2. the owner has made the progress or final payment; 3. the subcontractor has invoiced the work; and 4. the contractor failed to make payment within seven days after either the invoice or the progress payment for the owner, whichever is later.¹⁵

The statute allows the contractor to withhold payment "in an amount equaling the value of any good faith claim against the invoicing . . . subcontractor,"² even if paid for that subcontractor's work by the owner. A subcontractor seeking recovery from a general contractor

¹ 10 M.R.S.A. § 1111 *et seq.*

² 10 M.S.R.A. § 1118(1).

must prove that the general contractor was paid by the owner in order to recover under the statute.

VII. DAMAGES LIMITATIONS

A. Personal Injury Damages vs. Construction Defect Damages

In Maine, the measure of damages for breach of a construction contract is difference in value between value of performance contracted for and value of performance actually rendered.¹⁶ This difference may be proved either by diminution in market value or by amount reasonably required to remedy defect.¹⁷

B. Attorneys' Fees

Attorney's fees generally are not recoverable unless expressly permitted by contract or by statute. A mere breach of contract does not permit a party to recovery attorney's fees unless the contract expressly provides for such a recovery.¹⁸ However, certain egregious conduct will warrant an award of attorney's fees for breaching a contract, for abusing legal process etc., but only in the most extraordinary circumstances.¹⁹

Maine has not recognized the "collateral litigation" exception to the American Rule governing the recovery of attorney's fees.²⁰ That exception applies in other jurisdictions to permit compensation of attorneys fees when prior collateral litigation with a third party was caused by the breach of a contract or breach of a duty and when tortious conduct caused the plaintiff to prosecute or defend an action with a third party.

C. Consequential Damages

The traditional remedies in Maine for breach of contract include full general and consequential damages.²¹ However, consequential damages in the nature of "special damages" are recoverable for a breach of contract under the venerable *Hadley v. Baxendale* principle: only if the parties contemplated the particular harm claimed at the time of contracting will damages be recoverable for that harm.²² The typical measure of recovery for defective or incomplete performance of a construction contract is the difference in value between the value of the performance contracted for and the value of the performance actually rendered.²³ This difference may be proved either by the diminution in market value or by the amount reasonably required to remedy the defect.

D. Delay and Disruption Damages

There is no *per se* rule pertaining to delay and disruption damages in Maine. The intent of the parties determined from the contract language will govern the recovery. Liquidated damages for delay, however, must meet two requirements in order to be recoverable: 1. the damages must be difficult to prove and 2. the amount fixed must be a reasonable forecast.²⁴

E. Economic Loss Doctrine

The economic loss doctrine is a matter of common law, not statute, but it has been adopted in Maine.²⁵

F. Interest

In all civil actions involving a contract or note that contains a provision relating to pre-judgment interest, it is allowed at the rate set forth in the contract or note. 14 M.R.S.A. §1602-B. Otherwise, pre-judgment interest is allowed at the one-year United States Treasury bill rate, plus 3%. Pre-judgment interest accrues from the time of notice of claim setting forth under oath the cause of action, served personally or by registered or certified mail, until the date on which an order of judgment is entered. If a notice of claim has not been given to the defendant, pre-judgment interest accrues from the date on which the complaint is filed. If the prevailing party at any time requests and obtains a continuance for a period in excess of 30 days, interest is suspended for the duration of the continuance. On petition of the non-prevailing party and on a showing of good cause, the trial court may order that interest be fully or partially waived.

In actions involving a contract or note that contains a provision relating to post-judgment interest, the rate set forth in the contract or note or the rate from the Treasury bill formula applies, whichever is greater. 14 M.R.S.A. §1602-C. In all other actions, the interest rate is equal to the one-year United States Treasury bill rate plus 6%. Post-judgment interest accrues from and after the date of entry of judgment and includes the period of any appeal. If the prevailing party at any time requests and obtains a continuance for a period in excess of 30 days, interest is suspended for the duration of the continuance. On petition of the non-prevailing party and on a showing of good cause, the trial court may order that interest be fully or partially waived.

G. Punitive Damages

No matter how egregious the breach, punitive damages are not available under Maine law for breach of contract.²⁶ Punitive damages are recoverable only for tortious conduct.²⁷ The actionable conduct must be motivated by malice. Malice is defined as actual ill-will or ill-will implied from the outrageousness of the conduct. Mere reckless disregard of the circumstances does not warrant a punitive damage award.²⁸

VIII. CASE LAW AND LEGISLATIVE UPDATE

Since the last Compendium, little has changed in the legislative landscape affecting construction law. The Home Construction Contract Act (“HCCA”), 10 M.R.S.A. §1486 *et seq.*, however, is subject to periodic changes—adding another requirement to the mandatory dispute resolution language about small claims actions. The HCCA always should be consulted prior to entering a contract with a homeowner to ensure the latest provisions are satisfied.

Significant construction-related decisions from the Law Court have been few. In *F.R. Carroll, Inc. v. TD Bank, N.A.*, 2010 ME 115, 8 A.3d 646, the Court considered the issue of consent as it applied to the priority of a mechanic’s lien over a mortgage under Maine’s mechanic’s lien statute, 10 M.R.S.A. §§ 3251 – 3269 (2009 & Supp. 2010). Although not defined, the Law Court decided that consent required the contractor to prove: (1) knowledge on

the part of the owner of the nature and extent of the work being performed on the premises, and (2) conduct on the part of the owner justifying the expectation and the belief on the part of the contractor that the owner consented to the work. The Court reiterated that the issue of consent is a fact-specific inquiry. The Court vacated the Superior Court's grant of summary judgment to F.R. Carroll, Inc., concerning whether its mechanic's lien had priority over TD Bank's mortgage. There was a factual dispute as to whether TD Bank had consented to Carroll's paving contract with the mortgagor.

In *Cellar Dwellers, Inc. v. D'Alessio*, 2010 ME 32, 993 A.2d 1, a homeowner entered into a written plumbing contract, a written heating contract, and an oral vacuum contract with a contractor. When the homeowner failed to pay, the contractor stopped working. The contractor eventually filed a mechanic's lien and Complaint against the homeowner for enforcement of the lien, unjust enrichment, breach of contract, and violation of Maine's Prompt Payment Act, 10 M.R.S.A. §§ 1111-1120 (2009 & Supp. 2010). The Maine Superior Court held that the homeowner had breached the contracts and had wrongfully withheld payment. The Court awarded the contractor penalties and attorney fees under Sections 1113 and 1118 of the Act.

On appeal, the Maine Law Court upheld the Superior Court's holding that the homeowner had committed a material breach of the contract by refusing to pay and failing to keep the basement clear for heating and plumbing installation. However, the Law Court concluded that the homeowner wrongfully withheld payment only with respect to the vacuum contract, which work had been fully completed by the contractor but not paid for by the homeowner. Consequently, the contractor was entitled to penalties and attorney fees only on that contract. The Law Court concluded that, with respect to the heating and plumbing contracts, the owners had paid for all work completed to date so that no due payments actually were withheld, wrongfully or otherwise.

¹ *Gennings v. Norton*, 35 Me. 308, 312- 13 (1853).

² *Oceanside at Pine Point Condo. Owners Ass'n v. Peachtree Doors, Inc.*, 659 A.2d 267 (Me. 1995).

³ *Id.*

⁴ *Bangor Water Dist. v. Malcolm Pirnie Engineers*, 534 A.2d 1326 (Me. 1988).

⁵ *Oceanside at Pine Point Condominium Owners Ass'n v. Peachtree Doors, Inc.*, 659 A.2d 267, 273 (Me. 1995).

⁶ *Foremost Ins. Co. v. Levesque*, 868 A.2d 244, 246 (Me. 2005).

⁷ *Elliott v. Hanover Insurance Co.*, 711 A.2d 1310 (Me. 1998).

⁸ *Vigna v. Allstate Insurance Co.*, 686 A.2d 598 (Me. 1996).

⁹ *Johnson v. Amica Mut. Ins. Co.*, 733 A.2d 977, 980 (Me. 1999).

¹⁰ *York Mut. Ins. Co. v. Continental Ins. Co.*, 560 A.2d 571, 573 (Me. 1989).

¹¹ *Carriers Ins. Co. v. American Policyholders' Ins. Co.*, 404 A.2d 216, 221 (Me. 1979); *York Mut. Ins. Co. v. Continental Ins. Co.*, 560 A.2d 571, 573 (Me. 1989).

¹² *McGraw v. S.D. Warren Co.*, 656 A.2d 1222, 1224 (Me. 1995); *Emery Waterhouse Co. v. Lea*, 467 A.2d 986, 993 (Me. 1983); *Doyle v. Bowdoin College*, 403 A.2d 1206, (Me. 1979).

¹³ *Fowler v. Boise Cascade Corp.*, 739 F.Supp. 671, 675 – 76 (D.Me. 1990), *aff'd* 948 F.2d 49, 57 (1st Cir. 1991).

¹⁴ *Acadia Ins. Co. v. Buck Const. Co.*, 756 A.2d 515 (Me. 2000).

¹⁵ *Jenkins v. Walsh*, 776 A.2d 1229 (Me. 2001).

¹⁶ *VanVoorhees v. Dodge*, 679 A.2d 1077, 1081 (Me. 1996).

¹⁷ *Id.*; *see also Kleinschmidt v. Morrow*, 642 A.2d 161, 165 (Me.1994) (approving calculation of compensatory damages as the difference between the contract price and the actual total cost to the homeowner of completing the home).

¹⁸ *Soley v. Karll*, 853 A.2d 755, 758 (Me. 2004).

¹⁹ *Id.*, 853 A.2d at 759; *Linscott v. Foy*, 716 A.2d 1017 (Me. 1998).

²⁰ *Soley v. Karll*, 853 A.2d 755, 758 n. 3 (Me. 2004).

²¹ *Marquis v. Farm Family Mut. Ins. Co.*, 628 A.2d 644, 652 (Me. 1993)

²² *Forbes v. Wells Beach Casino, Inc.*, 409 A.2d 646 (Me. 1979)(no special damages recoverable for loss of use of property as mini-mall and motel where defendant did not know about plaintiff's plans for such uses at the time the contract was entered into); *Susi v. Simonds*, 85 A.2d 178 (Me. 1951)(no knowledge of intended use of property at time of contracting means no recovery of special damages in the nature of lost profits).

²³ *VanVoorhees v. Dodge*, 679 A.2d 1077, 1081 (Me. 1996).

²⁴ *Brignull v. Albert*, 666 A.2d 82, 84 (Me. 1995).

²⁵ *Oceanside at Pine Point Condo. Owners Ass'n v. Peachtree Doors, Inc.*, 659 A.2d 267 (Me. 1995).

²⁶ *Drinkwater v. Patten Realty Corp.*, 563 A.2d 772, 776 (Me. 1989).

²⁷ *Jolovitz v. Alfa Romeo Distributors of North America*, 760 A.2d 625, 629 (Me. 2000)(citing *DiPietro v. Boynton*, 628 A.2d 1019, 1025 (Me. 1993)). *Colford v. Chubb Life Ins. Co. of America*, 687 A.2d 609, 616 (Me. 1996)(tort recovery for intentional infliction of emotional distress and punitive damages must be based on actions that are separable from the actual breach of contract).

²⁸ *Tuttle v. Raymond*, 494 A.2d 1353 (Me. 1985).

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I. MECHANIC'S LIEN BASICS

A. Requirements

Within 120 days after doing the work or furnishing the materials, a subcontractor must provide written notice of an intention to claim a lien as specified in MD. CODE ANN., Real PROP. § 9-104(a)(2). The notice of intention to claim a lien must include the name of the subcontractor, a description of the work performed or material furnished, a description of the building or property where the work was performed or the material was furnished, the total amount earned to date under the subcontractor's undertaking, and the amount due and unpaid to the subcontractor.¹ Notice must be delivered in any one of the methods specified in the statute, including by registered or certified mail, return receipt requested, or by personal delivery to the owner by the Claimant or his agent.² If there is more than one owner, the subcontractor may comply with § 9-104 by giving notice to any of the owners.³ If notice cannot be given on account of absence or other causes, the subcontractor or his agent, in the presence of a competent witness and within 120 days, may place the notice on the door or other front part of the building.⁴ Notice by posting according to this method is sufficient in all cases where the owner of the property has died and his successors in title do not appear on the public records of the county.⁵

Proceedings to establish and enforce a mechanic's lien must be filed in the Circuit Court for the county where the land or any part of the land is located within 180 days after the work has been finished or the materials furnished.⁶ The petition must include: the name and address of the petitioner; the name and address of the owner; the nature or kind of work done and amount of materials furnished; the time when the work was done or materials furnished; the name of the person for whom the work was done or to whom the materials were furnished; the amount or sum claimed to be due, less any credit recognized by the petitioner; and a description of the land, including a statement whether part of the land is located in another county and a description adequate to identify the building.⁷ If the petitioner is a subcontractor, the petitioner must also set forth facts showing that the notice required in § 9-104 was properly mailed or served upon the owner or, if so authorized, posted on the building.⁸ In either case, whether contractor or subcontractor, the petitioner must supply an affidavit setting forth the facts upon which the petitioner claims entitlement to the lien and copies of the documents which constitute the basis for the lien claim.⁹ Upon the filing of the Mechanic's Lien Petition, the clerk shall docket the

proceedings as an action in equity, and all process shall issue out of and all pleadings shall be filed in the one action.¹⁰

B. Enforcement and Foreclosure

The property is sold pursuant to normal foreclosure rules.¹¹ All liens and encumbrances on the property shall be satisfied in accordance with their priority.¹² In the event that a mechanic's lien is established on the property and the proceeds of the sale are insufficient to satisfy all of the liens on the property, then all of the proceeds available to satisfy each lien shall be treated as one fund and the money produced as a proceed of the foreclosure sale shall be distributed to each mechanic's lien holder in a *pro rata* ratio, without regard to seniority.¹³

C. Ability to Waive and Limitations on Lien Rights

Under Maryland law, there are two types of agreements which will waive the right to file a mechanic's lien: an express agreement¹⁴ or an agreement which is inconsistent with the existence of a lien.¹⁵ In some unique circumstances, an agreement may have the effect of waiving the priority of a mechanic's lien, while not waiving the right to file and enforce the lien itself.¹⁶ A contract between a contractor and a subcontractor that is involved in the construction, alteration, or repair of a building, structure, or improvement may not waive or require the subcontractor to waive the right to claim a mechanic's lien or sue on a contractor's bond.¹⁷ Similarly, a "pay if paid" or "pay when paid" clause in the contract between a contractor and a subcontractor that is related to construction, alteration, or repair of a building, structure, or improvement will also not act as a waiver of the subcontractor's right to claim a mechanic's lien or sue on a contractor's bond.¹⁸ The right to file a mechanic's lien is individual to each potential lienholder, so it cannot be waived by a third party.¹⁹

MD. CODE ANN., REAL PROP. § 9-109 and MD. RULE 12-305 provide that the right to enforce a mechanic's lien, once established, expires one year from the date on which the petition to establish the mechanic's lien was first filed. In practice, this requirement simply obligates the mechanic's lien petitioner to file a petition to enforce a mechanic's lien within the one-year period; it does not obligate the mechanic's lien petitioner to foreclose on the mechanic's lien so quickly.

Public works bonds are required under both Federal and State law for all federal and state public works' construction projects, including those of any public instrumentality or political subdivision of Maryland. Federal projects are governed by the "Miller Act" under 40 U.S.C. § 3131, *et seq.* In Maryland, state and local public construction projects are governed by the "Little Miller Act" found in MD. CODE ANN., STATE FIN. & PROC. § 17-101, *et seq.* Both acts require performance and payment bonds with the payment bond affording protection to material suppliers and subcontractors who have no mechanic's lien by reason of sovereign immunity. The Miller Act applies to contracts exceeding \$100,000 in amount and designates minimum amounts necessary on payment bonds.²⁰ Similarly, the "Little Miller Act" requires performance and payment bonds in contracts exceeding \$100,000 and also provides for a required minimum payment bond amount.²¹

II. STATUTES OF LIMITATION AND REPOSE

A. Statutes of Limitations and Limitations on Application of Statutes

- (1) General tort and contract actions – three years.²²
- (2) Breach of implied warranties for improvements to realty – two years from the date the defect was discovered or should have been discovered.²³
- (3) Breach of UCC warranties - four years, but can be reduced by the terms of contract to not less than one year and cannot be extended by the contract.²⁴ A cause of action accrues when the breach occurs, regardless of the aggrieved party's lack of knowledge of the breach.²⁵ A breach of warranty occurs when tender of delivery is made, except that where a warranty explicitly extends to future performance of the goods and discovery of the breach must await the time of such performance, the cause of action accrues when the breach is or should have been discovered.²⁶ The four year statute of limitations applies to actions for breach of warranty brought by third parties.²⁷

B. Statutes of Repose and Limitations on Application of Statutes

MD. CODE ANN., CTS. & JUD. PROC. § 5-108(a) states:

No cause of action for damages accrues and a person may not seek contribution or indemnity for damages incurred when wrongful death, personal injury, or injury to real or personal property resulting from the defective and unsafe condition of an improvement to real property occurs more than 20 years after the date the entire improvement first becomes available for its intended use.

§ 5-108(b) goes on to state:

[A] cause of action for damages does not accrue and a person may not seek contribution or indemnity from any architect, professional engineer, or contractor for damages incurred when wrongful death, personal injury, or injury to real or personal property, resulting from the defective and unsafe condition of an improvement to real property, occurs more than 10 years after the date the entire improvement first became available for its intended use.

The Maryland Statute of Repose for actions resulting from improvements to real property applies to both contractors and subcontractors²⁸ and to actions for contribution and indemnity.²⁹ A purely financial injury does not fall within the purview of the 20 year statute of repose.³⁰

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

There are no statutory requirements in Maryland for a claimant to provide pre-suit notice or the opportunity to cure with respect to improvements to realty. However, such requirements may be included in the contract documents. A thorough analysis of the contract documents should be performed in each case to determine whether a claimant is required to provide pre-suit notice or the opportunity to cure.

IV. INSURANCE COVERAGE AND ALLOCATION ISSUES

A. General Coverage Issues

Maryland courts interpret insurance policies like any other contracts.³¹ In turn, courts construe the policy terms according to their sense and meaning.³² Additionally, any ambiguities are resolved against the policy's drafter.³³

Under a typical liability policy, an insurer has a duty to both provide the insured with a defense and to indemnify the insured for a judgment up to policy limits. The damages for breach of these contractual promises are the insured's defense expenses, including attorney fees, and the amount of an underlying tort judgment against the insured up to policy limits.³⁴

In Maryland, a commercial general liability (CGL) policy is understood to cover bodily injury or damage to the property caused by goods, products, or work of the insured other than damage to the product or the completed work itself.³⁵ The policy does not cover the insured's economic loss stemming from contractual liability for defective workmanship.³⁶ In other words, when the product or completed work is not that for which the damaged person bargained, the insureds cannot recover subsequent liability through a CGL policy.³⁷

B. Trigger of Coverage

Under an "occurrence" liability policy, property damage that is continuous over the course of several policy periods triggers coverage under all policies in effect during those periods, irrespective of when an actual claim is presented.³⁸ The insured bears the burden to show that property damage occurred within the coverage of any policy; and coverage may be triggered during a policy period earlier than discovery or manifestation.³⁹ A "claims made" or "discovery" policy covers liability inducing events if and when a claim is made during the policy term, irrespective of when the events occurred.⁴⁰

C. Allocation Among Insurers

Maryland courts have rejected an "all sums" and "joint and several" approach when allocating responsibility among insurers under "occurrence" policies for damages arising from continued harm that spans the course of several policy periods.⁴¹ Instead, courts have applied a *pro-rata* allocation based on each insurer's "time on the risk."⁴² Essentially, each insurer is liable for that period of time it was on the risk compared to the entire period during which

damages occurred.⁴³ Further, losses are prorated to the insured, unless a gap in coverage is due to the insured's inability to obtain insurance.⁴⁴

V. CONTRACTUAL INDEMNIFICATION

MD. CODE ANN., CTS. & JUD. PROC. § 5-401 renders void indemnity agreements in construction contracts purporting to indemnify the promisee against liability for damages arising out of bodily injury or property damage resulting from the sole negligence of the indemnitee. To fall within the scope of § 5-401, the damage or injury must have been caused solely by the party contracting for indemnification.⁴⁵

In *Bethlehem Steel Corp. v. G.C. Zarnas & Co., Inc.*, the Court of Appeals, held that it is the strong public policy of Maryland to void such indemnity clauses in contracts.⁴⁶ In that case, a Maryland corporation contracted with a Delaware corporation in Pennsylvania to perform painting services. The contract included an indemnification clause in which the contractor would indemnify the owner for all liability arising from the owner's sole or partial negligence.⁴⁷ The initial question before the Court was whether Maryland or Pennsylvania law should apply. The Court held that under normal circumstances the law of the state where the contract was made would control (in this case Pennsylvania), however, where the law of the foreign state contradicted the strong public policy of Maryland, Maryland law was controlling.⁴⁸ The Court went on to state that the legislature made it clear in MD. CODE ANN., CTS. & JUD. PROC. § 5-305 (now codified in § 5-401) that it was the strong public policy of Maryland that the indemnification clause would be void.⁴⁹ The Court, however, stated that only the portion of the indemnification clause relating to the sole liability of the owner was void and that to the extent that the contract clause discussed partial liability of the owner, it was not covered by § 5-305.⁵⁰

In *Heat & Power Corp. v. Air Products & Chemicals, Inc.*,⁵¹ the Maryland Court of Appeals considered an indemnification clause between a contractor and an owner that included a requirement that the contract provide insurance with respect to the liability covered in the indemnity clause.⁵² Citing *Bethlehem Steel*, the Court held that the indemnity clause would fall or stand under MD. CODE ANN., CTS. & JUD. PROC. § 5-305 (now codified in § 5-401) independently of the insurance clause.⁵³ It then went on to hold that because the indemnity clause was not exclusively in reference to the owner's sole liability and was also too vague to be enforceable, it would not be voided.⁵⁴ It necessarily followed that because the clause was not covered by § 5-305, it did not purport to indemnify the owner for its own negligence.⁵⁵ Notably, the requirement that the contractor purchase insurance covering "such liability" did not include insurance for the owner's liability because the owner's liability was not included in the indemnity clause.⁵⁶

VI. CONTINGENT PAYMENT AGREEMENTS

A. Enforceability

"Pay if paid" clauses are generally enforceable as a condition precedent to payment, provided that they are explicit.⁵⁷ "Pay when paid" clauses are interpreted to suggest a time

period when the subcontractor should be paid, but they will not prevent compensation of the subcontractor, even if payment from an owner is never received.⁵⁸

B. Requirements

Typically, the insolvency of an owner will not prevent the claim of a subcontractor against a contractor for non-payment.⁵⁹ However, if the “pay if paid” clause makes clear that payment by the owner is a condition precedent to payment of the subcontractor, it will be enforced, even if the parties have not specifically discussed the possibility of owner insolvency.⁶⁰ A clause that provides for the payment of a subcontractor *when* the general contractor is paid will not be interpreted as a condition precedent, so the general contractor will still owe the subcontractor for work performed regardless of whether or not the owner ever pays the contractor.⁶¹ In any case, a contingent payment clause will not prevent the subcontractor from collecting from other sources, such as the contractor’s bond or from the property owner himself.⁶²

VII. DAMAGES LIMITATIONS

A. Personal Injury Damages vs. Construction Defect Damages

Section 11-108 of the Courts and Judicial Procedure Article of Maryland’s Annotated Code applies a non-economic damages cap on any action for personal injury or wrongful death.⁶³ For construction defects, however, the measure of damages is the sum which would place the plaintiff in as good a position as that in which the plaintiff would have been, had the contract been performed.⁶⁴ This primarily includes the cost of repairing or remedying the defect.⁶⁵ It can also include expectation damages and gains lost, if they can be proven to a reasonable degree of certainty.⁶⁶ If repair is infeasible or impracticable, then the measure of damages is the loss in value of the property caused by the defect.⁶⁷

Additionally, there is a general three year statute of limitations when bringing a breach of contract claim in Maryland.⁶⁸ The statute begins running when the plaintiff knows or reasonably should know of the defect.⁶⁹

B. Attorney’s Fees Shifting and Limitations on Recovery

Under Maryland’s common law, attorney’s fees are not recoverable unless specifically included in the contract documents.⁷⁰ However, in a few instances, attorney’s fees are recoverable by statute, including the Maryland Consumer Protection Act.⁷¹ Attorney’s fees are also allowed where the parties’ contract provides such recovery.⁷²

C. Consequential Damages

Consequential damages are those which the cause in question naturally but indirectly produces.⁷³ They can include various items such as direct costs, acceleration costs, or lost profits from delay in construction. Consequential damages are increasingly a subject of contract law;

therefore, a thorough analysis of the contract documents should be performed in each case to determine whether a party is liable for, or has waived entitlement to, any consequential damages.

D. Delay and Disruption Damages

In Maryland, consequential damages may be recovered by the claimant upon proving a delay or disruption in its work on the project.⁷⁴ Types of owner-caused delays include defective plans and/or specifications.⁷⁵ In addition, liquidated damages for delay, as well as contractual provisions disclaiming delay damages, are generally enforceable in Maryland.⁷⁶

E. Economic Loss Doctrine

Typically, in Maryland, there is no recovery in tort for economic losses.⁷⁷

In delineating the “economic loss doctrine” for contractor liability cases, the Maryland Court of Special Appeals in *Heritage Harbour, LLC v. John J. Reynolds, Inc.*,⁷⁸ explained as follows:

It is generally said that a contractor’s liability for economic loss is fixed by the terms of his [or her] contract. Tort liability is in general limited to situations where the conduct of the builder causes an accident out of which physical harm occurs to some person or tangible thing other than the building itself that is under construction.⁷⁹

Over the years, Maryland courts have established several exceptions to the economic loss doctrine. First, a tort duty for purely economic losses exists where the parties have contractual privity or its legal equivalent.⁸⁰ Second, recovery in tort is permitted when the product defect “creates a substantial and unreasonable risk of death or personal injury.”⁸¹ Third, physical injury to tangible property other than damage to the defective product itself is recoverable under a negligence cause of action.⁸²

F. Interest

The post-judgment interest rate, as provided by statute, is ten percent per annum on the amount of the judgment.⁸³ This ten percent interest rate applies to post-judgment interest and not to pre-judgment obligations.⁸⁴ Absent statutory authority to the contrary, the legal rate of prejudgment interest is equal to the general legal rate of six percent as set by the Maryland Constitution.⁸⁵

G. Punitive Damages

Maryland has an extremely high bar to punitive damages. Maryland courts have long held that punitive damages may not be recovered in breach of contract claims.⁸⁶ In cases of fraud or deceit, a plaintiff may not recover punitive damages merely by proving that a defendant’s statements were made with reckless disregard or reckless indifference to the truth.⁸⁷ In order to establish the malice required to support a claim for punitive damages, a plaintiff must

prove by clear and convincing evidence the defendant's actual knowledge of the falsity of his statements coupled with the intent to deceive the plaintiff.⁸⁸

VIII. CASE LAW AND LEGISLATION UPDATE

While the past year has produced several notable appellate court opinions, there have not been particularly significant changes in Maryland construction law.

In *Burns v. Bechtel Corp.*, 212 Md. App. 237 (2013), Maryland's intermediate appellate court addressed the applicability of Maryland's Statute of Repose.⁸⁹ The Plaintiff worked for Potomac Electric Power Company (PEPCO) as a maintenance mechanic. During the course of Burns' employment, PEPCO hired Bechtel Corporation to be its general contractor for various construction projects. The Plaintiff was diagnosed with mesothelioma and brought suit against Bechtel for exposure to asbestos as a result of its work at PEPCO.

The Court of Special Appeals considered whether Bechtel was excluded from repose because the contractor was "in actual possession and control of the property as owner, tenant, or otherwise when the injury occurred."⁹⁰ The court found the statute did apply as the contractor exercised control "of the project," but not control "of the premises."⁹¹ Bechtel's rights as a general contractor were limited to the scope of its duties to perform construction work.

The Court of Special Appeals also addressed when a *per diem* damages provision could be recognized as a valid liquidated damages clause.⁹² The parties engaged in a sale of property which also required construction of a demising wall by the seller, to be completed within 30 days of closing. The contract required the buyer to "pay a penalty" of \$126 per day for each day the work was not completed. While the wall was built in compliance with the agreement, no building permit was obtained, which the Court held was a failure to comply with the requirement that the construction be completed in a manner consistent with the law.

The Court applied Maryland's two-part test that (1) requires that a liquidated damages clause provide a fair estimate of potential damages at the time the contract was entered and (2) that the damages be incapable of estimation.⁹³ The court found that the provision was enforceable, and noted that the use of the word "penalty" does not necessarily render the clause a penalty.⁹⁴

¹ MD. CODE ANN., REAL PROP. § 9-104(b).

² *Id.* at § 9-104(c).

³ *Id.* at § 9-104(d).

⁴ *Id.* at § 9-104(e).

⁵ *Id.*
⁶ *Id.* at § 9-105(a).
⁷ *Id.* at § 9-105(a)(1)(i)–(iv).
⁸ *Id.* at § 9-105(a)(1)(v).
⁹ *Id.* at § 9-105(a)(2)–(3).
¹⁰ *Id.* at § 9-105(b).
¹¹ For the normal foreclosure rules, *see* Title 14 of the MARYLAND RULES.
¹² MD. CODE ANN., REAL PROP. § 9-108.
¹³ *Id.*
¹⁴ *Port City Const. Co. v. Adams & Douglass, Inc.*, 260 Md. 585, 273 A.2d 121 (1971)
¹⁵ *Willison v. Douglass*, 66 Md. 99, 6 A. 530 (1886).
¹⁶ *Perper v. Fayed*, 247 Md. 639, 642–43, 234 A.2d 144, 145–46 (1967).
¹⁷ MD. CODE ANN., REAL PROP. §9-113 (a)
¹⁸ MD. CODE ANN., REAL PROP. §9-113 (b)
¹⁹ *Judd Fire Protection, Inc. v. Davidson*, 138 Md. App. 654, 665, 773 A.2d 573, 580 (2001).
²⁰ 40 U.S.C. § 3131(b).
²¹ MD. CODE ANN., STATE FIN. & PROC. § 17-103(a).
²² MD. CODE ANN., CTS. & JUD. PROC. §5-101.
²³ MD. CODE ANN., REAL PROP. § 10-204; *see also*, *Lumsden v. Design Tech Builders, Inc.*, 358 Md. 435, 749 A.2d 796 (2000).
²⁴ MD. CODE ANN., COM. LAW § 2-725(1).
²⁵ *Id.* at § 2-725(2).
²⁶ *Id.*
²⁷ *Shaw v. Brown Williamson Tobacco Corp.*, 973 F. Supp. 539 (D. Md. 1997).
²⁸ *Hartford Ins. Co. of Midwest v. American Automatic Sprinkler Systems, Inc.*, 23 F. Supp. 2d 623, *aff'd*, 201 F.3d 538 (1998).
²⁹ MD. CODE ANN., CTS. & JUD. PROC. § 5-108(a)–(b).
³⁰ *Carven v. Hickman*, 135 Md. App. 645, 763 A.2d 1207, *aff'd sub nom.*, 366 Md. 362, 784 A.2d 31 (2000).
³¹ *United States Fid. & Guar. v. Nat'l Paving & Contract Co.*, 228 Md. 40, 50, 178 A.2d 872, 876–77 (1962).
³² *Id.*
³³ *Id.*
³⁴ *Mesmer v. Maryland Auto. Ins. Fund*, 353 Md. 241, 266, 725 A.2d 1053, 1065 (1999).
³⁵ *Lerner Corp. v. Assurance Co. of Am.*, 120 Md. App. 525, 530–31, 707 A.2d 906, 909 (1998).
³⁶ *Id.*
³⁷ *Id.*
³⁸ *Harford County v. Harford Mut. Ins. Co.*, 327 Md. 418, 434–37, 610 A.2d 286, 294–95 (1992); *see also*, *Scottsdale Ins. Co. v. American Empire Surplus Lines Ins. Co.*, 811 F. Supp. 210 (D. Md. 1993).
³⁹ *Harford County v. Harford Mut. Ins. Co.*, 327 Md. 418, 610 A.2d 286 (1992).
⁴⁰ *See Mut. Fire, Marine & Inland Ins v. Vollmer*, 306 Md. 243, 252–55, 508 A.2d 130, 134–36 (1986).
⁴¹ *Mayor & City Council of Baltimore v. Utica Mut. Ins. Co.*, 145 Md. App. 256, 313, 802 A.2d 1070, 1104 (2002).
⁴² *Id.*
⁴³ *Id.*
⁴⁴ *Id.*
⁴⁵ MD. CODE ANN., CTS. & JUD. PROC. § 5-401; *Bethlehem Steel Corp. v. G.C. Zarnas & Co., Inc.*, 304 Md. 183, 498 A.2d 605 (1985); *Ins. Co. of Am. v. Interstate Serv. Co., Inc.*, 118 Md. App. 126, 701 A.2d 1213 (1997).
⁴⁶ 304 Md. at 193, 498 A.2d at 610.
⁴⁷ *Id.* at 185–86, 498 A.2d at 605.
⁴⁸ *Id.* at 193; 498 A.2d at 610.
⁴⁹ *Id.*
⁵⁰ *Id.* at 195; 498 A.2d at 611.
⁵¹ 320 Md. 584, 578 A.2d 1202 (1990).
⁵² *Id.* at 588; 578 A.2d at 1204.
⁵³ *Id.* at 593–94; 578 A.2d 1207.
⁵⁴ *Id.*
⁵⁵ *Id.*

⁵⁶ *Id.* at 594; 578 A.2d at 1207.

⁵⁷ *Gilbane Bldg. Co. v. Brisk Waterproofing Co., Inc.*, 86 Md. App. 21, 25, 585 A.2d 248, 250 (1991).

⁵⁸ *Atlantic States Constr. Co. v. Drummond & Co., Inc.*, 251 Md. 77, 79–82, 246 A.2d 251, 252–54 (1968).

⁵⁹ *Id.* See also *Richard F. Kline, Inc. v. Shook Excavating & Hauling, Inc.*, 165 Md. App. 262, 273, 885 A.2d 381, 388 (2005) (“Although no particular language is required to create a condition precedent, words and phrases such as ‘if,’ ‘provided that,’ ‘when,’ ‘after,’ ‘as soon as’ and ‘subject to,’ have commonly been associated with creating express conditions.”) (citing *Gilbane* 86 Md. App. at 26–27).

⁶⁰ *Gilbane*, 86 Md. App. at 26, 585 A.2d at 250–51.

⁶¹ *Id.*

⁶² MD. CODE ANN., REAL PROP. §9-113.

⁶³ MD. CODE ANN., CTS. & JUD. PROC. § 11-108.

⁶⁴ *Beard v. E/S Joint Venture*, 321 Md. 126, 133, 581 A.2d 1275, 1278 (1990).

⁶⁵ *Gilbert Const. Co. v. Gross*, 212 Md. 402, 411, 128 A.2d 518, 522 (1957)

⁶⁶ *Beard*, 321 Md. at 133, 581 A.2d at 1278.

⁶⁷ *Gilbert Const. Co.*, 212 Md. at 411, 128 A.2d at 522.

⁶⁸ MD. CODE ANN., CTS. & JUD. PROC. § 5-101.

⁶⁹ *DeGroft v. Lancaster Silo Co., Inc.*, 72 Md. App. 154, 164, 527 A.2d 1316, 1320 (1987).

⁷⁰ *Myers v. Kayhoe*, 391 Md. 188, 207, 892 A.2d 520, 532 (2006).

⁷¹ See, e.g., MD. CODE ANN., STATE FIN. & PROC. § 15-221.2 (providing that attorneys’ fees are payable if state employees act in bad faith or without substantial justification); MD. CODE ANN., REAL PROP. § 9-303 (attorneys’ fees may be awarded under Prompt Payment Act if proven the owner or contractor refused to pay undisputed amounts in bad faith); MD. CODE ANN., COM. LAW § 13-408(b) (providing that any person who brings an action to recover damages for injury or loss under the Maryland Consumer Protection Act and is awarded damages may also seek, and the court may award, reasonable attorneys’ fees).

⁷² See *Atlantic Contracting Mat’l Co. Inc. v. Ulico Cas. Co.*, 380 Md. 285, 844 A.2d 460 (2004).

⁷³ *Fowler v. Printers II, Inc.*, 89 Md. App. 448, 598 A.2d 794 (1991).

⁷⁴ *Dewey Jordan, Inc. v. Maryland Nat’l Capitol Park & Planning Commission*, 258 Md. 490, 265 A.2d 892 (1970).

⁷⁵ Regarding defective plans, see, e.g., *Dewey Jordan, Inc.*, 258 Md. 490, 265 A.2d 892 (holding that the owner, through the use of defective plans, commits a breach of its implied warranty in its contract that plans are fit for the purpose of building the project); regarding interference by the owner, see, e.g., *The Orange Alexandria & Manassas R.r. v. Placide*, 35 Md. 315 (1872); regarding denial of access to the site and suspension of the work, see, e.g., *Iron Clad Mfg. Co. v. Stanfield*, 112 Md. 360, 76 A. 854 (1910). These cases demonstrate that Maryland law recognizes that the contractor is entitled to be compensated if the owner, overtly or impliedly, stops the work.

⁷⁶ *Cowan v. Meyer*, 125 Md. 450, 94 A. 18 (1915).

⁷⁷ *Champion Billiards Cafe, Inc. v. Hall*, 112 Md. App. 560, 569, 685 A.2d 901, 906 (1996). See also *Morris v. Osmose Wood Preserving*, 340 Md. 519, 531, 667 A.2d 624, 631 (1995) (plaintiff cannot “recover in tort for losses in third category – purely economic losses”); *A. J. Decoster Co. v. Westinghouse Elec. Corp.*, 333 Md. 245, 249–50, 634 A.2d 1330, 1332 (1994) (a purchaser suffering economic losses cannot maintain a negligence action; instead are limited to contract actions for breach of warranty or tort actions for fraud or deceit); *Council of Co-owners Atlantis Condo. v. Whiting-Turner Contracting Co.*, 308 Md. 18, 33, 517 A.2d 336, 344 (1986) (“[i]n products cases, liability in negligence for economic loss alone, unaccompanied by physical injury, is often denied regardless of privity”); *The Milton Co. v. Council of Unit Owners of Bentley Place Condo.*, 121 Md. App. 100, 115, 708 A.2d 1047, 1054 (1998) (“[t]ort recovery for purely economic losses is ordinarily not allowed in product defect cases”).

⁷⁸ 143 Md. App. 698, 795 A.2d 806.

⁷⁹ 143 Md. App. at 707, 795 A.2d at 811 (quoting *Council of Co-owners Atlantis Condo.*, 308 Md. at 33, 517 A.2d at 344).

⁸⁰ *Jacques v. First Nat’l Bank*, 307 Md. 527, 537, 541, 515 A.2d 756, 761, 763 (1986); *Champion Billiards Cafe, Inc.*, 112 Md. App. at 567–71, 685 A.2d at 905–06.

⁸¹ *US Gypsum Co. v. Mayor & City Council of Balt.*, 336 Md. 145, 156–57, 647 A.2d 405, 410 (1992); *Whiting-Turner*, 308 Md. at 35, 517 A.2d at 345; *Heritage Harbour LLC*, 143 Md. App. at 707–08, 795 A.2d at 811–12; *Morris*, 340 Md. at 535, 667 A.2d at 632. The Maryland Court of Appeals expanded this exception to the economic loss rule several years ago. In *Lloyd v. General Motors Corp.*, 397 Md. 108, 916 A.2d 251 (2007) the court held that a defect constitutes an unreasonable risk of death or serious injury if the defect is alleged to have caused death or serious injury in other cases. Economic loss is recoverable in tort to fix such a defect.

⁸² *A. J. Decoster Co. v. Westinghouse Elec. Corp.*, 333 Md. 245, 254, 634 A.2d 1330, 1334 (1994).

⁸³ MD. CODE ANN., CTS. & JUD. PROC. § 11-107.

⁸⁴ *Crystal v. West & Callahan, Inc.*, 328 Md. 318, 342, 614 A.2d 560, 572 (1992); *Travel Comm., Inc. v. Pan Am. World Airways, Inc.*, 91 Md. App. 123, 189, 603 A.2d 1301, 1333, *cert. denied*, 327 Md. 525, 610 A.2d 797 (1992).

⁸⁵ MD. CONST. Art. III, § 57; *Crystal*, 328 Md. at 342, 614 A.2d. at 572.

⁸⁶ *Baltimore County v. RTKL Associates, Inc.*, 380 Md. 670, 677, 846 A.2d 433, 437 (2004); *Adams v. Coates*, 331 Md. 1, 13–14, 626 A.2d 36, 42–43 (1993).

⁸⁷ *Id.*

⁸⁸ *Id.*

⁸⁹ MD. CODE ANN., CTS. & JUD. PROC. § 5-108.

⁹⁰ *Id.*

⁹¹ 212 Md. App. at 242.

⁹² *Cuesport Properties, LLC v. Critical Development, LLC*, 209 Md. App. 607 (2013).

⁹³ *Id.* at 617.

⁹⁴ *Id.* at 617-18.

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I. MECHANICS' LIEN BASICS

Massachusetts General Laws (M.G.L.) c. 254, et seq., governs the procedure for obtaining and enforcing mechanics' liens. Claimants that furnish labor and/or materials in connection with the construction, repair, removal or alteration of a building or structure may obtain a mechanics' lien upon real property.¹ With a limited exception, the statute requires that the party seeking to enforce the lien be acting under a written contract.² A party with a direct contract with an owner, or someone acting on behalf of the owner, may enforce a mechanic's lien against the property that is the subject of the improvement.³ A subcontractor or supplier may also enforce a mechanics' lien against the "real property, land, building, structure or improvement owned by the party who entered into the original contract as appears of record at the time of such filing."⁴

A mechanics' lien claimant is not entitled to a lien for attorney's fees or interest associated with the claim.⁵ A mechanics' lien may not be placed on public property.⁶ The mechanics' lien statute sets forth a four step procedure to establish and enforce a mechanics' lien for general contractor and subcontractor/supplier liens. Strict compliance with the terms of the statute is necessary to obtain a valid lien.⁷ A party may move for summary dissolution of an improper or procedurally defective lien, and is entitled to a prompt hearing on such application.⁸ Lien waivers in a contract are prohibited by statute and will be void.⁹

The procedures to perfect and enforce a mechanics' lien differ depending on whether or not the claimant has a direct contractual relationship with the owner.

A. Direct Contract with Owner (General Contractor's Lien):

(1) Notice of Contract. The general contractor claimant must record a Notice of Contract in the Registry of Deeds of the county or district where the project is located, per M.G.L. c. 254, § 2. The Notice of Contract must include the name of the general contractor and owner, as well as a statement that a written contract between them exists. The Notice of Contract requires a detailed description of the property in question. The Notice of Contract may be filed or recorded at any time after the execution of the written contract, but no later than the earliest of: (1) 60 days after filing or recording a notice of substantial completion under M.G.L. c. 254, § 2A; (2) 90 days after the filing or recording or a notice of termination under M.G.L. c. 254, § 2B; or (3) 90 days after the general contractor, or any person by, through or under the general contractor last performed or furnished labor and/or materials.¹⁰

(2) Statement of Account. The general contractor claimant must next record with the Registry of Deeds a “Statement of Amount Due,” also referred to as a “Statement of Claim” or “Statement of Account,” per M.G.L. c. 254, § 8. The Statement of Account must set forth “a just and true account of the amount due or to become due him, with all just credits” as well as a brief description of the property, and the names of the owners as set forth in the Notice of Contract.¹¹ The Statement of Account must be filed or recorded within 90 days after notice of substantial completion, 120 days after notice of termination; or 120 days after the general contractor, or anyone claiming by, through, or under him last furnished the labor or materials.¹²

(3) File Civil Action. The general contractor claimant must next file a civil action to enforce the lien, and must do so within 90 days after the recording of the Statement of Amount Due. This action must be brought in either the Superior Court for the county where the land is located, or in the District Court in the Judicial District where the land is located.¹³

(4) Record Attested Copy of Complaint. The general contractor claimant must record in the Registry of Deeds an attested-to copy of the complaint, and must do so within 30 days of the commencement of the action in the previous step.¹⁴

B. No Direct Contract With Owner (Subcontractor/Supplier’s Lien):

The above steps are generally the same, however M.G.L. c. 254, § 4 governs the Notice of Contract.¹⁵ The Notice of Contract under Section 4 must include an accounting of the current status of payment as of the date of the notice, and the regular mailing address of the party recording or filing the notice. The subcontractor/supplier claimant must also provide the owner with actual notice of the filing of the Notice of Contract.¹⁶

The subcontractor/supplier claimant may record a Notice of Contract at any time after the execution of the written contract, but not later than the first of the following to occur: (1) 60 days after filing of the notice of substantial completion under Section 2A; (2) 90 days after filing the notice of termination under Section 2B; or (3) 90 days after the last day a person entitled to enforce the Section 2 lien or anyone claiming by, under or through him performs or furnishes labor or materials under the general contract.

The remaining three steps for the subcontractor/supplier claimant are the same as for the general contractor’s lien as discussed above.

A subcontractor’s lien is limited by statute in that it “shall not exceed the amount due or to become due under the original contract as of the date notice of the filing of the subcontract is given by the subcontractor to the owner.”¹⁷ Thus, the amount of the subcontractor’s lien may not exceed the amount owed by the owner to the general contractor at the time the Section 4 written notice (see above) is provided to the owner.

C. Claimant With No Contract with General Contractor:

Where a subcontractor/supplier claimant has no direct contract with the general contractor (a sub-subcontractor), the amount of the lien may not exceed the amount due or to become due under *the subcontract between the original contractor and the subcontractor whose work includes the work of the claimant*, as of the date the claimant files a notice of contract,

unless the claimant provided to the general contractor a “Notice of Identification” within 30 days of commencement of work.¹⁸ The form of the Notice of Identification is provided M.G.L. c. 254, § 4. The failure to meet this step does not deprive the second tier subcontractor of the lien, but further limits the amount of the lien.

D. Discharge of Liens

Liens may be discharged by recording a judgment dissolving the lien¹⁹, by recording a voluntary “Notice of Dissolution of Lien,”²⁰ or by the recording of a lien removal bond in response to the lien.²¹ If a lien removal bond is recorded and served on the claimant, the lien is dissolved and the claimant must then bring the action against the surety.²² A party may also record a lien prevention bond prior to a lien being recorded.²³ Where a lien prevention bond is in place, the claimant must follow the steps to perfect and enforce the lien, but must file suit against the surety, not the property owner.

II. STATUTES OF LIMITATION & REPOSE

A. Statute Of Limitations

1. Breach of Contract

The statute of limitations for breach of contract is six years from the date of breach.²⁴ If the transaction is primarily for the sale of goods under the U.C.C., the limitations period is four years from the date of breach. This can be reduced by the terms of contract to not less than one year, and cannot be extended by the contract.²⁵

2. Negligence

For tort actions related to “damages arising out of any deficiency or neglect in the design, planning, construction or general administration of an improvement to real property,” three years.²⁶ A tort cause of action accrues either when the plaintiff is injured as a result of the defendant’s unlawful act or omission.²⁷ If the wrong is “inherently unknowable,” Massachusetts law recognizes the “discovery rule,” and the cause of action accrues when the plaintiff knows or should know that she has been injured.²⁸ The knowledge required to trigger the statute of limitations “is not notice of every fact which must eventually be proved in support of the claim,” but rather “knowledge that an injury has occurred.”²⁹

3. Breach of Warranty

If the claim is akin to a product liability suit for personal injuries or property damage, M.G.L. c. 106, § 2-318 provides a three year statute of limitations from the date that injury and damage occurs, subject to the discovery rule for tort actions as set forth above. If the claim is a contract based breach of warranty claim, and involves the sale of goods, M.G.L. c. 106, § 2-725 provides a four year limitations period, which runs from the date of “tender of delivery” of the goods, unless “the warranty explicitly extends to future performance of the goods and discovery of the breach must await the time of such performance.”³⁰

4. Mass. Gen. Laws. Chapter 93A

Mass. Gen. Laws ch. 93A is Massachusetts Consumer Protection Statute. It prohibits against unfair or deceptive trade practices. The statute of limitations under the statute is four years.³¹

B. Statute of Repose

Massachusetts law provides for an absolute statute of repose with regard to actions in tort related to “damages arising out of any deficiency or neglect in the design, planning, construction or general administration of an improvement to real property.”³² The Statute of Repose will bar tort claims, regardless of the operation of the “discovery rule,” set forth above. For private construction projects, the Statute of Repose runs from the earlier of: (a) the opening of the improvement to use or (b) substantial completion and the taking of possession for occupancy by the owner. For public construction projects, the Statute of Repose runs from the earlier of: (a) official acceptance of the project by the agency; (b) its opening to public use; (c) the contractor’s acceptance of a final estimate by a public agency; or (d) substantial completion and the taking of possession for occupancy by the awarding authority.

The Statute of Repose protects those who “perform acts of individual expertise akin to those commonly thought to be performed by architects and contractors - that is to say, to parties who render particularized services for the design and construction of particular improvements to particular pieces of real property. The Statute of Repose does not protect manufacturers and materialmen, or “mere suppliers of standardized products.”³³

The Statute of Repose does not apply to claims for breach of contract.³⁴ This includes claims between defendants based upon contractual indemnification clauses.³⁵ Claims based upon breach of express warranty are considered to be breach of contract actions, and thus outside the scope of the statute of repose.³⁶ The Statute of Repose bars the addition of protected parties in an action that had previously been commenced against other parties, and does not allow amended claims to relate back to the date of commencement as otherwise allowed under Mass. R. Civ. P 15(c).³⁷ The Statute of Repose also applies to claims for statutory contribution.³⁸

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

At least 30 days before a consumer complaint for violation of M.G.L. c 93A may be filed, the consumer claimant is required to serve a demand letter upon the defendant.³⁹ Chapter 93A proscribes acts in trade or commerce that may be considered “unfair” or “deceptive.” Chapter 93A allows recovery of double or treble damages and attorney’s fees. Double or treble damages are allowed if the Court finds a “knowing or willful” violation of the statute. A finding of a violation Chapter 93A mandates an award of attorney’s fees and costs.

A consumer claimant must serve a written Chapter 93A demand letter prior to filing suit. This is a jurisdictional prerequisite to maintaining such claim, wherein the plaintiff is a consumer alleging a violation of Section 9.⁴⁰ A finding of multiple damages and attorney’s fees under Chapter 93A may be avoided if the defendant, after receipt of a demand letter under M.G.L. c. 93A, makes a reasonable offer of settlement within 30 days. If the court subsequently finds that the tender of settlement was reasonable, timely, and rejected by the claimant, the plaintiff will be

barred from recovery of attorney's fees and multiple damages, even if the court finds that the violation of G.L. c. 93A was willful or knowing.⁴¹

IV. INSURANCE COVERAGE AND ALLOCATION ISSUES

A. General Coverage Issues

Commercial General Liability (CGL) insurance provides coverage for legal liability, as well as defense costs, if an alleged lawsuit covered under the policy arises out of an accidental occurrence. Typically, CGL coverage protects against claims of damage to third party property. However, the "business risk exclusion" which is common in most policies may preclude coverage of risks to the project itself.⁴²

B. Trigger of Coverage

Coverage is triggered on the date that the complaining party is actually damaged. An occurrence policy covers a claims that took place during the applicable policy period.⁴³ The Supreme Judicial Court of Massachusetts has ruled that coverage for latent injury claims is not restricted to the year in which damage "manifests."⁴⁴ Thus, regardless of the date of discovery, if the complaining party is actually damaged during the policy period the claim should be covered.

C. Allocation Among Insurers

As of yet, Massachusetts courts have not addressed allocation issues in the specific context of construction defect claims. Such case law as exists with respect to pollution and toxic tort claims suggests, however, that Massachusetts will not permit allocation of orphan shares to policyholders and will instead allow insureds to maximize their coverage through an "all sums" approach.⁴⁵

V. CONTRACTUAL INDEMNIFICATION

Massachusetts law does not interpret indemnification contracts in favor of the indemnitee. Rather, indemnification provisions are to be read without any bias for the indemnitor or against the indemnitee. They are to be interpreted like any other contract, with attention to language, background, and purpose.⁴⁶

Pursuant to M.G.L. c. 149, § 29C, an indemnity provision will be declared void if it "requires a subcontractor to indemnify any party for injury to persons or damage to property not caused by the subcontractor or its employees, agents, or subcontractors."⁴⁷ The court will look at the language on its face, and will not base its decision on the particular facts of the case, in examining the validity of a clause under the statute.⁴⁸ While the statute refers to claims "caused by" the subcontractor, the language arising out of or in consequence of the performance of the subcontractor's work" has been deemed acceptable.⁴⁹ Savings language ("to the fullest extent permitted by law") will allow the Court to excise any offensive portions of indemnity provision and enforce remainder to the extent that the remainder was consistent with the statute.⁵⁰

Where a party is entitled to indemnification, the indemnitee may recover reasonable attorney's fees incurred in defending a claim within the scope of the indemnity clause, regardless of whether the indemnity clause provides for recovery of attorney's fees.⁵¹ It has been held that late notice may preclude a claim, where the contract requires prompt notice as a condition precedent.⁵²

The Appeals Court has held that an indemnity provision in a subcontract agreement was a proportional indemnity provision and that M.G.L. c. 149, §29C, the Massachusetts indemnity limiting statute, does not prohibit proportional indemnity.⁵³ The clause obligated the subcontractor to indemnify the general contractor against any claims arising out of the performance of the subcontractor's work, "but only to the extent caused in whole or in part by the negligent or willful acts or omissions" of the subcontractor. The Appeals Court agreed that the prefatory phrase "but only to the extent" restricted the indemnity obligation to "only" those losses caused by its negligent conduct, and held that it imposed a proportional indemnity obligation.

VI. CONTINGENT PAYMENT AGREEMENTS

On public projects, Massachusetts has long required prompt payment of contractors and subcontractors. Now, under the newly enacted Prompt Payment Law, M.G.L. c. 149, § 29E, such protections are also given to contractors on private projects. The new law, which generally will cause "pay if paid clauses" to be unenforceable, applies to all private projects of \$3 million or more, with the exception of small-scale residential projects (four or fewer units).

The prompt payment law requires that payment applications be submitted on a cycle of no more than 30 days. The requisition then must be either approved or rejected within 15 days of submission, with opportunity for a 7 day extension for each tier below the prime contract. Any rejection of a requisition has to be in writing, has to explain the basis for the rejection, and has to include a certification that the rejection is made in good faith. If there is no written rejection meeting those requirements within the 15-day period, the requisition is "deemed to be approved." Payment must be made within 45 days after approval or "deemed" approval.

There are two exceptions to prompt payment which must be clearly expressed in the subcontract: (1) money not paid due to nonperformance (after notice and opportunity to cure) of the person seeking payment; and (2) allows nonpayment if the payor is insolvent or becomes insolvent within 90 days after pay request is made. Notwithstanding the exception, the person seeking to enforce the paid if paid clause due to insolvency must file a Notice of Contract prior to the first payment requisition and pursue all other reasonable legal remedies against the insolvent party.⁵⁴

VII. DAMAGES LIMITATIONS

A. Personal Injury Damages vs. Construction Defect Damages

In Massachusetts, tort claims for personal injury and property damage are permitted without limitation.⁵⁵ On the other hand, construction defect damages are limited. A claim for property damage resulting from negligent construction is only permitted when the property

damage exceeds the value of the defective work itself.⁵⁶

B. Attorney's Fees

Attorney's fees are not recoverable, unless agreed to by contract, or where allowed by statute. A significant statute allowing recovery of attorney's fees is M.G.L. c. 93A, et seq., Massachusetts Consumer Protection Statute. M.G.L. C. 93A claims may be brought both in a consumer and business to business context. To prevail, the claimant must prove that the defendant, in the course or trade or commerce, committed an "unfair" or "deceptive" practice.⁵⁷ Under Massachusetts law, a breach of warranty in a consumer context⁵⁸, or a violation of the Massachusetts Home Improvement Contractors Act (M.G.L. c. 142A, et seq.) is a *per se* violation of Chapter 93A.⁵⁹

C. Consequential Damages

In a breach of contract action, a plaintiff is entitled to be made whole, and no more.⁶⁰ The plaintiff is allowed damages so that the plaintiff is "placed in the same position he would have been in, if the contract had been performed, so far as loss can be ascertained to have followed as a natural consequence, and to have been within the contemplation of the parties as reasonable men as a probable result of the breach, as so far a compensation therefor in money can be computed by rational methods upon a firm basis of facts."⁶¹

D. Delay and Disruption Damages

Delay and disruption damages are recoverable if allowed by contract, and if not otherwise precluded by operation of law. "No damage for delay" clauses are upheld under Massachusetts law.⁶² In public construction projects in Massachusetts, M.G.L. c. 30, § 39O, as interpreted by the Supreme Judicial Court, greatly restricts claims for delay damages in public projects.⁶³

E. Economic Loss Doctrine

The economic loss rule provides that economic losses are not recoverable in tort, unless arising from physical damage to a plaintiff's property or personal injury.⁶⁴ In the absence of personal injury or physical damage to a plaintiff's property, a negligent actor is not liable in tort for economic losses.⁶⁵ Economic loss includes "damages for inadequate value, costs of repair and replacement of the defective product or consequent loss of profits without any claim of personal injury or damage to other property."⁶⁶ The economic loss doctrine is applicable to construction claims.⁶⁷

F. Interest

In Massachusetts state court, the statutory interest rate for pre-judgment interest on contract and tort actions is 12%.⁶⁸ For tort action, interest runs from the date of filing the action.⁶⁹ For breach of contract actions, interest runs from the date of breach, if established, or the date of demand, if established, or otherwise from the date of filing suit.⁷⁰

G. Punitive Damages

Absent statutory authority, none. A statutory source of punitive damages in Massachusetts for construction defect claims is M.G.L. c. 93A, et seq.. To prevail under Chapter 93A, the claimant must prove that the defendant, in the course or trade or commerce, committed an “unfair” or “deceptive” practice. If the Court finds a “knowing or willful” violation of the statute, the Court must award not more than treble, but not less than double damages. M.G.L. c. 93A, §§ 9(3) & 11.

Punitive damages are allowed in wrongful death actions if the decedent’s death “was caused by the malicious, willful, wanton or reckless conduct of the defendant or by the gross negligence of the defendant.”⁷¹

VIII. Case Law and legislative update

1. MiddleOak Insurance Co. v. Tri-State Sprinkler Corp., 77 Mass. App. Ct. 336 (2010).

In 2010, the Massachusetts Appeals Court decided that a standard American Institute of Architects (“AIA”) waiver of subrogation clause in a construction contract applies to both construction and post-construction losses. As a result of the decision, one needs to ensure that a waiver of subrogation provision properly reflect the parties’ intent to extend the waiver of subrogation to both construction and post-construction losses. Where a waiver of subrogation provision applies to the “Work” and the contract defines “the Work” as construction and services, whether completed or not, the waiver provision applies to insurance coverage provided even after completion of the project.

2. Trace Construction, Inc. v. Dana Barros Sports Complex, LLC, 459 Mass. 346 (2011)

In 2011, the Supreme Judicial Court clarified the distinction between the rights of a general contractor and subcontractor to establish a mechanics lien when performing work for a tenant. The Court held that a general contractor, hired by a lessee to perform renovation work on leased property, may, under M.G.L. c. 254, §2, establish a mechanics lien on the lessor’s fee interest if the work was performed with the consent of the lessor.

The Court additionally held that a subcontractor may not establish a mechanics lien against the lessor’s fee interest because the language in G.L. c. 254, §4 is notably different than §2 in that that §4 limits the subcontractor’s lien to property owned by the party who entered into the original contract. Unlike a general contractor, a subcontractor cannot therefore establish a lien against property owned by a person for whom, on whose behalf, or with whose consent the contract was made.

3. Costa v. Brait Builders Corporation, 463 Mass. 65 (2012)

In 2012, the Supreme Judicial Court held that a subcontractor’s contractual waiver of claims against general contractor’s payment bond for a public project violated public policy and, therefore was unenforceable. The Court reasoned that M.G.L. c. 149, §29 was originally enacted by the legislature to provide contractors working on a public project similar security to that which a mechanics lien provides on a private project. The Court reasoned that if the right to file a mechanics lien cannot be waived, then neither should the right to pursue a payment bond claim.

¹ M.G.L. c. 254, § 2 (general contractor's lien); M.G.L. c. 254, § 4 (subcontractor's lien).

² Absent a written contract, a mechanics' lien may be obtained only for personal labor for "not more than thirty days' work actually performed" during the 90 days preceding recording a statement of claim. M.G.L. c. 254, § 1.

³ A party with a written contract with "the owner of any interest in real property, or with any person acting for, on behalf of, or with the consent of such owner," for "the whole or part of the erection, alteration, repair or removal of a building, structure, or other improvement to real property, or for furnishing material or rental equipment, appliances, or tools therefor," may enforce a lien upon such property as "owned by the party with whom or on behalf of whom the contract was entered into, as appears of record on the date when notice of said contract is filed or recorded in the registry of deeds for the county or district where such land lies." M.G.L. c. 254, § 2.

⁴ M.G.L. c. 254, § 4.

⁵ *Nat'l Lumber Co. v. United Cas. & Sur. Ins. Co.*, 440 Mass. 723, 728 (2004).

⁶ M.G.L. c. 254, § 6 ("No lien shall attach to any land, building or structure thereon owned by the commonwealth, or by a county, city, town, water or fire district.")

⁷ *Nat'l Lumber Co. v. United Cas. & Sur. Ins. Co.*, 440 Mass. 723 (2003); *NG Bros. Constr. v. Cranney*, 436 Mass. 638, 644 (2002); *East Coast Steel Erectors, Inc. v. Ciolfi*, 417 Mass. 602, 605 (1994); *Pratt & Forrest Co. v. Strand Realty Co.*, 233 Mass. 314, 318 (1919).

⁸ M.G.L. c. 254, § 15A.

⁹ M.G.L. c. 254, § 32.

¹⁰ The form of the Notice of Contract is set forth in the statute, M.G.L. c. 254, § 2.

¹¹ M.G.L. c. 254, § 8.

¹² M.G.L. c. 254, § 8.

¹³ M.G.L. c. 254, § 11.

¹⁴ M.G.L. c. 254, § 5.

¹⁵ The form of the Notice of Contract is set forth in the statute, M.G.L. c. 254, § 4.

¹⁶ M.G.L. c. 254, § 4.

¹⁷ M.G.L. c. 254, § 4; *BloomSouth Flooring Corp. v. Boys' and Girls' Club of Taunton*, 440 Mass. 618, 620 (2003).

¹⁸ M.G.L. c. 254, § 4.

¹⁹ M.G.L. c. 254, § 15.

²⁰ M.G.L. c. 254, § 10.

²¹ M.G.L. c. 254, § 14.

²² M.G.L. c. 254, § 14.

²³ M.G.L. c. 254, § 12.

²⁴ M.G.L. c. 260, § 2.

²⁵ M.G.L. c. 106, § 2-725.

²⁶ M.G.L. c. 260, § 2B.

²⁷ *Pagliuca v. Boston*, 35 Mass. App. Ct. 820, 824 (1994).

²⁸ *Riley v. Presnell*, 409 Mass. 239, 245-48 (1991).

²⁹ *White v. Peabody Constr. Co.*, 386 Mass. 121, 130 (1982).

³⁰ M.G.L. c. 106, § 2-725 (2007); *Bay State-Spray & Provincetown S.S., Inc. v. Caterpillar Tractor Co.*, 404 Mass. 103, 110-11 (1989); *Wilson v. Hammer Holdings, Inc.*, 850 F.2d 3, 7 (1st Cir. 1988).

³¹ M.G.L. c. 260, § 5A.

³² M.G.L. c. 260, § 2B.

³³ *Dighton v. Federal Pacific Elec. Co.*, 399 Mass. 687, 695 (1987), *cert. denied* 484 U.S. 953 (1987); *Fine v. Huygens*, 57 Mass. App. Ct. 397, 401-02 (2003) (manufacturer of custom GFRC panels deemed protected actor).

³⁴ *Klein v. Catalano*, 386 Mass. 701, 718 (1982).

³⁵ *Gomes v. Pan American Assoc.*, 406 Mass. 647, 648 (1990).

³⁶ *Anthony's Pier Four, Inc. v. Crandall Dry Dock Engineers, Inc.*, 396 Mass. 818, 823 (1986).

³⁷ *Tindol v. Boston Housing Authority*, 396 Mass. 515, 519 (1986).

³⁸ *Ferrera & Sons, Inc. v. Samuels*, 21 Mass. App. Ct. 170, 174 (1985), *rev. denied* 396 Mass. 1106 (1986).

³⁹ M.G.L. c. 93A, § 9.

⁴⁰ M.G.L. c. 93A, § 9; *Spring v. Geriatric Authority of Holyoke*, 394 Mass. 274, 287 (1985).

⁴¹ *Kohl v. Silver Lake Motors, Inc.*, 369 Mass. 795, 801-02 (1976).

⁴² *Commerce Ins. Co. v. Betty Caplette Builders, Inc.*, 420 Mass. 87, 92 (1995).

⁴³ *Boston Gas Co. v. Century Indem. Co.*, 454 Mass. 337, 350 (2009).

⁴⁴ *Trustees of Tufts University v. Commercial Union Ins. Co.*, 415 Mass. 844, 853-54 (1993) (persistence of pollution from earlier industrial activity held to trigger insurers' duty to defend).

⁴⁵ In *Rubenstein v. Royal Ins. Co. of Am.*, 44 Mass. App. Ct. 842, 853-54 (1998), the Appeals Court ruled that a trial court had not erred in refusing to apportion the insureds' damages among all of the years in which pollution occurred holding that each insurer is jointly and severally liable for the entire claim. As the trial court had concluded that property was continuously being contaminated by the leakage of oil during Royal's 1969-72 policy, the Appeals court ruled that it was this continuous exposure to contaminants that was decisive and that Royal's claim for allocating damage awards among other years of coverage must fail. The Appeals Court ruled in *Chicago Bridge & Iron Co. v. Certain Underwriters at Lloyds*, 59 Mass. App. Ct. 646 (2003), *rev. denied* 441 Mass. 1101 (2004) (Illinois law) that a Superior Court had correctly ruled that a polluter was entitled to recover the entirety of its loss under certain umbrella policies issued before 1970. See also *Boston Gas Co. v. Century Indem. Co.*, No. 02-12062 (D. Mass. June 21, 2006) (opining that there is no reason to believe the Supreme Judicial Court would not follow "all sums" approach).

⁴⁶ *Herson v. New Boston Garden Corp.*, 40 Mass. App. Ct. 779, 782 (1996), *rev. denied* 423 Mass. 1108 (1996); *Speers v. H.P. Hood, Inc.*, 22 Mass. App. Ct. 598, 600 (1986), *rev. denied* 398 Mass. 1105 (1986).

⁴⁷ M.G.L. c. 149, § 29C provides as follows: "Any provision for or in connection with a contract for construction, reconstruction, installation, alteration, remodeling, repair, demolition or maintenance work, including without limitation, excavation, backfilling or grading, on any building or structure, whether underground or above ground, or on any real property, including without limitation any road, bridge, tunnel, sewer, water or other utility line, which requires a subcontractor to indemnify any party for injury to persons or damage to property not caused by the subcontractor or its employees, agents or subcontractors, shall be void."

⁴⁸ In *Harnois v. Quannapowitt Dev.*, 35 Mass. App. Ct. 286, 288 (1993), *rev. denied* 416 Mass. 1106 (1993), the Appeals Court ignored the effect of the indemnification provision as applied to the facts of the particular case before it. The court recognized that indemnity disputes between general contractors and subcontractors were unduly burdening the courts and parties with time-consuming assessments of negligence and comparative negligence.

⁴⁹ In *M. DeMatteo Construction Co. v. A.C. Dellovade, Inc.*, 39 Mass. App. Ct. 1, 3-4 (1995), *rev. denied* 421 Mass. 1103 (1995), the Massachusetts Appeals Court determined that an indemnity provision which contained the language "arising out of or in consequence of the performance of the subcontractor's work" survived the state's anti-indemnity statute because the language limited the subcontractor's indemnity obligation to situations where there was a causal connection between the subcontractor's work and the injury. In addition, the Court determined that the anti-indemnity statute does not require a finding of negligence in order to trigger the indemnity obligation.

⁵⁰ *Callahan v. A.J. Welch Equip. Corp.*, 36 Mass. App. Ct. 608, 611-613 (1994).

⁵¹ *Id.* at 614 n. 6 (1994); *Amoco Oil Co. v. Buckley Heating, Inc.*, 22 Mass. App. Ct. 973, 973 (1986).

⁵² In *Cheschi v. Boston Edison Co., et al.*, 39 Mass. App. Ct. 133, 142 (1995), *rev. denied* 421 Mass. 1102 (1995), *rev. denied* 421 Mass. 1105 (1995), the Massachusetts Appeals Court determined that the owner's failure to give the contractor notice of a negligence claim brought against it by an employee of the contractor until four years after the accident and two and one-half years after the negligence action was filed relieved the contractor of its obligation to defend and indemnify the owner, where the indemnity provision specifically required prompt notification as a condition precedent to the contractor's indemnification.

⁵³ *North American Site Developers, Inc. v. MRP Site Development, Inc.*, 63 Mass. App. Ct. 529, 534-35 (2005).

⁵⁴ M.G.L.c. 149 § 29E (e).

⁵⁵ *McDonough v. Whalen*, 365 Mass. 506, 515 (1974).

⁵⁶ *Id.* at 512; *Zompetti v. Fleetwood Travel Trailers of Maryland, Inc.*, 63 U.C.C. Rep. Serv. 2d 333 (Mass. Super. Ct. 2007).

⁵⁷ M.G.L. c. 93A, § 2.

⁵⁸ *Maillet v. ATF-Davidson Co.*, 407 Mass. 185, 193 (1990); 940 C.M.R. 3.08(2).

⁵⁹ M.G.L. c. 142A, § 17.

⁶⁰ *Ficara v. Belleau*, 331 Mass. 80, 82 (1954).

⁶¹ *John Hetherington & Sons, Ltd. v. William Firth Co.*, 210 Mass. 8, 21 (1911).

⁶² *Bonacorso Construction Corp. v. Commonwealth*, 41 Mass. App. Ct. 8, 13 (1996); *Reynolds Bros. v. Commonwealth*, 412 Mass. 1, 7 (1992); *B.J. Harland Electrical Co. v. Granger Bros.*, 24 Mass. App. Ct. 506, 509 (1987), *rev. denied* 400 Mass. 1105 (1987), *rev. denied* 401 Mass. 1101 (1995).

⁶³ *Reynolds Bros. v. Commonwealth*, 412 Mass. 1, 7 (1992).

⁶⁴ *Fisher v. Stop & Shop*, 387 Mass. 889, 893-94 (1983).

⁶⁵ *Berish v. Bornstein*, 437 Mass. 252, 267 (2002).

⁶⁶ *Marcil v. John Deere Indus. Equip. Co.*, 9 Mass. App. Ct. 625, 630 n. 3 (1980).

⁶⁷ *McDonough v. Whalen*, 365 Mass. 506, 513-14. (1974)

⁶⁸ M.G.L. c. 231, §§ 6B & 6C.

⁶⁹ M.G.L. c. 231, § 6B.

⁷⁰ M.G.L. c. 231, § 6C.

⁷¹ M.G.L. c. 229, § 2.

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I. MECHANIC'S LIEN BASICS

Contractors, subcontractors, suppliers, and laborers who provide an improvement to real property have the right to record a lien against the property upon which an improvement was provided.¹ An owner must notify everyone that a construction project is about to begin through the notice of commencement of physical improvements to real property.² The notice of commencement provides the basic information which a lien claimant needs to perfect its construction lien.

A. Requirements

A subcontractor or supplier must provide a notice of furnishing to the designee and the general contractor identified in the notice of commencement either personally or by certified mail within 20 days after furnishing the first labor or materials. A contractor that has a direct contract with the owner is not required to provide a notice of furnishing to preserve lien rights.³ A laborer is required to provide a notice of furnishing to the designee and the general contractor either personally or by first-class mail, postage pre-paid, within 30 days after wages were contractually due, but not paid.⁴ With respect to withholding benefits, a laborer must provide a notice of furnishing to the designee and the general contractor either personally or by certified mail by the fifth day of the second month following the month in which fringe benefits or withholding from wages were contractually due, but not paid.

All lien claimants must record a claim of lien in the office of the register of deeds for the county where the property is located within 90 days after the lien claimant's last furnishing of labor or materials for the improvement.⁵ The claim of lien must have attached to it a proof of service of notice of furnishing if the lien claimant did not have a direct contract with the owner. The lien and proof of service also must be served within 15 days after the date of recording either by service upon the designee, personally, or by certified mail, return receipt requested.

The claim of lien must include the first day of providing labor or materials for an improvement, the last day of providing labor and materials for an improvement, the name of the owner of the property, the legal description, the amount of the contract, and what was received from a contractor (the difference between the amount of the claim of lien) or (with respect to laborers) the hourly rate, including fringe benefits and withholding in the amount owing.

B. Enforcement and Foreclosure

Substantial compliance with the 90-day recording requirement is dealt with on a case-by-case basis as to whether it is sufficient to create a valid lien.⁶ Suits to enforce liens must be brought in the circuit court for the county where the real property is located within one year after the date the claim of lien was recorded.⁷ The parties to be named in the complaint will be the owner and co-owner, any lessee who is contracted for the improvement, land contract vendees, land contract vendors who have consented to a mortgage and any other person whose interest in the land or improvement is claimed to be subordinate to the construction lien. At the time of filing suit, the lien claimant must record a notice of lis pendens in the register of deeds of the county where the real property is located. Further, the complaint must show that the owner or lessee was provided a sworn statement if one was requested or required.⁸

C. Ability to Waive and Limitations on Lien Rights

An owner of real property shall not require, as part of any contract for an improvement to the real property, that the right to a construction lien be waived in advance of work performed.⁹ A waiver obtained as part of a contract for an improvement is contrary to public policy, and shall be invalid, except to the extent that payment for labor and material furnished was actually made to the person giving the waiver. Acceptance by a lien claimant of a promissory note or other evidence of indebtedness from an owner, lessee, or contractor shall not of itself serve to waive or discharge otherwise valid construction lien rights.¹⁰

II. STATUTES OF LIMITATION AND REPOSE

A. Statutes of Limitation and Limitations on Application of Statutes

The statute of limitations for an action involving death, personal injury or property damage against a state licensed architect, state licensed engineer or professional surveyor is two (2) years.¹¹ The statute of limitations for an action against a contractor arising out of death, personal injury or property damage is three (3) years.¹² The statute of repose against a state licensed architect, state licensed engineer, professional surveyor, and contractor is six (6) years.¹³ The statute of repose allows for one (1) additional year to maintain an action after the defect “is discovered or should have been discovered, provided that the defect constitutes the proximate cause of the injury or damage for which the action is brought and is the result of gross negligence on the part of the contractor or licensed architect or professional engineer.”¹⁴

Also, Minors’ personal injury claims are not tolled under MCL 600.5839.¹⁵

B. Statutes of Repose and Limitations on Application of Statutes

The statute of repose for an action involving death, personal injury or property damage against a state licensed architect, engineer, land surveyor or contractor is six (6) years from the “time of occupancy of the completed improvement, use, or acceptance of the improvement...”¹⁶

This statute of repose applies to a licensed architect, professional engineer and professional surveyor from any state. Michigan licensure is not required.¹⁷

The statute of limitations and statute of repose for a breach of contract action relating to a defect in a building improvement are governed by the general statute of limitations for breach of contract actions and are not governed by the professional malpractice and contractor statute of limitations and statute of repose.¹⁸

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

With respect to legal claims being pursued in litigation, Michigan has no statutory or common law requiring pre-suit notice of a claim or an opportunity to cure a defect. With respect to complaints filed against a residential builder's license, once a proceeding has been initiated and necessary repairs have been identified, but not performed, the complainant is required to demonstrate that notice was provided to the licensee describing reasonable times and dates that the residential structure was accessible for the needed repairs.¹⁹ In addition, the complainant shall provide acceptable proof that the repairs were not made within 60 days after the sending of the notice.²⁰

IV. INSURANCE COVERAGE AND ALLOCATION ISSUES

A. General Coverage Issues

A Comprehensive General Liability ("CGL") insurance policy, in its simplest sense, provides coverage for operations of an entity and for an injury or property damage which may result from operations of the insured which are put to their intended use. These are occurrence-based policies which provide coverage to the insured during the applicable policy period, based upon the time when the act or conduct giving rise to the claim occurs.

B. Trigger of Coverage

As with contract actions, the language of the insurance policy governs. Interpretation of an insurance policy requires a two-step inquiry: (1) a determination of coverage according to the general insurance agreement; and (2) a decision whether an exclusion applies to negate coverage.²¹

The first issue which arises from any construction project is whether an "occurrence" has taken place. The courts generally will look to whether a bodily injury or property damage is caused by an occurrence that takes place in the coverage territory and during the policy period. The definition of "occurrence" requires an "accident".²² An accident has been defined as a "undesigned contingency, a casualty, a happening by chance, something out of the usual course of things, unusual, fortuitous, not anticipated, and not naturally to be expected."²³ No accident occurs when a builder supplies a defective product or performs in an unacceptable manner.²⁴ Conversely, when an insured's defective workmanship results in damage to the property of others, an "accident" exists within the meaning of the standard comprehensive liability policy.²⁵

This interpretation is consistent with the overall scheme of liability insurance which is to provide coverage for unforeseen events, and not to serve as a substitute for a bond.

Even with an occurrence, construction-related claims also raise the issue regarding the scope of “builders-risk” exclusions within the policy. These exclusions, such as the “your work” exclusion, bar coverage for the insured’s work without additional damage. Again, the language of the policy governs.

C. Allocation Among Insurers

Where concurrent duties to defend are triggered, allocation of defense costs is typically made on the same basis as allocation of the loss with regard to those policies with a duty to defend.²⁶ The inquiry should be whether the terms of the policies at issue cover the same loss, the same risk, and the same subject matter. If there is concurring coverage, an analysis should be conducted to determine whether it is appropriate to prorate the costs of defense. Since shares of loss are often governed by contract, applying these same shares to cost of defense makes contractual as well as equitable sense.²⁷

Thus, it is often presumed that if there is more than one primary insurer, each will share the duty to defend and prorate their contributions.

V. CONTRACTUAL INDEMNIFICATION

MCL 691.991 voids an indemnity agreement in a construction contract which purports to indemnify the indemnitee for the consequence of the indemnitee’s “sole negligence”.²⁸ It has been held that “sole negligence” means 100% fault for the totality of the personal injury or property damage claim.²⁹

Michigan does not require an indemnity provision to expressly state that the indemnitor must indemnify the indemnitee for the consequences of the indemnitee’s own (as opposed to “sole”) negligence so long as the language of the indemnity provision, the situation of the parties, and the surrounding circumstances established that was the parties’ intent. For example, employment of “all-inclusive” language such as “any” or “all” or “any and all” when referring to claims has been interpreted in Michigan as inclusive of the indemnitee’s own negligence.³⁰

MCL 691.991 also has been limited to contracts calling for the performance of work on the site and is not, for example, applicable to contracts pertaining to the lease of construction equipment to be used at a job site.³¹

Michigan permits indemnity invalidity language to be severed from an indemnity provision so long as the language which remains complies with MCL 691.991. Thus, for example, an indemnity provision which requires an indemnitor to indemnify the indemnitee for claims caused “in whole or in part” by the negligence of the indemnitee can be validated under the statute by simply severing the words “in whole” from the indemnity provision.³²

The Michigan Supreme Court recently held that failure to indemnify pursuant to a clear and unambiguous indemnity provision is a distinct breach of contract action from a claim based on the failure to install the structure according to specifications, and that any indemnity action necessarily accrued at a later point.³³

VI. CONTINGENT PAYMENT AGREEMENTS

A. Enforceability

Michigan courts will enforce a properly drafted “pay-if-paid” provision as a condition precedent to pay downstream subcontractors.³⁴ Failure to satisfy a condition precedent prevents a cause of action for failure to perform; hence a downstream contractor has no cause of action against an upstream contractor who has not been paid for its work.³⁵ Moreover, Michigan courts have held that so long as the upstream contractor fulfills any condition that requires it to take active measures to collect money due from the owner/general contractor, downstream subcontractors will be bound to the “pay-if-paid” provision and will only be paid when the upstream contractor is, itself, paid.³⁶

B. Requirements

In *Berkel*, the Court clarified that a “pay-if-paid” clause must be carefully drafted and payment by the owner or the upstream contractor must be a specifically acknowledged condition precedent to the upstream contractor’s obligation to pay the downstream contractor. Although not expressly provided in the *Berkel* decision, a valid contingent payment provision should: (1) use the term “condition precedent”; (2) avoid language suggesting the upstream contractor is deferring payment to the subcontractor, only; and (3) explicitly state that the downstream contractor will be paid only when the upstream contractor is paid.

VII. DAMAGE LIMITATIONS

A. Personal Injury Damages vs. Construction Defect Damages

For a claim based on deficiencies in the structure itself brought by the party who hired an architect, professional engineer or professional surveyor, the measure of damages is the standard damages awarded in breach of contract actions. Thus, the “benefit of the bargain” will be awarded as damages and all expectation damages that were in the contemplation of the parties at the time of the contract may be awarded. In actions involving personal injuries due to structural deficiencies, all economic and noneconomic damages awarded in ordinary negligence actions are recoverable.

B. Attorney’s Fees Shifting and Limitations on Recovery

In Michigan, the general rule is that attorney fees are not recoverable as either costs or damages unless recovery is expressly authorized by contract, statute, court rule, or a recognized exception to the general rule.³⁷ Exceptions are to be narrowly construed and may include limited

situations in which a party has incurred legal expenses as a result of another parties' fraudulent or unlawful conduct.³⁸

C. Consequential Damages

Generally, parties may only recover actual damages. Consequential damages are those which a party has reason to foresee as ordinary, natural consequences of a breach when the contract was made. To recover consequential damages, they must be reasonably within the contemplation of the parties at the time they enter into the contract.³⁹

D. Delay and Disruption Damages

Delay and disruption damages may be allowed if there is evidence of active interference of the contract by a defendant or other contractors.⁴⁰ The plain language of the contract must support the party's contention that these types of claims were outside the scope of plaintiff's duties. When analyzing the plaintiff's claims for delay and disruption, the court is not bound by the plaintiff's choice of labels for the alleged damages.⁴¹

Pursuant to recent case law, however, a contractor cannot sue a design professional for damages when things go awry on a project due to the alleged negligence of the design professional.⁴² Under previous Michigan Law, a contractor could file suit against a design professional to recover damages caused by the design professional's negligence despite the absence of direct contractual privity.⁴³ In *Keller, supra*, the Michigan Court of Appeals held, as a matter of law, a contractor cannot maintain a claim for damages stemming from the design professionals negligence in performing its contract duties on a project where the duties arose from the design professionals contract. Only where the contractor can point to a breach of a duty separate and distinct from the design professional's responsibilities set forth in the contract documents can a contractor maintain a claim against a design professional.

E. Economic Loss Doctrine

In cases involving defective goods, Michigan courts have applied the economic loss doctrine to bar tort theories of recovery where the loss is economic.⁴⁴ The economic loss doctrine bars tort remedies where a sale of goods is involved, the only injury is damage to the goods themselves, and the only losses alleged are economic. The doctrine applies even in the absence of contractual privity.⁴⁵ The economic loss doctrine has also been applied to a claim for negligent misrepresentation.⁴⁶

In Michigan, the application of the economic loss doctrine has been limited to contracts for the sale of goods. The doctrine has not been applied to contracts for services or to contracts for mixed goods and contracts that predominantly involve services.

F. Interest

The Michigan judgment interest statute is found at MCL 600.6013 and provides for judgment interest to be awarded only from the date that the judgment was entered. Pre-complaint interest is awardable by the trier of fact as an element of damages in some cases.⁴⁷

G. Punitive Damages

Michigan courts do not permit punitive damages, except as provided by statute.⁴⁸ Exemplary damages, on the other hand, are those awarded to compensate for mental anguish, humiliation, outrage or increased injury to the plaintiff's feelings that he or she suffers due to the defendant's willful, malicious, or wanton conduct or reckless disregard for the plaintiff's rights.⁴⁹ Exemplary damages are not punitive in nature. Thus, exemplary damages generally are awarded in the context of intentional torts, slander, libel, deceit, seduction, and other intentional, malicious acts.⁵⁰

Exemplary damages generally are not available for breach of a commercial contract.⁵¹ In terms of construction contracts, an allegation of promissory fraud was not sufficiently independent of the contract breach to permit recovery of exemplary damages.⁵²

VIII. CASE LAW AND LEGISLATION UPDATE

A. Content of Contract Do Not Preempt Common Law Legal Duty

Common law governs Michigan tort cases. The rule in Michigan is that if a party fails to perform a contractual obligation, it cannot be held liable to a third party.⁵³ If a party does perform a contractual obligation, it may have a common law duty to third persons to do so in a non-negligent manner so as to not injure them. Accordingly, the question turns on whether, aside from a contract, a party owed any independent legal duty to a third person.⁵⁴

B. Common Work Area Doctrine

A subcontractor injured on the project may bring a cause of action against the project owner or general contractor if he is able to establish: (1) the defendant, either the property owner or general contractor, failed to take reasonable steps within its supervisory and coordinating authority (2) to guard against readily observable and avoidable dangers (3) that created a high degree of risk to a significant number of workmen (4) in a common work area.⁵⁵ Moreover, for the project owner to be liable, the plaintiff must prove that the owner "retained control" of the project and that the mere right to control an independent contractor's work is insufficient to establish the "retained control" theory against the owner.⁵⁶

C. Residential Builders

The Michigan Consumer Protection Act (MCPA) exempts any transaction or conduct specifically authorized under laws administered by a regulatory board or officer acting under

statutory authority of this state or the United States.⁵⁷ Accordingly, licensed residential home builders are exempt from the MCPA because the general transaction of residential home building, including contracting to perform such transaction, is “specifically authorized” by the Michigan Occupational Code.⁵⁸

¹ MCL 570.1107

² MCL 570.1108

³ MCL 570.1109

⁴ MCL 570.1109

⁵ MCL 570.1111

⁶ *Cent Ceiling & Partition, Inc. v. Dep’t. of Commerce*, 249 Mich. App. 438, 440; 642 N.W.2d 397, 399 (2002), aff’d 470 Mich. 877 (2004); *Northern Concrete Pipe, Inc. v. Sinachola Companies- Midwest, Inc.*, 603 N.W.2d 257 (Mich. 1999).

⁷ MCL 570.1117

⁸ MCL 570.1117

⁹ MCL 570.1115

¹⁰ MCL 570.1115

¹¹ MCL 600.5805(14). Previously, the Michigan Supreme Court ruled that MCL 600.5839(1) acted as both a statute of limitations and repose. Accordingly, the Supreme Court imposed a six (6) year statute of limitations as to all claims for personal injury or property damage against a state licensed architect, engineer or contractor. *Ostroth v. Warren Regency, GP, LLC*, 474 Mich. 36, 709 N.W.2d 589 (2006). Effective January 1, 2012, the Michigan Legislature took action to return MCL 600.5839(1) to a six (6) year statute of repose, only.

¹² MCL 600.5805(10)

¹³ MCL 600.5839(1).

¹⁴ *Id.*

¹⁵ *Smith v. Quality Constr. Co.*, 503 N.W.2d 753 (Mich. App. 1994).

¹⁶ MCL 600.5839(1).

¹⁷ *Cliffs Forest Products Co. v. Al Disendro Lumber Co.*, 375 N.W.2d 397 (Mich. App. 1985), appeal denied, 384 N.W.2d 8 (Mich. 1986).

¹⁸ The Michigan Supreme Court recently held that the contractor statute of limitations and repose applies to tort actions against contractors for injury to person or property or for defective and unsafe conditions, but actions against contractors for breach of contract, relating to a defect in a building improvement, are governed by the general statute of limitations for breach of contract actions and are not governed by the contractor statute of repose, *Miller-Davis Co. v. Ahrens Const., Inc.*, 489 Mich. 355, 802 N.W.2d 33 (2011) overruling *Michigan Millers Mut. Ins. Co. v. West Detroit Bldg. Co.*, 196 Mich. App. 367, 494 N.W.2d 1.

¹⁹ MCL 339.2411(4)(f)

²⁰ *Id.*

²¹ *Hastings Mut. Ins. Co. v. Mosher, Dolan, Cataldo & Kelly, Inc.*, 2006 WL 1360404 (Mich. App. 2006).

²² *Id.*

²³ *Hawkeye-Security Ins. Co. v. Vector Construction Co.*, 460 N.W.2d 329 (Mich. App. 1990).

²⁴ *Id.*

²⁵ *Radenbaugh v. Farm Bureau Gen. Ins. Co. of Michigan*, 610 N.W.2d 272, 279-80 (Mich. App. 2000).

²⁶ *Insurance Co. of North America v. Forty-Eight Insulations, Inc.*, 633 F.2d 1212, (6th Cir 1980); *Frankenmuth Mut. Ins. Co. v. Continental Ins. Co.*, 450 Mich. 429, 537 N.W.2d 879 (1995).

²⁷ *Frankenmuth Mut. Ins. Co. v. Continental Ins. Co.*, 450 Mich. 429, 537 N.W.2d 879 (1995).

²⁸ The statute reads as follows: A covenant, promise, agreement or understanding in or in connection with or collateral to, a contract or agreement relative to the construction, alteration, repair or maintenance of a building, structure, appurtenance and appliance, including moving, demolition and excavating connected therewith, purporting to indemnify the promisee against liability for damages arising out of bodily injury to persons or damage to property caused by or resulting from the sole negligence of the promisee or indemnitee, his agents, or employees, as against public policy and is void and unenforceable.

²⁹ *Fischbach-Natkin Co. v. Power Process Piping, Inc.*, 403 N.W.2d 569 (Mich. App. 1987).

³⁰ *Paquin v. Harnischfeger Corp.*, 317 N.W.2d 279 (Mich. App. 1982).

³¹ *Pritts v. J.I. Case Co.*, 310 N.W.2d 261 (Mich. App. 1981).

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- ³² *Trim v. Clark Equip. Co.*, 274 N.W.2d 33 (Mich. App. 1978).
- ³³ *Miller-Davis Company v. Ahrens Construction Inc.* __ Mich. __ (Filed April 15, 2014).
- ³⁴ *Berkel & Co. Contractors v. Christman Co.*, 210 Mich. App. 416; 533 N.W.2d 838 (1995) (sometimes cited as *Christman Co. v. Anthony S. Brown Dev. Co.*, 533 N.W.2d 838 (1995)).
- ³⁵ *Lee v. Auto-Owners Ins. Co.*, 201 Mich. App. 39, 43, 505 N.W.2d 866 (1993).
- ³⁶ *Berkel*, *surpa* at 420.
- ³⁷ *Nemeth v. Abonmarche Dev., Inc.*, 576 N.W.2d 641 (Mich. 1998); *Burnside v. State Farm Fire and Cas. Co.*, 528 N.W.2d 749 (Mich. App. 1995).
- ³⁸ *Brooks v. Rose*, 478 N.W.2d 731 (Mich. App. 1991).
- ³⁹ *Kewin v. Massachusetts Mutual Life*, 295 N.W.2d 50 (Mich. 1980); *Lawrence v. Will Derrah & Assoc., Inc.*, 516 N.W.2d 43 (Mich. 1994).
- ⁴⁰ *Phoenix Contractors, Inc. v. General Motors Corp.*, 355 N.W.2d 673 (Mich. App. 1984).
- ⁴¹ *Johnston v. City of Livonia*, 441 N.W.2d 41 (Mich. App. 1989).
- ⁴² *Keller Construction, Inc., v. U.P. Engineers & Architect, Inc.*, 2008 WL 2665113 (July 8, 2008) lv den 482 Mich. 1068; 757 N.W.2d 500 (2008).
- ⁴³ *Bacco Constr. Co. v. American Colloid Co.*, 148 Mich. App. 397; 384 N.W.2d 427 (1986).
- ⁴⁴ *Neibarger v. Universal Cooperatives, Inc.* 486 N.W.2d 612 (Mich. 1992).
- ⁴⁵ *Sullivan Industries, Inc. v. Double Seal Glass Company, Inc.* 480 N.W.2d 623 (Mich. App. 1991).
- ⁴⁶ *Bailey Farms, Inc. v. NOR-AM Chemical Company*, 27 F.3d 188 (6th. Cir. 1994).
- ⁴⁷ M Civ J I 53.04.
- ⁴⁸ *Jackson Printing Co. v. Mitani*, 425 N.W.2d 791 (Mich. App. 1988).
- ⁴⁹ *Peisner v. Detroit Free Press*, 364 N.W.2d 600 (Mich. 1984).
- ⁵⁰ *Veselenak v. Smith*, 327 N.W.2d 261 (Mich. 1982).
- ⁵¹ *Kewin v. Massachusetts Mut. Life Ins. Co.*, 295 N.W.2d 50 (Mich. 1980).
- ⁵² *Tempo, Inc. v. Rapid Electric Sales and Service, Inc.* 347 N.W.2d 728 (Mich. App. 1984).
- ⁵³ *Loweke v. Ann Arbor Ceiling & Partition Co., LLC*, 489 Mich. 157 (2011), 809 N.W.2d 553 (June 6, 2011).
- ⁵⁴ *Id.*
- ⁵⁵ *Ormsby v. Capital Welding, Inc.*, 471 Mich. 45, 684 N.W.2d 320 (2004).
- ⁵⁶ *Candelaria v. BC General Contractors, Inc.*, 236 Mich. App. 67, 600 N.W.2d 348 (1999).
- ⁵⁷ MCL 445.904(1)(a).
- ⁵⁸ *Liss v. Lewiston-Richards, Inc.*, 732 N.W.2d 514, (Mich. App. 2007).

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I. MECHANIC'S LIEN BASICS

Chapter 514 of Minnesota Statutes provides for and governs mechanic's liens on private projects. Mechanic's liens provide a vehicle by which contractors, subcontractors, and certain suppliers can obtain a security interest in real property they improved, and, if necessary, compel the sale of the property in order to pay for the improvements they provided. The basic steps to preserve and perfect a mechanic's lien are described below. The failure to comply with these statutory requirements most likely will result in the loss of lien rights.

A. Requirements

Pre-Lien Notice. The person seeking the lien must provide the project owner a notice of that person's right to assert a lien for the value of work and/or materials that person provides to the property. The notice requirements differ depending on what kind of work the person provides. Minn. Stat. § 514.011 (2013) sets forth the requirements for general contractors, subcontractors, and material suppliers.¹ Some exceptions exist for pre-lien notice, including when the contractor is also the owner of the improved property, and when the work is done on an apartment building of more than four dwelling units or a non-agricultural commercial property.² When notice is required, it is important that those seeking a lien follow the specific timing provisions for the kind of work they perform.³

Mechanic's Lien Statement. If a contractor, subcontractor, or materials supplier has complied with the pre-lien notice requirements and does not receive payment, a mechanic's lien statement should be recorded against the owner's property. The lien holder must serve upon the owner and file with the appropriate state office a mechanic's lien statement.⁴ The recording of the mechanic's lien statement must be done within 120 days of the lien holder's last day of work or from the last supply of materials on a job.⁵ A contractor's last day of work is defined as when the work reaches "substantial completion." The statement must contain all of the information required by Minn. Stat. § 514.08, subd. 2 (2013). Certain circumstances may extend the lien deadline.⁶

B. Enforcement and Foreclosure

To secure the benefit of any mechanic's lien, the contractor, subcontractor, or materials supplier must commence foreclosure of its lien claim within one year of the last date of contribution to the property.⁷ If not commenced within one year, the mechanic's lien becomes unenforceable. Under Minnesota law, there are several advantages to a mechanic's lien foreclosure versus a regular civil action, including an earlier court hearing date and the right to collect attorney's fees if successful in foreclosing on the lien.⁸

A sheriff's sale of the property may be initiated following a successful foreclosure action. At the sale, the property is sold and the proceeds from the sale are used to pay off the interest holders in the property based upon their priority of interest. *See* Minn. Stat. § 514.15 (2013). Each mechanic's lien holder assumes priority based upon the date of the first visible improvement to the property made by the contractor, subcontractor or materials provider.⁹

Note for Public Projects: On a public project, there should be a payment bond in place for the protection of the subcontractors. The requirements for making a claim against the bond are essentially the same as the mechanic's lien requirements.

II. STATUTES OF LIMITATION AND REPOSE

The statutes of limitation and the repose periods applicable to construction defect claims are contained in one statute, Minn. Stat. § 541.051.¹⁰ This section provides a brief overview of the limits the statute places on potential causes of action arising from damage sustained from any service or construction that improves real property, and explores some of the important case law interpreting these provisions.

A. Statute of Limitations

Under Minn. Stat. § 541.051, subd. 1(a) (2013), absent fraud, all claims arising out of "the defective and unsafe condition of an improvement to real property" must be brought within two (2) years of discovery of the injury. Contribution and indemnification claims must be brought within two (2) years of the accrual of the cause of action.¹¹ For purposes of a construction defect, an action "accrues upon discovery of the injury,"¹² regardless of whether the full extent of the injury is known.¹³ In the case of an action for contribution or indemnity, an action accrues upon "the earlier of commencement of the action against the party seeking contribution or indemnity, or payment of a final judgment, arbitration award, or settlement arising out of the defective and unsafe condition."¹⁴

The date of discovery is determined by examining when a defect was actually discovered or, in the exercise of reasonable diligence, should have been discovered.¹⁵ This occurs when the claimants "[have] enough facts to be on notice that a potential injury may exist."¹⁶ The statute also requires claimants to act on what is known and to conduct a reasonable investigation to discover any injury.¹⁷

Minn. Stat. § 541.051 further sets the limitations period for new home warranties as provided in Minn. Stat. § 327A.02 (2013) – creating one, two, and 10-year warranties for purchasers of new residential construction.¹⁸ The warranties begin to run from the time the

initial purchaser first occupies or takes possession of the dwelling, whichever is earlier.¹⁹ A breach of warranty claim on a new home must be brought within two years of the date the homeowner discovers, or reasonably should have discovered, the builder's inability or refusal to honor the statutory warranties of Minn. Stat. § 327A.02 or any express written warranty.²⁰

B. Statutes of Repose

Minn. Stat. § 541.051 also contains statutes of repose applicable to construction defect claims. Minn. Stat. § 541.051, subd. 1(a) provides that a cause of action shall not accrue “more than ten years after the date of substantial completion of construction.” However, if the claim accrues (i.e., the injury is discovered) in the 9th or 10th year after substantial completion, a claim “may be brought within two years after the date on which the action accrued, but in no event may an action be brought more than 12 years after substantial completion of the construction.”²¹

In 2013, the statute of repose was again amended in regards to contribution and indemnity claims for defective and unsafe conditions resulting from improvements to real property. Back in 2007, § 541.051 was revised so that contribution and indemnity claims were no longer subject to the 10-year statute of repose.²² Pursuant to the 2007 amendments, therefore, all contribution and indemnity claims could be brought within two years of accrual regardless of whether the claims arose within 10 years of substantial completion of the project.²³ However, the 2013 amendment to § 541.051 reinstated a repose period for contribution and indemnity claims that was eliminated under the 2007 version of the statute.

Pursuant to amended § 541.051, contribution and indemnity claims now must be brought within 14 years after substantial completion of the improvement project. Moreover, these claims must also be brought no later than two years after accrual of any claim.²⁴

Critically, the 2013 amendment applies to all actions commenced on or after August 1, 2013. Yet, because the 2007 version of Minn. Stat. § 541.051 (which was made retroactive to June 30, 2006), applies to cases pending or commenced prior to August 1, 2013, contribution and indemnity claims in Minnesota can now fall into one of three categories: (1) claims barred by the repose statute prior to June 30, 2006, which continue to be barred, (2) claims for which the repose period did not expire by June 30, 2006, and commenced prior to August 1, 2013, are only subject to the two-year limitations period, and (3) claims for which the repose period did not expire by June 30, 2006, and are commenced after August 1, 2013 are subject both to the 14-year repose period and the two-year limitations period.

Last, the statute sets a repose period of 12 years for breach of warranty claims.²⁵ Any claim for breach of warranty must be brought within 12 years of the date the owner takes occupancy or legal title, whichever is earlier. In no event may any claim for breach of warranty accrue more than 12 years from this “warranty date.”²⁶

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

Before an owner may bring a claim for breach of statutory warranty, as provided for in Minn. Stat. § 327A.02, subd. (1), the vendor or home improvement contractor is entitled to notice of the claim and is given an opportunity to cure the alleged defect.²⁷

Minnesota requires a homeowner to provide the vendor or home improvement contractor with written notice “within six months after the [homeowner] discovers or should have discovered the loss or damage; unless the [homeowner] establishes that the vendor or home improvement contractor had actual notice of the loss or damage.”²⁸ Upon giving notice, the vendee or homeowner must allow for an inspection and give the vendor or home improvement contractor an “opportunity to offer to repair the known loss or damage.”²⁹

The vendor or home improvement contractor must conduct the inspection within thirty (30) days of receiving the notice. After the inspection, the vendor or contractor is provided fifteen (15) days to provide a written offer to repair the alleged defects.³⁰

If, after the inspection and the vendor’s or home improvement contractor’s delivery of an offer to repair, the parties agree to a scope of work for the repairs, the vendor/home improvement contractor must complete the repairs in accordance with the offer of repair.³¹ Upon completion of the repairs, the contractor must provide the homeowner with a “written notice that the scope of work agreed upon has been completed,” together with “a list of the repairs made and a notice that the [homeowner] may have a right to pursue a warranty claim[.]”³² If the homeowner and vendor/contractor cannot agree to a scope of work, the parties must submit the matter to Minnesota’s new home warranty dispute resolution process.³³ An action in district court cannot be commenced until the earlier of (1) completion of the dispute resolution process, or (2) sixty days after the offer of repair is provided to the homeowner.³⁴

However, should a homeowner fail to provide written notice within six months of discovering the loss or damage, the homeowner’s claims for breach of statutory warranty are barred unless the vendor/contractor had actual notice of the loss or damage.³⁵ This six-month statute of limitations begins to run when “an actionable injury is discovered, or with due diligence, should have been discovered.”³⁶ If appropriate notice is given, it is important that the vendor or contractor respond to the homeowner’s allegations and perform an inspection of the alleged damage within 30 days in order to prevent a possible future claim for breach of warranty.

IV. INSURANCE COVERAGE AND ALLOCATION ISSUES

A. General Coverage Issues

A standard commercial general liability (“CGL”) policy provides coverage for those amounts that the insured is legally liable to pay due to property damage that occurs during the applicable policy period. In construction defect cases, this obligation has proven difficult to apply. An insurer must first determine what insurance policy (or policies) is “triggered,” meaning, what policy applies to the loss.

B. Trigger of Coverage

Minnesota follows the “actual injury” rule to determine what liability policy or policies have been triggered.³⁷ Under the “actual injury” rule, “the time of the occurrence is not the time that the act resulting in liability is committed, but rather the time that the complaining party is actually damaged.”³⁸ Minnesota case law determining when damage has actually occurred and,

consequently, which policies have been triggered is wide-ranging and highly dependent upon the specific facts of each case.

The first question that must be answered when more than one policy is involved is whether the injury was continuous; for example, is it a progressive injury existing over multiple policy periods?³⁹ If the injury was not continuous, the policies on the risk at the time of the injury pay for all losses arising from the injury.⁴⁰ Next, if the injury was continuous, it must be determined whether the injury arose from a discrete, identifiable event.⁴¹ If it did, the policies on the risk at the time of that event are responsible for all damages arising out of that event.⁴² When an injury is both continuous and did not arise out of a discrete identifiable event, the damages are split based upon a modified “pro-rata-by-time-on-the-risk” analysis.⁴³ Minnesota courts place an emphasis on avoiding the allocation of damages between multiple insurers whenever possible.⁴⁴ Allocation is meant to be an exception and not the rule.⁴⁵ If it is possible to identify a discrete, identifiable originating event that allows for the avoidance of allocation, courts are encouraged to do so.⁴⁶

C. Allocation Among Insurers

As mentioned above, Minnesota courts are encouraged to avoid allocating damages between multiple insurers when possible. However, in those cases where the damage involved is continuous and not arising out of a discrete, identifiable event, Minnesota courts rely on pro-rata-by-time-on-the-risk approach to allocate damages. The pro-rata-by-time approach is applied as follows: (1) triggered policies are given a pro-rata allocation based upon their entire policy period irrespective of the date of construction; (2) allocation ends when the policyholder receives a notice of a claim, not the date of remediation; (3) policyholders who become voluntarily self-insured bear a proportionate share of liability; and (4) if insurance was unavailable during a part of the continuous period, the insurers on the risk cover the uninsured time.⁴⁷

In a pro-rata allocation scenario, defense costs are apportioned equally among all insurers involved, not pro-rata-by-time-on-the-risk.⁴⁸

D. Additional Insurance

Another risk shifting method that is utilized in construction contracts is the requirement that subcontractors procure insurance adding the general contractor as an additional insured. In Minnesota, the general rule is that construction contracts that require a subcontractor to indemnify the general contractor for liability for the subcontractor’s own negligence are not enforceable unless the construction contract requires procurement of specific insurance coverage of indemnity obligations. Minn. Stat. § 337.01 *eq seq.*⁴⁹ In such instances, Minnesota courts have interpreted additional insurance endorsements that limit coverage to damages caused by the subcontractor to require some showing of fault.⁵⁰

V. CONTRACTUAL INDEMNIFICATION

Minnesota does not allow indemnification in building and construction contracts unless there is a specific agreement to insure against the risk.⁵¹

Minn. Stat. § 337.02 (2013) provides that an indemnification agreement in a building

and construction contract is unenforceable except to the extent that the underlying injury or damage is attributable to the negligence of, or breach of contract by, the promisor or promisor's independent contractors, agents, employees, or delegates.⁵² In other words, each link in the chain of construction is responsible for the consequences of its own negligence.⁵³

On August 1, 2013, a significant amendment was made to Minn. Stat. § 337.05, subd. 1 – governing indemnification and risk-shifting insurance in construction contracts. The pre-amendment version of Minn. Stat. § 337.05, subd. 1 created an exception to this general prohibition by stating that “agreements whereby a promisor agrees to provide specific insurance coverage for the benefit of others” are valid,⁵⁴ thus allowing contracting parties to procure insurance benefiting each other. The newly amended version of §§ 337.05, subd. 1 now expressly bars “provision[s] that require[s] a party to provide insurance coverage to one or more other parties, including third parties, for the negligence or intentional acts or omissions of any of those other parties, including third parties” As a result, any additional insurance coverage provisions should be limited to the promisor's negligence or intentional acts to ensure enforceability.⁵⁵

Next, Minn. Stat. § 337.05, subd. 2 provides that a party who was required to purchase specific insurance and fails to do so will be obligated to indemnify the promisee to the extent of the specified insurance.⁵⁶ If the specific insurance would not have provided coverage for the damages alleged, no claim for indemnification exists.⁵⁷ Consequently, if the subcontractor agrees to procure insurance only to cover its own negligence, an indemnification provision in a contract requiring a subcontractor to indemnify a general contractor for its own negligence or the negligence of others is unenforceable.⁵⁸

Under Minn. Stat. § 337.05, subd. 3, indemnification is not available under a contractual agreement to provide insurance if the specified insurance was: (1) not reasonably available in the market; and (2) the promisor specifically informed the other party to insure itself before signing the contract or the contract was signed subject to a written exception to the unavailable insurance.

Finally, under Minn. Stat. § 337.05, subd. 5, the promisor's obligation to provide the specified insurance is not waived by the promisee's: (1) failure to require or insist upon certificates or other evidence insurance; or (2) the acceptance of a certificate or other evidence of insurance showing a variance from the specified coverage.

VI. CONTINGENT PAYMENT AGREEMENTS

The existence of contingent payment agreements between general contractors and subcontractors is almost standard in construction contracts. Generally speaking, these contingency provisions are known as “pay-when-paid” or “pay-if-paid” clauses. Pay-when-paid clauses provide that the subcontractors are paid when the general contractor, or surety company, is paid by the owner, while pay-if-paid provisions provide less assurance to the subcontractors and can work to shift the burden of nonpayment by owner.

Under Minnesota law, both types of contingent payment agreements are enforceable. However, when the clause is ambiguous it will be interpreted as a pay-when-paid contingency provision.⁵⁹ This is because Minnesota courts have adopted the rule that “court[s] will not

construe a subcontract to require payment to the general contractor as a condition precedent to payment to the subcontractor, absent unequivocal, unambiguous language to that effect.”⁶⁰

It should also be noted that Minnesota courts have not considered the validity of “no damage for delay” provisions, but they are statutorily unenforceable as to public works contracts.⁶¹

VII. DAMAGES LIMITATIONS

A. Personal Injury Damages vs. Construction Defect Damages

In an action for damages caused by personal injury Minnesota, particularly in negligence cases, the rule “is that one who commits a tort is liable for all the proximate consequences thereof. The test of the extent of liability is in causation and not in probability or foreseeability. The measure of recovery in each damage case depends upon its particular facts.”⁶² This standard allows the fact-finder in a particular case a great deal of latitude in determining the appropriate measure of damages based upon the circumstances involved.

In a construction defect case (not governed by statutory warranties), the measure of damages is generally “the cost of making the work conform to the contract.”⁶³ To achieve this standard, Minnesota courts use “either the cost of reconstruction in accordance with the contract, if this is possible without unreasonable economic waste, or the difference in the value of the building as contracted for and the value as actually built, if reconstruction would constitute unreasonable waste.”⁶⁴

Damages for defects in residential construction that violate Minnesota’s statutory warranties are governed by statute. Section 327A.05 of Minnesota Statutes limits these damages to “the amount necessary to remedy the defect or breach” or “the difference between the value of the dwelling without the defect and the value of the dwelling with the defect.”⁶⁵

B. Attorneys’ Fees

Attorney’s fees are available through contract, or by statute if a party acts in bad faith, and certain third-party practice.⁶⁶

C. Consequential Damages

Consequential damages are recoverable under a breach of contract claim in Minnesota.⁶⁷ Consequential damages are defined as damages naturally flowing from a contractual breach or that were reasonably contemplated as probable at the time of contract formation.⁶⁸ These damages can include expenses due to a defendant’s failure to perform in a workmanlike manner, costs to settle with the owner for a subcontractor’s breach, excess costs, loss of use, and lost profits to a reasonable certainty.⁶⁹

D. Delay and Disruption Damages

Delay and disruption damages may be calculated from the reasonable value of work done, including actual costs, overhead, and profits based on the bid price (i.e., total cost

method).⁷⁰ Escalation damages, arising where material and labor costs increase as well as idle equipment costs from delay or shutdown, are also collectable.⁷¹

E. Economic Loss Doctrine

The economic loss doctrine in Minnesota is codified in Minn. Stat. § 604.10 (2013) and applies to claims specified in Minn. Stat. § 604.101 (2013). Construction contracts can be treated as a commercial sale of goods unless predominantly for services.⁷² However, in actions for property damages arising from a sale of goods between parties not “merchants in goods of the kind,” recovery under negligence and strict liability theories is possible.⁷³

F. Interest

In Minnesota, claims collect simple interest on an annual basis at an established rate from the date the lawsuit is commenced.⁷⁴ The interest rate on awards in excess of \$50,000 is statutorily set at ten percent (10%).⁷⁵ For judgments less than \$50,000, the annual interest rate is set on an annual basis.⁷⁶ This rate is set at 4 percent (4%) for 2014.⁷⁷

G. Punitive Damages

A party claiming breach of contract is generally not entitled to punitive damages unless the breach constitutes an independent tort.⁷⁸ However, punitive damages are sometimes available for intentional property damage.⁷⁹ In such instances, the complaint should not seek punitive damages and the plaintiff should later make a motion to amend the pleadings to claim punitive damages.⁸⁰

VIII. CASE LAW AND LEGISLATION UPDATE

As mentioned briefly in Section II, the term “substantial completion” is used by Minn. Stat. § 541.051, subd. 1(a) (2013) to determine the triggering event for the 10-year statute of repose for claims arising out of construction projects to improve real property. On March 10, 2014, the Minnesota Court of Appeals in *Rosso v. Hallmark Homes of Minneapolis, Inc.*, 2014 Minn. App. LEXIS 22, *6 (Minn. Ct. App. Mar. 10, 2014) dealt with an issue of first impression – the interpretation of the phrase “substantial completion.” In *Rosso*, the Rossos argued that their claims were not barred by the statute of repose “because the city required a certificate of occupancy as a condition to occupy the home legally and that the home’s construction was not substantially completed until the certificate was issued,” thus delaying the triggering event long enough to allow for their defect claim to proceed.⁸¹

Applying a plain reading to the statute, defining the date of substantial completion to mean “the date when construction is sufficiently completed so that the owner or the owner's representative can occupy or use the improvement for the intended purpose,” Minn. Stat. § 541.051, subd. 1(a), the court rejected the Rossos’ argument.⁸² While the Rossos argued that such a holding would undermine the public policy reasons for requiring a certificate of occupancy, the court reiterated that the statute “specifically focuses on the extent to which a structure has been built as the measuring stick.”

In ruling, the court explicitly recognized that its holding very well might lead to critical factual questions regarding the degree to which a physical structure must be completed to reach “substantial completion.” Nevertheless, the court declined the opportunity to set a “bright-line rule that a structure that is 75, 85, or 95 percent complete has met this threshold.” As a result, more litigation regarding whether a project was “substantially completed” will likely follow the *Rosso* decision, as both owners and contractors alike work within the court system to more narrowly define the triggering event of Minn. Stat. § 541.051.

¹ For contractors, notice is required in the written contract for services or, if no written agreement is entered into, by a separate document delivered personally or by certified mail within ten (10) days of the work of improvement being agreed upon. Minn. Stat. § 514.011, Subd. 1 (2013). For subcontractors and material suppliers, notice is due within 45 days of first providing work or supplies to the property. *Id.* at Subd. 2.

² See Minn. Stat. § 514.011, Subd. 4a-4c (2013).

³ See Minn. Stat. § 514.011, Subd. 1-2 (2013).

⁴ The statement must be personally served or sent by certified mail to the owner or party who entered into the contract. Minn. Stat. § 514.08, Subd. 2 (2013).

⁵ Minn. Stat. § 514.08, Subd. 1 (2013).

⁶ See *Kahle v. McClary*, 255 Minn. 239, 242 (Minn. 1959)(although *de minimus* operations performed for the sole purpose of extending the time for the lien and the work is otherwise substantially completed will not allow for lien revival).

⁷ Minn. Stat. § 514.12, Subd. 3 (2013).

⁸ Minn. Stat. § 514.10 (2013); see also *Lyman Lumber Co. v. Cornerstone Const., Inc.*, 487 N.W.2d 251 (Minn. Ct. App. 1992) (further clarifying what amount of attorney's are recoverable in a mechanic's lien foreclosure action).

⁹ *Chicago Title Ins. Co. v. Resolution Trust Corp.*, 53 F.3d 899, 902 (8th Cir. 1995) (applying Minnesota law).

¹⁰ The distinction between a limitations and repose period is important. Critically, “. . . a statute of limitations limits the time within which a party can pursue a remedy, whereas a statute of repose limits the time within which a party can acquire a cause of action.” *Weston v. McWilliams Assoc., Inc.*, 716 N.W.2d 634, 641 (Minn. 2006).

¹¹ Minn. Stat. § 541.051, Subd. 1(b)

¹² *Id.* at Subd. 1(c)

¹³ See, e.g., *Hyland Hill North Condo. Ass'n v. Hyland Hill Co.*, 549 N.W.2d 617, 621 (Minn. 1996) (overruled on other grounds) (discovery of injury was when inspector first noted roof needed repairs rather than the later determination that the entire roof needed to be replaced); *Pamida, Inc. v. Christenson Building Corp.*, 285 F.3d 701 (8th Cir. 2003) (applying Minnesota law) (retailer discovered significant cracking in concrete floor along north and south sides of store in 1991 and 1996; court held that “[t]hough greater damage materialized in 1997 and 1998, the two-year limitations period in § 541.051, subd. 1(a), does not await a leisurely discovery of the full details of the injury”) (internal citations omitted).

¹⁴ *Id.*

¹⁵ *Greenbrier Village Condominium Two Ass'n, Inc. v. Keller Inv., Inc.*, 409 N.W.2d 519, 524 (Minn. Ct. App. 1987).

¹⁶ *Appletree Square One Limited v. W.R. Grace & Co.*, 815 F.Supp. 1266, 1279 (D. Minn. 1993) (applying and interpreting Minnesota and 8th Circuit law); see also *Greenbrier Village*, 409 N.W.2d at 524 (limitation period began when plaintiffs discovered only two of eight defects and merely “suspected underlying structural deficiencies”).

¹⁷ *Appletree Square*, 815 F.Supp. at 1279.

¹⁸ Minn. Stat. § 541.051, Subd. 4 (2013).

¹⁹ Minn. Stat. § 327A.01, Subds. 6, 8 (2013). These warranties run with the dwelling and extend to subsequent purchasers, however, the warranty is not reset when a subsequent purchaser occupies or takes title to the property.

²⁰ Minn. Stat. § 541.051, Subd. 4. See, e.g., *Vlahos v. R & I Const. of Bloomington, Inc.*, 676 N.W.2d 672 (Minn. 2004) (discussing the 10-year warranty applicable to “major construction defects”).

²¹ Minn. Stat. § 541.051, Subd. 2.

²² *Id.* at Subd. 1(b), 2 (2007).

²³ *Id.* at Subd. 1(b).

²⁴ Contribution and indemnity claims accrue “upon the earlier of commencement of the action against the party seeking contribution or indemnity, or payment of a final judgment, arbitration award, or settlement arising out of the defective and unsafe condition.” Minn. Stat. § 541.051, Subd. 1(c)(2013).

²⁵ *Id.* at Subd. 4.

²⁶ Minn. Stat. § 327A.01, Subd. 8 (2013).

27 Once appropriate notice has been provided by the homeowner, the statute of limitations is tolled until the latest of (1) the date of completion of a home warranty dispute resolution process under Minnesota Statutes § 327A.051, or (2) 180 days.

28 Minn. Stat. § 327A.03 (a) (2013). The “actual knowledge” exception was added to the statute by the Minnesota Legislature in 2010.

29 Minn. Stat. § 327A.02, Subd. 4(a) (2013).

30 *Id.* at Subd. 4(a), 5(a).

31 *Id.* at Subd. 5(c).

32 *Id.* at Subd. 4(c).

33 *Id.* at Subd. 5(c).

34 *Id.* at Subd. 7.

35 Minn. Stat. § 327A.03 (a).

36 *Independent School Dist. 775 v. Holm Bros. Plumbing and Heating, Inc.*, 660 N.W.2d 146, 150 (Minn. Ct. App. 2003).

37 *Singsaas v. Diederich*, 307 Minn. 153, 156-57, 238 N.W.2d 878, 880-81 (1976).

38 *Jenoff, Inc. v. New Hampshire Ins. Co.*, 558 N.W.2d 260, 261-62 (Minn. 1997).

39 *Kootenia Homes, Inc. vs. Federated Mutual Insurance Co.*, No. A05-278, 2006 WL 224162, *6 (Minn. Ct. App., Jan. 31, 2006), *pet. for rev. denied* (Minn., Apr. 18, 2006).

40 *Id.*

41 *Id.*

42 *Id.*

43 *Wooddale Builders, Inc. v. Maryland Cas. Co.*, 722 N.W.2d 283, 294 (Minn. 2006).

44 *Tony Eiden Co. v. State Auto Property and Cas. Ins. Co.*, No. A07-2222, 2009 WL 233883, *4 (Minn. Ct. App., Jan. 26, 2009) (citing *In re Silicone Implant Ins. Coverage Litig.*, 667 N.W.2d 405, 421-22 (Minn. 2003)).

45 *Id.*

46 *Id.*

47 *Wooddale*, 722 N.W.2d at 292-301.

48 *Id.* at 301-04.

49 *See Holmes v. Watson-Forsberg Co.*, 488 N.W.2d 473 (Minn. 1992).

50 *See Engineering & Construction Innovations Inc. v. L.H. Bolduc Co.*, 825 N.W.2d 695 (Minn. 2013).

51 Minn. Stat. § 337.01 *et. seq.*

52 Minn. Stat. § 337.01 contains the definition section of the statute and specifically defines “building and construction contract,” “indemnification agreement,” and “promise.” *See* Minn. Stat. § 337.01 (2010). *See also Katzner v. Kelleher Canst.*, 545 N.W.2d 378 (Minn. 1996) (holding that an attempt to indemnify a party in a construction contract from liability for its own actions is unenforceable).

53 *Seward Hous. Corp. v. Conroy Bros.*, 573 N.W.2d 364, 366 (Minn. 1998).

54 *See also Van Vickie v. C. W. Scheurer & Sons, Inc.*, 556 N.W.2d 238, 241-42 (Minn. Ct. App. 1996).

55 Although it should be noted that Minn. Stat. 337.05, Subd. 1 (c) reads as follows:
Paragraph (b) does not affect the validity of a provision that requires a party to provide or obtain workers compensation insurance, construction performance or payment bonds, or project-specific insurance, including, without limitation, builder’s risk policies or owner or contractor-controlled insurance programs or policies. The term “project-specific insurance” is not defined or a term of art, and until Minnesota courts determine its meaning some may argue that the term refers to CGL policies for a given project. *See also, Yang v. Voyagaire Houseboats, Inc.*, 701 N.W.2d 783 (Minn. 2005) (noting that it is against public policy for an individual to be required to indemnify a company for the company’s own negligence resulting in injuries to others).

56 *See also Van Vickie*, 556 N.W.2d at 241-42.

57 *Seward*, 573 N.W.2d 364.

58 *Katzner*, 545 N.W.2d 378.

59 *Mrozik Constr., Inc. v. Lovering Assocs., Inc.*, 461 N.W.2d 49, 52 (Minn. App. Ct. 1990) (holding that ambiguous language will be interpreted to “mean merely that the timing of payment to the subcontractor must not be delayed after the general contractor receives funds from the owner”).

60 *Ryan Contracting, Inc. v. Brandt*, 1997 WL 526393 (Minn. App. Ct. 1984); *see also Mrozik Constr., Inc.*, 461 N.W.2d at 52.

61 *See* Minn. Stat. § 15.411.

62 *Marlowe v. Gunderson*, 109 N.W.2d 323, 326 (Minn. 1961) (citing 5 Dunnell, Dig. (3 ed.) § 2570).

⁶³ *Eveleth v. Ruble*, 225 N.W.2d 521, 528 (Minn. 1974) (quoting *H. P. Droher and Sons v. Toushin*, 85 N.W.2d 273 (Minn. 1957)).

⁶⁴ *Northern Petrochemical Co. v. Thorsen & Thorshov, Inc.*, 211 N.W.2d 159, 165 (Minn. 1973) (citing *Marshall v. Marvin H. Anderson Const. Co.*, 167 N.W. 2d 724 (Minn. 1969); *H. P. Droher & Sons v. Toushin*, 85 N.W. 2d 273 (Minn. 1957); Restatement of Contracts § 346).

⁶⁵ Minn. Stat. § 327A.05 Subd. 1.

⁶⁶ See *Barr/Nelson, Inc. v. Tonto's Inc.*, 336 N.W.2d 46, 53 (Minn. 1983); *Material Movers, Inc. v. Hill*, 316 N.W.2d 13, 18 (Minn. 1982); *Prior Lake State Bank v. Groth*, 108 N.W.2d 619, 622 (Minn. 1961).

⁶⁷ *Les Jones Roofing, Inc. v. City of Minneapolis*, 373 N.W.2d 807 (Minn. Ct. App. 1985).

⁶⁸ *Indieke v. Blenda-Life, Inc.*, 363 N.W.2d 121, 125 (Minn. Ct. App. 1985).

⁶⁹ *Northern Petrochem. Co. v. Thorsen & Thorshov, Inc.*, 211 N.W.2d 159, 166 (Minn. 1973); *McCarthy Well Co. v. Aladdin Elec. Co.*, 364 N.W.2d 441, 445 (Minn. Ct. App. 1985).

⁷⁰ *Prichard Bros., Inc. v. Grady Co.*, 436 N.W.2d 460, 468 (Minn. Ct. App. 1989).

⁷¹ *Eric A. Carlstrom Const. Co. v. Ind. School Dist. No. 77*, 256 N.W.2d 479, 484 (Minn. 1997); *McCree & Co. v. State*, 91 N.W.2d 713, 726 (Minn. 1958).

⁷² *Valley Farmers' Elev. v. Lindsay Bros. Co.*, 398 N.W.2d 553, 556 (Minn. 1987), *overruled on other grounds*, *Hapka v. Panquin Farms*, 458 N.W.2d 683 (Minn. 1990).

⁷³ *Smith v. Den-Tal-Ez, Inc.*, 491 N.W.2d 11, 17 (Minn. 1992).

⁷⁴ Minn. Stat. § 549.09 (b) (2013).

⁷⁵ *Id.* at Subd. 1(c)(2).

⁷⁶ *Id.* at Subd. 1(c)(1). This interest rate also applies to any and all awards for or against the state or a political subdivision of the state. *Id.*

⁷⁷ The Minnesota State Court Administrator's office sets this interest rate according to the formula stated in Minn. Stat. § 549.09, Subd. 1(c)(1). The rate can be found at: <http://www.mncourts.gov/?page=1641>.

⁷⁸ *Barr/Nelson, Inc.*, 336 N.W.2d at 52.

⁷⁹ *Jensen v. Walsh*, 623 N.W.2d 247, 250 (Minn. 2001).

⁸⁰ The motion must alleged the applicable legal basis under Minn. Stat. § 549.20 or other law for awarding punitive damages. Minn. Stat. § 549.191 (2013). Under Minn. Stat. § 549.20, subd. 1(a), punitive damages shall be allowed "only upon clear and convincing evidence that the acts of the defendant show deliberate disregard for the rights or safety of others."

⁸¹ *Rosso v. Hallmark Homes of Minneapolis, Inc.*, 2014 Minn. App. LEXIS 22, *7 (Minn. Ct. App. Mar. 10, 2014). The Rossos' cited to *Nolan v. Paramount Homes, Inc.*, 135 N.C. App. 73, 518 S.E.2d 789, 791 (N.C. App. 1999) in support of their position. (Interpreting a similar statute that defined "substantial completion" as the "degree of completion of a project, improvement or specified area or portion thereof upon attainment of which the owner can use the same for the purpose for which it was intended" and holding that the home was not substantially completed until a "certificate of compliance" was issued). *Rosso*, 2014 Minn. App. LEXIS at *7.

⁸² In rejecting the Rossos' argument, the court's ruling has effectively shortened the time available to owners to bring defect claims and works to shield contractors from those same claims. *Id.*

MISSISSIPPI

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I. MECHANIC'S LIEN BASICS.

Historically, Mississippi limited traditional lien rights on construction projects to parties who contracted directly with the owner. Thus, subcontractors and materialmen who provided work or materials for the project could not place a lien on the property in order to protect their rights. To cure that problem, Mississippi's Stop Notice statute, Mississippi Code Annotated Section 85-7-181, gave subcontractors or materialmen who had not been paid by the contractor the right to send notice of non-payment to the owner of the property, thereby binding any money the owner owed to the general contractor in the hands of such owner.

However, in October 2013, the Fifth Circuit ruled that the Stop Notice statute was unconstitutional on the basis that it lacked procedural safeguards and violated the prime contractor's due process rights.¹ The decision effectively removed the ability for an unpaid subcontractor or material supplier to secure payment without filing suit.

Following this decision, the legislature dramatically reformed the lien laws in Mississippi. The Revised Mississippi Lien Law (hereinafter the "Act"), Mississippi Code Annotated Sections 85-7-401, *et. seq.*, which became effective on April 11, 2014, conferred lien rights to prime contractors, first and second tier suppliers and contractors as well as certain design professionals. While this Act was recently placed into law, the following paragraphs describe its basic structure. As this law is new, this information is general in nature based on the original text of the bill and practitioners are strongly encouraged to refer to the text of the Act.

A. Requirements.

To enjoy the benefits of the Act, the party must strictly follow the enumerated requirements set forth in Section 85-7-405(1) or the lien will be rendered ineffective or unenforceable.²

1. The lien claimant must have substantially complied with the provisions of the contract, subcontract, or purchase order in the provision of work, services, or materials provided.³
2. The lien must be filed within 90 days after the claimant's claimant's last work performed, labor, services or materials provided, the furnishing of architectural services, or the furnishing or performing of surveying or engineering services.⁴

MISSOURI

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I. MECHANICS' LIENS

RSMo. § 429.010, *et seq.*, governs the filing and perfection of a mechanic's lien. The purpose of the lien is to protect contractors, subcontractors, and materialmen whose labor and materials increase the value of a property. It provides special priorities over other encumbrances against the property. Courts have developed a general policy of upholding, wherever possible, the rights of laborers and materialmen.

A. Requirements

Every original contractor (aka general contractor) must provide to the person for whom the work or labor is provided a written notice, before payment is received, containing the following disclosure language in ten point bold face type:

NOTICE TO OWNER

FAILURE OF THIS CONTRACTOR TO PAY THOSE PERSONS SUPPLYING MATERIAL OR SERVICES TO COMPLETE THIS CONTRACT CAN RESULT IN THE FILING OF A MECHANIC'S LIEN ON THE PROPERTY WHICH IS THE SUBJECT OF THIS CONTRACT PURSUANT TO CHAPTER 429, RSMo. TO AVOID THIS RESULT YOU MAY ASK THIS CONTRACTOR FOR "LIEN WAIVERS" FROM ALL PERSONS SUPPLYING MATERIAL OR SERVICES FOR THE WORK DESCRIBED IN THIS CONTRACT. FAILURE TO SECURE LIEN WAIVERS MAY RESULT IN YOUR PAYING FOR LABOR AND MATERIAL TWICE.²

For owner-occupied residential property of four units or less, no person, other than the original contractor, may have a lien under Chapter 429 unless the owner has agreed to be liable for such costs in the event that the costs are not paid. Such consent shall be in the same typeset as the above notice, signed separately and shall contain the following words:

CONSENT OF OWNER

CONSENT IS HEREBY GIVEN FOR FILING OF MECHANIC'S LIENS BY ANY PERSON WHO SUPPLIES MATERIALS OR SERVICES FOR THE WORK DESCRIBED IN THIS CONTRACT ON THE PROPERTY ON WHICH IT IS LOCATED IF HE IS NOT PAID.³

B. Enforcement and Foreclosure

All actions shall be commenced within six months after the lien has been filed. A mechanic's lien suit is commenced when the petition is filed. Generally, a subcontractor should also name the original contractor as a party. The petition must (1) contain a description of the property to be charged with the lien, and (2) allege facts necessary for securing a lien, including identity of parties, existence and terms of the contract, dates work was performed, and satisfaction of notice requirements.

The following prescribes general comments regarding collecting:

- If the principal debtor has been personally served – personal judgment and judgment lien;⁴
- If service is by publication – judgment can only be levied against the owner's interest in the land;⁵ and
- Interest is includable in any mechanic's lien judgment.⁶

C. Ability to Waive and Limitations on Lien Rights

Within six months of the indebtedness, a claimant must file with the circuit clerk of the proper county the lien containing a "just and true account" of the amount owed.⁷ This requirement has been construed by courts as a condition precedent to the right to establish a mechanic's lien.⁸

II. STATUTES OF LIMITATIONS AND REPOSE

A. Statute of Limitations and Limitations on Application of Statutes

1. Ten Years:

- a. Action to recover possession of land.⁹
- b. Action for payment of money or property pursuant to written obligation (does not include U.C.C. actions).¹⁰
- c. Action against architect, engineer, or builder for defective or unsafe condition of an improvement to real property.¹¹
- d. Civil actions not otherwise mentioned.¹²

2. Five Years:

- a.. Construction defect (from ascertainable damage).¹³

- b. Action for trespass.¹⁴
- c. Contract actions not covered by RSMo. § 516.110(1).¹⁵
- d. Action for tort.¹⁶
- e. Action for fraud.¹⁷

3. Accrual

- a. A cause of action for professional malpractice cannot begin to run until the plaintiff knew or should have known for any reason to question the professional's work.¹⁸

4. Inability to Contractually Alter

- a. “All parts of any contract or agreement hereafter made or entered into which either directly or indirectly limit or tend to limit the time in which any suit or action may be instituted, shall be null and void.”¹⁹

5. Fraudulent Concealment

- a. “If any person, by absconding or concealing himself, or by any other improper act, prevent the commencement of an action, such action may be commenced within the time herein limited, after the commencement of such action shall have ceased to be so prevented.”²⁰

B. Statute of Repose and Limitations on Application of Statutes

1. Generally

Under RSMo. § 516.097, tort actions against builders, architects, and engineers for a defective improvement to real property must be brought within ten (10) years of the improvement's completion.²¹ The purpose of the statute is to protect those who provide construction services from “indeterminate liability.”²² A party recently joined in an action by such builder, architect or engineer under the statute has one year to file a third party action (notwithstanding the ten year deadline) arising out of the allegations.²³

2. Analyzing the Application

The first issue to determine under the statute is whether the construction services constituted an “improvement” to the property. Missouri law has defined the term “improvement” as “[a] permanent addition to or betterment of real property that enhances its capital value and that involves the expenditure of labor or money and is designed to make the property more useful or valuable as distinguished from ordinary repairs.”²⁴

The second issue to determine whether the alleged property damage occurred within ten years after the builder completed the improvement.²⁵

The final issue is whether the claimed defect which allegedly caused the damage was “concealed.” Missouri cases have interpreted “concealed” to mean “an affirmative act, something actually done directly intended to prevent discovery or to thwart investigation.”²⁶ A concealed defective condition is “one that is not discoverable by reasonable diligence.”²⁷

3. Application to Manufacturers

A manufacturer that fabricates or assembles building materials or component parts incorporated within the real property in the construction of an improvement is “performing or furnishing. . . construction services” under Section 516.097.2.²⁸ The statute does not protect a manufacturer whose standard product is fabricated at the manufacturer's factory, made available to the general public, and then “furnished for the inclusion in the improvement by the persons constructing the improvement under circumstances where the manufacturer has no substantial on-site construction activity.”²⁹ To invoke the affirmative defense, a manufacturer must have “substantial participation at the construction site in significant activities in installing or incorporating the product into the real property.”³⁰

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

A. Express Warranties

Typically, express warranties that accompany a product from the manufacturer will incorporate a time limit by which notice must be given to the manufacturer in order to honor the warranty.

B. Residential Construction Defects

Under RSMo. 436.350, *et seq.*, a contractor may provide notice to a homebuyer that notice and an opportunity to cure must be given to the contractor before seeking a claim in court.³¹ The contractor must give notice to the homeowner of such a requirement “in substantially the following form”:

SECTIONS 436.350 TO 436.365 OF MISSOURI REVISED STATUTES PROVIDE YOU WITH CERTAIN RIGHTS IF YOU HAVE A DISPUTE WITH A CONTRACTOR REGARDING CONSTRUCTION DEFECTS. EXCEPT FOR CLAIMS FILED IN SMALL CLAIMS COURT, IF YOU HAVE A DISPUTE WITH A CONTRACTOR, YOU MUST DELIVER

TO THE CONTRACTOR A WRITTEN CLAIM OF ANY CONSTRUCTION CONDITIONS YOU ALLEGE ARE DEFECTIVE AND PROVIDE YOUR CONTRACTOR THE OPPORTUNITY TO MAKE AN OFFER TO REPAIR OR PAY FOR THE DEFECTS. YOU ARE NOT OBLIGATED TO ACCEPT ANY OFFER MADE BY THE CONTRACTOR. READ THIS NOTICE CAREFULLY. THERE ARE STRICT DEADLINES AND PROCEDURES UNDER SECTIONS 436.350 TO 436.365 WHICH MUST BE OBEYED IN ORDER TO PRESERVE YOUR ABILITY TO FILE A LAWSUIT. OTHER THAN REPAIRS TO WORK DONE BY THE CONTRACTOR THAT ARE NECESSARY TO PROTECT THE LIFE, HEALTH, OR SAFETY OF PERSONS LIVING IN A RESIDENCE, OR TO AVOID ADDITIONAL SIGNIFICANT AND MATERIAL DAMAGE TO THE RESIDENCE PURSUANT TO SUBSECTION 10 OF SECTION 436.356, YOU MAY NOT INCLUDE IN CLAIMS AGAINST YOUR CONTRACTOR THE COSTS OF OTHER REPAIRS YOU PERFORM BEFORE YOU ARE ENTITLED TO FILE A LAWSUIT UNDER SECTIONS 436.350 TO 436.365.³²

The claimant/homeowner's written notice or claim "shall state that the claimant asserts a construction defect claim against the contractor and shall describe the claim in reasonable detail sufficient to determine the general nature of the defect as well as any known results of the defect."³³ The contractor then has fourteen days (from service of the notice) to respond in writing, which shall:

- (1) Propose to inspect the residence that is the subject of the claim and to complete the inspection within a specified time frame. The proposal shall include the statement that the contractor shall, based on the inspection, thereafter offer to remedy the defect within a specified time frame, compromise by payment, or dispute the claim; or
- (2) Offer to remedy the claim without an inspection within a specified time frame; or
- (3) Offer to remedy part of the claim without inspection and compromise and settle the remainder of the claim by monetary payment within a specified time frame; or
- (4) Offer to compromise and settle all of a claim without inspection. A contractor's offer pursuant to this subdivision to compromise and settle a claimant's or association's claim may include, but is not limited to, an express offer to purchase the claimant's residence that is the subject of the claim; or

- (5) State that the contractor disputes the claim and will neither remedy the construction defect nor compromise and settle the claim.³⁴

The statute then sets out further procedures to be taken, including the ability of the homeowner if the contractor disputes the claim or fails to respond to the homeowner's notice.³⁵ Nothing in the statute interferes with the contractual rights to arbitrate³⁶ or mediate³⁷ the claim. The statute is inapplicable if the homeowner's action against the contractor is in a counterclaim.³⁸

IV. INSURANCE COVERAGE AND ALLOCATION ISSUES

A. General Coverage Issues

The burden of showing that a loss and damages are covered under an insurance policy is placed upon the insured, while the burden of showing that there is an applicable exclusion is on the insurer.³⁹ Under this principle, the insurer will be required to demonstrate to a Missouri court that there are applicable exclusions to the insurance agreement that negate coverage. An insurer need not show that each exclusion is applicable to preclude coverage, but that any one exclusion is sufficient.⁴⁰

Punitive damages are not covered unless the policy specifically provides coverage.⁴¹

More than one person or organization may be an insured in respect to the same occurrence. Such policies customarily contain a clause that, in effect, makes the policy apply separately to each of the persons insured.

B. Trigger of Coverage

Language of an insurance contract must be given its plain meaning, without unduly straining the language.⁴² A standard Commercial General Liability ("CGL") policy will contain a clause that states:

b. This insurance applies to 'bodily injury' and property damage' only if:

(2) The 'bodily injury' or 'property damage' occurs during the policy period.

Coverage generally does not exist under a CGL policy for contract claims and breach of warranty.

A claim for defective workmanship will be considered an "occurrence" within the meaning of the CGL policy if the defect was unforeseen.⁴³ If the damage was not unforeseen, then there will not be coverage because the CGL policy is not intended function as a performance bond or warranty for the goods or services provided.⁴⁴ The

rationale is that a CGL policy is not intended to protect business owners against every risk of operating a business, nor is it intended as a guarantee of the quality of an insured's product or work.⁴⁵

C. Allocation Among Insurers

When two or more liability insurers are liable for the same loss, that liability is to be apportioned according to the terms of the policies involved.⁴⁶ However, in the absence of terms controlling apportionment or when such terms are repugnant, generally the loss will be apportioned according to the coverage afforded by each policy involved.⁴⁷ When several limits of coverage are stacked, the insurers are required to contribute pro rata to a loss that is below the combined limits of the several policies.⁴⁸

D. Issues with Additional Insurance

One method of risk shifting is to require persons with whom you are contracting to obtain insurance and provide a certificate naming you as an additional insured. The certificate itself will likely contain the following limitation:

THIS CERTIFICATE IS ISSUED AS A MATTER OF INFORMATION ONLY AND CONFERS NO RIGHTS UPON THE CERTIFICATE HOLDER. THIS CERTIFICATE DOES NOT AMEND, EXTEND OR ALTER THE COVERAGE AFFORDED BY THE POLICIES BELOW.

Beware that insurance companies may not be aware of certificates issued by brokers and may attempt to deny that any insurance is afforded as a result of an unauthorized certificate of insurance. You should always request a copy of the policy pursuant to which the additional insured endorsement is issued. This will allow you to review the policy to determine whether the policy contains a blanket insured endorsement.

The two most common additional insured forms are 2033 and 2010. Form CG 20 33 03 97, which is captioned: "Additional Insured – Owners, Lessees or Contractors – Automatic Status When Required in Construction Agreement." This endorsement provides as follows:

This endorsement modifies insurance provided under the following:

COMMERCIAL GENERAL LIABILITY COVERAGE PART

A. Who Is An Insured (Section II) is amended to include as an insured any person or organization for whom you are performing operations when you and such person or organization have agreed in writing in a contract or agreement that such person or organization be added as an additional insured on your policy. Such person or

organization is an additional insured only with respect to liability arising out of your ongoing operations performed for that insured. A person's or organization's status as an insured ends when your operations for that insured are completed. . . .

Form CG 20 10 11 85, provides as follows:

WHO IS AN INSURED (Section II) is amended to include as an insured the person or organization shown in the Schedule, but only with respect to liability arising out of "your work" for that insured by or for you.

Form 20 33 limits coverage to liability arising out of ongoing operations. No coverage is afforded for damages that arise after the insured has completed its work on the project. This can leave the additional insured high and dry for damages that are not immediately discovered.

B. With respect to the insurance afforded these additional insureds, the following exclusion, typical for CGL policies, may apply:

This insurance does not apply to:

"Bodily injury," "property damage", "personal injury" or "advertising injury" arising out of the rendering of, or the failure to render, any professional architectural, engineering or surveying services, including:

1. The preparing, approving, or failing to prepare or approve, maps, shop drawings, opinions, reports, surveys, field orders, change orders or drawings and specifications; and
2. Supervisory, inspection, architectural or engineering activities.

Insurance coverage presents myriad complex issues that should be reviewed by your attorney and insurance broker to determine the nature and scope of coverage provided.

V. CONTRACTUAL INDEMNIFICATION

Actions for contractual indemnity are governed by the terms of the contract and are separate from the action against the indemnitee that gives rise to the claim for indemnification. The necessity of a demand for indemnification as a condition precedent to performance by the indemnitor will be governed by the terms of the contract. Indemnity claims are often pled as cross-claims or third-party claims.⁴⁹

In general, indemnity agreements are valid and enforceable, but must be very clear.⁵⁰ In 1999, Missouri enacted its first anti-indemnity statute that essentially provides, subject to several exceptions: “[I]n any contract or agreement for public or private construction work, a party's covenant, promise or agreement to indemnify or hold harmless another person from that person's own negligence or wrongdoing is void as against public policy and wholly unenforceable.”⁵¹

The elements of a contractual indemnity claim are fundamentally the same as any other claim for breach of contract:

- 1) an agreement between parties capable of contracting;
- 2) supported by consideration;
- 3) providing that one party secures or protects the other against liability or loss, or a combination of the two; and
- 4) a breach of the obligation of indemnity.⁵²

A petition seeking recovery on a contractual indemnity theory should contain:

- 1) a description of the parties;
- 2) allegations of jurisdiction and venue (if the indemnity claim is a cross-claim or third-party claim jurisdiction and venue may be established by alleging the circumstances of the pending action);
- 3) allegations showing the existence of a contract of indemnity or other contract giving rise to a claim for indemnity, including allegations of capacity of the parties, the substance of the contract, and consideration,⁵³
- 4) allegations showing the breach of contract by the indemnitor, such as where the indemnitee is liable in tort due to a contract breach by the indemnitor,⁵⁴
- 5) allegations showing breach by the defendant by failing to reimburse plaintiff's actual loss (loss indemnity) or by failing to discharge plaintiff's liability as finally fixed and determined, either by a good-faith settlement or by adjudication (liability indemnity or mixed loss/liability);
- 6) allegations of demand or tender of defense, if necessary,⁵⁵ and
- 7) allegations of damage, including sums sought for costs and expenses of the defense of the underlying claim, if appropriate.

A contract for indemnity, like other contracts, must be sufficiently definite and certain to permit the court to enforce it. If the essential terms of the contract of indemnity are not sufficiently definite for a court to give them an exact meaning, such as where the contract does not clearly specify who is the indemnitor, enforcement will be denied.⁵⁶

VI. CONTINGENT PAYMENT AGREEMENTS

A. Pay-if-paid clauses:

1. Generally, pay-if-paid clauses, which attempt to shift the payment risk from the general contractor to the subcontractor by relieving the general contractor of payment obligations unless and until it receives payment from the owner, are enforceable.
2. Missouri Courts have not directly addressed the issue of whether pay-if-paid clauses in construction agreements violate public policy.
3. Missouri Courts will most likely look disfavorably upon conditions precedent, and will only construe contract provisions regarding payment to be a condition precedent if the contract terms are plain and unambiguous. When a general contractor puts a risk-shifting provision in a subcontract, the burden of clear expression will be on the general contractor.⁵⁷
4. A Court will look at all incorporated and referenced documents in the subcontract.⁵⁸
5. If the clause is ambiguous, then it will be interpreted as fixing a reasonable time for payment to the subcontractor.⁵⁹

B. Pay-when-paid clauses:

1. Generally, pay-when-paid clauses address the timing of payment, rather than the right to payment, and are enforceable.
2. If the language is ambiguous, the pay-when-paid clause will be construed as establishing a reasonable period for payment to subcontractor.⁶⁰

VI. DAMAGES LIMITATIONS

A. Personal Injury Damages vs. Construction Defect Damages

The ultimate test for damages is whether the award will fairly and reasonably compensate the plaintiff for his or her injuries.⁶¹

1. Personal Injury Damages

The following are basic areas of recovery in personal injury law:

- a. Actual or Compensatory Damages – including pain and suffering;
- b. Special Damages – such as hospitalization, medical expenses or loss of wages (both past and future);⁶²

- c. Future Medical Expenses;
- d. Economic Loss;⁶³
- e. Punitive Damages;⁶⁴ and
- f. Loss of Consortium – of spouse.

2. Construction Defect Damages

Generally on a construction defect case under a theory of breach of contract, “plaintiffs are entitled to recover as damages only a sum which is the equivalent of performance of the bargain—to be placed in the position they would be in if the contract had been fulfilled in a workmanlike manner.”⁶⁵ These may incorporate actual damages, consequential damages, and lost profits.⁶⁶ “The burden of proving that damages exist, and the amount of those damages, rests with the party claiming breach of contract.”⁶⁷ “Further, that party must demonstrate the level of damages with reasonable certainty.”⁶⁸ “Such proof must rise to the level of substantial evidence, which has been defined as that which a reasonable mind would accept as sufficient to support a particular conclusion, granting all reasonable inference[s] which can be drawn from it.”⁶⁹

Hensic v. Afshari Enterprises, Inc., states as follows:

When a building contractor breaches his contract by defective performance, . . . two methods are commonly used to measure the resulting damages. One method, called ‘cost of repair’ is, as its name implies, the cost of repairing the defective work. 5 Corbin, Contracts, § 1089 (1964); Restatement of Contracts, § 346(1)(a) (1932). The second method, called ‘diminution in value,’ is the difference between the value of the building as promised and its value as actually constructed. *See Kahn v. Prahl*, 414 S.W.2d 269, 282–283 (Mo.1967); *Hotchner v. Liebowits*, 341 S.W.2d 319, 332 (Mo.App.1960). The particular facts of each case determine which measure of damages is to be used.⁷⁰

The basic rule is that a plaintiff is entitled to recover the lesser of the cost of repair or the diminution of value of the property with the defective condition.⁷¹

B. Attorneys’ Fees Shifting and Limitations on Recovery

Unlike court costs, attorneys’ fees are not generally recoverable from the other party.⁷² Attorney fees are ordinarily only recoverable when 1) called for by contract 2)

expressly provided for by statute, 3) as an item of collateral damage, or 4) where equity requires (“very unusual circumstances”).⁷³

C. Consequential Damages

“Consequential damages are those damages naturally and proximately caused by the commission of the breach and those damages that reasonably could have been contemplated by the defendant at the time of the parties' agreement.”⁷⁴ Missouri Courts recognize the recovery of consequential damages.

D. Delay and Disruption Damages

1. Delay Damages

John D. Darling has explained delay as the following:

Excusable delay occurs as a result of events outside a contractor's control, such as acts of God (floods, hurricanes), labor strikes, unusually severe weather, and an inability to obtain critical materials due to plant closings and product shortages. Inexcusable delay is caused by the contractor, due to a failure to properly schedule or supervise the work or to prosecute the work diligently. Generally, an excusable delay entitles a contractor to a contract time extension and relief from a potential or actual liquidated damages assessment but does not allow the contractor to recover the costs of delay.⁷⁵

A contractual provision that instructs a contractor on a procedure and time limit within which that contractor must request an extension due to delay is enforceable, and failure to abide by such a provision renders delays inexcusable.⁷⁶ In addition, many contracts will require notice before delay is “excused.”⁷⁷ In *Bloomfield*, a school and a contractor agreed to the construction of a building on the school's campus.⁷⁸ After differences arose, the school sued the contractor to terminate the contract.⁷⁹ In the *Bloomfield* contract, a provision specified: “Extensions of time will be granted for delays beyond the control of the Contractor.”⁸⁰ A later provision stated: “No such extension shall be made for delay occurring more than seven days before claim therefore [sic] is made in writing to the Architect.”⁸¹ The contractor applied for an extension nineteen days after the agreed completion date, and testified during trial as follows:

[The contractor] testified that there were delays due to a cement and steel shortage and to the weather, over which neither party had any control. He claimed that there were numerous delays attributable to the misconduct of the architect: denial of permission to fabricate his own steel,

delay in approving various shop drawings, delay in furnishing a paint schedule, delay in supplying information as to light fixtures, refusal to answer inquiries as to two stairways and, in short, just about every item in the plans and specifications.⁸²

The Missouri Supreme Court ruled the school was entitled to liquidated damages for inexcusable delay.⁸³ In so ruling, the *Bloomfield* Court noted: “All of these listed delays had occurred in the past, not ‘seven days before claim therefore [sic] is made,’” and, “While the contractual provision [the article discussing delay] may have been intended for the contractor's benefit, he did not comply with it and he is therefore not to be excused for the delays.”⁸⁴

2. Disruption Damages

Disruption damages may occur when a change in the project schedule leads to additional labor, time or expenses on the project by the contractor/subcontractor. They are contractual in nature.⁸⁵

E. Economic Loss Doctrine

Damages for economic loss may be recovered in certain negligence actions in Missouri. “Economic loss includes cost of repair and replacement of defective property which is the subject of the transaction, as well as commercial loss for inadequate value and consequent loss of profits or use.”⁸⁶ Such damages may be recovered in actions for personal injury, damage to property other than the property at issue, and in actions involving negligent rendition of services by a professional.⁸⁷ In 2011, the Missouri Supreme Court held comparative fault applies to property damages and economic loss damages.⁸⁸

In Missouri, the economic loss doctrine has been observed to prohibit a plaintiff from seeking to recover in tort for economic losses that are contractual in nature.⁸⁹ In other words, a defendant who has contracted with another owes no duty to a plaintiff who was not the party to the contract, nor can that plaintiff sue for the negligent performance of the contract.⁹⁰ The policy considerations behind this rule is to prevent excessive and unlimited liability as well as to prevent restricting and embarrassing the right to make contracts by burdening them with obligations and liabilities to others which parties would not voluntarily assume.⁹¹

F. Interest

1. Prejudgment Interest

a. Contract Actions

i. Prejudgment interest is available.⁹²

- ii. Absent an agreement between the parties, prejudgment interest is allowed at the rate of 9% annually.⁹³
- iii. In the case of written contracts, prejudgment interest begins to accrue when the amount owing becomes “due and payable.”⁹⁴
- iv. In contractual obligations other than written agreements, prejudgment interest does not begin to accrue until a demand is made, reasonably certain as to amount and time.⁹⁵
- v. For actions based upon Missouri’s Prompt Pay Act, which concern private construction projects, interest accrues at the rate of 18% per year.⁹⁶

b. Tort Actions

- i. Prejudgment interest is difficult to recover in tort actions, due to the stringent requirements of RSMo. § 408.040.⁹⁷

- ii. Compliance with RSMo. § 408.040 entails the following:

“If a claimant has made a demand for payment of a claim or an offer of settlement of a claim, to the party, parties or their representatives, and to such party's liability insurer if known to the claimant, and the amount of the judgment or order exceeds the demand for payment or offer of settlement, then prejudgment interest shall be awarded, calculated from a date ninety days after the demand or offer was received, as shown by the certified mail return receipt, or from the date the demand or offer was rejected without counter offer, whichever is earlier. In order to qualify as a demand or offer pursuant to this section, such demand must:

- (1) Be in writing and sent by certified mail return receipt requested; and
- (2) Be accompanied by an affidavit of the claimant describing the nature of the claim, the nature of any injuries claimed and a general computation of any category of damages sought by the claimant with

supporting documentation, if any is reasonably available; and

- (3) For wrongful death, personal injury, and bodily injury claims, be accompanied by a list of the names and addresses of medical providers who have provided treatment to the claimant or decedent for such injuries, copies of all reasonably available medical bills, a list of employers if the claimant is seeking damages for loss of wages or earning, and written authorizations sufficient to allow the party, its representatives, and liability insurer if known to the claimant to obtain records from all employers and medical care providers; and
- (4) Reference this section and be left open for ninety days.

Unless the parties agree in writing to a cause of action in circuit court prior to a date one hundred twenty days after the demand or offer was received, then the court shall not award prejudgment interest to the claimant. If the claimant is a minor or incompetent or deceased, the affidavit may be signed by any person who reasonably appears to be qualified to act as next friend or conservator or personal representative. If the claim is one for wrongful death, the affidavit may be signed by any person qualified pursuant to section 537.080, RSMo, to make claim for the death. Nothing contained herein shall limit the right of a claimant, in actions other than tort actions, to recover prejudgment interest as otherwise provided by law or contract.⁹⁸

- iii. Prejudgment interest in tort actions bears interest at a per annum interest rate equal to the intended Federal Funds Rate, as established by the Federal Reserve Board, plus three percent.⁹⁹ The judgment shall state the applicable interest rate, which shall not vary once entered.¹⁰⁰

2. Post-judgment Interest

a. Contract Actions

- i. Judgments in Missouri regarding actions in contract accrue interest at the rate of 9% annually, where there is no agreement for a higher rate of interest. However, where the judgment is founded upon a contract providing for a higher rate of interest, the higher rate applies.¹⁰¹
 - ii. Interest begins to accrue from the day the judgment is rendered regardless of whether the judgment itself mentions a right to the interest.¹⁰²
 - iii. Normally, the pendency of an appeal does not affect accrual of interest.¹⁰³
- b. Tort Actions
 - i. Judgments in Missouri regarding actions in tort accrue interest from the date judgment is entered by the trial court at a per annum interest rate equal to the intended Federal Funds Rate, as established by the Federal Reserve Board, plus five percent, until full satisfaction is made.¹⁰⁴
 - ii. The judgment shall state the applicable interest rate, which shall not vary once entered.¹⁰⁵

G. Punitive Damages

- 1. Courts are reluctant in reading punitive damages into standard insurance clauses, though stop short of addressing the issue of whether punitive damages are uninsurable due to violation of public policy.¹⁰⁶
- 2. Negligence cases:
 - a. Standard “complete indifference to or conscious disregard for the safety of others.”
 - b. Punitive damages are intended to punish and deter defendant and others from like conduct.¹⁰⁷
- 3. Intentional tort cases:
 - Standard “outrageous conduct because of defendant’s evil motive or reckless indifference to the rights of others.”¹⁰⁸
- 4. Discovery
 - Discovery as to a defendant’s assets shall be allowed only after a finding by the trial court that it is more likely than not that the

plaintiff will be able to present a submissible case on plaintiff's claim for punitive damages.¹⁰⁹

5. Maximum allowed.

a. \$500,000; or

b. Five times the amount of the judgment.¹¹⁰

H. Other Damage Limitations

1. Liquidated Damages

Missouri case law allows sophisticated parties to have the freedom to contractually limit future liability.¹¹¹ The court's reason that parties have the freedom to make a bad bargain or relinquish fundamental rights.¹¹² Further, a contract that did not include a limitation clause, such as a liquidated damages clause, would presumably carry a different price than one that does include such a provision.¹¹³

The term "liquidated damages" refers to "that amount which, at the time of contracting, the parties agree shall be payable in the case of breach."¹¹⁴ In Missouri, liquidated damages provisions in contracts are generally upheld by the courts provided they are reasonable and the parties agreed in good faith upon a sum as damages that would likely ensue if the contract were breached."¹¹⁵

¹ Mr. Koehler wishes to acknowledge the contributions to this compendium that were made by Lawrence B. Grebel and Robert T. Plunkert, who both provided substantial assistance in researching and drafting this reference paper.

² RSMo. § 429.012.

³ RSMo. § 429.013.

³ RSMo. § 429.240.

⁴ RSMo. § 429.230.

⁵ RSMo. § 429.210.

⁷ RSMo. § 429.170.

⁶ *Farmington Bldg. Supply Co. v. L.D. Pyatt Const. Co.*, 627 S.W.2d 648, 650 (Mo. App. 1981).

⁷ RSMo. § 516.010.

⁸ *Id.*

⁹ RSMo. § 516.097; *see infra*, Section II.B.

¹⁰ RSMo. § 516.110(3).

¹¹ RSMo. § 516.100.

¹⁴ RSMo. § 516.120(3).

¹⁵ RSMo. § 516.120(1).

¹⁶ RSMo. § 516.120(4).

¹⁷ RSMo. § 516.120(5).

¹⁸ *Deutsch v. Wolff*, 994 S.W.2d 561, 572 (Mo. banc 1999).

¹⁹ RSMo. § 431.030.

²⁰ RSMo. § 516.280.

²¹ RSMo. § 516.097. The statute mentions the issuance of an occupancy permit triggers the accrual time. RSMo. § 516.097.6.

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- ²² *Magee v. Blue Ridge Professional Bldg. Co., Inc.*, 821 S.W.2d 839, 843 (Mo. App. 1991).
- ²³ RSMo. § 516.097.3.
- ²⁴ *Hayslett v. Harnischfeger Corp.*, 815 F. Supp. 1294 (W.D. Mo. 1993) (crane was “improvement” for purposes of applying Statute of Repose). *See also, Blaske v. Smith & Entzeroth, Inc.*, 821 S.W.2d 822 (Mo. banc 1999) (a central air handling unit was an improvement to real property).
- ²⁵ *Fueston v. Burns and McDonnell Engineering*, 877 S.W.2d 631, 637-638 (Mo. App. 1994).
- ²⁶ *Magee v. Blue Ridge Professional Bldg. Co., Inc.*, 821 S.W.2d 839, 844 (Mo. App. 1991) (steps in a stairwell were not a concealed defect even though there was a subtle variation in the height and width of the individual steps).
- ²⁷ *Butler v. Mitchell-Hugeback, Inc.*, 895 S.W.2d 15, 20 (Mo. banc 1995).
- ²⁸ *Travelers Indemnity Co. of America v. The Williams- Carver Co.*, 326 S.W.3d 45, 49 (Mo. App. 2010) (citing *Blaske v. Smith & Entzeroth, Inc.*, 821 S.W.2d 822, 837 (Mo. banc 1991)).
- ²⁹ *Id.*
- ³⁰ *Id.*
- ³¹ RSMo. § 436.353.1.
- ³² RSMo. § 436.353.2.
- ³³ RSMo. § 436.356.1.
- ³⁴ RSMo. § 436.356.2.
- ³⁵ RSMo. § 436.356.3 (1).
- ³⁶ RSMo. § 436.365.2.
- ³⁷ RSMo. § 436.362. This statute suggests mandatory mediation upon “offer.”
- ³⁸ RSMo. § 436.353.4.
- ³⁹ *Am. States Ins. Co. v. Herman Kempker Const. Co.*, 71 S.W.3d 232, 235 (Mo. App. 2002).
- ⁴⁰ *See id.*
- ⁴¹ *Union L.P. Gas Systems, Inc. v. International Surplus Lines Ins. Co.*, 869 F.2d 1109 (8th Cir. 1989) (citing *Schnucks Markets, Inc. v. TransAmerica Ins. Co.*, 652 S.W.2d 206, 208-9 (Mo. App. 1983); *Crull v. Gleb*, 382 S.W.2d 17, 23 (Mo. App. 1964).
- ⁴² *Hawkeye-Security Insurance Co. v. Davis*, 6 S.W.3d 419, 424 (Mo. App. 1999).
- ⁴³ *D.R. Sherry Constr., Ltd. v. American Family Mut. Ins. Co.*, 316 S.W.3d 899, 906 (Mo. banc 2010).
- ⁴⁴ *Employers Mut. Casualty Co. v. Luke Draily Constr. Co.*, No. 10-00361-CV-W-DGK, 2011 WL 2582551, at *5 (W.D. Mo. June 29, 2011).
- ⁴⁵ *Id.*
- ⁴⁶ *Empire Ins. Co. v. Farm Bureau, Etc.*, 633 S.W.2d 215, 217 (Mo. App. 1982).
- ⁴⁷ *National Indemnity Co. v. Liberty Mutual Ins. Co.*, 513 S.W.2d 461 (Mo. banc 1974).
- ⁴⁸ *State Farm Mut. Auto Ins. v. MFA Mut. Ins. Co.*, 671 S.W.2d 276, 278 (Mo. banc 1984).
- ⁴⁹ *See Burns & McDonnell Eng'g Co. v. Torson Constr. Co.*, 834 S.W.2d 755 (Mo. App. 1992).
- ⁵⁰ *See Purcell Tire and Rubber Company, Inc. v. Executive Beechcraft, Inc.*, 59 S.W.3d 505 (Mo. banc 2001) (sophisticated users deal at “arms length,” whereas non-sophisticated users must use the terms “negligence,” “fault,” or the substantial equivalent). *See also Alack v. Vic Tanny Intern. of Missouri, Inc.*, 923 S.W.2d 330 (Mo. banc 1996); *Utility Service and Maintenance, Inc. v. Noranda Aluminum, Inc.*, 163 S.W. 3d 910 (Mo. banc 2005); *Pernoud v. Martin*, 891 S.W.2d 528, 537 (Mo. App. 1995) (“In determining whether written agreements establish a duty to indemnify, a specific and express intent to indemnify is required.”).
- ⁵¹ RSMo. § 434.100:

434.100. Contracts for public or private construction work with party's covenant, promise or agreement to indemnify or hold harmless another person from that person's own negligence or wrongdoing—exemptions

1. Except as provided in subsection 2 of this section, in any contract or agreement for public or private construction work, a party's covenant, promise or agreement to indemnify or hold harmless another person from that person's own negligence or wrongdoing is void as against public policy and wholly unenforceable.
2. The provisions of subsection 1 of this section shall not apply to:

(1) A party's covenant, promise or agreement to indemnify or hold harmless another person from the party's own negligence or wrongdoing or the negligence or wrongdoing of the party's subcontractors and suppliers of any tier;

(2) A party's promise to cause another person or entity to be covered as an insured or additional insured in an insurance contract;

(3) A contract or agreement between state agencies or political subdivisions or between such governmental agencies;

(4) A contract or agreement between a private person and such governmental entities for the use or operation of public property or a public facility;

(5) A contract or agreement with the owner of the public property for the construction, use, maintenance or operation of a private facility when it is located on such public property;

(6) A permit, authorization or contract with such governmental entities for the movement of property on the public highways, roads or streets of this state or any political subdivision;

(7) Construction bonds, or insurance contracts or agreements;

(8) An agreement containing a party's promise to indemnify, defend or hold harmless another person, if the agreement also requires the party to obtain specified limits of insurance to insure the indemnity obligation and the party had the opportunity to recover the cost of the required insurance in its contract price; provided, however, that in such case the party's liability under the indemnity obligation shall be limited to the coverage and limits of the required insurance; or

(9) Railroads regulated by the Federal Railroad Administration.

3. For the purposes of this section, "construction work" shall include, but not be limited to, the construction, alteration, maintenance or repair of any building, structure, highway, bridge, viaduct, or pipeline, or demolition, moving or excavation connected therewith, and shall include the furnishing of surveying, design, engineering, planning or management services, or labor, materials or equipment, in connection with such work.

4. The provisions of this section shall apply only to contracts or agreements entered into after August 28, 1999.

⁵² See *Lone Star Industries, Inc. v. Howell Trucking, Inc.*, 199 S.W.3d 900 (Mo. App. 2006); *Keveney v. Missouri Military Academy*, 304 S.W.3d 98, 104 (Mo. banc 2010); *Eggers v. Centrifugal & Mechanical Industries, Inc.*, 440 S.W.2d 512, 515 (Mo. App. 1969); *Scott v. Union Planters Bank, N.A.*, 196 S.W.3d 574, 580 (Mo. App. 2006).

⁵³ *Id.*

⁵⁴ *Honey v. Barnes Hosp.*, 708 S.W.2d 686 (Mo. App. 1986).

⁵⁵ *Stephenson v. First Missouri Corp.*, 861 S.W.2d 651 (Mo. App. 1993).

⁵⁶ *Minden v. Otis Elevator Co.*, 793 S.W.2d 461 (Mo. App. 1990).

⁵⁷ *MECO Systems, Inc. v. Dancing Bear Entertainment, Inc.*, 42 S.W.3d 794, 806 (Mo. App. 2001) (citing, among other cases, *American Drilling Service Co. v. City of Springfield*, 614 S.W.2d 266, 273 (Mo. App. 1981)).

⁵⁸ *MECO*, 42 S.W.3d at 806–07 (finding ambiguity in general contractor's contract with subcontractors when comparing general contractor's contracts with owner and subcontractor).

⁵⁹ *Id.*

⁶⁰ *Id.* at 808 (where the ambiguous pay if paid provision was "construed as establishing a reasonable time to pay by MECO rather than creating a condition precedent to MECO's obligation to pay Subcontractors").

⁶¹ *Sampson v. Missouri Pac. R. Co.*, 560 S.W.2d 573, 588 (Mo. banc 1978).

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- ⁶² See, e.g., *Hanson v. Tucker*, 303 S.W.2d 126, 129 (Mo. 1957).
- ⁶³ See *infra*, Section VI.E.
- ⁶⁴ See *infra*, Section VI.G.
- ⁶⁵ *Steffens v. Paramount Properties, Inc.*, 667 S.W.2d 725, 727–28 (Mo. App. 1984).
- ⁶⁶ See, e.g., *Catroppa v. Metal Bldg. Supply, Inc.*, 267 S.W.3d 812, 818 (Mo. App. 2008).
- ⁶⁷ *Id.* at 817 (internal quotations and citation omitted).
- ⁶⁸ *Id.*
- ⁶⁹ *Id.*
- ⁷⁰ 599 S.W.2d 522, 524 (Mo. App. 1980).
- ⁷¹ *Steffens*, 667 S.W.2d at 728.
- ⁷² *Julian v. Burns*, 600 S.W.2d 133, 141 (Mo. App. 1980).
- ⁷³ *Boone Valley Farm, Inc. v. Historic Daniel Boone Home, Inc.*, 941 S.W.2d 720, 721–22 (Mo. App. E.D. 1997).
- ⁷⁴ *Catroppa*, 267 S.W.3d at 818 (internal quotations omitted). The theory of consequential damages arises from the English case, *Hadley v. Baxendale*, 9 Ex. 341, 26 Eng. L. & Eq. 398.
- ⁷⁵ John D. Darling, *Delay of Game*, 26 CONSTR. LAW. 5, 6 (2006).
- ⁷⁶ See *Bloomfield Reorganized School Dist. No. R-14, Stoddard County v. Stites*, 336 S.W.2d 95, 100 (Mo. 1960).
- ⁷⁷ *Id.*
- ⁷⁸ *Id.* at 97.
- ⁷⁹ *Id.*
- ⁸⁰ *Id.* at 99–100.
- ⁸¹ *Id.* at 100.
- ⁸² *Bloomfield*, 336 S.W.2d at 100.
- ⁸³ *Id.* at 102.
- ⁸⁴ *Id.* at 100.
- ⁸⁵ Missouri law does not address these provisions specifically. For further discussion, please see John D. Darling, *Delay of Game*, 26 CONSTR. LAW. 5 (2006).
- ⁸⁶ *Groppel Company, Inc. v. U.S. Gypsum Co.*, 616 S.W.2d 49 (Mo. App. 1981).
- ⁸⁷ *Crowder v. Vandendeale*, 564 S.W.2d 879, 881 (Mo. banc 1978).
- ⁸⁸ *Children's Wish Foundation Intern., Inc. v. Mayer Hoffman McCann, P.C.*, 331 S.W.3d 648, 653 (Mo. banc 2011).
- ⁸⁹ *Autry Morlan Chevrolet Cadillac, Inc. v. RJF Agencies, Inc.*, 332 S.W.3d 184, 192 (Mo. App. 2010).
- ⁹⁰ *Fleischer v. Hellmuth, Obata & Kassabaum, Inc.*, 870 S.W.2d 832, 834, 837 (Mo. App. 1993) (a professional negligence suit, the Court found the architect was not liable to a general contractor for professional negligence arising out of performance of a contract between the architect and the owner).
- ⁹¹ *Id.*
- ⁹² RSMo. § 408.021.
- ⁹³ RSMo. § 408.020.
- ⁹⁴ *Doerflinger Realty Co. v. Fields*, 281 S.W.2d 609, 613 (Mo. App. 1955).
- ⁹⁵ *General Aggregate Corp. v. LaBrayere*, 666 S.W.2d 901 (Mo. App. 1984).
- ⁹⁶ RSMo. § 431.180.
- ⁹⁷ *Lober v. Kansas City*, 100 S.W.2d 267 (Mo. banc 1936).
- ⁹⁸ 408.040.2.
- ⁹⁹ 408.040.3.
- ¹⁰⁰ *Id.*
- ¹⁰¹ RSMo. § 408.040.1
- ¹⁰² *Reimers v. Frank B. Connet Lumber Co.*, 273 S.W.2d 348 (Mo. banc 1954).
- ¹⁰³ *In re Thomasson's Estate*, 192 S.W.2d 867 (Mo. banc 1946).
- ¹⁰⁴ RSMo. § 408.040.2.
- ¹⁰⁵ *Id.*
- ¹⁰⁶ *Schnuck Markets, Inc. v. Transamerica Ins. Co.*, 652 S.W.2d 206, 212 (Mo. App. 1983).
- ¹⁰⁷ M.A.I. 10.02; *Sharp v. Robberson*, 495 S.W.2d 394 (Mo. banc 1973).
- ¹⁰⁸ M.A.I. 10.01; *Burnett v. Griffeth*, 769 S.W.2d 780 (Mo. banc 1989).
- ¹⁰⁹ RSMo. § 510.263.
- ¹¹⁰ RSMo. § 510.265.
- ¹¹¹ *Purcell Tire and Rubber Company, Inc. v. Executive Beechcraft, Inc.*, 59 S.W.3d 505 (Mo. banc 2001).

¹¹² *Malan Realty Investors, Inc. v. Harris*, 953 S.W.2d 624 (Mo. banc 1997) (contractual agreement to waive right to a jury trial is enforceable); *High Life Sales Co. v. Brown-Forman Corp.*, 823 S.W.2d 493 (Mo. banc 1992) (forum selection clause in contract is valid so long as not unfair or unreasonable).

¹¹³ *Utility Service and Maintenance, Inc. v. Noranda Aluminum, Inc.*, 163 S.W. 3d 910, 914 (Mo. banc 2005).

¹¹⁴ *Warstler v. Cibrian*, 859 S.W.2d 162, 165 (Mo. App. 1993), citing *Goldberg v. Charlie's Chevrolet, Inc.*, 672 S.W.2d 177, 179 (Mo. App. 1984); *see also Taos Const. Co., Inc. v. Penzel Const. Co., Inc.*, 750 S.W.2d 522, 525–26 (Mo. App. 1988).

¹¹⁵ *Warstler*, 859 S.W.2d at 165; *see also Bloomfield Reorganized School Dist. No. R-14, Stoddard County v. Stites*, 336 S.W.2d 95 (Mo. 1960).

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I. MECHANIC'S LIEN BASICS

Montana Code Ann. § 71-3-521 *et. seq.* provides for and governs constructions liens on real estate. The statutes provide the exclusive means for the attachment and enforceability of a construction lien against real estate by persons furnishing labor or materials under a real estate improvement contract to secure payment of the person's contract price.

A. Requirements

Prior to filing a construction lien, the lien claimant generally must give to the contracting owner, by certified mail or personal delivery, written notice of the right to claim a lien no later than 20 days after the date on which the services or materials are first furnished to the contracting owner. MCA § 71-3-531. If notice is not given within 20 days of the date of commencement, the construction lien is enforceable only for the services or materials within the 20 day period before the date on which notice was given. *Id.* The notice must then be filed in the county clerk and recorder's office within five (5) days after the contracting owner receives notice. *Id.* A notice of right to claim a lien is effective for 1 year, upon which it expires if no notice of continuation is filed. *Id.* A sample form is provided in MCA § 71-3-532.

The following persons are not required to give notice of the right to claim a lien: (1) an original contractor who furnishes services or materials directly to the owner at the owner's request; (2) a wage earner or laborer who performs personal labor services for a person furnishing any service or material pursuant to a real estate improvement contract; (3) a person who furnishes services or materials pursuant to a real estate improvement contract that relates to a dwelling for five or more families; and (4) a person who furnishes services or materials pursuant to a real estate improvement contract that relates to an improvement that is partly or wholly commercial in character. *Id.*

In order for a construction lien to attach and be enforced, it must be filed not later than 90 days after the lien claimant's final furnishing of labor or materials, or the owner's filing a notice of completion. MCA § 71-3-535. The lien must be filed in the office of the County Clerk and Recorder of the county in which the improved real estate is located, and must certify that a copy has been served, either by certified mail return receipt requested or personal delivery, upon each owner of record of the subject property. MCA §§ 71-3-534 and 535. A sample form is provided in MCA § 71-3-536.

The Montana Supreme Court has consistently held that the procedural requirements of the construction lien statutes must be strictly construed. *Swain v. Battershell*, 294 Mont. 282,

983 P.2d 873 (1999). This includes not only the time and notice requirements, but also the language that must be contained in the lien itself. *Id.* Once that procedure has been fulfilled, the statutes will be liberally construed so as to give effect to their remedial purpose. *Id.*

B. Enforcement and Foreclosure

A construction lien claimant must file an action to foreclose the lien within two (2) years from the date the lien was filed. MCA § 71-3-562. Reasonable attorney fees and costs are allowed to the prevailing party in an action to enforce or foreclose a lien. MCA § 71-3-124. The priority of construction liens relative to other liens and encumbrances is governed by MCA §§ 71-3-541 and 542.

C. Ability to Waive and Limitations on Lien Rights

Contractors routinely execute lien waivers in exchange for payment. However, a construction contract may not contain provisions requiring the contractor, subcontractors or suppliers to waive the right to claim a construction lien (or the right to make a claim against a payment bond) before payment has been made. MCA § 28-2-723.

II. STATUTES OF LIMITATION AND REPOSE

A. Statutes of Limitation and Limitations on Application of Statutes

There is no specific statute of limitations for construction-related claims in Montana. Therefore, the claim is subject to the statute of limitations applicable to the underlying cause of action. The statute of limitations for actions on written contracts is 8 years. MCA § 27-2-202(a). The statute of limitations for non-written contracts is 5 years. MCA § 27-2-202(b). The statute of limitations for actions based in unjust enrichment/quantum meruit is 3 years. MCA § 27-2-202(c). The statute of limitations for a torts claim is three years. MCA § 27-2-204. The statute of limitations for injuries involving property is 2 years. MCA § 27-2-207. Montana's statutes on residential construction defects allow for limited tolling of applicable statutes of limitations upon certain conditions related to notice and opportunity to repair. MCA § 70-19-427.

B. Statutes of Repose and Limitations on Application of Statutes

MCA § 27-2-208 provides a 10 year statute of repose for actions for damages arising out of work on improvements to real property or land surveying. See *Assoc. of Unit Owners of Deer Lodge Condominium v. Big Sky of Mont., Inc.*, 245 Mont. 64, 798 P.2d 1018 (1990)(confirming statute is one of repose rather than limitation). This includes actions for damages arising out of design, planning, supervision, inspection, construction, or observation of construction. MCA § 27-2-208.

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

Montana has a series of statutes related to residential construction defect claims which require the claimant, prior to bringing an action against a construction professional, to provide the construction professional with written notice of the defect and an opportunity to cure. MCA § 70-19-426 *et seq.* The construction professional has twenty-one (21) days to respond to the claimant either proposing inspection of the property, offering to compromise/settle, or denying responsibility. MCA § 70-19-427. The statute outlines the procedures the parties must follow in each circumstance. *Id.* However, for a construction professional to avail himself of these procedures he must have provided the home owner notice of the applicable statutes. *Id.*

The statutes also limit the damages in residential construction defect actions to the cost of repairs to cure the defect, the expenses of temporary housing during the repair period, the reduction in market value due to the defect, and costs and attorneys' fees. MCA § 70-19-428.

Aside from residential construction defect claims, and the requirements pertaining to notice of the right to claim a construction lien (discussed above), there are no statutes requiring pre-suit notice of claims and opportunity to cure in construction disputes in general.

IV. INSURANCE COVERAGE AND ALLOCATION ISSUES

A. General Coverage Issues

Montana courts have issued a number of decisions in recent years addressing CGL liability coverage and the insurer's duty to defend construction-related claims. Generally speaking, coverage exclusions must be narrowly construed, while ambiguities are interpreted against the insurer and in favor of extending coverage. *Lukes v. Mid-Continent Cas. Co.*, 2013 WL 496203 (D.Mont. 2013).

B. Trigger of Coverage

The duty to defend is independent from and broader than the duty to indemnify created by the same insurance contract. *United National Ins. Co. v. St. Paul Fire & Marine Ins. Co.*, 352 Mont. 105, 214 P.3d 1260 (2008). The duty to defend arises when a complaint against the insured alleges facts that, if proven, represent a risk covered by the terms of the policy. *Id.* Unless there exists an unequivocal demonstration that the claim against the insured does not fall within the policy coverage, the insurer has a duty to defend. *Farmers Union Mut. Ins. Co. v. Staples*, 321 Mont. 99, 90 P.3d 381 (2004). If there is a duty to defend one claim alleged in a complaint, the insured must provide a defense for the whole case even if there is no possibility the remaining claims would be covered. *Haskins Const., Inc. v. Mid-Continent Cas. Co.*, 2011 WL 5325734 (D.Mont. 2011). While the duty to defend thus arises where the alleged facts even potentially fall within the scope of coverage, the duty to indemnify does not arise unless the policy actually covers the alleged harm. *Skinner v. Allstate Ins. Co.*, 329 Mont. 511, 127 P.3d 359 (2005).

In determining whether CGL coverage exists for a particular claim, Montana Courts have frequently interpreted the term “occurrence.” In policies defining “occurrence” as an “accident,” the Montana Supreme Court has held that term ‘accident’ reasonably refers to any unexpected happening that occurs without intention or design on the part of the insured.” *Blair v. Mid-Continent Cas.Co.*, 339 Mont. 8, 167 P.3d 888 (2007). Under that rationale “occurrence” has been held to encompass claims of property damage or other injury arising out of faulty workmanship. *Thomas v. Nautilus Ins. Co.*, 2011 WL 4369519 (D.Mont. 2011).

Montana courts have upheld unambiguous policy provisions (i.e., “your work” exclusions, and products-completed operations hazard provisions) excluding coverage for property damage to the insured’s own work product and materials. See *Lukes v. Mid-Continent Cas. Co.*, 2013 WL 496203 (D.Mont. 2013); *Taylor-McDonnell Construction Co. v. Commercial Union Ins.* 229 Mont. 34, 744 P.2d 892 (1997); and *Generali-U.S. Branch v. Alexander d/b/a Pioneer Plumbing and Heating*, 320 Mont. 450, 87 P.3d 1000 (2004).

C. Allocation Among Insurers

There are no Montana cases directly addressing issues of allocation among CGL carriers in construction-related disputes. Generally speaking, when multiple insurance policies apply to the same loss, the “other insurance” policies are examined to determine the proper allocation of the loss. *Mountain West Ins. Co. v. Credit General Ins. Co.*, 247 Mont. 161, 805 P.2d 569 (1991). In situations where there is a conflict between two insurance policies covering the same interest (i.e., one specifying excess coverage and one specifying pro-rata coverage), Montana has adopted the majority rule that the terms of the excess clause prevail over the terms of the pro-rata clause. *Id.* Therefore, the policy containing the pro-rata clause is considered the primary insurance for the loss, and must be exhausted prior to any allocation to the excess policy. *Id.*

V. CONTRACTUAL INDEMNIFICATION

Construction contract provisions that require one party to the contract to indemnify, hold harmless, insure, or defend the other party to the contract (or the other party's officers, employees, or agents) for liability, damages, losses, or costs that are caused by the negligence, recklessness, or intentional misconduct of the other party (or the other party's officers, employees, or agents) generally are void as against Montana public policy. MCA § 28-2-2111. However, the statute does expressly allow for contractual provisions requiring a party to indemnify, hold harmless, or insure the other party for liability, damages, losses, or costs, including but not limited to reasonable attorney fees, caused by the negligence, recklessness, or intentional misconduct of a third party or of the indemnifying party (or the indemnifying party's officers, employees, or agents). *Id.* Moreover, construction contracts may require a party to the contract to purchase a project-specific insurance policy, such as a builder’s risk policy. *Id.*

VI. CONTINGENT PAYMENT AGREEMENTS

The Montana Code contains no provisions for contingent payment agreements, and Montana courts have not yet addressed the issue. However, other statutory language suggests

“pay-if-paid” clauses may be unenforceable on grounds of public policy. For example, under Montana’s prompt pay statutes, performance by a contractor of a construction contract in accordance with the provisions of the contract entitles a contractor to payment from the owner; and performance by a subcontractor of a subcontract entitles the subcontractor to payment from the contractor. MCA § 28-2-2102. Construction contract provisions which state that a party to the contract may not suspend performance or terminate the contract if another party to the contract fails to make prompt payments are against public policy and are void and unenforceable. MCA § 28-2-2116(2). Moreover, as previously discussed, a construction contract may not require a party to waive the right to file a construction lien or make a claim on a payment bond before the party has been paid. MCA § 28-2-723.

VII. DAMAGES LIMITATIONS

A. Personal Injury Damages vs. Construction Defect Damages

In personal injury actions, the statutory measure of damages is the amount which will compensate the injured party for all the detriment proximately caused thereby, whether it could have been anticipated or not. MCA § 27-1-317. Each case must depend upon its own peculiar facts, and the award rests in the discretion of the trier of fact. *Sheehan v. DeWitt*, 150 Mont. 86, 430 P.2d 652 (1967). For breach of contract claims, recovery is prohibited for emotional or mental distress, except in those actions involving actual physical injury to the plaintiff. MCA § 27-1-310.

There are statutory limitations on the recovery of damages for residential construction defects. MCA § 70-19-428 limits such damages to the cost of repairs to cure the defect, the expenses of temporary housing during the repair period, the reduction in market value due to the defect, and reasonable costs and attorneys’ fees.

B. Attorney’s Fees Shifting and Limitations on Recovery

Attorney’s fees are generally not awarded in Montana unless allowed by statute or agreement of the parties. However, in construction disputes there are various statutes allowing for the recovery of attorney fees by the prevailing party. Montana’s prompt pay statutes provide for an award of attorney’s fees to the prevailing party in actions brought by contractors or subcontractors to collect payment. MCA § 28-2-2105. Attorney’s fees are also allowed in construction lien enforcement and foreclosure actions. MCA § 71-3-124. Another statutory basis for the recovery of attorney’s fees is for residential construction disputes. MCA § 70-19-427. If attorneys’ fees are provided for in a construction contract, the right to those fees is reciprocal. MCA § 28-3-704.

C. Consequential Damages

Damages for breach of contract are generally “the amount which will compensate the party aggrieved for all the detriment which was proximately caused [by the breach]...” MCA § 27-1-311. The measure of damages for breach of contract is expectancy; to put the party in the position he would have been had the contract been properly performed. *Bradley v. Crow Tribe of Indians*, 329 Mont. 448, 124 P.3d 1143 (2005). Any damages that cannot be clearly

ascertained are not recoverable. *Id.* Plaintiffs in breach of contract cases are entitled to the “benefit of the bargain” that the defendants promised to deliver, and are therefore entitled to damages in the amount that will put them in that position. *Poulsen v. Treasure State Industries.*, 192 Mont. 69, 626 P.2d 822 (1981).

D. Delay and Disruption Damages

Montana law contains no specific limitations on the recovery of delay and disruption damages. Absent a contractual provision that limits or excludes them, actual damages from delay and disruption may be recovered provided that they are foreseeable and otherwise qualify as consequential damages. The Montana Supreme Court has held that a subcontractor cannot recover delay damages from the general contractor when the subcontractor works “as directed” by the general, according to the terms of the construction contract. *Keeney Const. v. James Talcott Const. Co., Inc.*, 309 Mont. 226, 45 P.3d 19 (2002). Contract provisions allowing for liquidated damages in cases of delay and disruption are enforceable when, from the nature of the case, it would be impracticable or extremely difficult to fix the actual damage. MCA § 28-2-721.

E. Economic Loss Doctrine

The Montana Supreme Court addressed the economic loss doctrine in a case involving a third party professional negligence claim against a design professional. Noting that the majority of jurisdictions have rejected the economic loss doctrine, the Court held that a third party contractor may successfully recover for purely economic loss against a project engineer or architect when the design professional knew or should have foreseen that the plaintiff was at risk in relying on the information supplied. *Jim's Excavating Service, Inc. v. HKM Associates*, 265 Mont. 494, 878 P.2d 248 (1994). Generally speaking, in order for a party to recover on a tort claim arising out of the same set of facts underlying a breach of contract claim, there must exist an independent duty, separate and distinct from the contract obligation. *Boise Cascade Corp. v. First Sec. Bank of Anaconda*, 183 Mont. 378, 600 P.2d 173 (1979).

F. Interest

Montana law entitles parties to recover interest for damages capable of being made certain by calculation from the day the right to damages is vested in him. MCA § 27-1-211. That right is discretionary in non-breach of contract cases. MCA § 27-1-212. Any legal rate of interest stipulated by a contract remains chargeable after a breach until the contract is superseded by a verdict. MCA § 27-1-213.

G. Punitive Damages

Under Montana law punitive damages may not be recovered in an action arising from contract or breach of contract. MCA § 27-1-220. However, the Montana Supreme Court has held that an underlying contract will not defeat a claim for punitive damages where the defendant’s conduct was fraudulent. *Lee v. Armstrong*, 244 Mont. 289, 798 P.2d 84 (1990). Further, the Court clarified that while MCA § 27-1-220 prohibits punitive damages in claims

arising from contract, punitives are nevertheless allowed where the plaintiff can prove by clear and convincing evidence that the defendant is guilty of actual fraud or actual malice (as defined by MCA § 27-1-221) outside the contract context. *Weter v. Archambault*, 313 Mont. 284, 61 P.3d 771 (2002).

H. Other Damages

Residential construction disputes may involve claims under the Montana Consumer Protection Act, which allows for treble damages in certain circumstances. *See* MCA § 30-14-133(1).

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I. MECHANIC’S LIENS BASICS

A. Requirements

The Nebraska Construction Lien Act (the “Act”) is found at NEB. REV. STAT. §§ 52-125 through 52-159 (1981). Generally, to perfect a construction lien under the Act, the lien must be recorded not later than 120 days after the final furnishing of services or materials.¹ The lien must be signed by the claimant and must include the legal description of the real estate, the entity against which the lien is filed, the name and address of the claimant, the name and address of the person with whom the claimant contracted, the general description of the services performed, the amount unpaid, and the time the last services or materials were furnished.² The lien must be recorded with the Register of Deeds for the county where the land is situated.³

Under NEB. REV. STAT. § 52-131 (2003), in order to obtain a construction lien, one must have a valid real estate improvement contract. NEB. REV. STAT. § 52-130 (1981) provides that a “real estate improvement contract is an agreement to perform services, including labor, or to furnish materials for the purpose of producing a change in the physical condition of land or of a structure including.” While this statute does not provide a definition for improvements, it does list examples including the alteration of a surface, construction or installation on the land, demolition, repair, remodeling, landscaping, surface testing, or preparing plans to change the land. The Nebraska Supreme Court has also explained that there must be a permanent improvement in the physical condition of the land in order for the Act to apply. As evident in *Taylor v. Taylor*, merely cleaning up a yard and removing personal property from buildings does not constitute an improvement to the physical condition of the land and therefore the construction lien obtained for such work was deemed void.⁴

Enforcement and Foreclosure

Pursuant to NEB. REV. STAT. § 52-140 (1981) a lien is enforceable for only two years and an action must be filed to foreclose the lien within that time period after the recording of the lien. Any entity or person who has a recorded lien may join as a plaintiff in a proceeding to foreclose a lien and if one has such a lien does not join as a plaintiff, it may join as a defendant.⁵ If an entity records a lien or obtains an interest in the property prior to a judgment, it may become a defendant, even if the foreclosure proceedings have already begun. The court will decide the amount owed to each party claimant and the foreclosure of any liens against the property.⁶

Ability to Waive and Limitations on Lien Rights

The requirements for a waiver of a construction lien are provided in NEB. REV. STAT. § 52-144 (1981), which states:

(1) A written waiver of construction lien rights signed by a claimant requires no consideration and is valid and binding, whether signed before or after the materials or services were contracted for or furnished. Ambiguities in a written waiver are construed against the claimant.

(2) A written waiver waives all construction lien rights of the claimant as to the improvement to which the waiver relates unless the waiver is specifically limited to a particular lien right or a particular portion of the services or materials furnished.

(3) A waiver of lien rights does not affect any contract rights of the claimant otherwise existing.

(4) Acceptance of a promissory note or other evidence of debt is not a waiver of lien rights unless the note or other instrument expressly so declares.

Furthermore, if a party with an interest in the property provides the claimant with a written demand to begin a judicial proceeding within thirty days, the lien will lapse unless the claimant does indeed institute judicial proceedings or “records an affidavit that the total contract price is not yet due under the contract for which [the party] recorded the lien.”⁷ If the claimant does commence a judicial proceeding within two years after recording or if requested, within thirty days of a request to do so, the lien will continue while the proceeding is pending.⁸

In addition, there are special statutory provisions regarding liens with respect to railroads, bridges and similar improvements.⁹ Furthermore, construction liens are not permitted upon public construction since bonds are statutorily required on such projects.¹⁰

II. STATUTES OF LIMITATION AND REPOSE

A. Statutes of Limitation

The contractual statutes of limitation in Nebraska provide for: a) four years within which to commence an action on an oral contract;¹¹ and b) five years from the date of breach within which to commence an action in the case of a written contract.¹²

The general statute of limitations with respect to improvements to real estate and the applicable statute of repose is NEB. REV. STAT. § 25-223 (1976) which provides as follows:

Any action to recover damages based on any alleged breach of warranty on improvements to real property or based on any alleged deficiency in the design, planning, supervision, or observation of construction, or construction of an improvement to real property shall be commenced within four years after any alleged act or omission constituting such breach of warranty or deficiency. If such cause of action is not discovered and could not be reasonably discovered within such four-year period, or within one year preceding the expiration of such four-year period, then the cause of action may be commenced within two years from the date of such discovery or from the date of discovery of facts which would reasonably lead to such discovery, whichever is earlier. In no event may any action be commenced to recover damages for an alleged breach of warranty on improvements to real property or deficiency in the design, planning, supervision, or observation of construction, or construction of an improvement to real property more than ten years beyond the time of the act giving rise to the cause of action.

This section, “as a special statute of limitations concerning negligent construction of an improvement on real estate, applies only to actions, whether based on negligence or breach of warranty, brought against contractors and builders.”¹³ Additionally, whether pled in tort or contract, the applicable period of repose for a breach of warranty on improvements to real property is found in this section.¹⁴

Under Nebraska law, “liability under a theory of implied warranty of workmanlike performance has been further implied and extended to subsequent home purchasers as against general contractors,” in some instances.¹⁵ “This extension of liability is . . . limited to latent defects which manifest themselves after the subsequent purchase and are not discoverable by the subsequent purchaser’s reasonably prudent inspection at the time of the subsequent purchase. Such liability is, however, subject to the statute of limitations found at § 25-223.”¹⁶

Any claims for professional negligence based on deficiency in the design and planning of improvements to real property is governed by § 25-222, rather than § 25-223.¹⁷ **The Nebraska Supreme Court has specifically held that § 25-222 applies to architects with a duty to inspect throughout construction and an engineer with no other duty than to provide a design to an architect.**¹⁸ NEB. REV. STAT. § 25-222 (1972) states:

Any action to recover damages based on alleged professional negligence or upon alleged breach of warranty in rendering or failure to render professional services shall be commenced within two years next after the alleged act or omission in rendering or failure to render professional services providing the basis for such action; PROVIDED, if the cause of action is not discovered and could not be reasonably discovered within such two-year period, then the action may be commenced within one year from the date of such discovery or from the date of discovery of facts which would reasonably lead to such discovery, whichever is earlier;

AND PROVIDED FURTHER, that in no event may any action be commenced to recover damages for professional negligence or breach of warranty in rendering or failure to render professional services more than ten years after the date of rendering or failure to render such professional service which provides the basis for the cause of action.

If a plaintiff's claims are "for professional malpractice, whether pled in tort or in contract, the statute of limitations for professional negligence contained in this section applies."¹⁹

"A cause of action accrues for negligence in professional services when 'the alleged act or omission in rendering or failure to render professional services' takes place."²⁰ This two-year statute of limitations may therefore begin to run at some time before the full extent of the damages has been sustained.²¹ However, the Nebraska Supreme Court has also stated that the two-year statute of limitations and the ten year period of repose in this section, when applied to an architect who had the responsibility and duty to inspect throughout construction, began to run when the construction was completed.²²

B. Statutes of Repose / Contribution and/or Indemnification Claims

As stated above, the statutes of repose for negligent construction of an improvement to real estate, and for negligence in design or planning for improvements to real estate, are both ten years.

As for contribution and indemnification claims, Nebraska law holds that "a claim for indemnity accrues at the time the indemnity claimant suffers loss or damage."²³ Further, "an action for contribution does not accrue until a co-obligor has paid more than his or her proportionate share of the debt as a whole."²⁴

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

There is no Nebraska law requiring any kind of pre-suit notice or opportunity to cure in a non-UCC context. The contract between the parties will be the sole source of law on the matter.

IV. INSURANCE COVERAGE AND ALLOCATION ISSUES

A. General Coverage Issues

The Nebraska Supreme Court has determined that waivers enforcing subrogation clauses do not violate public policy in regards to gross negligence claims.

Concluding that waivers of subrogation cannot be enforced against gross negligence claims would undermine this underlying policy by encouraging costly litigation to contest whether a party's conduct was grossly negligent. Therefore, we conclude that "public policy favors enforcement of waivers of subrogation even in the face of gross negligence [claims]."²⁵

See also *Hearst-Argyle Properties, Inc. v. Entrex Communication Services, Inc.*, which held that public policy permits contract terms encouraging the anticipation of risks and obtaining insurance against those risks when a contractor was grossly negligent.²⁶

B. Trigger of Coverage

The most recent Nebraska case of note on coverage issues is *Auto-Owners Ins. Co. v. Home Pride Cos.*, in which the court held that “although a standard CGL policy does not provide coverage for faulty workmanship that damages only the resulting work product, if faulty workmanship causes bodily injury or property damage to something other than the insured's work product, an unintended and unexpected event has occurred, and coverage exists.”²⁷ See also *Farr. v. Designer Phosphate & Premix Internat.*,²⁸ stating that the time of the occurrence of an accident within the meaning of a policy is not the time when the wrongful act was committed, but the time when the complaining party was actually damaged.

C. Allocation Among Insurers

As to allocation among insurers, it is not entirely clear how a court would apportion a loss among multiple insurers. Factors that would likely be considered in making such allocation may include time on the risk, policy limits, number of insured, extent of damage in the policy period, or others. However, no specific Nebraska Supreme Court case exists on the issue in the construction arena, and we are left only to speculate as to what the court would consider in a given case. But see *Polenz v. Farm Bureau Ins. Co. of Nebraska*.²⁹

V. CONTRACTUAL INDEMNIFICATION

Nebraska law (§ 25-21,187) provides that indemnification provisions are void to the extent that indemnity is applicable in a situation where an entity would be protected from its own negligence. Section 25-21,187 (1987) provides, in part, as follows:

In the event that a public or private contract or agreement for the construction, alteration, repair, or maintenance of a building, structure, highway bridge, viaduct, water, sewer, or gas distribution system, or other work dealing with construction or for any moving, demolition, or excavation connected with such construction contains a covenant, promise, agreement, or combination thereof to indemnify or hold harmless another person from such person's own negligence, then such covenant, promise, agreement, or combination thereof shall be void as against public policy and wholly unenforceable. This subsection shall not apply to construction bonds or insurance contracts or agreements.

The Nebraska Supreme Court in *Hiway 20 Terminal, Inc. v. Tri-County Agri-Supply, Inc.*, made it clear that it was willing to enforce contractual indemnification provisions by striking language which would be contrary to NEB. REV. STAT. § 25-21,187.³⁰ In *Hiway 20 Terminal*, the court enforced a contractual provision for indemnification after striking a portion of the indemnification clause which, on its face, provided for indemnification without respect to negligence. Additionally, in *Hiway 20 Terminal*, the court also made it clear that indemnification existed under

Nebraska law without respect to a contractual indemnification requirement by applying common law rules with respect to indemnity. In that regard, the court relied upon a series of prior Nebraska cases for the proposition that indemnity will be allowed where the indemnitee has incurred liability to a third person because of the negligent reliance upon the care that the indemnitor should have exercised (in other words, the court has simply adopted a passive vs. active test).³¹

Of further interest is an additional provision of § 25-21,187 limited to architects and engineers. Subsection (2) of that statute expressly provides that architects and engineers are not liable in tort for personal injuries of employees on construction projects arising out of and in the course of employment on a construction project and occurring as a result of a violation of a safety practice by any third party unless the responsibility for supervision of safety practices "has been assumed by contract or by other conduct."

VI. CONTINGENT PAYMENT AGREEMENTS

A. Enforceability

Construction contingent payment agreements are not addressed in Nebraska statutes and therefore, Nebraska contract law would determine whether such an agreement is enforceable. See also *Muller Enterprises, Inc. v. Gerber*, which explained that when the event fixed by the contract for which a party has a contingent liability of payment occurs, the obligation to pay becomes absolute.³²

B. Requirements

Nebraska does not provide for any specific requirements for a contingent payment agreement in the construction arena. As such, the requirements for an agreement would be those of any other contract.

VII. DAMAGES LIMITATIONS

A. Personal Injury Damages vs. Construction Defect Damages

As explained in *Jones v. Elliott*, there is a limit on damages for defects. The court explained that "where defects in materials, construction or workmanship are remediable without materially injuring or reconstructing any substantial portion of the building, the damage which the owner is entitled to recover is the expense of making the work conform to contractual requirements."³³ However, when the defects cannot be corrected without reconstructing a substantial portion of the building, "the measure of the owner's damages is the difference between its value when constructed and what its value would have been if built according to contract."³⁴ It should also be noted that the Nebraska Supreme Court has held that the implied warranty of workmanlike performance can be extended to subsequent purchasers against general contractors. This extension is limited to latent defects that could not be reasonably discovered and subject to the statute of limitations.³⁵

However, when damages are awarded for a personal injury, the amount is not so limited. The plaintiff in *Orduna v. Total Construction Services Inc.* fell after his contractor removed a

staircase. The plaintiff was awarded damages for past medical expenses, lost wages, pain and suffering, and permanent disfigurement.³⁶

B. Attorney's Fees

As a general matter, attorneys fees and expenses are not available in Nebraska unless specifically provided for by statute. This remains true even if the contract between the parties provides for attorneys fees in the event of a breach, and even in cases of bad faith. One exception, however, is suits brought on insurance policies. NEB. REV. STAT. § 44-359 (1987) provides:

In all cases when the beneficiary or other person entitled thereto brings an action upon any type of insurance policy, except workers' compensation insurance, or upon any certificate issued by a fraternal benefit society, against any company, person, or association doing business in this state, the court, upon rendering judgment against such company, person, or association, shall allow the plaintiff a reasonable sum as an attorney's fee in addition to the amount of his or her recovery, to be taxed as part of the costs. If such cause is appealed, the appellate court shall likewise allow a reasonable sum as an attorney's fee for the appellate proceedings, except that if the plaintiff fails to obtain judgment for more than may have been offered by such company, person, or association in accordance with section 25-901, then the plaintiff shall not recover the attorney's fee provided by this section.

The current statute plainly states that a successful plaintiff may recover a reasonable sum as an attorney fee in "all cases" brought by the entitled person on "any type of insurance policy, except workers' compensation insurance."³⁷

C. Consequential Damages

The Nebraska Supreme Court has said:

[I]n construction contract cases that if the contract is substantially performed, the damages which the owner suffers because of defective workmanship or the use of unsuitable materials are measured by the reasonable cost of remedying the defects, if remediable; if the defects are not remediable without reconstruction of or material injury to a substantial portion of the building, the damages are measured by the difference between the value of the building as constructed compared to what its value would have been if constructed according to the contract.³⁸

D. Delay and Disruption Damages

The Nebraska Supreme Court has also stated that

[A] contractor has the right to recover damages resulting from delay caused by a breach of contract by the other party. Thus, where there is a breach of the contract by the owner or other party, and the breach of contract results in delay in the work of the contractor, and the delay in the work causes damage to the contractor, the contractor has a right of recovery in the absence of a “no-damage clause” or other provision to the contrary in the contract and even though the contract contains a provision for an extension of time.³⁹

Additionally, any claim for delay or disruption damages must show that the damages complained of are not “uncertain, conjectural, or speculative as to the existence, nature, or proximate cause thereof.” *Omaha P. P. Dist. v. Armstrong, Inc.*,⁴⁰ (disapproving of a “ripple effect” theory of delay damages).

E. Economic Loss Doctrine

The most recent Nebraska Supreme Court case on the economic loss doctrine is *Dobrovolny v. Ford Motor Co.*⁴¹ That case involved a dispute over defective car parts which resulted in damage to the Plaintiff’s truck. *Dubrovolny* held that there can be no “recovery in tort when the damages are to the product alone”⁴² Thus, because the only damage was to the Plaintiff’s truck, “the economic loss doctrine bars recovery under products liability law.”⁴³

F. Interest

For disputes in which the rate of interest is not specified by contract between the parties, or by special statute, interest on decrees and judgments for the payment of money are fixed at a rate equal to two percentage points above the bond investment yield, as published by the Secretary of the Treasury of the United States, of the average accepted auction price for the first auction of each annual quarter of the twenty-six-week United States Treasury bills in effect on the date of entry of the judgment. These rates can be found at the following internet address: <http://supremecourt.ne.gov/5017/judgment-interest-rate>.

Prejudgment accrues if the plaintiff makes an offer of settlement in compliance with NEB. REV. STAT. § 45-103.02 (1999). That statute provides:

(1) Except as provided in section 45-103.04, interest . . . shall accrue on the unpaid balance of unliquidated claims from the date of the plaintiff’s first offer of settlement which is exceeded by the judgment until the entry of judgment if all of the following conditions are met:

(a) The offer is made in writing upon the defendant by certified mail, return receipt requested, to allow judgment to be taken in accordance with the terms and conditions stated in the offer;

(b) The offer is made not less than ten days prior to the commencement of the trial;

(c) A copy of the offer and proof of delivery to the defendant in the form of a receipt signed by the party or his or her attorney is filed with the clerk of the court in which the action is pending; and

(d) The offer is not accepted prior to trial or within thirty days of the date of the offer, whichever occurs first.

(2) Except as provided in section 45-103.04, interest as provided in section 45-104 shall accrue on the unpaid balance of liquidated claims from the date the cause of action arose until the entry of judgment.

The exceptions to this rule in NEB. REV. STAT. § 45-103.04 (1999) relate to cases of divorce or suits against the state or its employees for negligence.

The final provision of Nebraska law relevant to pre-judgment interest is NEB. REV. STAT. § 45-104 (1980):

Unless otherwise agreed, interest shall be allowed at the rate of twelve percent per annum on money due on any instrument in writing, or on settlement of the account from the day the balance shall be agreed upon, on money received to the use of another and retained without the owner's consent, express or implied, from the receipt thereof, and on money loaned or due and withheld by unreasonable delay of payment. Unless otherwise agreed or provided by law, each charge with respect to unsettled accounts between parties shall bear interest from the date of billing unless paid within thirty days from the date of billing.

This provision is applied in the context of contracts that provide for liquidated damages.

G. Punitive Damages

It is generally accepted that punitive damages are expressly prohibited in Nebraska by the Nebraska Constitution.⁴⁴

VIII. CASE LAW AND LEGISLATION UPDATE

There are no other additional cases or statutes of relevance.

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- ¹ NEB. REV. STAT. § 52-137 (1981).
- ² NEB. REV. STAT. § 52-147(1) (1981).
- ³ NEB. REV. STAT. § 52-127(13) (1981).
- ⁴ *Taylor v. Taylor*, 277 Neb. 617, 764 N.W. 2d 101 (2009).
- ⁵ NEB. REV. STAT. § 52-155 (1981).
- ⁶ *Id.*
- ⁷ NEB. REV. STAT. § 52-140(2) (1981).
- ⁸ NEB. REV. STAT. § 52-140(3) (1981).
- ⁹ NEB. REV. STAT. §§ 52-115 - 52-116 (1943); NEB. REV. STAT. § 52-117 (1961).
- ¹⁰ NEB. REV. STAT. § 52-132 (1981).
- ¹¹ NEB. REV. STAT. § 25-206 (1943).
- ¹² NEB. REV. STAT. § 25-205 (1999).
- ¹³ *Murphy v. Spelts - Schultz Lumber Co.*, 240 Neb. 275, 281, 481 N.W. 2d 422, 428 (1992).
- ¹⁴ *Witherspoon v. Sides Constr. Co.*, 219 Neb. 117, 362 N.W. 2d 35 (1985).
- ¹⁵ *Moglia v. McNeil Co.*, 270 Neb. 241, 248, 700 N.W. 2d 608, 615-16 (2005).
- ¹⁶ *Id.*
- ¹⁷ *Omaha v. Hellmuth, Obata & Kassabaum, Inc.*, 767 F.2d 457 (8th Cir. 1985).
- ¹⁸ *Witherspoon v. Sides Constr. Co.*, 219 Neb. 117, 362 N.W. 2d 35 (1985).
- ¹⁹ *Reinke Mfg. Co. v. Hayes*, 256 Neb. 442, 449, 590 N.W. 2d 380, 388 (1999) (quoting NEB. REV. STAT. § 25-222(1972)).
- ²⁰ *Murphy v. Spelts-Schultz Lumber Co.*, 240 Neb. 275, 281, 481 N.W. 2d 422, 427 (1992).
- ²¹ *Sass v. Hanson*, 5 Neb. App. 28, 37, 554 N.W. 2d 642, 648 (1996).
- ²² *Williams v. Kingery Constr. Co.*, 225 Neb. 235, 404 N.W. 2d 32 (1987).
- ²³ *Wood River v. Geer-Melkus Constr. Co.*, 233 Neb. 179, 188, 444 N.W. 2d 305, 311 (1989).
- ²⁴ *Cepel v. Smallcomb*, 261 Neb. 934, 941, 628 N.W. 2d 654, 660 (2001).
- ²⁵ *Lexington Ins. Co. v. Entrex Communications Services, Inc.*, 275 Neb. 702, 711, 749 N.W. 2d 124, 131 (2008) (citing *Reliance National Indem. V. Knowles Industrial Service Corp.*, 868 A.2d 220, 226 (Me. 2005)) (emphasis in original).
- ²⁶ *Hearst-Argyle Properties, Inc. v. Entrex Communications Services, Inc.*, 279 Neb. 468, 478, 778 N.W. 2d 465, 473 (2010).
- ²⁷ *Auto-Owners Ins. Co. v. Home Pride Cos.*, 268 Neb. 528, 535, 684 N.W. 2d 571, 578 (2004).
- ²⁸ *Farr v. Designer Phosphate & Premix Internat.*, 253 Neb. 201, 570 N.W. 2d 320 (1997).
- ²⁹ *Polenz v. Farm Bureau Ins. Co. of Nebraska*, 227 Neb. 703, 419 N.W. 2d 677 (1988).
- ³⁰ *Hiway 20 Terminal, Inc. v. Tri-County Agri-Supply, Inc.*, 232 Neb. 763, 443 N.W. 2d 872 (1989).
- ³¹ *Id.*
- ³² *Muller Enterprises, Inc. v. Gerber*, 178 Neb. 463, 471, 133 N.W. 2d 913, 919 (1965).
- ³³ *Jones v. Elliot*, 172 Neb. 96, 107, 108 N.W. 2d 742, 748 (1961) (citing *Graham v. Anderson*, 121 Neb. 733, 735-36, 238 N.W. 362, 363 (1931)).
- ³⁴ *Id.*
- ³⁵ *Moglia v. McNeil Co., Inc.*, 270 Neb. 241, 248, 700 N.W. 2d 608, 616 (2005).
- ³⁶ *Orduna v. Total Const. Services Inc.*, 271 Neb. 557, 569-70, 713 N.W. 2d 471, 482 (2006).
- ³⁷ NEB. REV. STAT. § 44-359 (1987).
- ³⁸ *Lis v. Moser Well Drilling & Serv.*, 221 Neb. 349, 352, 377 N.W. 2d 98, 100 (1985).
- ³⁹ *In re Roberts Const. Co.*, 172 Neb. 819, 825, 111 N.W. 2d 767, 771 (1961).
- ⁴⁰ *Omaha P. P. Dist. v. Armstrong, Inc.*, 205 Neb. 484, 497, 288 N.W. 2d 467, 474 (1980) (quoting *Siefford v. Housing Authority*, 192 Neb. 643, 658, 223 N.W. 2d 816, 824 (1974)).
- ⁴¹ *Dobrovolny v. Ford Motor Co.* 281 Neb. 86, 92, 793 N.W. 2d 445, 449 (2011).
- ⁴² *Id.*
- ⁴³ *Id.*
- ⁴⁴ *Qualley v. Chrysler Credit Corp.*, 191 Neb. 787, 789, 217 N.W. 2d 914, 916 (1974).

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I. STATUTES OF LIMITATION AND REPOSE

The statute of limitations on construction defects in Nevada is not a simple issue. Generally, a claimant has four (4) years from the date he knew or should have known about the existence of the defect. However, for defects that are not immediately apparent at the time the building was purchased, there is an eight (8) year (or possibly longer) limitation period from the date of completion. The statutes of limitation and the repose periods applicable to construction defect claims are contained in the Nevada Revised Statutes ("NRS").

This section provides a brief overview of their application and the general limitation periods.

In a Nevada construction defect case, both the periods of repose and the statutes of limitation apply. The Nevada Supreme Court has explained the difference between statutes of repose and statutes of limitation as follows: Statutes of repose bar causes of action after a certain period of time, regardless of whether damage or an injury has been discovered. On the other hand, statutes of limitation foreclose suits after a fixed period of time following occurrence or discovery of an injury. *Allstate Ins. Co. v. Ferguson*, 104 Nev. 772, 775 n.2, 766 P.2d 904 (1988).

A party's claim arises when he discovers or should have discovered a construction defect. General notice of a construction defect claim given to the general contractor is sufficient to toll the statute of limitations for claims against a third-party subcontractor, even when the subcontractor is not involved in the initial proceedings against the general contractor. *Desert Fireplaces Plus, Inc. v. Dist. Ct.*, 120 Nev. 632, 635-36, 97 P.3d 607, 609 (2004).

- NRS 11.203 provides a 10-year statute of repose to bar claims against the owner, occupier, or any person furnishing the design or construction of an improvement to real property more than 10 years after substantial completion of the improvement for any damages regarding "any deficiency in the design, planning, supervision or observation of construction or the construction of such an improvement which is known or through the use of reasonable diligence should have been known" to the claimant.

* Updated through 2012.

- NRS 11.204 provides an eight-year limitation period for latent deficiencies in the design or construction of real property improvements.
- NRS 11.205 provides a six-year limitation period for filing claims arising from patent deficiencies in the design or construction of the improvement.

II. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

In construction defect cases, pre-suit notices and the associated opportunity to cure are governed by NRS Chapter 40. As such, before a Chapter 40 claimant commences an action or amends a complaint to add a cause of action for a constructional defect, a contractor, subcontractor, supplier or design professional is entitled to notice of the claim, and must be given an opportunity to cure the alleged defects. Nevada requires a homeowner to provide the contractor, subcontractor, supplier or design professional with notice of defect by certified mail.

The notice of defect must: (a) include a statement that the notice is being given to satisfy the requirements of Chapter 40; (b) specify in reasonable detail the defects or any damages or injuries to each residence or appurtenance that is the subject of the claim; and (c) describe in reasonable detail the cause of the defects, the nature and extent of the damage resulting from the defects and the location of each defect to the extent known. NRS 40.645. Moreover, a representative of a homeowner's association may send the notice (for common area defects). *Id.*

Not later than 60 days after a contractor receives a notice, the contractor may respond to the named owners of the residences and may provide a disclosure of the notice of the alleged common construction defects to each unnamed owner of a residence or appurtenance within the development to whom the notice may apply. NRS 40.6452. Additionally, not later than 30 days after the date on which a contractor receives notice of a construction defect pursuant to NRS 40.645, the contractor shall forward a copy of the notice by certified mail, return receipt requested, to the last known address of each subcontractor, supplier or design professional whom the contractor reasonably believes is responsible for a defect specified in the notice. NRS 40.646.

The contractor may be precluded from filing suit against the subcontractor, supplier or design professional if the contractor fails to send the notice as required. Within 30 days of their receipt of the notice, the subcontractor, supplier or design professional must inspect the alleged construction defect and notify the contractor if it intends to repair the defect and, if so, the length of time required for the repairs and at least two dates for the commencement of the repairs. Following the notice, but before a claimant may commence an action or amend a complaint to add a cause of action for a construction defect, the homeowner must allow an inspection and give the contractor, "a reasonable opportunity to repair the construction defect or cause the defect to be repaired if an election to repair is made pursuant to NRS 40.6472." NRS 40.647 (1) (b).

If a claimant commences an action without providing the right to repair, the court shall, "[d]ismiss the action, without prejudice, and compel the claimant to comply . . .," or, "[i]f dismissal of the action would prevent the claimant from filing another action because the action would be procedurally barred by the statute of limitations or statute of repose, the court shall stay the proceeding pending compliance . . ." *Id.* at (2).

In *Anse, Inc. v. Eighth Judicial Dist. Court of State ex rei. County*, 192 P. 2d 738 (Nev. 2008), the Supreme Court of Nevada held that a homeowner who is not the home's original purchaser can obtain the remedies available under NRS Chapter 40. The court ruled that a "residence is new for constructional defect purposes if it is a product of original construction that has been unoccupied as a dwelling from the completion of its construction until the point of its original sale. Therefore, the subsequent owner of a home that is a product of original construction, unoccupied as a dwelling from the completion of its construction until the point of its first sale, is not precluded under NRS 40.615 from seeking NRS Chapter 40 residential constructional defect remedies, so long as he or she does so within the limitation period provided by the applicable statute of repose."

Anse, supra followed the Nevada Supreme Court's ruling in *Westmark Owners' Ass'n v. Eighth Judicial Dist. Court ex rei.*, 167 P.3d 421 (Nev. 2007). In *Westmark*, the court held that condominiums, which were originally leased as apartments prior to their sale, were not subject to Chapter 40.

III. CONTRACTUAL INDEMNIFICATION

Nevada law recognizes contractual indemnity generally, without a separate analysis for construction contracts. "Contractual indemnity is where, pursuant to a contractual provision, two parties agree that one party will reimburse the other party for liability resulting from the former's work." *Medallion Dev., Inc. v. Converse Consultants*, 113 Nev. 27, 33, 930 P.2d 115, 119 (1997). Indemnity is "a complete shifting of liability to the party primarily responsible." *The Doctors Company v. Vincent*, 120 Nev. 644, 98 P.3d 681 (2004), citing *Medallion* supra.

Indemnity is defined, as follows:

Reimbursement or an undertaking whereby one agrees to indemnify another upon the occurrence of an anticipated loss. A contractual or equitable right under which the entire loss is shifted from a tortfeasor who is only technically or passively at fault to another who is primarily or actively responsible.

Medallion, 113 Nev. at 32; citing Black's Law Dictionary 326 (6th ed. 1991).

Moreover, attorneys' fees and costs are also generally recoverable under an indemnification action. Again, this depends upon the language of the contract and whether it includes recovery of attorneys' fees. However, in *Piedmont Equipment Co., Inc. v. Eberhard Mfg. Co.*, 665 P.2d 256, 260 (Nev. 1983), the Nevada Supreme Court held, "that where an indemnitee would be entitled to recover from an indemnitor the amount of a judgment paid to the plaintiff, as determined by the facts as found by the trier of fact, the indemnitee is entitled to recover in indemnity. . . ." (discussing right to recovery of attorneys' fees and costs). As such, even where silent as to attorneys' fees, there may still be a basis for recovery.

IV. MECHANIC'S LIEN BASICS

Nevada Revised Statute Chapter 108 governs mechanics' and materialmen's liens on a primary building or other superstructure, together with all garages, outbuildings and other appurtenant structures. The law allows any contractor, subcontractor, laborer, supplier or other person who performs work or furnishes materials valued at \$500.00 or more to be paid for his or her work or supplies. If unpaid, a lien may be placed on the home, land or property where the work was performed. The notice and recording requirements of the statute must be strictly followed.

A. Notice of Right to Lien

Pursuant to NRS 108.245, a Notice of Right to Lien may be given at any time after commencement of work. A lien claimant required to give this notice has a right to lien for materials or equipment furnished or for work or services performed in the 31 days before the date the Notice of Right to Lien is given and for the materials or equipment furnished or for work or services performed anytime thereafter until the completion of the work of improvement.

B. Notice of Intent to Lien

NRS 108.226 (6) provides that before a mechanic's lien is placed on residential property, the claimant must provide a "Notice of Intent to Lien." This section states in pertinent part as follows:

If a work of improvement involves the construction, alteration or repair of multifamily or single-family residences, a lien claimant, except laborers, must serve a 15 day notice of intent to lien incorporating substantially the same information required in a notice of lien upon both the owner and the prime contractor before recording a notice of lien. Service of the notice of intent to lien must be by personal delivery or certified mail and will extend the time for recording the notice of lien by 15 days.

The statute additionally states that a lien on multifamily or single-family residences, "may not be perfected or enforced" unless the 15 day notice of intent to lien has been given. The law does not provide a statutorily required form of Notice of Intent to Lien, but only that it be substantially similar to the Notice of Lien.

C. The Notice of Lien and Recording

A Notice of Lien becomes the lien itself and must later be recorded in the county where the work or improvement is located. To perfect his lien, a lien claimant must record his notice of lien in the office of the county recorder of the county where the property or some part thereof is located as follows:

- (a) Within 90 days after the date on which the latest of the following occurs:
 - (1) The completion of the work of improvement;

(2) The last delivery of material or furnishing of equipment by the lien claimant for the work of improvement; or

(3) The last performance of work by the lien claimant for the work of improvement; or

(b) Within 40 days after the recording of a valid notice of completion, if the notice of completion is recorded and served in the manner required pursuant to NRS 108.228.

Pursuant to NRS 108.226, the Notice of Lien must include a statement of the amount of the lien after deducting all just credits and offsets, the name of the owner, if known, the name of the person by whom he was employed or to whom he furnished the material or equipment, a brief statement of the terms of payment of his contract and a description of the property to be charged with the Notice of Lien sufficient for identification. NRS 108.226(5) sets forth the form of the Notice of Lien.

D. Discharge or Release of Notice of Lien, Waiver and Release

Pursuant to NRS 108.2437, as amended, a discharge or release of the Notice of Lien must be recorded by a lien claimant, "as soon as practicable, but not later than 10 days after discharged." A form is included in the statute. Once there has been full satisfaction of the lien amount, a Discharge or Release of Notice of Lien should be filed, but this should not be used for partial payments. The failure of a lien claimant to satisfy this requirement can lead to civil liability.

NRS 108.2457 states that the waiver and release given by any lien claimant is unenforceable unless it is in the form and made under circumstances set forth in the statute.

These include:

1. **Conditional Waiver and Release Upon Progress Payment** is to be used where the lien claimant is required to execute a waiver and release in exchange for or to induce the payment of a progress billing, but has not yet been actually paid. The waiver is "conditional" upon receipt of the payment specified in the release or upon the check clearing the bank.

2. **Unconditional Waiver and Release Upon Progress Payment** is to be used where the lien claimant has been paid a progress billing. In other words, the lien claimant has been paid a progress payment in good funds or a check has cleared the bank at the time the release is executed.

3. **Conditional Waiver and Release Upon Final Payment** is to be used where the lien claimant is required to execute a waiver and release in exchange for or to induce payment of a final billing and the lien claimant has not yet been paid the amount represented in the waiver. As provided in the document, it is only effective when good funds have been paid to the lien claimant or a check in the full amount cleared the bank.

4. **Unconditional Waiver and Release Upon Final Payment** is to be used where the lien claimant has been paid the final monies in good funds. Note that this document would be used prior to the actual recording of any mechanic's lien. Where a mechanic's lien has been recorded, the Discharge or Release of Notice of Lien (#3 above) would be the appropriate document.

E. Foreclosure

Pursuant to NRS 108.244, a lien claimant (or assignee) may not file a complaint for foreclosure of his Notice of Lien or the assigned Notice of Lien or Notices of Lien until 30 days have expired immediately following the recording of his Notice of Lien. This provision does not apply to or prohibit the filing of any statement of fact constituting a lien in an action already filed for foreclosure of a Notice of Lien; or in order to comply with the provisions of NRS 108.239, which limits foreclosure unless certain service requirements are met. The suit must be filed prior to the lapse of six (6) months from the recording of the lien.

At the time the lawsuit is filed, the lien claimant must record a Lis Pendens with the county recorder where the project is located. Furthermore, the lien claimant must also publish a notice of the suit once a week for three (3) successive weeks in a newspaper where the project is located. Finally, the lien claimant must serve a notice on the other lien holders of record.

F. Sale

The court shall cause the property to be sold in satisfaction of all liens and the costs of sale, including all amounts awarded to all lien claimants. Each mechanic's lien holder assumes priority based upon NRS 108.225.

The priority list is as follows:

1. Any lien, mortgage or other encumbrance which may have attached to the property after the commencement of construction of a work of improvement.
2. Any lien, mortgage or other encumbrance of which the lien claimant had no notice and which was unrecorded against the property at the commencement of construction of a work of improvement.
3. Every mortgage or encumbrance imposed upon, or conveyance made of, property affected by the liens after the commencement of construction of a work of improvement are subordinate and subject to the liens provided for in NRS 108.221 to 108.246, inclusive, regardless of the date of recording the notices of liens.

V. COVERAGE AND ALLOCATION ISSUES

As with most states, the duty to indemnify in Nevada is narrower than the duty to defend. The duty to indemnify arises only in the event of final imposition on the insured of covered, non-excluded liability through judgment or settlement. In Nevada, limitations of liability provisions are recognized by the courts and are enforceable. *Bernstein v. GTE Directories Corp.*, 827 F.2d 480 (9th Cir. 1987).

Upon receipt of a claim, an insurer must promptly provide all necessary forms, items, statements, instructions, and necessary "reasonable assistance" within 20 working days. If the insurer is unable to do so, it must, at a minimum, acknowledge the claim within the 20-day period. An insurer must also reply within 20 working days to any later communication that suggests a response is expected. Nevada Administrative Code ("NAC") 686A.665. Notice given to an agent is notice to the insurer. NAC 686A.645.

All denials must be in writing and accompanied by (a) a statement of any specific policy provisions relied upon, and (b) a reasonable explanation for the decision. If the claim is accepted, payment must be made within 30 days or interest will begin accruing on the payment. Upon payment, the specific coverage under which payment is made should be referenced. NAC 686A.675; NRS 686A.31 1(i).

Once a claim is made, an insurer must fully disclose all pertinent coverage and policy provisions under which the claim is presented. Ideally, these disclosures should be made in the insurer's initial response. NAC 686A.660.

For first-party property insurance claims, Nevada generally uses the "manifestation" trigger rule to determine what liability policy or policies have been triggered. Under the "manifestation" rule, the occurrence, which triggers coverage, is when the complaining party became aware of facts such that a claim could be made. "'Manifestation of loss' is defined as that point when appreciable damage occurs and is or should be known to the insured such that a reasonable insured would be aware that the notification duty under the policy has been triggered." *Jackson v. State Farm Fire and Cas. Co.*, 108 Nev. 504, 509, 835 P.2d 786, 790 (1992). The manifestation rule applies in first-party progressive property loss cases. *Id.*, citing *Prudential-LMI Ins. v. Superior Court*, 274 Cal.Rptr. 387, 403, 798 P.2d 1230, 1246 (1990).

Thus, in allocating between multiple insurers, the carrier whose policy was effective when progressive damage became manifest is liable.

VI. DAMAGES LIMITATIONS

Under NRS 40.655, the damages available in a constructional defect case are limited to those listed in the statute. Specifically, Nevada law allows for the recovery of the following costs:

- a) Any reasonable attorneys' fees;
- b) The cost of repairs that are necessary to cure any defect;
- c) Any reduction in the fair market value of the home due to structural failure;
- d) The value of the loss of use of all or any portion of the residence caused by the defect;
- e) The reasonable value of any other property damaged by the defect;
- f) Any related expert fees; and

- g) Interest on the amount of the claim.

In a construction defect action, when a jury determines that the claimant is entitled to recover damages proximately caused by a construction defect, a court can presume that the claimant is entitled to the recovery of attorneys' fees, whether or not the jury verdict explicitly so states. *Albios v. Horizon Communities, Inc.*, 132 P.3d 1022 (Nev. 2006). This case also holds that prejudgment interest is recoverable on an attorneys' fee award when the attorneys' fees are awarded as an element of damages in actions for construction defects, and the fees award draws interest from the time of service of the summons and complaint.

Nevada's offers of judgment rules apply to construction defect cases as well. When a party is barred from recouping costs and fees under NRS 17.115 and NRCP 68, that party is also barred from recouping costs pursuant to NRS 40.655. When multiple offers are made, a successive offer extinguishes the prior offer. *Albios v. Horizon Communities, Inc.*, 132 P.3d 1022 (Nev. 2006).

NRS 17.115 subsections 1-5 state:

1. At any time more than 10 days before trial, any party may serve upon one or more other parties a written offer to allow judgment to be taken in accordance with the terms and conditions of the offer of judgment.

2. Except as otherwise provided in subsection 7, if, within 10 days after the date of service of an offer of judgment, the party to whom the offer was made serves written notice that the offer is accepted, the party who made the offer or the party who accepted the offer may file the offer, the notice of acceptance and proof of service with the clerk. Upon receipt by the clerk:

(a) The clerk shall enter judgment according to the terms of the offer unless:

(1) A party who is required to pay the amount of the offer requests dismissal of the claim instead of entry of the judgment; and

(2) the party pays the amount of the offer within a reasonable time after the offer is accepted.

(b) Regardless of whether a judgment or dismissal is entered pursuant to paragraph (a), the court shall award costs in accordance with NRS 18.110 to each party who is entitled to be paid under the terms of the offer, unless the terms of the offer preclude a separate award of costs. Any judgment entered pursuant to this section shall be deemed a compromise settlement.

3. If the offer of judgment is not accepted pursuant to subsection 2 within 10 days after the date of service, the offer shall be deemed rejected by the party to whom it was made and withdrawn by the party who made it. The rejection of an offer does not preclude any party from making another offer pursuant to this section. Evidence of a rejected offer is not admissible in any proceeding other than a proceeding to determine costs and fees.

4. Except as otherwise provided in this section, if a party who rejects an offer of judgment fails to obtain a more favorable judgment, the court:
- (a) May not award to the party any costs or attorneys' fees;
 - (b) May not award to the party any interest on the judgment for the period from the date of service of the offer to the date of entry of the judgment;
 - (c) Shall order the party to pay the taxable costs incurred by the party who made the offer; and
 - (d) May order the party to pay to the party who made the offer any or all of the following:
 - (1) A reasonable sum to cover any costs incurred by the party who made the offer for each expert witness whose services were reasonably necessary to prepare for and conduct the trial of the case.
 - (2) Any applicable interest on the judgment for the period from the date of service of the offer to the date of entry of the judgment.
 - (3) Reasonable attorneys' fees incurred by the party who made the offer for the period from the date of service of the offer to the date of entry of the judgment. If the attorney of the party who made the offer is collecting a contingent fee, the amount of any attorneys' fees awarded to the party pursuant to this subparagraph must be deducted from that contingent fee.
5. To determine whether a party who rejected an offer of judgment failed to obtain a more favorable judgment:
- (a) If the offer provided that the court would award costs, the court must compare the amount of the offer with the principal amount of the judgment, without inclusion of costs.
 - (b) If the offer precluded a separate award of costs, the court must compare the amount of the offer with the sum of:
 - (1) The principal amount of the judgment; and
 - (2) The amount of taxable costs that the claimant who obtained the judgment incurred before the date of service of the offer. As used in this subsection, "claimant" means a plaintiff, counterclaimant, cross-claimant or third-party plaintiff.

NRCP 68(a) and (d)-(f) state:

(a) The Offer. At any time more than 10 days before trial, any party may serve an offer in writing to allow judgment to be taken in accordance with its terms and conditions.

* * *

(d) Judgment Entered Upon Acceptance. If within 10 days after the service of the offer, the offeree serves written notice that the offer is accepted, either party may then file the offer and notice of acceptance together with proof of service. The clerk shall enter judgment accordingly. The court shall allow costs in accordance with NRS 18.110 unless the terms of the offer preclude a separate award of costs. Any judgment entered pursuant to this section shall be expressly designated a compromise settlement. At his option, a defendant may within a reasonable time pay the amount of the offer and obtain a dismissal of the claim, rather than a judgment.

(e) Failure to Accept Offer. If the offer is not accepted within 10 days after service, it shall be considered rejected by the offeree and deemed withdrawn by the offeror. Evidence of the offer is not admissible except in a proceeding to determine costs and fees. The fact that an offer is made but not accepted does not preclude a subsequent offer. With offers to multiple offerees, each offeree may serve a separate acceptance of the apportioned offer, but if the offer is not accepted by all offerees, the action shall proceed as to all. Any offeree who fails to accept the offer may be subject to the penalties of this rule.

(f) Penalties for Rejection of Offer. If the offeree rejects an offer and fails to obtain a more favorable judgment,

(1) The offeree cannot recover any costs or attorneys' fees and shall not recover interest for the period after the service of the offer and before the judgment; and

(2) The offeree shall pay the offeror's post-offer costs, applicable interest on the judgment from the time of the offer to the time of entry of the judgment and reasonable attorneys' fees, if any be allowed, actually incurred by the offeror from the time of the offer. If the offeror's attorney is collecting a contingent fee, the amount of any attorneys' fees awarded to the party for whom the offer is made must be deducted from that contingent fee.

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I. MECHANIC'S LIEN BASICS

New Hampshire Revised Statutes Annotated ("RSA") 447 provides for and governs mechanic's liens on private projects. The purpose of the mechanic's lien is to provide effective security to those individuals who furnished labor or materials that were used to enhance the value of the property of another. *Innie v. W & R, Inc.*, 116 N.H. 315, 317, 359 A.2d 616 (1976).

A. Requirements

RSA 447:2 states that any person who, by himself or others, performs labor, furnishes professional design services or furnishes materials in the amount of \$15 or more for erecting or repairing a home or other building, or for building a dam, canal, sluiceway, well or bridge, or for consumption or use in the prosecution of such work, by virtue of a contract with the owner thereof, shall have a lien on said structure, and on any right of the owner to the lot of land on which it stands.

Notice. The property owner must receive notice of the right to assert a lien. RSA 447:6. This notice may be given in the first instance after the provision of labor, services or supplies by a general contractor. Subcontractors providing labor or furnishing materials in the amount of \$15 or more by virtue of a contract with an agent, contractor, or subcontractor of the owner have separate notice requirements. *See* RSA 447:5.

Account. Subcontractors giving notice "shall, as often as once in 30 days, furnish to the owner, or person having charge of the property on which the lien is claimed," a written account of the labor performed or materials furnished during successive 30 day periods. RSA 447:8. These accountings may be given at the same time as the first notice given in the case of general contractors, though subcontractors must provide such accountings while the project is ongoing. RSA 447:6.

B. Enforcement and Foreclosure

Duration/Priority of the lien. Liens created under RSA 447:2 continue for 120 days after the services are performed, or the materials, services, supplies or other things are furnished,

unless payment is made in full. Such liens take precedence over all prior claims except tax liens. RSA 447:9.

How secured. Mechanic's liens may be "secured by attachment of the property on which the lien exists at any time while the lien continues, the writ and return thereon distinctly expressing that purpose." RSA 447:10. A person possessing a mechanic's lien must bring suit and seek pre-judgment attachment of the secured property. *Id.* As long as "the writ and return taken together distinctly express that the attachment is made to secure a mechanic's lien, the purpose of the attachment is sufficiently stated." *Holden Eng'g & Surveying, Inc. v. Law Offices of Raymond P. D'Amante, P.A.*, 142 N.H. 213, 216, 698 A.2d 3 (1997). The attachment generally has priority over all lien claims for labor, materials or other things done or furnished after the attachment was made. RSA 447:11. Exceptions to this rule are set forth in RSA 447:12-a.

Public Projects. A bond is required for public projects involving expenditures of \$35,000 or more. RSA 447:16. Other requirements for public projects are set forth in RSA 447:15-18.

C. Ability to Waive and Limitations on Lien Rights

The New Hampshire Supreme Court has discussed the waiver of mechanic's liens extensively and, although it has never expressly approved or disapproved of the practice, such waivers appear to be effective. *See Guyotte v. O'Neill*, 157 N.H. 616, 618-22, 958 A.2d 939, 943-46 (2008). A waiver of the right to assert a mechanic's lien under the statute, however, does not act as a general release of all claims to payment for work performed. *Id.* at 620-21, 958 A.2d 944-45. Under the mechanic's lien statute, it is clear that a contractor does not waive its lien rights by taking a note on the attached property. RSA 447:14. Such a note will not defeat a lien unless the note was expressly given in satisfaction of the lien and covers the amount due thereon.

II. **STATUTES OF LIMITATION AND REPOSE**

A. Statutes of Limitation and Limitations on Their Application

New Hampshire's statute of limitations for personal actions applies in construction cases. *Big League Entertainment Inc. v. Brox Indus. Inc.*, 149 N.H. 480, 484, 821 A.2d 1054, 1057-58 (2003) (*citing* RSA 508:4). As expressly noted in the statute, the "discovery rule" applies in New Hampshire. Additionally, a party's age or mental infirmity tolls the statute of limitations, which will not run until two years after the disability of age or incompetence is removed. RSA 508:8.

B. Statutes of Repose and Limitations on Their Application

RSA 508:4-b, I states that "all actions to recover damages for injury to property, injury to the person, wrongful death or economic loss arising out of any deficiency in the creation of an improvement to real property including without limitation, the design, labor, materials, engineering, planning, surveying, construction, observation, supervision or inspection of that improvement, shall be brought within 8 years from the date of substantial completion of the improvement, and not thereafter." This has been expressly held to be a statute of repose, rather

than a statute of limitations, by the New Hampshire Supreme Court. *Big League Entertainment*, 149 N.H. at 484, 821 A.2d at 1057-58. A project is “substantially complete” when “construction is sufficiently complete so that an improvement may be utilized by its owner or lawful possessor for the purposes intended.” RSA 508:4-b, II.

The statute of repose is extended in cases involving “fraudulent misrepresentations, or actions involving fraudulent concealment of material facts.” RSA 508:4-b, V(a). In such cases, the statute of repose does not begin to run until “all relevant facts are, or with due care ought to be, discovered by the person bringing the action.” *Id.* Although this may seem to create a new statute of limitations, rather than extending the statute of repose, the Supreme Court’s decision in *Big League Entertainment* strongly suggests otherwise. See *Big League Entertainment*, 149 N.H. at 484, 821 A.2d at 1057-58. The statute of repose is inapplicable to cases involving design or construction defects in nuclear energy facilities. RSA 508:4-b, V(b). The repose period may be extended by written agreement of the parties. RSA 508:4-b, III.

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

Pursuant to RSA 359-G:4, in all actions by homeowners against contractors where the contract was entered into after January 1, 2006, the homeowner must, at least 60 days before initiating an action against a contractor, provide service of written notice of the claim on the contractor.

The notice must state that “the homeowner asserts a construction defect claim and is providing notice of the claim pursuant to” RSA 359-G:4, I. The notice must “describe the claim in detail sufficient to explain the nature of the alleged construction defect and the result of the defect,” and the homeowner must provide the contractor with “any evidence in possession of the homeowner that depicts the nature and cause of the construction defect.” RSA 359-G:4, I.

Within 30 days after service of the notice of claim, the contractor is required to serve on the homeowner, and any other contractor that has received the notice of claim, a written response to the claim or claims, which discloses any evidence in the possession of the contractor that depicts the nature and cause of the construction defect and which:

- a. offers to settle the claim by monetary payment, the making of repairs, or a combination of both, without inspection;
- b. proposes to inspect the residence that is the subject of the claim; or
- c. wholly rejects the claim.

RSA 359-G:4, II.

If the contractor proposes to inspect, the homeowner may, “within 15 days of receiving a contractor’s proposal, provide the contractor and its subcontractors, agents, experts, and consultants prompt and complete access to the residence to inspect the residence, document any alleged construction defect and, if authorized in writing by the homeowner, perform any destructive or non-destructive testing required to fully and completely evaluate the nature, extent, and cause of the claimed defect and the nature and extent of any repairs or replacements that may

be necessary to remedy the alleged defect.” RSA 359-G:4, IV. Within 15 days of the completion of the inspection and testing, the contractor must serve the homeowner with a response “disclosing any inspection or testing records in the possession of the contractor that depict the nature and cause of the construction defect, and:

- a. A written offer to fully or partially remedy the construction defect at no cost to the homeowner;
- b. A written offer to settle the claim by monetary payment;
- c. A written offer including a combination of repairs and monetary payment; or
- d. A written statement that the contractor will not proceed further to remedy the defect.

RSA 359-G:4, V. No later than 30 days after receipt of the contractor’s offer, the homeowner must serve the contractor with written notice of acceptance; otherwise, the offer is deemed rejected. RSA 359-G:4, X.

Service of a written notice of claim tolls the expiration of the statute of limitations for sixty (60) days. RSA 359-G:4, XII. Service does not toll the statute of repose. *Id.* Actions filed by homeowners that have not complied with RSA 359-G shall be stayed for a maximum of sixty (60) days, without prejudice, until the homeowner has complied with the requirements of RSA 359-G. RSA 359-G:3.

If, after providing the contractor with the notice required by RSA 359-G:4, the homeowner discovers additional defects that are “substantially related to the factual circumstances, acts, or omissions giving rise to the construction defects alleged in the initial notice,” those additional defects may be “alleged in an action involving the claims in the initial notice without following the notice of claim procedure provided in RSA 359-G:4.” RSA 359-G:5. If a homeowner accepts an offer, and the contractor complies with the terms of the offer, the homeowner is thereafter barred from bringing an action for the claim. RSA 359-G:6.

IV. INSURANCE COVERAGE AND ALLOCATION ISSUES

A. General Coverage Issues

When disputes over coverage arise, the insurer bears the burden of establishing that the insurer is not covered. *Weeks v. St. Paul Fire & Marine Ins. Co.*, 140 N.H. 641, 643, 673 A.2d 772 (1996). Any ambiguities in policy language will be resolved in favor of the insured. *Id.* Within six months after the filing of the writ, complaint, or other pleading initiating the action giving rise to the coverage question, the insured or insurer may file a petition for declaratory judgment to determine whether an insurance policy provides coverage for the allegations contained in the writ. RSA 491:22, III. This provision also applies to indemnification actions. *See The Craftsbury Co., Inc. v. Assurance Co. of Am.*, 149 N.H. 717, 834 A.2d 267 (2003). The six month limitations period does not apply when “the facts giving rise to such coverage dispute are not known to, or reasonably discoverable by, the insurer until after expiration of such 6-

month period” or if the failure to file within six months resulted from “accident, mistake or misfortune” and not neglect. RSA 491:22, III

B. Trigger of Coverage Issues

New Hampshire has not specifically adopted one of the four approaches generally used to determine how coverage is triggered; instead, New Hampshire courts determine whether coverage has been triggered by looking at the language of the relevant insurance policy (or policies). *EnergyNorth Natural Gas, Inc. v. Underwriters at Lloyd's*, 150 N.H. 828, 848 A.2d 715 (2004); *see also Pro Con Constr., Inc. v. Acadia Ins. Co.*, 147 N.H. 470, 472-73, 794 A.2d 108 (2002) (holding that coverage was not triggered because the policy only extended coverage to an additional insured when liability “arose out of . . . ongoing operations performed for that insured, and no causal nexus linked the ongoing operations and the injuries”). New Hampshire courts have utilized both the “injury-in-fact” or “actual damage” and the exposure rules. *EnergyNorth Natural Gas, Inc.*, 150 N.H. 828. Under the “injury-in-fact” rule, “all of the policy periods during which the insured proves some injury or damage” are implicated. *Id.* at 831. In contrast, under the “exposure” rule “all insurance contracts in effect when the property was exposed . . . would be triggered.” *Id.*

The New Hampshire Supreme Court applied the injury-in-fact rule to occurrence-based policies. It held that if the alleged event and resulting damage are continuing, the injury-in-fact triggering coverage is also continuing. *Id.* at 835-36.

The exposure rule was applied to accident-based policies, which covered “accidents occurring during the policy period.” *Id.* at 837. While the accident triggering the coverage must occur during the policy period, the accident does not need to be limited to a single, discrete event; if the accident “is continuing, multiple exposures triggering coverage are also continuing.” *Id.* at 838.

The exposure rule was also applied to an occurrence-based policy, which provided that coverage was “triggered by occurrences happening during the currency hereof.” *Id.* at 840. Under the policy in question, the occurrence which caused the property damage was required to occur during the policy period; however, the policy did not require that the resulting property damage occur during the policy period. *Id.*

C. Allocation Among Insurers

The New Hampshire Supreme Court has addressed allocation of damages among multiple triggered insurance policies in a long-term environmental pollution case. *EnergyNorth Natural Gas, Inc. v. Certain Underwriters at Lloyd's*, 156 N.H. 333 (2007). The Court adopted a pro rata approach to allocating liability among multiple insurers, and without selecting a method of pro-rata, suggested that courts should apply the pro-rata by years and limits, if possible. *Id.* at 345. Under that method, “loss is allocated among policies based on both the number of years a policy is on the risk as well as that policy’s limits of liability. The basis of an individual insurer’s liability is the aggregate coverage it underwrote during the period in which the loss occurred.” *Id.* at 341 (internal quotation and citation omitted).

D. Issues With Additional Insurance

The predominant issue that arises in construction cases in New Hampshire concerning additional insurance involves the determination of which insurance policy is “primary” and which is “excess.” *See, e.g., Peerless Ins. v. Vermont Mut. Ins. Co.*, 151 N.H. 71, 849 A.2d 100 (2004). These disputes are resolved by interpreting the relevant policy language, though where each policy has “mutually repugnant” excess-insurance provisions, the Court will order each insurance company to pay its pro rata share of settlements, judgments, and defense costs. *Id.* at 74, 849 A.2d at 103.

V. **CONTRACTUAL INDEMNIFICATION**

Indemnification agreements that require a party to indemnify any person or entity for personal injury or property damage that was not caused by that party or its employees, agents, or subcontractors are prohibited. RSA 338-A:2. This prohibition applies to contracts for construction, reconstruction, installation, alteration, remodeling, repair, demolition, or maintenance work, so long as those contracts took effect on or after March 5, 2004. *Id.*

Other indemnification agreements are permitted, and implied agreements to indemnify may exist where an individual “performs a service under contract negligently and, as a result, causes harm to a third party in breach of a nondelegable duty of the indemnitee.” *Jaswell Drill Corp. v. Gen. Motors Corp.*, 129 N.H. 341, 346, 529 A.2d 875 (1987); *see also* RSA 359-G:8, II.

VI. **CONTINGENT PAYMENT AGREEMENTS**

A. Enforceability

New Hampshire’s courts view contingent payment agreements with disfavor, and so will not enforce such agreements unless they are expressed clearly in the agreement between the parties. *Holden Engineering and Surveying, Inc. v. Pembroke Road Realty Trust*, 137 N.H. 393, 396, 628 A.2d 260, 262 (1993).

B. Requirements

As noted above, any contingent payment agreement must, to be enforceable, be expressed in the clearest possible terms. *Id.* New Hampshire’s courts have not weighed in on any specific requirements for either “pay-if-paid” or “pay-when-paid” contingent payment agreements beyond requiring such agreements to be clearly expressed.

VII. **DAMAGES LIMITATIONS**

A. Personal Injury Damages Versus Construction Defect Damages

The Economic Loss Doctrine generally operates in New Hampshire to limit the damages available to plaintiffs in construction defect cases. The doctrine is a “judicially-created remed[y] principle that operates generally to preclude contracting parties from pursuing tort recovery for

purely economic or commercial losses associated with the contract relationship.” *Tietsworth v. Harley-Davidson, Inc.*, 677 N.W.2d 233, 241 (Wis. 2004).

Of course, tort damages may be available if a construction defect amounts to a breach of New Hampshire’s Consumer Protection Act. *See* RSA 358-A:3, RSA 358-A:10. The same is true if the homeowner properly pleads and proves claims for negligent or intentional misrepresentation, which constitute exceptions to the Economic Loss Doctrine. *See Plourde Sand & Gravel v. JGI Eastern, Inc.*, 154 N.H. 791, 795-96.

B. Attorney’s Fees Shifting and Limitations on Recovery

New Hampshire follows the “American Rule,” and parties generally bear their own attorneys’ fees in construction defect litigation. *See Taber v. Town of Westmoreland*, 140 NH 613, 615 (1998). The exceptions to this rule are where the parties agree to an allocation of attorney’s fees, where a statute creates a right to recovery of attorney’s fees, or where a judicially-created exception to the American Rule applies. *Id.* The common-law exceptions include situations where a party must sue to secure “a clearly defined right which should have been freely enjoyed without such intervention.” *Id.*

Attorney’s fee awards are generally supervised by the courts, and will only be awarded to the extent they are reasonable. *See George v. Al Hoyt & Sons*, 162 N.H. 123, 138-39, 27 A.3d 697, 712 (2011).

C. Consequential Damages

Consequential damages are the “losses that flow from a breach of contract.” *Bell v. Liberty Mut. Ins. Co.*, 146 N.H. 190, 194, 776 A.2d 1260, 1263-64 (2001). The party seeking damages must prove, by a preponderance of evidence, the extent and amount of the damages sought. Consequential damages are only available “if the harm was a reasonably foreseeable result at the time the parties entered into the contract.” *Independent Mech. Contractors v. Gordon T. Burke & Sons*, 138 N.H. 110, 114, 635 A.2d 487, 489 (1993).

Consequential damages for breach of a construction contract include: lost profits, *Id.* at 115, the difference between the value of the building as constructed and the value the building would have had if constructed as promised, *Bailey v. Sommovigo*, 137 N.H. 526, 530, 631 A.2d 913 (1993) (citation omitted), the difference between the cost of finishing the work and the balance due the plaintiff on the contract, *McMullin v. Downing*, 135 N.H. 675, 677, 609 A.2d 1226 (1992), and recovery of the cost of completion from the Subcontractor if the cost of completion exceeds the value of the subcontract. *Parex Contracting Corp. v. Welch Constr. Co., Inc.*, 128 N.H. 254, 258, 512 A.2d 1104 (1986).

D. Delay and Disruption Damages

A plaintiff is entitled to reasonable damages caused by a contractor’s disruption or delay of a construction project. *See Tardiff v. Twin Oaks Realty Trust*, 130 N.H. 673, 677 (1988). This is especially so where a contract states that “time is of the essence.” *Id.* In such cases, the damages allowed may include such items as carrying costs and increased costs to the plaintiff—and may cover claims for lost profits if plead and proved properly. *Id.*

E. Economic Loss Doctrine

For a discussion of the Economic Loss Doctrine, see Section VII, A, *supra*.

F. Interest

As a general rule, claims collect interest at an established rate from the date the lawsuit is commenced. *See* RSA 524:1-a; RSA 524:1-b; *see also* RSA 336:1-2.

G. Punitive Damages

Punitive damages are not available in New Hampshire except when expressly authorized by statute. *Stewart v. Bader*, 154 N.H. 75 (2006) (*citing* RSA 507:16). New Hampshire courts may award enhanced compensatory damages, or “liberal compensatory damages,” when damages result from “wanton, malicious, or oppressive” conduct. Such damages must be *compensatory* in nature, i.e., they must compensate a plaintiff for an aggravated injury caused by the nature of defendant’s conduct. Such awards cannot be given to punish a defendant or to make an example of it. *Vratsenes v. N.H. Auto., Inc.*, 112 NH 71, 73 (1972).

VII. CASE LAW AND LEGISLATION UPDATE

The most notable development for construction law litigants in the decade has been the establishment of the Business and Commercial Dispute Docket. In 2008, the New Hampshire General Court enacted RSA 491:7-a, establishing the Business and Commercial Dispute docket. The BCDD is simply a separate docket in the Superior Court. It sits in Merrimack County, and is presided over by a judge with substantial experience handling business disputes, including construction disputes.

To qualify for the BCDD, all parties to an action must consent to its jurisdiction; one party must be a “business entity” as defined by the statute; the case cannot involve an individual who has purchased or leased merchandise for personal, family or household use; and the amount in controversy must be \$50,000 or greater, RSA 491:7-a, I. The BCDD is granted jurisdiction under the above circumstances, over several categories of cases that arise in the construction context: “Claims arising from breach of contract[,]” “Claims relating to surety bonds,” and “other complex disputes of a business or commercial nature.” RSA 491:7-a, VI (a), (d) & (m).

In the past two years, construction disputes have commanded a significant portion of the BCDD’s attention. *See, e.g., Dartmouth College v. North Branch Construction, Inc.*, No. 2009-CV-152 (Mar. 24, 2014); *Town of Bow v. Provan & Lorber, Inc. and Gordon Construction, Inc.*, No. 2009-CV-190 (Feb 14, 2014). In addition to offering litigants a chance to submit their case to a judge who specializes in commercial litigation, the BCDD also maintains a roster of mediators who have a high degree of expertise and experience resolving commercial disputes, including construction claims.

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Note to Reader: Since 2007, there have been discussions and suggested revisions to the New Jersey Construction Lien Law. In June and November, 2010, the New Jersey Assembly and New Jersey Senate, respectively, unanimously passed revisions to the Construction Lien Law, codified at N.J.S.A. 2A:44A-1 to -38, which had been in need of revision and clarification.¹ The revisions to the Construction Lien Law attempted to clarify ambiguities in the scope and procedure and extended the time frame to file a lien in residential construction cases.

I. MECHANIC'S LIEN IN NEW JERSEY

A. Basics

In New Jersey, mechanics' liens are governed by the Construction Lien Law ("CLL"), N.J.S.A. § 2A:44A-1 to -38, which took effect on April 22, 1994 and replaced the old Mechanics' Lien Law ("MLL"). Under the old regime, as a condition precedent to filing a lien claim, a supplier of labor and/or materials for residential or commercial construction contracts was required to file a mechanic's notice of intention before performing any labor or furnishing any materials.² After satisfying this requirement, an unpaid contractor or supplier had four months from the date the last labor was performed or materials were provided to bring an action to enforce the lien.³ If the unpaid contractor or supplier failed to file the notice of intention, that party was precluded from later filing a lien claim. In addition to being complicated and confusing for contractors and suppliers alike, the old statute engendered distrust and friction between contractors and owners.

The CLL was passed to simplify the lien process, promote contractors' lien rights, and eliminate the tension created between contractors and owners by the prior statutory framework. Under the current statute, "[a]ny contractor, subcontractor or supplier who provides work, services, material or equipment pursuant to a contract, shall be entitled to a lien for the value of the work or services performed, or materials or equipment furnished in accordance with the contract and based upon the contract price." N.J.S.A. § 2A:44A-3. N.J.S.A. § 2A:44A-2 defines a "contract" as "any agreement, or amendment thereto, in writing . . . evidencing the respective responsibilities of the contracting parties . . . [which] in the case of a supplier . . . shall include a delivery or order slip . . . signed by the party against whom the lien claim is asserted."⁴ Thus, a party can file a lien for unpaid monies only pursuant to a written contract.⁵ The CLL bars lien waivers as void against public policy unless the waiver is given "in consideration for payment for the work, services, materials, or equipment" provided. N.J.S.A. § 2A:44A-38. Even then, a waiver is effective only upon and to the extent that the payment is actually received.

B. Lien Statement and Notice

The CLL eliminated the requirement from the MLL that as a condition precedent to filing a lien claim, for a residential or non-residential construction contract, a contractor or supplier had to file a mechanic's notice of intention before performing any labor or furnishing any materials. For non-residential construction contract cases, the CLL requires that a party file a lien claim within 90 days following the date the last work, services or materials were provided for which payment is claimed. N.J.S.A. § 2A:44A-6(a)(2). In residential cases, the maximum time period to file a lien has been extended from 90 days to 120 days. The lien claim must be filed in “substantially” the same form as that shown in N.J.S.A. § 2A:44A-8. Once a lien claim has been filed, the lien claimant must bring an action to enforce the lien in the Superior Court in the county where the property is located within one year of the date of the last work, services, material, or payment for which the lien claim was filed, or within 30 days following receipt of written notice requiring the claimant to begin the action to enforce the lien claim. N.J.S.A. § 2A:44A-14(a). Failure to comply with these requirements results in forfeiture of all rights to enforce the lien. A party seeking to enforce a lien will also forfeit its rights if the lien claim is without basis, is willfully overstated, or is not filed in the form or manner required by the statute. N.J.S.A. § 2A:44A-15(a).

Under N.J.S.A. § 2A:44A-7, within 10 days following the filing of a lien claim, the claimant must serve notice on the owner through a copy of the completed and signed lien claim substantially in the form in N.J.S.A. § 2A:44A-8 by personal service or mail (registered or certified). The lien claimant must serve or mail a copy of the lien claim to the last known business address or place of residence of the owner, community association, or any contractor and/or subcontractor against whom the claim is asserted. Before filing the lien claim for residential construction contracts, the lien claimant must have also complied with the additional requirements of N.J.S.A. §§ 2A:44-20 and -21, discussed below.

A lien claim may be amended for “appropriate” reasons, including but not limited to correcting inaccuracies or errors in the original claim form, revising the amount claimed because of either partial payment of the claim or release of a proportionate share of an interest in real property from the lien, and adjusting for additional work, services, material or equipment provided. N.J.S.A. § 2A:44A-11. However, a lien claim may not be amended to cure a violation of N.J.S.A. § 2A:44A-15, which outlines the improper filing of lien claims and forfeiture of rights.

C. Community Associations

The revisions to the CLL provide that community associations are subject to lien claims and clarify that a construction lien can attach to a community association the same way it can attach to a property owner. N.J.S.A. § 2A:44A-2 defines a community association as “a condominium association, a homeowners' association, a cooperative association, or any other entity created to administer or manage the common elements and facilities of a real property development that, directly or through an authorized agent, enters into a contract for improvement of the real property.”

After reasonable notice, and in a manner directed by the court, an unpaid judgment obtained against a community association may be enforced by assessment against unit owners in the same way liability would be assessed for any other common expense payable by the unit owners. N.J.S.A. § 2A:44A-24.1(h). In ordering assessments, the court should look to the master deed, bylaws or other documents governing the association. The CLL prohibits judgments from being enforced by the sale of any common elements, common areas or common buildings or structures of the property development.

D. Residential Property

The MLL did not differentiate between residential and non-residential (commercial) construction contracts, but the CLL does, and the revisions further clarified the meaning of a residential construction as “construction of or improvement to a dwelling, or any portion thereof, or any residential unit, or any portion thereof.” N.J.S.A. § 2A:44A-2. The revised CLL also clarifies the definition of a “residential construction contract” to include the construction or improvement of units, dwellings, or any other portion of a residential real property development. N.J.S.A. § 2A:44A-2.⁶ Where a residential construction contract is at issue,⁷ the CLL imposes not only the timing, notice, and form of lien statement requirements discussed above but also additional requirements on contractors or suppliers seeking to file a mechanics’ lien.⁸ For residential construction contracts a lien claimant must file and serve a Notice of Unpaid Balance and Right to File Lien (“NUB”) as a condition precedent to the filing of any lien claim. N.J.S.A. §§ 2A:44A-20 and -21. While a lien claimant must always file a NUB when residential property is at issue, a lien claimant may also file a NUB when non-residential property is at issue. The NUB is essentially notice to the owner of the property of a “potential construction lien.”⁹ The NUB must be in substantially the same form as shown in N.J.S.A. § 2A:44A-20, and it must be filed within 60 days from the last day that work or materials were provided. The NUB remains effective for 120 days, but it does not constitute the filing of a lien claim, nor does it extend the time for the filing of a lien claim. N.J.S.A. § 2A:44A-20(f). The lien claimant must also represent and verify certain information, including that the NUB was filed within the 60-day period. N.J.S.A. § 2A:44A-20(b).

The CLL imposes mandatory arbitration on parties to a residential construction contract. N.J.S.A. § 2A:44A-21(b)(3). Unless the parties have otherwise agreed in writing to an alternative dispute resolution mechanism, the lien claimant must serve a demand for arbitration within ten days of service of the NUB, and fulfill all the requirements and procedures of the American Arbitration Association. N.J.S.A. § 2A:44A-21(b)(3). The revised CLL attempts to streamline the arbitration process by providing that, whenever possible, all arbitrations of NUB’s pertaining to the same residential construction shall be determined by the same arbitrator. N.J.S.A. § 2A:44A-21(b)(3). The contractor or supplier must also comply with any additional requirements contained in N.J.S.A. §§ 2A:44A-20 and -21 for the lien to attach and be enforceable.

E. Non-Residential Property

As previously discussed, the CLL eliminated the MLL requirement that as a condition precedent to filing a lien claim, for either a residential or non-residential construction contract, a

contractor or supplier had to file a mechanic's notice of intention before performing any labor or furnishing any materials. Under the CLL, where a non-residential construction contract is at issue, a lien claimant must comply only with the timing, notice, and form of lien statement requirements discussed above or contained elsewhere in the statute.

While a lien claimant must always file a NUB when residential property is the subject of the potential lien claim, a lien claimant may also file a NUB when non-residential property is at issue and the "potential lien claimant desires to seek priority over subsequently filed conveyances, leases, or mortgages affecting the real property to which improvements have been made."¹⁰ N.J.S.A. § 2A:44A-20. The NUB serves as appropriate notice on the record of the lien claimant's desire for priority.¹¹ However, the filing of a NUB does not constitute the filing of a lien claim, nor does it extend the time for the filing of a lien claim. N.J.S.A. § 2A:44A-20(f).

F. Owner's Options

Once a lien claim is filed, the owner basically has four options under the CLL: (1) the owner or the party owing the lien claimant can pay the lien claimant, and the claimant must discharge the lien claim;¹² N.J.S.A §§ 2A:44A-12 and -30 (2) the owner can post a bond equal to 110% of the lien claim as substitute security for the lien property; N.J.S.A. § 2A:44A-31 (3) the owner can serve a demand on the lien claimant to commence a lawsuit within 30 days; N.J.S.A. § 2A:44A-14(a)(2) or (4) the owner can do nothing, and the lien claimant has one year from the date the last work was provided to initiate a lawsuit.¹³ N.J.S.A. § 2A:44A-14(a)(1).

Once the claim has been paid, satisfied or settled by the parties or forfeited by the claimant, the claimant or his successor in interest or attorney must file a certificate with the county clerk directing the clerk to discharge the lien claim of record. N.J.S.A. § 2A:44A-30(a). The certificate must be filed within 30 days of payment, satisfaction or settlement or within 7 days of demand by any interested party. Failure to file this certificate allows any interested party to file an order to show cause with the Superior Court, and a judge may then order the lien claim discharged. N.J.S.A. § 2A:44A-30(b).

G. Prohibited Liens

The CLL prohibits certain liens, as enumerated in N.J.S.A. § 2A:44A-5. In brief, no lien may attach or be filed (1) for materials that are provided subject to a security agreement under N.J.S.A. § 12A:9-101 et seq.; (2) for public works or improvements to real property contracted for and awarded by a public entity (although this provision does not affect any rights or remedies available under the "municipal mechanic's lien law," found at N.J.S.A § 2A:44-125 et seq.); or (3) for work or materials provided pursuant to a residential construction contract, unless there is strict adherence to the requirements of N.J.S.A. §§ 2A:44A-20 and -21.

II. STATUTES OF LIMITATION AND REPOSE

A statute of limitations sets a time limit within which a party can file a lawsuit or claim after that party has discovered injury or deficiency. A statute of repose, on the other hand, sets a time limit within which a party can file a lawsuit or claim following substantial completion of construction or services and operates without regard to the discovery of the injury or deficiency.¹⁴

A. Statutes of Limitations

New Jersey provides that an action for breach of any contract for sale must be commenced within four years after the accrual of the cause of action. N.J.S.A. § 12A:2-725(1). Under this statute, a cause of action accrues when the breach occurs, regardless of the aggrieved party's lack of knowledge of the breach. N.J.S.A. § 12A:2-725(2).

The statute of limitations generally governing breach of contract claims, express or implied, is six years. N.J.S.A. § 2A:14-1. The statute expressly states that its time bar does not apply to any action governed by N.J.S.A. § 12A:2-725, contracts for sale. However, courts have ruled that whether N.J.S.A. § 12A:2-725 applies depends on how the contract between the parties may be accurately characterized: as one involving a transaction of goods plus incidental services, or as one for services plus the incidental sale of goods.¹⁵

The statute of limitations governing personal injury actions is two years from the date the cause of action accrues. N.J.S.A. § 2A:14-2. A cause of action accrues on the date when "the right to institute and maintain a suit" first arises.¹⁶

B. Statutes of Repose

New Jersey's statute of repose, N.J.S.A. § 2A:14-1.1, provides that "[n]o action, whether in contract, in tort, or otherwise, to recover damages for any deficiency in the design, planning, surveying, supervision or construction of an improvement to real property . . . or for an injury to the person, or for bodily injury or wrongful death, arising out of the defective and unsafe condition of an improvement to real property . . . shall be brought against any person performing or furnishing the design, planning, surveying or supervision of construction or construction of such improvement to real property, more than 10 years after the performance or furnishing of such services and construction." N.J.S.A. § 2A:14-1.1(a).

The ten-year limitation does not apply "to actions against any person in actual possession and control as owner, tenant, or otherwise, of the improvement at the time the defective and unsafe condition of such improvement constitutes the proximate cause of the injury or damage for which the action is brought." N.J.S.A. § 2A:14-1.1(a).¹⁷ The statute of repose's limitation period begins to run when there has been "substantial completion," which generally occurs with the issuance of a certificate of occupancy.¹⁸

The statute of repose "impliedly incorporates" the two-year statute of limitations for all personal injury actions found under N.J.S.A. § 2A:14-2, which thus "restrict[s] the period in which actions can be initiated for accidents occurring within ten years after construction."¹⁹ In other words, an injured party must bring a personal injury claim arising out of any deficiency of an improvement to real property within two years of discovering the injury, which in addition, must have been discovered within ten years of substantial completion. Claims for contribution and indemnification must also be brought within the ten year period, commencing from substantial completion. N.J.S.A. § 2A:14-1.1(a).²⁰

The purpose behind the enactment of the statute of repose was to limit the expanding liability of contractors, builders, planners and designers.²¹ The New Jersey Supreme Court has explained that the New Jersey Legislature passed the statute in response to the expanding application of the discovery rule, the abandonment of the completed and accepted rule, and the expansion of strict liability and tort for personal injuries caused by defects in new homes to builders and sellers of those homes.²² Based on that legislative purpose, New Jersey courts tend to read the statute broadly.²³ However, application of the statute of repose is restricted in that only designs that result in unsafe and defective conditions implicate the statute.²⁴

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

In 1978, the New Jersey Legislature enacted The New Home Warranty and Builders' Registration Act [the "Act"], N.J.S.A. §§ 46:3B-1 to -20, creating the Home Warranty Security Fund [the "Fund"] to provide moneys sufficient to pay claims by owners against participating builders for defects in new homes covered by the Act. N.J.S.A. § 46:3B-7(a).²⁵ The Fund receives its moneys from the builders of new homes. If the builder fails to make repairs "within a reasonable time or . . . [if the repairs] are not satisfactory to the owner," the homeowner is then allowed to make a claim against the Fund. N.J.S.A. § 46:3B-7(c).²⁶ Section 46:3B-3(b) sets forth the types of claims covered and the applicable periods of the warranty for each claim: (1) one year for "defects caused by faulty workmanship and defective materials due to noncompliance with the building standards;" (2) two years for "defects caused by faulty installation of plumbing, electrical, heating and cooling delivery systems;" and (3) ten years for "major construction defects," as defined by the Act. N.J.S.A. § 46:3B-3(b)(1), (2) and (3).²⁷

Under the Act and its implementing regulations, all entities engaged in the business of constructing new homes must register with the Department of Community Affairs prior to constructing or advertising as being able to construct new homes. N.J.A.C. § 5:25-2.1.

If a defect falls within the purview of the Act, the builder may choose to repair or replace the defect or pay the owner the reasonable costs of repair or replacement. N.J.A.C. § 5:25-3.3(b). The builder is also responsible for "reasonable shelter expenses" incurred by the homeowner while repairs are ongoing. N.J.A.C. § 5:25-3.3(b).

Prior to making a claim against the Fund for defects covered by the warranty, an owner must first notify the builder in writing of the defects found in the home and must allow the builder a reasonable time to make repairs. N.J.S.A. § 46:3B-7(c). Once the builder receives notice, the builder has 30 days to inspect the defect and provide the owner with a "written statement setting forth the action the builder will take to correct the defect and the time by which the defect will be corrected." N.J.A.C. § 5:25-5.5(a)(5). If the repairs are not made within a reasonable time or are not satisfactory to the owner, the owner may then file a claim against the Fund. N.J.S.A. § 46:3B-7(c). The Act contains procedures governing the dispute resolution process. N.J.A.C. § 5:25-5.5(c)(3).

IV. COVERAGE AND ALLOCATION ISSUES

Generally, under a commercial general liability (CGL) policy, the insurer is required to pay sums that the insured would be liable to pay as damages because of property damage caused by an “occurrence” during the policy period in question.

For liability to attach under a CGL policy, the occurrence must arise during the policy period. Under New Jersey law, to determine the time of the occurrence and thus whether a liability policy has been triggered, the time of the occurrence of an accident “is not the time the wrongful act was committed but the time when the complaining party was actually damaged.”²⁸ As in many other jurisdictions, determinations regarding when a complaining party was actually damaged and thus which indemnity policies are triggered hinge on the specific facts of the case.

New Jersey follows the majority rule that faulty or defective workmanship resulting in only damage to the work product does not qualify as an occurrence under a contractor’s CGL policy.²⁹ This “business risk” exclusion is justified on the grounds that the contractor is in the best position to control the quality of products and workmanship and should thus bear the risk of repairing or replacing construction defects.³⁰ The exclusion to CGL coverage applies only to damage claims arising out of an insured contractor's own faulty workmanship and does not apply to claims for damages caused by the defective work to the property of others or to personal injuries arising out of the faulty workmanship.³¹

If the injury or damage is caused by a single occurrence, then the insurers who issued the policy or policies covering the risk at the time of the occurrence are liable for the losses. Where the occurrence is ongoing (the injury or damage is continuous over a number of policy periods), the “continuous-trigger” theory applies.³² That is, multiple insurance policies are “triggered,” making it necessary to determine to what extent each triggered policy covers the loss. The New Jersey Supreme Court has held that losses are to be allocated among insurers on a pro rata basis in proportion to the degree of risk transferred or retained during the years of exposure.³³ Any model or formula used must reflect both time on the risk and degree of risk assumed, with weight given to certain circumstances including primary and excess coverage and the order in which the policies were triggered.³⁴

V. CONTRACTUAL INDEMNIFICATION

In New Jersey, a promise or agreement in a construction contract purporting to indemnify for “sole negligence” is void and unenforceable. N.J.S.A. § 2A:40A-1. The statute provides that “[a] . . . promise . . . [or] agreement . . . relative to the construction, alteration, repair, maintenance, servicing or security of a building, structure [or] highway . . . purporting to indemnify or hold harmless the promisee against liability for damages arising out of bodily injury . . . caused by or resulting from the sole negligence of the promisee, his agents, or employees, is against public policy and is void and unenforceable; provided that this section shall not affect the validity of any insurance contract, workmen's compensation or agreement issued by an authorized insurer.” In light of this statute, New Jersey courts have held that parties to a construction contract “may no longer agree that the indemnitor shall indemnify the indemnitee for injuries caused by the sole negligence of the indemnitee.”³⁵

A similar statute expressly extends the prohibition against the indemnitee assuming liability for the sole negligence of architects, engineers and surveyors. N.J.S.A § 2A:40A-2. This statute allows an indemnitor to indemnify an engineer, architect or surveyor for its own negligence, but not for injuries resulting solely from that negligence. In other words, under N.J.S.A. § 2A:40A-2, a “hold harmless”³⁶ construction agreement indemnifying an architect or engineer constitutes a per se violation of public policy if it indemnifies the architect or engineer for “damages . . . caused by or resulting from the sole negligence of the [indemnitee] in the giving of or the failure to give directions or instructions.”³⁷

The Assembly Committee Statement accompanying N.J.S.A. § 2A:40A-1 expressly recognizes that it would “effectively allow indemnification clauses where contributory negligence is involved.”³⁸ The law as written, however, does not indicate what degree of contributory negligence by the indemnitee might trigger the invalidation clause. At least one court in New Jersey has said that under this statute, while “a promise to indemnify for sole negligence is unenforceable . . . a promise to indemnify for 99% negligence may be enforced.”³⁹

Where an indemnitor agrees to indemnify for the indemnitee’s own negligence, the promise must be clearly expressed.⁴⁰ This principle also applies to the indemnitee’s defense costs.⁴¹

VI. DAMAGES LIMITATIONS

A. Attorneys’ Fees

In New Jersey, attorneys’ fees are recoverable if made available through statute, court rule, contract, certain third party practice, certain cases involving attorney malpractice, and bad faith by a party during an action.⁴² In addition, the CLL provides that a party may be liable for reasonable legal expenses, including attorneys’ fees, “incurred by the owner, contractor or subcontractor, or any combination . . . in defending or causing the discharge of the lien claim” that is “without basis,” is “willfully overstated,” or “is not lodged for record in substantially the form or in the manner or at a time not in accordance with this act.” N.J.S.A. § 2A:44A-15.

B. Consequential Damages

A party who breaches a contract is liable for the natural and probable consequences resulting from that breach.⁴³ The amount of the damages must have been reasonably within the contemplation of the parties at the time the contract was formed.⁴⁴

C. Delay and Disruption Damages

New Jersey allows “no damage for delay” clauses in construction contracts.⁴⁵ In cases involving “multi-prime construction” contracts, the intent of the parties governs whether to afford a third party a right to sue for delay. If the requisite contractual intent is found, contractors may have valid causes of action against one another for damages caused by the unjustifiable delay of one of the contractors.⁴⁶

D. Economic Loss Doctrine

The “economic loss” doctrine prohibits recovery of damages in tort in cases where a product defect results in an economic loss but does not damage other property or cause any personal injury, i.e. the product defect causes damage only to the product itself.⁴⁷ Regarding construction contracts, New Jersey applies the “predominant factor” test, which states that a construction contract will be treated as a contract for goods or services depending on whether the predominant factor is for services, with goods incidentally involved, or vice versa.⁴⁸

E. Interest

N.J. Court Rule 4:42-11(a) sets the interest rate on judgments at fixed percentages based on the date of entry, “[e]xcept as otherwise ordered by the court or provided by law.” Under this rule, claims collect simple interest at a specified rate from the date of judgment until payment.⁴⁹

According to New Jersey case law, post-judgment interest is “ordinarily not an equitable matter within the court's discretion but is, as a matter of long-standing practice, routinely allowed.”⁵⁰ On the other hand, pre-judgment interest is governed by court rule only in tort actions. N.J. Court Rule 4:42-11(b). In contract actions, litigants do not have a right to pre-judgment interest, and the decision whether or not to award it is within the court’s discretion, guided by equitable considerations and principles, even if the claim is liquidated.⁵¹

Under certain circumstances in contract actions, where the court finds “particular equitable reasons for doing so,” a judgment creditor may be awarded a higher interest rate than the one specified in N.J. Court Rule 4:42-11(a).⁵²

F. Punitive Damages

In breach of contract cases, punitive damages are not available unless the breach of contract also constitutes a tort.⁵³ One other exception in New Jersey arises where a fiduciary relationship exists between the parties.⁵⁴

¹The New Jersey Law Revision Commission was created pursuant to N.J.S.A. 1:12A-1 et seq. The Commission’s statutory mandate is to simplify, clarify and modernize New Jersey statutes by conducting an ongoing review of the statutes to identify areas of the law that require revision. The Commission also considers recommendations from the American Law Institute, the National Conference of Commissioners on Uniform State Laws and other learned bodies as well as members of the legal community and the public. In March, 2007, Commissioner Andrew Bunn of the New Jersey Law Revision Commission (“Commission”) indicated that the Construction Lien Law, codified at N.J.S.A. 2A:44A-1 to -38, was in need of revision and clarification. *New Jersey Law Revision Commission*, retrieved June 30, 2011, from <<http://www.lawrev.state.nj.us/>>.

² See, e.g., *Mansion Supply Co. v. Bapat*, 702 A.2d 509, 510 (N.J. App. Div. 1997) (discussing the requirements of N.J.S.A. § 2A:44-71 (repealed April 22, 1994)).

³ N.J.S.A. § 2A:44-98 (repealed April 22, 1994).

⁴ The contract must be “signed” in accordance with the decision in *Gallo v. Sphere Construction Corp.*, 293 N.J. Super. 558, 564, 566 (Ch. Div. 1996) and *D.D.B. Interior Contr., Inc. v. Trends Urban Renewal Ass’n, Ltd.*, 176 N.J. 164, 167 (2003). See comments by the court in *Legge Industries v. Joseph Kushner Hebrew Academy*, 333

N.J.Super. 537, 559-60 (App. Div. 2000) regarding delivery of separate delivery slips “signed for” by authorized representatives of the parties in the construction chain.

⁵ N.J.S.A. 2A:44A-2 defines “contract” as any agreement, or amendment thereto, in writing, evidencing the respective responsibilities of the contracting parties, which, in the case of a supplier, shall include a delivery or order slip signed by the owner, contractor, or subcontractor having a direct contractual relation with a contractor, or an authorized agent of any of them. *Patock Constr. Co. v. GVK Enters.*, 858 A.2d 1148, 1152 (N.J. App. Div. 2004) (“Under the construction lien law, only a contractor who performs services pursuant to a contract is entitled to file a lien.”).

⁶ This definition is an adoption of the New Jersey Bankruptcy Court’s holding in *Kara Homes v. Central Kitchens*, 374 B.R. 542, 552 (Bankr. D.N.J. 2007).

⁷ The statute defines a residential construction contract as any written contract for the construction or improvement to a one-, two-, or three-family dwelling, or any portion of the dwelling, which shall include any residential unit in a condominium, any residential unit in a housing cooperative, any residential unit contained in a fee simple townhouse development, any residential unit contained in a horizontal property regime, and any residential unit contained in a planned unit development.

⁸ These additional requirements are contained in N.J.S.A. §§ 2A:44A-18, -20 and -21, subject to certain exceptions contained in N.J.S.A. §§ 2A:44A-7 and -8 (as specified by N.J.S.A. § 2A:44A-6).

⁹ *Mansion Supply Co. v. Bapat*, 702 A.2d at 511.

¹⁰ *Id.*

¹¹ *Id.*

¹² Although not expressly provided by statute, the court in *Kvaerner Process, Inc. v. Barham-McBride Joint Venture*, 368 N.J. Super 190, 198-200 (App. Div. 2004), held that a summary proceeding to discharge a construction lien, brought by the general contractor, not the owner, was nonetheless appropriate for those lien claims that were paid, satisfied, settled or forfeited in the event the claimant fails or refuses to file a certificate discharging the lien.

¹³ *Thomas Group v. Wharton Senior Citizen Housing*, 750 A.2d 743, 746 (N.J. 2000).

¹⁴ A statute of repose is a “statute barring any suit that is brought after a specified time since the defendant acted (such as by designing or manufacturing a product), even if this period ends before the plaintiff has suffered a resulting injury.” A statute of limitations is a “law that bars claims after a specified period; a statute establishing a time limit for suing . . . based on the date when the claim accrued (as when the injury occurred or was discovered).” Black’s Law Dictionary, (9th ed. 2009). *Greczyn v. Colgate-Palmolive*, 842 A.2d 895, 898 (N.J. App. Div. 2004), *rev’d on other grounds*, 869 A.2d 866 (N.J. 2005).

¹⁵ *Custom Communications Eng’g v. E.F. Johnson Co.*, 636 A.2d 80, 83 (N.J. App. Div. 1993).

¹⁶ *Russo Farms v. Vineland Board of Educ.*, 675 A.2d 1077, 1083-84 (N.J. 1996).

¹⁷ The New Jersey Supreme Court noted this distinction in *Town of Kearny v. Brandt*, 67 A.3d 601, 611 (N.J. 2013). Other courts in New Jersey found that this phrase “insulate[s] contractors, architects, planners and designers from all claims, whether in tort or contract or by way of contribution or indemnity, by owners, tenants or third persons after ten years . . . [but] preserve[s] . . . the right to make a claim against a person ‘in actual possession or control as owner, tenant or otherwise’ at the time of the injury.” *Salesian Society v. Formigli Corp.*, 295 A.2d 19, 22-24 (N.J. Sup. Ct. Law Div. 1972), *aff’d* by 306 A.2d 466 (N.J. App. Div. 1973); *O’Connor v. Altus*, 303 A.2d 329, 333 (N.J. App. Div. 1973); *Gilliam v. Admiral Corp.*, 268 A.2d 338, 341 (N.J. Sup. Ct. Law Div. 1970).

¹⁸ *Russo Farms, Inc. v. Vineland Board of Educ.*, 675 A.2d at 1093-94.

¹⁹ *O’Connor v. Altus*, 335 A.2d 545, 553 (N.J. 1975).

²⁰ *Salesian Society v. Formigli Corp.*, 306 A.2d 466, 466 (N.J. App. Div. 1973) (rejecting plaintiff’s argument that the statute of repose did not apply to a cause of action based in part on claims breach of warranty and strict liability in tort. “The act by its operative terms provides – ‘no action whether in contract, in tort, or otherwise [. . .] shall be brought [. . .] more than ten years after [. . .] performance [. . .] construction.’” Court was satisfied that this language limited any action to which the statute applied, “regardless of its genesis or label.”

²¹ *Newark Beth Israel Medical Center v. Gruzen*, 590 A.2d 1171, 1173-74 (N.J. 1991).

²² *Id.* (stating that “[t]hose judicial trends created the potential for liability for injuries occurring long after design and construction professionals had completed a project” and the statute was enacted in order to “cut back on the potential of this group to be subject to liability for life.”) (internal citations omitted).

²³ *Id.* at 1174.

²⁴ *Id.*

²⁵ *Aqua Beach Condominium Ass’n v. Dep’t of Cmty. Affairs, Bureau of Homeowner Protection*, 890 A.2d 922, 930 (N.J. 2006).

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- ²⁶ *Id.*
- ²⁷ *Id.*
- ²⁸ *Yarrington v. Camarota*, 351 A.2d 353, 355 (N.J. App. Div. 1971).
- ²⁹ *Firemen's Ins. Co. of Newark v. National Union Fire Ins. Co.*, 904 A.2d 754, 762-63 (N.J. App. Div. 2006) (stating that if the court reached a contrary holding, “the CGL policy would be more like a performance bond, which guarantees the work, rather than like an insurance policy, which is intended to insure against accidents.”).
- ³⁰ *Weedo v. Stone-E-Brick, Inc.*, 405 A.2d 788, 791 (N.J. 1979) (“The insured-contractor can take pains to control the quality of the goods and services supplied. At the same time he undertakes the risk that he may fail in this endeavor and thereby incur contractual liability whether express or implied. The consequence of not performing well is part of every business venture; the replacement or repair of faulty goods and works is a business expense, to be borne by the insured-contractor in order to satisfy customers.”).
- ³¹ *Aetna Cas. & Sur. Co. v. Ply Gem Indus.*, 778 A.2d 1132, 1142-43 (N.J. App. Div. 2001).
- ³² *Id.* At 1145-49 (discussing the continuous trigger theory).
- ³³ *Carter-Wallace, Inc. v. Admiral Insurance Co.*, 712 A.2d 1116, 1124-25 (N.J. 1998); *see also Universal-Rundle Corp. v. Commercial Union Insurance Co.*, 725 A.2d 76, 86-87 (N.J. App. Div. 1999) (stating that the New Jersey Supreme Court has determined that insurers’ liability for losses is pro rata in the continuous trigger context).
- ³⁴ *Universal-Rundle Corp.*, 725 A.2d at 86-87 (discussing *Owens-Illinois, Inc. v. United Insurance Co.*, 650 A.2d 974 (N.J. 1994)).
- ³⁵ *Grippio v. Schrenell & Co.*, 538 A.2d 404, 409 (N.J. App. Div. 1988).
- ³⁶ The phrase “hold harmless” comes from the statutory language providing that a contract is void where such contract allows for a party to “be indemnified or held harmless for damages, claims, losses or expenses.” N.J.S.A. § 2A:40A-2.
- ³⁷ *Cidalina O. Carvalho v. Toll Bros. & Developers*, 675 A.2d 209, 215 (N.J. 1996).
- ³⁸ *Secallus v. Muscarelle*, 586 A.2d 305, 306 (N.J. App. Div. 1991), *aff’d* by 597 A.2d 1083 (N.J. 1991).
- ³⁹ *Secallus v. Muscarelle*, 586 A.2d at 306.
- ⁴⁰ *Ramos v. Browning-Ferris Industries of South Jersey, Inc.*, 510 A.2d 1152, 1159 (N.J. 1986).
- ⁴¹ *Mantilla v. NC Mall Assocs.*, 770 A.2d 1144, 1152 (N.J. 2001) (“[A]bsent explicit contractual language to the contrary, an indemnitee who has defended against allegations of its own independent fault may not recover the costs of its defense from an indemnitor.”).
- ⁴² *Packard-Bamberger & Co., Inc. v. Collier*, 771 A.2d 1194, 1202 (N.J. 2001); *Saffer v. Willoughby*, 670 A.2d 527, 534-35 (N.J. 1996); N.J.S.A. § 2A:15-59.1 (governing frivolous claims and/or defenses brought in bad faith).
- ⁴³ *Pickett v. Lloyd's*, 621 A.2d 445, 454 (N.J. 1993).
- ⁴⁴ *Id.*
- ⁴⁵ *Broadway Maintenance Corp. v. Rutgers State University*, 434 A.2d 1125, 1130 (N.J. App. Div. 1981), *aff’d* by 447 A.2d 906 (N.J. 1982).
- ⁴⁶ *Broadway Maintenance Corp. v. Rutgers State University*, 447 A.2d 906, 909 (N.J. 1982).
- ⁴⁷ *Alloway v. General Marine Indus., L.P.*, 695 A.2d 264, 275 (N.J. 1997) (discussing the economic loss doctrine and stating that “a tort cause of action for economic loss duplicating the one provided by the U.C.C. is superfluous and counterproductive.”).
- ⁴⁸ *Docteroff v. Barra Corp. of America, Inc.*, 659 A.2d 948, 953 (N.J. App. Div. 1995).
- ⁴⁹ *Estate of Kolker*, 515 A.2d 286, 292 (N.J. Sup. Ct. Law Div. 1986).
- ⁵⁰ *Id.* at 291.
- ⁵¹ *Id.* at 292 (discussing *Bak-A-Lum Corp., v. Alcoa Building Prod.*, 351 A.2d 349, 353 (N.J. 1976)).
- ⁵² *R. Jennings Mfg. v. Northern Electric*, 669 A.2d 819, 822 (N.J. App. Div. 1995).
- ⁵³ *See e.g., Ellmex Constr. Co. v. Republic Ins. Co.*, 494 A.2d 339, 345-46 (N.J. App. Div. 1985); *Villa Enters. Mgmt. v. Fed. Ins. Co.* 821 A.2d 1174, 1189 (N.J. Sup. Ct. Law Div. 2002).
- ⁵⁴ *Milcarek v. Nationwide Ins. Co.*, 463 A.2d 950, 952 (N.J. App. Div. 1983).

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I. MECHANIC'S LIEN BASICS

In New Mexico, NMSA 1978, Sections 48-2-1 through 48-2-17 govern mechanics' liens. A mechanic's lien allows every person who performs labor, provides or hauls equipment, tools or machinery or who furnishes materials to be used in the construction of any building or who surveys real property to obtain a security interest in real property.¹

A. **Pre-Lien Notice.** NMSA 1978, Section 48-2-2.1 governs pre-lien notice. A claimant for a lien of more than \$5,000 must give notice of his right to claim a lien for nonpayment.² This notice must be given to the owner or the original contractor not more than sixty (60) days after initially furnishing work or materials. The notice must contain a description of the property; the name, address and phone number of the claimant; and the name and address of the person with whom the claimant contracted or to whom the claimant furnished labor or materials.³ This notice requirement does not apply to claims of liens made on residential property of four (4) or less units or to claims of liens made by mechanics or materialmen who contract directly with the original contractor.⁴

B. **Lien Perfection.** To perfect a lien, every claimant must:

1. Record the lien in the county clerk of the county in which the property is located. The statement must contain all of the information required by the statute, and it must be verified.⁵

2. If a general contractor is recording the lien, it must be recorded within one hundred and twenty (120) days after the completion of the contract.⁶ If a subcontractor is recording the lien, it must be recorded within ninety (90) days after the completion of the project or repair.⁷

3. To perfect a lien on a residential construction project, the lien holder must file his lien before the closing of the residential construction project.⁸ If the lien is filed after closing, the lien holder's lien is invalid, unless the owner is not an innocent actor.

C. **Lien Enforcement.** According to NMSA 1978, Section 48-2-10, no lien provided for in Sections 48-2-1 through 48-2-17 remains valid for more than two (2) years. An

enforcement action must be filed within two (2) years after the lien is recorded. If proceedings are not commenced within two (2) years, the mechanic's lien becomes unenforceable. Any person holding a mechanics lien on any real estate may subject that real estate to foreclosure action.⁹

D. **Sale.** According to NMSA 1978, Section 39-4-1, a sheriff's sale of the property may be initiated following successful enforcement of the lien. Proceeds from the sale are used to pay off interest holders in the property based upon their priority. A mechanic's lien-holder assumes priority when the lien-holder commences to improve any building or structure, or when the lien-holder first provides materials.¹⁰ For purposes of determining the priority of liens, a lien recorded after work has begun on a construction project relates back to the date when the lien filer first started working on the construction project.¹¹

II. STATUTES OF LIMITATION AND REPOSE

A. **Statute of Limitations.** New Mexico does not have a statute of limitation applicable to defective or unsafe conditions of improved real property. However, the following general statute of limitations may apply to certain construction contracts:

1. A claim based on a written contract must be filed within six (6) years.¹²
2. A claim based on a verbal contract must be filed within four (4) years.¹³
3. A personal injury claim must be brought within three (3) years.¹⁴ The limitation period begins to run from the time the injury manifests itself in a physically objective manner and is ascertainable.¹⁵ In other words, the statute of limitation period begins to run when the person knew or should have known of the injury.

B. **Statute of Repose.**

1. NMSA 1978, Section 37-1-27 contains a statute of repose, which is applicable to construction claims. The statute states that no action to recover damages for any injury to property or person arising out of the defective or unsafe condition of a physical improvement to real property against a person involved with the construction or improvement of that property shall be brought against that person after ten (10) years from the date of substantial completion of the construction or improvement project.¹⁶ This limitation does not apply to contract or warranty actions that contain express provisions to the contrary.

The word "improvement," as used in the context of NMSA 1978, Section 37-1-27, means the enhancement or augmentation of value or quality: a permanent addition to or betterment of real property that enhances its capital value and that involves the expenditure of labor or money and is designed to make the property more useful or valuable as distinguished from ordinary repairs.¹⁷

NMSA 1978, Section 37-1-27 does not eliminate the duty to exercise reasonable care in the design, construction, planning, or inspection of an improvement in the first place; it

merely forecloses suit for redress after ten years have passed since the substantial completion of an improvement.¹⁸

2. Contribution and indemnification claims arising out of defective or unsafe conditions of improvements cannot be brought after ten (10) years from the date of substantial completion of the construction or improvement project.¹⁹

It is important to note that although a claimant has ten (10) years to bring a claim arising out of a construction project's defective or unsafe conditions under the applicable statute of repose, the claimant's claim may nevertheless be time barred. Because New Mexico does not have a statute of limitation applicable to construction claims arising out of defective or unsafe conditions, the above general statute of limitations apply. As such, a claimant's claim may be time barred even if the claimant brings the claim within the applicable ten-year statute of repose. For example, a claimant injured by a new construction project's defective or unsafe condition has three years to file his personal injury claim. If the claimant files his claim five years after substantial completion of the construction project, the claimant's claim will be barred by the personal injury statute of limitation period even though the claim was filed within the applicable statute or repose time period.

On the other hand, the statute of repose can operate to bar a claimant's claim even though it was brought within the applicable statute of limitations period. For example, the personal injury statute of limitation period does not begin to run until the injured person knows or should know of his injury. If a claimant is injured eight years after substantial completion of a construction project, but the claimant does not know or have reason to know of his injury until year eleven, his claim would be untimely under the applicable statute of repose even though the claim was filed within the applicable statute of limitations period.

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

Currently, New Mexico does not have statutes or cases dealing with this section.

IV. COVERAGE AND ALLOCATION ISSUES

According to New Mexico's Uniform Jury Instruction 13-1703, a liability insurance company has a duty to defend its insured against all claims, which fall within the coverage of the insurance policy. A liability insurance company must act reasonably under the circumstances to conduct a timely investigation and fair evaluation of its duty to defend.

No New Mexico case has decided what trigger of coverage theory should apply under any particular fact pattern in New Mexico. The question of what event triggers coverage under an insurance policy or policies has been a matter of debate in various other jurisdictions.

The first common trigger theory used is the first contact trigger. Under this theory, the date on which the injury-producing event first occurs triggers coverage.²⁰

The second common trigger theory used is the manifestation trigger. Under this theory, the insurer insuring the property at the time the damage first manifests itself is solely responsible for the indemnification of the insured. This theory is mainly used in the context of first party property claims.²¹

The third common trigger theory is the “injury-in-fact” trigger. Under this theory, coverage is first triggered at that point in time where an actual injury can be shown to have been first suffered. This trigger is frequently used in property damage third-party liability cases, but difficulty arises when the court is faced with a continuous, deteriorating type of property damage.²²

New Mexico has not yet decided which insurance trigger theory applies to construction law claims. However, New Mexico is likely to adopt the majority view adopted in *Montrose v. Admiral Ins. Co.*, 913 P.2d 878 (Cal. 1995). In *Montrose*, the California Supreme Court developed or popularized the continuous trigger-of-coverage theory for use in continuous or progressively deteriorating property damage cases.²³ Under this theory, bodily injuries and property damage that are continuous or progressively deteriorating throughout successive policy periods are covered by all policies in effect during those periods.²⁴

V. CONTRACTUAL INDEMNIFICATION

Generally, New Mexico does not allow indemnification in construction contracts.²⁵ Construction contracts are defined by the statute as a “public, private, foreign or domestic contract or agreement relating to construction, alteration, repair or maintenance of any real property in New Mexico.”²⁶ This includes agreements for architectural services, demolition, design services, development, engineering services, excavation or other improvement to real property, including buildings, shafts, wells and structures.²⁷ Where a contract is so generic that one cannot tell what type of work will be performed, New Mexico courts will look past the contract to the nature of the work being performed at the time of accident to determine whether the anti-indemnity statute will apply.²⁸

NMSA 1978, Section 56-7-1(A) holds that provisions requiring indemnification for the indemnitee’s negligence to be void and unenforceable.²⁹ The New Mexico Court of Appeals has held that this section refers only to the particular provision within the indemnity clause, and not to the entire indemnity clause.³⁰ This holding is based on 2003 and 2005 amendments to the statute creating two exceptions to the general rule provided by section A. First, indemnity provisions that require indemnification against the indemnitor’s negligence are enforceable.³¹ Second, an indemnity provision is valid where there is a specific agreement to insure against the risk of a construction project.³² To hold an entire indemnity clause void under NMSA 1978, Section 56-7-1 (A) would negate the purpose of sections B(1) and (2) of the statute, allowing for these two exceptions.³³ Additionally, a contract indemnification clause is not invalid against public policy simply because it fails to expressly exclude indemnification prohibited under Section 56-7-1.³⁴

VI. CONTINGENT PAYMENT AGREEMENTS

New Mexico has yet to determine the enforceability of contingent payment agreements within construction contracts. The Tenth Circuit,³⁵ interpreting New Mexico's Retainage Act,³⁶ held that the New Mexico Supreme Court would – if presented with a contingent payment agreement – likely enforce a contingent payment agreement. New Mexico's Retainage Act requires all construction contracts to “provide that contractors and subcontractors make prompt payment to their subcontractors and suppliers for amounts owed for work performed . . . within seven days after receipt of payment from the owner, contractor or subcontractor.”³⁷ In accordance with the Retainage Act, retainage may be held until substantial completion of the applicable work only “if the escrow arrangement described in [NMSA 1978,] Section 57-28-6 of the Retainage Act is used.”³⁸

VII. DAMAGE LIMITATIONS

A. Attorneys' Fees.

New Mexico allows recovery of attorney fees in three situations. First, attorney fees may be awarded based on contract.³⁹ Second, attorney fees may be awarded based on bad faith or frivolous litigation.⁴⁰ Finally, attorney fees may be recovered where allowed by statute.⁴¹

B. Consequential Damages.

Generally, breaches of contract recoveries are limited to general or consequential damages.⁴² General damages are damages that arise naturally and necessarily as a result of the contractual breach.⁴³ General damages are based on the concept that the plaintiff should be awarded the value of the very thing promised so that his balance sheet will reflect capital assets he would have had upon the defendant's full performance.⁴⁴ Specifically, New Mexico has held that where a contract creates an at-will business relationship, future profits are not within the contemplation of the parties, and therefore not recoverable on a breach of contract claim.⁴⁵

In a contract action, a defendant is liable only for those consequential damages that were objectively foreseeable as a probable result of his or her breach when the contract was made.⁴⁶ Additionally, New Mexico allows recovery for emotional distress as long as the distress is causally connected to the underlying breach of contract.⁴⁷

C. Delay and Disruption Damages.

Delay and disruption damages are available in New Mexico.⁴⁸ Additionally, incidental damages resulting from a seller's breach include expenses reasonably incurred in inspection, receipt, transportation and care and custody of goods rightfully rejected, any commercially reasonable charges, expenses or commissions in connection with effecting cover and any other reasonable expense incident to the delay or other breach.⁴⁹

D. Economic Loss Doctrine.

New Mexico follows the economic loss doctrine.⁵⁰ The purpose of the economic loss doctrine is to preserve the contract principle that contract damages should be limited to those within the contemplation and control of the parties.

E. Interest.

Interest is allowed on judgments from the time of entry and shall be calculated at the rate of eight and three-fourths percent per year.⁵¹ When judgment is rendered on a written instrument having a different rate of interest, interest must be computed at a rate no higher than the percentage rate specified in the instrument.⁵² But, when the judgment is based on tortious conduct, bad faith or intentional or willful acts, interest is computed at the rate of fifteen percent.⁵³

F. Punitive Damages.

Although no New Mexico construction law case has decided this issue, New Mexico allows recovery of punitive damages in other contract actions. As such, it is likely New Mexico would allow recovery of punitive damages in construction contract claims. But, punitive damages may be recovered under a breach of contract action only when the wrongful conduct was willful, wanton, or malicious.⁵⁴

VIII. NEW DEVELOPMENTS

New Mexico requires contractors to be licensed.⁵⁵ In 2008, the New Mexico Court of Appeals held that New Mexico's Construction Industries Licensing Act ("CILA") does not prohibit a licensed general contractor from suing a homeowner for payment on a construction contract where the general contractor employed an unlicensed individual or crew to perform work under said construction contract.⁵⁶ However, in 2010 the New Mexico Supreme Court overturned this ruling, holding that CILA precludes a licensed contractor from bringing or maintaining an action to collect compensation for work performed by an unlicensed contractor.⁵⁷

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- ¹ NMSA 1978, § 48-2-2.
- ² NMSA 1978, § 48-2-2.1(B).
- ³ NMSA 1978, § 48-2-2.1(D).
- ⁴ NMSA 1978, § 48-2-2 (A).
- ⁵ NMSA 1978, § 48-2-6.
- ⁶ *Id.*
- ⁷ *Id.*
- ⁸ NMSA 1978, § 48-2A-11; NMSA 1978, § 48-2A-12.
- ⁹ NMSA 1978, § 39-4-13.
- ¹⁰ NMSA 1978, § 48-2-5.
- ¹¹ *Valley Fed. Sav. & Loan Ass'n v. T-Bird Home Centers, Inc.*, 741 P.2d 826 (N.M.1987).
- ¹² NMSA 1978, § 37-1-3(A).
- ¹³ NMSA 1978, § 37-1-4.
- ¹⁴ NMSA 1978, § 37-1-8.
- ¹⁵ *Pacheco v. Cohen*, 2009-NMCA-070, ¶ 8 146 N.M. 643, 213 P.3d 793.
- ¹⁶ *Id.*
- ¹⁷ *Mora-San Miguel Elec. Coop. v. Hicks & Ragland Consulting & Eng'r Co.*, 1979-NMCA-082, 93 N.M. 175, 598 P.2d 218.
- ¹⁸ *Coleman v. United Eng'rs & Constructors, Inc.*, 1994-NMSC-074, 118 N.M. 47, 878 P.2d 996.
- ¹⁹ NMSA 1978, § 37-1-27.
- ²⁰ *Montrose v. Admiral Ins. Co.*, 913 P.2d 878, 893 (Cal. 1995).
- ²¹ *Id.*
- ²² *Id.* at 894.
- ²³ *Id.* at 881.
- ²⁴ *Id.* at 893.
- ²⁵ NMSA 1978, § 56-7-1(A).
- ²⁶ NMSA 1978, § 56-7-1(E).
- ²⁷ *Id.*
- ²⁸ *Holguin v. Fulco Oil Services LLC*, 2010-NMCA-091, ¶ 16, 149 N.M. 98, 245 P.3d 42.
- ²⁹ NMSA 1978 § 56-7-1(A).
- ³⁰ *Holguin*, 2010-NMCA-091, ¶ 38.
- ³¹ NMSA 1978, § 56-7-1(B)(1).
- ³² NMSA 1978, § 56-7-1(B)(2).
- ³³ *Holguin*, 2010-NMCA-091, ¶ 38.
- ³⁴ *J.R. Hale Contracting Co., Inc., v. Union Pacific Railroad*, 2008-NMCA-037, ¶ 63, 143 N.M. 574, 179 P.3d 579.
- ³⁵ *MidAmerica Constr. Mgt., Inc. v. MasTec N. Am., Inc.*, 436 F.3d 1257, 1265 (10th Cir. 2006).
- ³⁶ NMSA 1978, § 57-28-5(A), (C) (“[A]ll construction contracts shall provide that payment for amounts due, except for retainage, shall be paid within twenty-one days after the owner receives an undisputed request for payment . . . All construction contracts shall provide that contractors and subcontractors make prompt payment to their subcontractors and suppliers for amounts owed for work performed on the construction project within seven days after receipt of payment from the owner, contractor or subcontractor . . . These payment provisions apply to all tiers of contractors subcontractors, and suppliers.”).
- ³⁷ *Id.*
- ³⁸ *Id.* (“[T]he form and provisions of the escrow arrangement shall be included in all solicitations for construction services and shall be given to the contractor and subcontractors prior to entering into a contract.”).
- ³⁹ *Aspen Landscaping Inc. v. Longford Homes of New Mexico, Inc.*, 2004-NMCA-063, ¶ 21, 135 N.M. 607, 92 P.3d 53; *see also Fort Knox Self Storage, Inc. v. Western Technologies, Inc.*, 2006-NMCA-096, ¶ 29, 140 N.M. 233, 142 P.3d 1.
- ⁴⁰ *Siepert v. Johnson*, 2003-NMCA-119, 134 N.M. 394, 77 P.3d 298.
- ⁴¹ NMSA 1978, § 39-2-2.1.
- ⁴² *Shaeffer v. Kelton*, 1980-NMSC-117, 95 N.M. 182, 619 P.2d 1226.

⁴³ *Camino Real Mobile Home Park Partnership v. Wolfe*, 1995-NMSC-013, ¶ 20, 119 N.M. 436, 891 P.2d 1190, overruled on other grounds by, *Sunnyland Farms, Inc. v. C. New Mexico Elec. Co-op., Inc.*, 2013-NMSC-017, 301 P.3d 387.

⁴⁴ *Id.*

⁴⁵ *Guest v. Allstate Ins. Co.*, 2010-NMSC-047, ¶ 54, 149 N.M. 74, 244 P.3d 342; *see also Santa Fe Custom Shutters & Doors, Inc. v. Home Depot U.S.A., Inc.*, 2005-NMCA-051, ¶ 43, 137, N.M. 524, 113 P.3d 347.

⁴⁶ *Sunnyland Farms, Inc. v. C. New Mexico Elec. Co-op., Inc.*, 2013-NMSC-017, ¶ 16, 301 P.3d 387.

⁴⁷ *Ettenson v. Burke*, 2001-NMCA-003, 130 N.M. 67, 17 P.3d 440.

⁴⁸ *Burt v. Horn*, 1982-NMCA-037, ¶ 20, 97 N.M. 515, 641 P.2d 546 (holding that the evidence sustained trial court's finding as to damages sustained by owner as result of delay and defects in construction of residence.).

⁴⁹ NMSA 1978, § 55-2-715.

⁵⁰ *In re Consolidated Vista Hills Retaining Wall Litigation*, 1995-NMSC-020, ¶ 26, 119 N.M. 542, 893 P.2d 438.

⁵¹ NMSA 1978, § 56-8-4(A).

⁵² *Id.*

⁵³ *Id.*

⁵⁴ *Ettenson v. Burke*, 2001-NMCA-003, ¶ 31, 130 N.M. 67, 17 P.3d 440.

⁵⁵ NMSA 1978, § 60-13-1 et. seq.

⁵⁶ *Reule Sun Corp. v. Valles*, 2008-NMCA-115, 114 N.M. 736, 191 P.3d 1197, overruled by *Reule Sun Corp. v. Valles*, 2010-NMSC-004, 147 N.M. 512, 226 P.3d 611.

⁵⁷ *Reule Sun Corp. v. Valles*, 2010-NMSC-004, 147 N.M. 512, 226 P.3d 611.

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I. MECHANIC'S LIEN BASICS

New York's Lien Law provides for the assertion of mechanic's liens when contractors, materialmen and certain other entities improve real property, whether such property is privately or publicly owned. A mechanic's lien for private improvements attaches to the property, whereas a lien for public improvements attaches against the state or municipal fund. *See* Lien Law §§12 & 42.¹

The basic steps to perfect a mechanic's lien and recover a debt for labor or materials rendered are discussed below.

A. Lien Notice

For private improvements in the context of commercial construction (*i.e.*, other than single family dwellings as defined by Lien Law §10), a lienor must serve a Notice of Lien upon the owner and the contractor by whom the lienor was engaged either five (5) days before filing the Notice with the county clerk in which the property is located or within thirty (30) days following such filing. Lien Law §§11 & 11-b. The lienor may file the Notice of Lien any time during the progress of the work, but no later than eight (8) months after completing the contract or rendering the last item of service or materials. Lien Law §10². After filing the Notice, the lienor has thirty-five (35) days to file proof that it served the Notice upon the owner and contractor; otherwise, the lien terminates. *Id.*

For liens arising out of public improvements, the lienor must file the Notice of Lien with (1) the bureau in charge of the construction and (2) the public entity's comptroller or financial officer during the progress of the work, but no later than thirty (30) days after acceptance of the performance. Lien Law §12. Additionally, the lienor must serve a copy of the Notice of Lien upon the contractor who engaged its services either five (5) days before or simultaneously with filing the Notice of Lien. Lien Law §§11 & 11-c.

B. Contents of the Notice

Whether arising out of improvements to private or public property, the Notice of Lien must identify the following:

- (1) the lienor;
- (2) the owner and its interest in the property;

- (3) the lienor's employer or the person/entity with whom the lienor contracted to provide improvements to the property;
- (4) the nature of the improvements provided and the agreed upon value of same;
- (5) the monetary amount owed to the lienor;
- (6) when the first and last component of the services or materials were provided;
- (7) a description of the subject property; and
- (8) a verification by the lienor or its agent that the information in the Notice of Lien is true to his/her knowledge or upon information and belief.

Lien Law §9.

C. Foreclosure

A lienor must foreclose upon the mechanic's lien within one (1) year from the filing of the Notice of Lien unless the lienor takes statutorily-proscribed measures to extend the lien. Lien Law §§17 and 18. Options available to the lienor include commencement of a foreclosure action and filing of a *lis pendens* with the clerk of the county where the property is located (for private improvements) or with the relevant governmental agency (for public improvements). Lien Law §9. The lienor may also file for an extension with the county clerk or relevant governmental agency, in which case, if the lienor does not file an action within the extended period, a court may order an additional extension.³

D. Sale

A mechanic's lien against private property may be enforced against the property and/or the person liable for the debt, whereas mechanic's liens for public improvements are enforceable only against a liable contractor and/or governmental funds. Lien Law §§ 41, 42 and 60. To enforce a lien against private property, the court may direct the sale of the property and distribution of the proceeds and may appoint a referee to effect such sale.⁴

II. STATUTES OF LIMITATION AND REPOSE

A. Statutes of Limitation and Limitations on Application of Statutes

Under New York's Civil Practice Law and Rules ("CPLR") §214, actions to recover damages for an injury to person or property must be commenced within three (3) years, whereas action upon a contractual obligation or liability, express or implied, to be commenced within six (6) years pursuant to §213. A contractor's claim accrues when its damages are ascertainable, which is generally the time at which the work is substantially completed or a detailed invoice of the work performed is submitted.⁵

In New York, statutes of limitation are generally considered procedural law because they are viewed as pertaining to the remedy, rather than the right.⁶ The expiration of the time period proscribed in a statute of limitation does not extinguish the underlying right; rather, it bars the remedy⁷ and serves as an affirmative defense.⁸

B. Statutes of Repose and Limitations on Application of Statutes

New York does not have a formal statute of repose. However, §202 of the CPLR sets forth New York's borrowing statute and may require a New York court to apply another state's statute of repose. Regardless of whether the relevant sister state holds that its statute of repose is procedural law, New York courts deem statutes of repose to be substantive law and will therefore borrow them if New York's choice of law jurisprudence requires it.⁹ In practice, when a New York court applies a statute of repose, the plaintiff is barred from asserting a cause of action, as opposed to being time-barred from recovery by a statute of limitations.¹⁰

A *de facto* statute of repose may exist in the form of conditions precedent to suit in cases against certain governmental entities that enjoy common law sovereign immunity. Where the sovereign waives its immunity on condition that a claimant commence its lawsuit within a specific time period, tolls which would ordinarily be applicable to a statute of limitations may not extend the time period.¹¹ However, because the State of New York waived its sovereign immunity in 1929 (including a concomitant waiver of immunity for its subdivisions, as well as its counties, cities, towns and villages),¹² notice requirements contained in claims against municipalities are generally not considered conditions precedent.¹³ As such, failure to comply timely with such requirements will not prevent the accrual of the action as would a statute of repose.

The general rule is that, when a statute creates a cause of action and attaches a time limit to its commencement, the time limit is an element of the cause of action. The time limit thereby functions as a statute of repose. If the cause was cognizable at common law or by another statute, a statutory time constraint is commonly taken as a statute of limitations and must be asserted as an affirmative defense or is otherwise waived.¹⁴ Statutes of limitations may enjoy the tolling provisions such as CPLR §205, while time limitations that are in the nature of conditions precedent to suit do not benefit from such tolls.¹⁵

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

New York's General Business Law §§777-a and 777-b attaches implied warranties to a merchant's sale of a new home unless the merchant and buyer adopt measures specified in the statute to waive them.¹⁶ An implied warranty begins to run on the date title passes to the first person who purchases the home for residential occupancy, or on the date residential occupancy actually occurs, whichever occurs first. *Id.* The following warranties are implied unless waived:

- One (1) year from and after the warranty date: The home will be free from defects due to a failure to have been "constructed in a skillful manner", defined as workmanship and materials meeting applicable building code standards or, in the absence of such standards, local accepted building practices;
- Two (2) years from and after the warranty date: The plumbing, electrical, heating, cooling and ventilation systems of the home will be free from defects due to a failure by the builder to have installed such systems in a skillful manner; and
- Six (6) years from and after the warranty date: The home will be free from material defects, defined as physical damage to certain load bearing systems

(*e.g.*, foundation systems and footings, beams, girders, *etc.*)

As a condition precedent to commencing an action for breach of implied warranty, the owner must notify the seller in writing of the warranty violation no later than thirty (30) days following the expiration of the relevant warranty period and thereafter shall afford the seller reasonable time to cure it. Gen. Bus. Law §777-a. After satisfying the conditions precedent, the owner must file the action no later than one (1) year following the expiration of the relevant warranty or within four (4) years after the warranty date, whichever of the two is longer. *Id.* In the context of new home sales, the statutory warranties supplant earlier common-law implied warranties.¹⁷

New York's General Business Law §§770-776 governs contracts for home improvements. Statutory warranties and conditions precedent to filing an action do not apply to contracts for home improvements or new homes built upon land that the contractee already owns,¹⁸ nor does a common-law merchant's implied warranty attach to such contracts.¹⁹ An owner has six (6) years to sue for breach of contract predicated upon contractual warranty violations, which period begins to run upon completion of the actual physical work.²⁰

IV. COVERAGE AND ALLOCATION ISSUES

A. Trigger of Coverage

The New York Court of Appeals adopted an "injury-in-fact" test, identified as "onset of disease, whether discovered or not".²¹ Under this test, an insurance policy is triggered when there is a covered "occurrence" which gives rise to an actual injury during the policy period.²² Therefore, a real but undiscovered injury proved to have existed at the relevant time may establish coverage irrespective of the time the injury became diagnosable.²³

New York courts have repeatedly held that the burden to prove coverage rests on the insured, while the burden to prove an exclusion to the policy rests with the insurer²⁴. To negate coverage by virtue of an exclusion, an insurer must establish that the exclusion is stated in clear and unmistakable language, is subject to no other reasonable interpretation and applies in a particular case. However, the burden to prove an exception to an exclusion rests once again with the insured. Exclusions are narrowly construed and ambiguities in the contract, including exclusions, are construed against the insurer.²⁵

B. Additional Insured Coverage

Additional insured endorsements vary widely as to the scope of the additional insured coverage provided. An endorsement tied to liability "arising out of" the named insured's work or operations is not limited to the vicarious liability of the additional insured, but also covers the additional insured's own negligence.²⁶ A claim by an employee injured on the jobsite, even if not actually working at the time of the accident, is also deemed to have "arisen out of the work".²⁷ However, where the injured party is not an employee of the named insured or its subcontractors, there must be some causal connection between the accident and the named insured's work for coverage to be triggered.²⁸

Other additional insured endorsements are tied to liability “arising out of [the named insured’s] ongoing operations”. Essentially, this type of endorsement depends on whether or not the named insured’s work had been completed prior to the time of the accident.²⁹ Evolving law appears to trend toward use of more restrictive additional insured endorsements which depend on a showing of the named insured’s negligent acts or omissions or exclude the additional insured’s own negligence. Other examples of restrictive additional insured endorsements include limitations for coverage as follows:

- (a) to liability “caused, in whole or in part, by [the named insured’s] acts or omissions”;
- (b) to the extent that the additional insured is held liable for [the named insured’s acts or omissions];
- (c) liability caused by the named insured’s negligent acts or omissions;
- (d) “only with respect to acts or omissions of the Named Insured”;
- (e) only for claims “determined to be solely the negligence or responsibility of [the named insured]; or
- (f) claims “arising solely out of your negligence.:

In addition, there are additional insured endorsements which exclude coverage for “the independent acts or omissions of such additional insured” or the additional insured’s sole negligence.

When an additional insured endorsement references the negligence of the additional or named insured, the insurer’s duty to indemnify the additional insured is immature and usually cannot be determined at the outset of the litigation.³⁰ The difficulty with these restrictive additional insured endorsements is that a defense must be provided by the carrier even when the indemnity obligations for additional insureds might not be resolved until a resolution of the underlying personal injury action.

C. Late Notice

The duty of an insured to promptly advise the insurer of a claim is well established in New York law. Effective January 19, 2009, New York became a state which required a showing of prejudice by the insurer asserting that it was provided with “late notice” of a claim in order for a denial of coverage to be upheld. Insurance Law §342.09(a)(5).

Despite this, an insurer’s knowledge of an occurrence from sources other than the insured is insufficient to establish notice, since the policy’s condition precedent to coverage requires notice of occurrence *by the insured*.³¹ Similarly, each insured has an independent and separate obligation to provide timely notice of the occurrence/claim and suit to the insurer, and thus, notice from one insured is insufficient to constitute notice by another insured. Obviously, however, receipt of notice from other sources makes a claim of “prejudice” by the insurer harder to substantiate.

Excess policies often contain notice provisions which are different from that of the primary policy. Generally speaking, an insured has a duty to notify an excess insurer when the

circumstances known to the insured, based on an objective test, suggest a “reasonable possibility of a claim that would trigger the excess insurer’s coverage”. Some guidance has been provided by the courts as cases have risen through litigation.³²

D. Timely Disclaimers

Where the policy is issued in New York and there is *bodily injury* or *death* caused by an accident, New York law imposes strict rules governing timely disclaimers by an insurance carrier. As a result, there has been significant litigation involving disclaimers. Insurance Law §3420 (d) requires that a disclaimer be issued “as soon as is reasonably possible” not only to the insured, but also to the injured person “or any other claimant.”³³

Failure to issue a disclaimer “as soon as reasonably possible” estops the insurer from denying or disclaiming coverage based upon the insured’s breach of condition precedent, as well as otherwise applicable policy exclusions.³⁴

Although circumstances will vary and an *ad hoc* evaluation will be made, disclaimers are generally considered untimely if issued more than two (2) months after the insurer becomes aware of facts upon which a disclaimer could be made.³⁵ However, a safer practice to follow is to issue the disclaimer no later than thirty (30) days after the insurer becomes aware of sufficient facts, since there is some caselaw holding that even disclaimers issued less than sixty (60) days could be untimely based upon the particular circumstances.

In situations involving property damage, the urgency of prompt disclaimer does not apply and an insured must demonstrate actual prejudice resulting from the insurer’s delay in disclaiming³⁶, which is a difficult burden for the would-be insured to carry.³⁷ The better practice is, of course, to provide notice as promptly as possible, regardless of the type of claim involved.

E. Duty to Defend

New York’s mantra “The duty to defend is broader than the duty to indemnify” reverberates throughout the body of coverage caselaw.³⁸ Thus, wherever a claim is raised where the potential for coverage exists—even where the claims are false or groundless—the duty to defend is triggered.³⁹ Thus, an insurer will be obligated to provide a defense as long as the allegations in the underlying complaint suggest a reasonable possibility of coverage.⁴⁰ In fact, an insurer can only avoid its defense obligation where it can demonstrate as a matter of law that there is *no possible* factual or legal basis on which it will be obligated to indemnify the insured (obviously, a very high bar).⁴¹

F. Allocation Among Insurers

New York has rejected a joint and several approach to allocation and has adopted a *pro rata* allocation approach.⁴² Under this methodology, liability for injury or damages is allocated among tortfeasors and, accordingly, among the triggered insurance policies (priority, of course, being governed by the policies’ “other insurance clauses”).

V. CONTRACTUAL INDEMNIFICATION

Under New York's Workers' Compensation Law §11, common law contribution or indemnity cannot be obtained from the injured worker's employer unless it is demonstrated that the injured worker sustained a "grave injury" as defined by statute. "Grave injury" is limited to:

- death
- permanent and total loss of use or amputation of an arm, leg, hand or foot
- loss of multiple fingers
- loss of multiple toes
- paraplegia or quadriplegia
- total and permanent blindness
- total and permanent deafness
- loss of nose
- loss of ear
- permanent and severe facial disfigurement
- loss of an index finger or
- an acquired injury to the brain caused by an external physical force resulting in permanent total disability.

Workers Compensation Law §11. Provided that the written agreement complies with New York's General Obligations Law §5-322.1 (which precludes owners and general contractors from exempting themselves from liability by contractually requiring another party to indemnify them for their own negligence by declaring such contracts to be "void and unenforceable"), contribution or indemnification for damages arising out of bodily injury to persons or damage to property caused by or resulting from the negligence of a party *other than the promisee*, whether the promisor is partially negligent or not, may be obtained if explicitly agreed to in writing. Gen. Obl. Law §5-322.1. In other words, owners and general contractors can contractually require subcontractors to indemnify them for the negligence of third-parties, just not for the owners' and general contractors' own negligence.

Courts have been presented with and have enforced "partial indemnity" provisions between contractors.⁴³ "Partial indemnity" provisions incorporate savings language whereby a subcontractor agrees to indemnify the owner and/or general contractor "to the fullest extent permitted by applicable law" and excludes from the subcontractor's responsibility liability created by the general contractor and/or owner's exclusive negligence.⁴⁴ Unlike a "full indemnity" agreement, a "partial indemnity" agreement entitles owners and general contractors only to indemnification commensurate with the subcontractor's apportioned liability.

The significance of this application is that it now permits an end run by an owner or general contractor around Workers Compensation Law bar by permitting imposition of liability on an employer for "contractual" contribution even where there is no "grave injury". It also exposes the employer's general liability carrier to contractual contribution claims in the absence

of “grave injury”, even though contribution exposure historically has already been paid under the employer’s liability coverage in the form of compensation benefits.

Any ambiguity about the propriety of such contract-allocated liability was put to rest by the Court of Appeals in 2008, when it ruled that an indemnification provision drafted in such a way so as to seek less than full indemnity can permit an owner or general contractor to secure “partial indemnity” or “contractual contribution” from the employer even where the owner or general contractor is partially negligent.⁴⁵

VI. DAMAGES LIMITATIONS

A. Attorneys’ Fees

A prevailing litigant in New York may not recover attorneys’ fees or disbursements from his adversary in the absence of an agreement between the parties, statute or court rule authorizing such award.⁴⁶ Under appropriate circumstances, however, attorneys’ fees and court costs may be awarded where frivolous claims, defenses, counter-claims and/or cross-claims have been raised. CPLR 8303-a(a).

B. Consequential Damages

Recovery for breach of contract is ordinarily limited to compensation for injuries naturally flowing from the breach or otherwise within the contemplation of the parties at the time they entered into the contract.⁴⁷ Consequential damages can include an owner’s costs to complete construction and cure defects and omissions, whereas a contractor may recover, among other things, reasonable lost profits, post-bid expenditures required to commence construction and costs arising from burdensome physical conditions unspecified in the contract.⁴⁸

C. Delay and Disruption Damages

Untimely completion of construction may entitle the owner to damages equal to additional income that the completed building would have generated during the time the owner was deprived of it.⁴⁹ Conversely, a contractor’s damages for an owner’s delay and disruption of construction may be determined either as: (a) the amount by which the contractor’s estimated costs plus overhead and profit exceed its bid for the contract or (b) the amount of the actual additional costs occasioned by the work disruption—including increased costs of equipment and materials, together with allowance for overhead and profit.⁵⁰

D. Economic Loss Doctrine

In the absence of injury to person or property, a plaintiff seeking recovery for economic loss arising out of a defective product is limited to contractual remedies.⁵¹ Where the transfer of personal property predominates, a construction contract constitutes a “sale of goods” such that New York’s U.C.C. applies and may permit a plaintiff to recover economic loss under breach of warranty theories.⁵² However, the U.C.C. is not applicable to construction contracts which predominantly govern the provision of services and labor.⁵³

E. Interest

Damages for breach of contract accrue interest from the date the claim accrues--in construction contracts, usually the date the work is completed. The judgment for damages continues to accrue interest after it is filed and entered.⁵⁴ CPLR 5004 provides for nine percent (9%) interest *per annum*, except where otherwise provided by statute.

F. Punitive Damages

Punitive damages arising from a breach of contract may be recovered only when necessary to deter conduct that is “gross”, “morally reprehensible” and of “such wanton dishonesty as to imply a criminal indifference to civil obligations.”⁵⁵ The complained-of conduct must be (1) actionable as an independent tort; (2) egregious in nature; (3) directed to the plaintiff; and (4) part of a pattern directed at the public, generally.⁵⁶

New York jurisprudence is clear that both punitive damages and statutory treble damages are uninsurable as a matter of public policy.⁵⁷

Notes

¹. *H.W. Palen's Sons v. Nelson & Caulkins*, 222 A.D.357, 358 (3d Dep't 1928).

². Where the improvement is related to real property improved or to be improved with a single-family dwelling, the end period is four (4) months from completion of the contract or rendering of the last item of services or materials. Lien Law §10(1).

³. A lien on real property improved or to be improved with a single family dwelling may only be extended by order of a court of record or a judge or justice thereof. Lien Law §17.

⁴. See, e.g., *McCoy v. Bailey*, 24 Misc.2d 875, 875 (Sup. Ct. N.Y. 1960).

⁵. *C.S.A. Contr. Corp. v. New York City School Const. Auth.*, 5 N.Y.3d 189 (2005).

⁶. *Portfolio Recovery Assoc., LLC v. King*, 14 N.Y.3d 410, 416 (N.Y. 2010); see also *Martin v. Julius Dierck Equipment Co.*, 43 N.Y.2d 583 (1978).

⁷. *Tanges v. Heidelberg North America, Inc.*, 93 N.Y.2d 48 (1999).

⁸. Siegel, *New York Practice*, §34.

⁹. *Tanges*, *supra*, at 53.

¹⁰. *Id.*

¹¹. *Yonkers Contracting Co., Inc. v. Port Authority Trans-Hudson Corp.*, 93 N.Y.2d 375 (1999).

¹². *Florence v. Goldberg*, 44 N.Y.2d 189 (1978).

¹³. *Campbell v. City of New York*, 4 N.Y.3d 200 (2005).

¹⁴. *Romano v. Romano*, 19 N.Y.2d 444 (1967).

¹⁵. *Village of Pelham v. City of Mount Vernon*, 302 A.D.2d 397, 398 (2d Dep't 2003).

¹⁶. Gen. Bus. Law §777(6) defines “owner” as the first person to whom the home is sold and, during the unexpired portion of the warranty period, each successor in title to the home and any mortgagee in possession.

¹⁷. *Fumarelli v. Marsham Dev't*, 92 N.Y.2d 298 (1998).

¹⁸. *Garan v. Don & Walt Sutton Builders, Inc.*, 5 A.D.3d 349, 350 (2d Dep't 2004); *Biggs v. O'Neill*, 309 A.D.2d 1110, 1110 (3d Dep't 2003).

¹⁹. *Meldrim v. Hill*, 260 A.D.2d 836, 838 (3d Dep't 1999).

²⁰. *Cabrini Med. Ctr. v. Desina*, 64 N.Y.2d 1059 (1985).

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21. *Cont. Cas. Co. v. Rapid-Am. Corp.*, 80 N.Y.2d 640 (1993).
22. *Greater New York Mut. Ins. Co. v. Royal Ins. Co.*, 238 A.D.2d 261 (1st Dep't 1997); *see also Cortland Pump & Equip. v. Firemen's Ins. Co. of Newark*, 194 A.D.2d 117, 121 (3d Dep't 1993).
23. *Am. Home Products Corp. v. Liberty Mut. Ins. Co.*, 748 F.2d 760 (2d Cir. 1984).
24. *Northville Ind. Corp. v. Nat. Union Fire Ins. Co. of Pittsburgh*, 89 N.Y.2d 621 (1997).
25. *See, e.g., Belt Painting Corp. v. TIG Ins. Co.*, 100 N.Y.2d 377 (2003); *see also Thomas J. Lipton, Inc. v. Liberty Mut. Ins. Co.*, 34 N.Y.2d 356 (1974).
26. *Tishman Const. Corp. v. CNA Ins. Co.*, 236 A.D.2d 211 (1st Dep't 1997); *Charter Oak Fire Ins. Co. v. Trustees of Columbia Univ.*, 198 A.D.2d 134 (1st Dep't 1993); *see also Hunter Roberts Construction Group, LLC, et al., Appellants, v. Arch Insurance Company et al.*, 75 A.D.3d 404 (1st Dep't 2010).
27. *See Sandy Creek Central School District v. United Nat. Ins. Co.*, 37 A.D.3d 812 (2nd Dep't 2007).
28. *See, e.g., Turner Const. Co. v. Kemper Ins. Co.*, 2006 WL 2942525 (2d Cir. 2006).
29. *See One Beacon Ins. v. Travelers Prop. Cas. Co. of Am.*, 51 A.D.3d (3d Dep't 2008).
30. *See American Guarantee and Liability Ins. Co.*, 16 A.D.3d 154 (1st Dep't 2005) (coverage for building owner for shooting of tenant by intruders under security guard company's insurance policy depended on a finding of the security guard company's negligence); *see also Crespo v. City of New York*, 303 A.D.2d 166, 756 (1st Dep't 2003) (negligence of parties yet to be determined); *FedEx Ground Package System, Inc. v. Transcontinental Ins. Co.*, 4 Misc.3d 1001 (Kings Cty. Sup.Ct. 2004).
31. *Am. Manufacturers Mut. Ins. Co. v. CMA Enterprises, Ltd.*, 246 A.D.2d 373 (1st Dep't 1998).
32. *Met. Cas. Ins. Co. V. Travelers Ins. Co.*, 21 A.D.3d 457 (2d Dep't 2005).
33. Ins. Law §3429(d)(2).
34. *Zappone v. Home Ins. Co.*, 55 N.Y.2d 131 (1982).
35. *See Mtr. of Fireman's Fund Ins. Co. v. Hopkins*, 88 N.Y.2d 836 (1996); *see also Mtr. of Nationwide Mut. Ins. Co. v. Steiner*, 199 A.D.2d 507 (2d Dep't 1993) (unexplained 41-day delay held to be unreasonable).
36. *See, Village of Pleasantville v. Calvert Ins. Co.*, 204 A.D.2d 689 (2d Dep't 1994).
37. *See Fairmount Funding, Ltd. v. Utica Mut. Ins. Co.*, 264 A.D.2d 581 (1st Dep't 1989).
38. *See Fitzpatrick v. Am. Honda Motor Co.*, 78 N.Y.2d 61, 65 (1991).
39. *Frontier Ins. Co. v. State of New York*, 87 N.Y.2d 864, 638 N.Y.S.2d 933 (1995).
40. *Automobile Ins. Co. of Hartford v. Cook*, 7 N.Y.3d 131 (2006); *Colon v. Aetna Life & Cas. Ins. Co.*, 66 N.Y.2d 6 (1985).
41. *Servidone Constr. Corp. v. Security Insurance Co.*, 64 N.Y.2d 419, (1985); *Hotel des Artistes, Inc. v. Gen. Acc. Ins. Co. of Am.*, 9 A.D.3d 181 (1st Dep't 2004).
42. *See Con. Ed. Co. of New York v. Allstate Ins. Co.*, 98 N.Y.2d 208 (2002).
43. *Dutton v. Charles Pankow Bldrs.*, 296 A.D.2d 32, 322 (1st Dep't 2002) *app. den'd* 790 N.E.2d 276, 276 (2003).
44. *Id.*
45. *Brooks, et al. v. Judlau Contracting, Inc.*, 11 N.Y.3d 204 (2008).
46. *A.G. Ship Maint. Corp. v. Lezak*, 69 N.Y.2d 1 (1986).
47. *Kenford Co. v. County of Erie*, 73 N.Y. 2d 312 (1989).
48. *Sarnelli v. Curzio*, 104 A.D.2d 552, 553 (2d Dep't 1984); *Brushton-Moira Central School Dist. v. Thomas Assoc.*, 91 N.Y.2d 256 (1998); *Peru Assoc. v. State of New York*, 70 Misc.2d 775, 777-79 (Ct. Claims 1971) *aff'd* 39 A.D.2d 1018, 1018 (3d Dep't 1972); *McGovern v. City of New York*, 202 A.D. 317, 332-34 (1st Dep't 1922).
49. *Losei Realty Corp. v. City of New York*, 254 N.Y. 41 (1930); *Bartz v. Drake Hewitt*, 296 A.D.2d 723, (3d Dep't 2002).
50. *Fehlhaber Corp. v. State of New York*, 69 A.D.2d 362, 368-371 (3d Dep't 1977); *Whitmyer Bros. v. State of New York*, 47 N.Y.2d 960 (1979).
51. *Hodgson, Russ, Andrews, Woods & Goodyear v. Isolatek Int'l Corp.*, 300 A.D.2d 1051, 1052-53 (4th Dep't 2002).
52. *Geelan Mech. Corp. v. Dember Constr. Corp.*, 97 A.D.2d 810, 811 (2d Dep't 1983); *Word Mgt Corp. v. AT&T Inf. Systems*, 135 A.D.3d 317, 321 (3d Dep't 1988).
53. *Milau Assoc. v. North Ave. Dev. Corp.*, 42 N.Y.2d 482 (1977).
54. *Brushton-Moira Central School Dist. V. Fred H. Thos. Assoc.*, 91 N.Y.2d 256 (1998); CPLR 5000-5003.
55. *New York University v. Cont'l Ins. Co.*, 87 N.Y.2d 308 (1995).
56. *Id.*
57. *See Home Ins. Co. v. Am. Prods. Corp.*, 75 N.Y.2d 196 (1990); *Rental & Mgt. Assocs. v. Hartford Ins. Co.*, 206 A.D.2d 288 (2d Dep't 1994).

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I. MECHANIC'S LIEN BASICS

N.C. Gen. Stat. Chapter 44A, Article 2. controls mechanics liens in North Carolina. Article 2 was substantially amended in the 2012 legislative session to change requirements on how liens are perfected. The amendments were patterned after Virginia's mechanics lien statute, and brought two major changes to North Carolina in the form of new notice requirements and the establishment of a Lien Agent that is designated by the owner that must be served with notice of liens in order for the lien to be perfected. These changes were enacted to address "hidden lien" problems that arose where owners or

Any person who performs or furnishes labor or professional design or surveying services or furnishes materials or rental equipment pursuant to a contract with the owner of real property for the making of an improvement on that property has the right to file a claim of lien on real property to secure payment of all debts for labor done, services rendered, or materials or equipment furnished. *See* N.C. Gen. Stat. § 44A-8. In addition, a first, second, or third tier subcontractor has the right to enforce by subrogation the property lien rights of the general contractor. N.C. Gen. Stat. § 44A-23.

A. Requirements

1. Filing with Clerk of Court

The claim of lien on real property must be filed in with the Clerk of Court in the county for each county where the property that is the subject of the claim of lien no later than 120 days after the last furnishing of labor or materials at the site. Claims of lien on real property are to follow the form laid out in N.C. Gen. Stat. § 44A-12(c) and must include the following:

- Name and address of person claiming the claim of lien on real property;
- Name and address of record owner of the real property, and if the lien is being asserted through subrogation, the name of the contractor through which subrogation is being asserted;
- Description of real property upon which the claim of lien on real property is claimed. "Street address, tax lot and block number, reference to recorded instrument, or any other description of real property is sufficient, whether or not it

is specific, if it reasonably identifies what is described." N.C. Gen. Stat. § 44A-12(c)(3);

- Name and address of person with whom claimant contracted;
- Date of first furnishing of labor or materials;
- Date of last furnishing of labor or materials;
- General description of the labor performed or materials furnished; and the amount claimed.
- A certification that the claimant has served the owner, any contractor through which subrogation is being claimed.

Once a notice of lien is filed, it may not be amended. N.C. Gen. Stat. § 44A-12(d). It may be withdrawn and re-submitted so long as it is done within the original 120 period for filing, however priority of the lien will not relate back to the original claim of lien.

2. Service on Lien Agent (Projects over \$30,000.00).

In addition to the filing requirements, on any projects involving \$30,000.00 or more in costs (except for improvements made to some existing residential buildings and public buildings) owners and claimants must comply with the Lien Agent provisions of N.C. Gen. Stat. §§ 44A11.1 and 11.2.

An owner is required to designate a lien agent at the time that the contract for improvements is entered into. N.C. Gen. Stat. § 44A-11.1(a). Contact information for the lien agent must be provided to contractors upon written request, and must be posted conspicuously on the property until the completion of construction. *See*, N.C. Gen. Stat. 44A-11.2. If an owner fails to comply with the provisions then potential claimants may be relieved of their obligations under N.C. Gen. Stat. § 44A-11.1.

Potential lien claimants may, but are not required to serve the lien agent with a Notice to Lien Agent that contains the following information:

- Contact information for the potential lien claimant, including email address;
- Name of the party that the potential lien claimant has contracted with to make improvements.
- Property description sufficient to identify the property subject to the lien (name of project or description on building permit is sufficient)
- Statement "I give notice of my right subsequently to pursue a claim of lien for improvements to the real property described in this notice."

As a practical matter, designation of lien agents and service of notices are handled online through LiensNC (www.liensnc.com). Online filing is not required, and physical filing information is available at http://www.liensnc.com/Filing_Locations.html.

For all projects where a lien agent is required, a lien is not considered to be perfected until the filing requirement with the Clerk of Court has been met and one of the following conditions is met:

- The lien agent has received a Notice to Lien Agent from the claimant no later than 15 days after claimant first furnished materials or labor, or
- The lien agent has received a Notice to Lien Agent from the claimant prior to the time that the property is subsequently conveyed to bona fide purchaser, or
- The lien agent has received a Notice to Lien Agent prior to recordation of the transfer to the bona fide purchaser.

N.C. Gen. Stat. § 44A11.2(l).

B. Action to Enforce Claim of Lien on Real Property

An action to enforce a claim of lien on real property must be commenced within 180 days after the last furnishing of labor or materials at the site. A judgment enforcing the lien may then be entered for the principal amount shown to be due, and the judgment shall direct a sale of the real property subject to the lien. The amount recoverable under the lien is limited to the amount claimed in the initial claim of lien on real property. *See* N.C. Gen. Stat. § 44A-13; *Jennings Glass Co., Inc. v. Brummer*, 88 N.C. App. 44, 51, 362 S.E.2d 578, 583 (1987).

C. Claim of Lien upon Funds

Subcontractors and suppliers who furnished labor, materials, or rental equipment at the site of the improvement are entitled to a lien upon funds owed to the contractor with whom the subcontractor dealt and that arise out of the improvement on which the subcontractor worked or furnished materials. In addition to the ability to lien funds owed to the party with whom the subcontractor dealt, second and third tier subcontractors and suppliers are entitled to a lien on funds owed to any party above them in the chain of their contract through subrogation. In other words, as long as money is owed to each party above them in the contract chain, these lower tiered subcontractors and suppliers can lien funds owed to the general contractor. N.C. Gen. Stat. § 44A-18. A Notice of Claim of Lien upon Funds must set out the information identified in N.C. Gen. Stat. § 44A-19:

- Name and address of person claiming the lien on funds;
- Description of real property upon which the claim of lien on real property is claimed;
- Name and address of person with whom claimant contracted;

- Name and address of each person against or through whom subrogation rights are claimed;
- General description of the contract and the person against whose interest the lien upon funds is claimed; and
- Amount of the lien upon funds claimed by the lien claimant under the contract.

Upon receipt of the notice of claim of lien upon funds, the obligor has a duty to retain any funds subject to the lien upon funds. *See* N.C. Gen. Stat. § 44A-20.

Note for Public Projects: Although public projects cannot be liened, when the total amount of construction contracts awarded for any one project exceeds \$300,000, a performance and payment bond is required by the contracting body from any contractor or construction manager at risk with a contract more than \$50,000. (Note, the size of the project changes to \$500,000 if the construction involves the University of North Carolina.) N.C. Gen. Stat. § 44A-25 *et seq.* governs actions on payment bonds.

While public property cannot be liened, the lien on funds discussed above can be utilized by subcontractors up to the general contractor.

E. Ability to Waive and Limitations on Lien Rights

When a claimant signs a lien waiver and accepts partial payment, such payment reduces the amount payable to the lien claimant by the amount of payment received but does not change the property lien or the Date of First Furnishing. *Wachovia Bank Nat. Ass'n v. Superior Const. Corp.*, 2010 WL 1655494, 5 (N.C. Super. 2010). Moreover, contractors can contract away or waive their lien rights on the underlying property, although this right is limited by N.C. Gen. Stat. § 44A-12(f), which prohibits waivers made “in anticipation of and in consideration for the awarding of a contract ... for the making of an improvement upon real property.” *Id.*

As referenced above, N.C. Gen. Stat. § 44a-23 grants to a first tier subcontractor a lien upon improved real property based upon a right of subrogation to the direct lien of the general contractor on the improved real property. Pursuant to N.C. Gen. Stat. § 44A-23, no action of the general contractor will be effective to prejudice the rights of the subcontractor without his written consent upon the filing of notice and claim of lien and the commencement of an action. Prior to that time, the general contractor is free to waive its lien rights and to bar effectively the subcontractor's rights by way of subrogation. *Mace v. Bryant Construction Corp.*, 48 N.C. App. 297, 269 S.E.2d 191 (1980).

F. Liens May be Bonded Off

As is typical, a lien may be bonded off pursuant to N.C. Gen. Stat. § 44A-16(6). When done, the bond takes the place of the real property and therefore the real property becomes unencumbered and is free of the lien.

II. STATUTES OF LIMITATION AND REPOSE

This section provides a brief overview of the statute of limitations and the statute of repose applicable to construction defect claims and highlights some of the important case law interpreting these provisions.

A. Statute of Limitations

The three year statute of limitations in N.C. Gen. Stat. § 1-52 applies to contract actions; torts, including negligence; and claims for indemnification or contribution.¹ See N.C. Gen. Stat. §§ 1-52(1), (2), (5). A statutory "discovery rule" offers a claimant additional time in certain contract or negligence actions to have the opportunity to discover the harm before the three-year statute of limitations begins to accrue. Pursuant to N.C. Gen. Stat. § 1-52(16), for personal injury or physical damage to property, the cause of action does not accrue until bodily harm to the claimant or physical damage to his property becomes apparent or should have become apparent to the claimant, whichever occurs first, although no cause of action may accrue more than 10 years from the last act or omission of the defendant giving rise to the cause of action. See *Pompano Masonry Corp. v. HDR Architecture, Inc.*, 165 N.C. App. 401, 409, 598 S.E.2d 608, 613 (2004) (holding that masonry subcontractor's negligence claim alleging that project expediter failed to properly schedule and coordinate work on public university's construction project accrued, and three-year limitations period began to run, when subcontractor discovered alleged negligence during coordination meetings.)

A four-year statute of limitations applies to breach of warranty actions involving the sale of goods under North Carolina's Uniform Commercial Code. See N.C. Gen. Stat. § 25-2-725(1). A cause of action for breach of warranty accrues when tender of delivery is made, even if the aggrieved party is unaware of the breach. See N.C. Gen. Stat. § 25-2-725(2). However, where a warranty expressly extends to future performance of goods so that discovery of the breach must await the time of such performance, the cause of action accrues when the breach is or should have been discovered. *Id.*

B. Statutes of Repose

The statute of repose for construction defect claims is six years. Pursuant to N.C. Gen. Stat. § 1-50(a)(5), "no action to recover damages based upon or arising out of the defective or unsafe condition of an improvement to real property shall be brought more than six years from the later of the specific last act or omission of the defendant giving rise to the cause of action or substantial completion of the improvement."

This statute of repose serves to shorten the 10-year statute of repose contained in N.C. Gen. Stat. § 1-52(16). See N.C. Gen. Stat. § 1-50(a)(5)(g) ("The limitation prescribed by this subdivision shall apply to the exclusion of ...G.S. 1-52(16)").

¹North Carolina follows the general rule that a cause of action on an obligation to indemnify normally accrues when the indemnitee suffers actual loss. The same rule applies to the accrual of a cause of action for contribution between joint tortfeasors. *Safety Mut. Cas. Corp. v. Spears, Barnes, Baker, Wainio, Brown & Whaley*, 104 N.C. App. 467, 471, 409 S.E.2d 736, 739 (1991).

According to *Monson v. Paramount Homes, Inc.*, 133 N.C. App. 235, 241, 515 S.E.2d 445, 450 (1999), repairs do not reset the running of the statute of repose. "A duty to complete performance may occur after the date of substantial completion, however, a 'repair' does not qualify as a 'last act' under N.C. Gen. Stat. § 1-50(5) unless it is required under the improvement contract by agreement of the parties." *Id.*

In *Roemer v. Preferred Roofing, Inc.*, 190 N.C. App. 813, 660 S.E.2d 920 (2008), the North Carolina Court of Appeals held that a homeowner's claim for monetary damages was barred by the six-year statute of repose. The complaint was filed seven years after substantial completion of the work at issue. *See id.* at 922. The Court of Appeals held that the claim was barred by the six-year statute of repose because the homeowner's remedy for breach of an alleged lifetime warranty claim "lies in specific performance, and not damages." *Id.*

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

Generally, North Carolina has no requirement of notice and opportunity to cure. However, on public construction projects, a lower-tiered subcontractor that has no contractual relationship with the contractor must give written notice to the contractor within 120 days of the date on which the claimant last performed labor or furnished material in order to bring an action against the contractor's payment bond. *See* N.C. Gen. Stat. § 44A-27.

IV. CONTRACTUAL INDEMNIFICATION

Generally speaking, under North Carolina law, indemnity and hold harmless provisions in construction contracts that attempt to indemnify or hold harmless a party against his own negligence are against public policy and are, therefore, void and unenforceable. N.C. Gen. Stat. § 22B-1.

V. DAMAGES LIMITATIONS

A. Attorneys' Fees

Attorney's fees have traditionally been generally unavailable in North Carolina unless the contract specifically provides for fee shifting. Even then, the Courts would only enforce fee shifting clauses on a sporadic basis. The North Carolina General Assembly in 2011 passed legislation that requires enforcement of fee shifting provisions. However, in lien actions, the law remains that any action brought under the lien statute may result in an award of attorneys' fees to the prevailing party "upon a finding that there was an unreasonable refusal by the losing party to fully resolve the matter" N.C. Gen. Stat. § 44A-35.

B. Consequential Damages

Parties may limit contractually or exclude **consequential damages** unless the limitation or exclusion is unconscionable. N.C. Gen. Stat. § 25-2-719(3).

C. Economic Loss Doctrine

The economic loss doctrine has been applied in the context of construction cases. For instance, in *Land v. Tall House Bldg. Co.*, 165 N.C. App. 880, 884, 602 S.E.2d 1, 4 (2004), the court recognized that the doctrine prohibits recovery for economic loss in tort, as such claims are governed by contract law. Moreover, the court recognized that when a component part of a product or a system injures the rest of the product or the system, only economic loss has occurred. In *Land*, the contractor applied direct exterior finish systems (“DEFS”) to a house. Negligence claims against the manufacturer of DEFS were barred because “any damage caused by the DEFS constitutes damage to the house itself. Since no other property damage has resulted, this is purely economic loss.”

D. Interest

In an action for breach of contract, the amount awarded on the contract bears interest from the date of the breach. N.C. Gen. Stat. § 24-5. The legal interest rate is 8 percent.

E. Punitive Damages

N.C. Gen. Stat. § 1D-15 provides that punitive damages may be awarded only if the claimant proves that the defendant is liable for compensatory damages and that one of the following aggravating factors was present and was related to the injury for which compensatory damages were awarded:

- 1) Fraud
- 2) Malice
- 3) Willful or wanton conduct.

Furthermore, the claimant must prove the existence of an aggravating factor by clear and convincing evidence. Punitive damages shall not be awarded against a person solely on the basis of vicarious liability or breach of contract. N.C. Gen. Stat. § 1D-15

VI. CASE LAW AND LEGISLATIVE UPDATE

As stated above, the most significant recent developments in North Carolina law are the amendments to the Lien Statutes. Any participant in a project in North Carolina will need to carefully consider the new requirements and proactively post a Notice to Lien Agent to protect its rights.

The North Carolina Court of Appeals issued a decision in 2011 which dramatically changes construction law in North Carolina, or at least homebuilding litigation. In *White v. Collins Bldg., Inc.*, 209 N.C. App. 48, 704 S.E.2d 307, 310 (2011), the purchasers of an oceanfront home filed a negligence claim against their building company’s president and sole shareholder, alleging that the defendant failed to supervise properly the construction of their home, such that the home sustained water, window, and plumbing damage. As a matter of first impression, the Court of Appeals held that the defendant could be personally liable for negligence in construction of the

home, even in the absence of facts sufficient to pierce the corporate veil. While no subsequent cases have been reported that discuss this ruling, plaintiffs in defect cases have begun to name principals of corporations as defendants in reliance upon the *Collins* decision.

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I. MECHANICS' LIENS BASICS

Following is a summary of construction liens as governed by Chapter 35-27 of the North Dakota Century Code.

A. Requirements

Any person who improves real estate by the contribution of labor, skill, or materials, whether under contract with the owner of such real estate or with any contractor, subcontractor, or agent of the owner, has a lien upon the improvement and upon the land on which it is situated. Provided, however, that the amount of lien is only for the difference between the price paid by the owner or agent and the price or value of the contribution. If the owner or agent has paid the full price or value of the contribution, no lien is allowed.¹

Thus, a subcontractor who performs his work, files a notice of intention to claim construction lien and otherwise complies with the construction lien law can still be precluded from obtaining any construction lien if the owner has already paid the full price to his contractor. This does not prohibit the subcontractor from suing the contractor, but merely prohibits the subcontractor from obtaining any construction lien on the land involved.

Written notice that a lien will be claimed must be given to the owner of the real estate by certified mail at least 10 days before the recording of the construction lien.²

The owner may withhold so much of the contract price from the contractor as may be necessary to meet the demands of all persons, other than the contractor, having a lien for which the contractor is liable.³

B. Enforcement and Foreclosure

Any lien-holder may bring an action to enforce in the district court in the county in which the property is located. Before a lien may be enforced, however, the lien-holder must give written notice, by personal service, upon the record owner of the property at least ten days before an action to enforce is commenced. Otherwise, if by registered mail, notice must be given at least twenty days before the action is commenced.⁴ A lien-holder may file for a deficiency if the same remains after sale of the property.⁵

C. Ability to Waive and Limitations on Lien Rights

The mingling of charges for materials to be used in the construction, alteration, repair, or improvement of the property of different persons, except in the cases of joint ownership or ownership in common, defeats the right to a lien against either or any of such persons.⁶

The entire land upon which any building, structure or improvement is placed is subject to a lien filed under Chapter 35-27.⁷

A construction lien shall be subordinate to a mortgage given for the purpose of providing funds for the payment of labor or materials for the improvement, unless a construction lien is filed prior to such mortgage.⁸

A lien may not be filed more than three years after the first materials are furnished.⁹

II. STATUTES OF LIMITATION AND REPOSE.

A. Statute of Limitations:

Contract for Sale Under UCC – 4 years. In the original agreement the parties may reduce the period of limitation to not less than one year, but may not extend it.¹⁰

Contract Action – 6 years.¹¹

B. Statue of Repose.

No action, whether in contract, oral or written, in tort or otherwise, to recover damages:

For any deficiency in the design, planning, supervision, or observation of construction or construction of an improvement to real property;

For injury to property, real or personal, arising out of any such deficiency; or

For injury to the person or for wrongful death arising out of any such deficiency, may be brought against any person performing or furnishing the design, planning, supervision, or observation of construction, or construction of such an improvement more than ten years after substantial completion of such an improvement.¹²

For injuries occurring during the tenth year after substantial completion, the action may be brought within two years after the date on which such injury occurred, but not later than twelve years after the substantial completion of such improvement.¹³

The statute may not be asserted by way of defense by any person in actual possession or control of such improvement at the time any deficiency constitutes the proximate cause of an injury for which it is proposed to bring an action.¹⁴

The statute does not apply to a manufacturer of building materials used in an improvement to real property.¹⁵

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

Before a lien holder may enforce a lien, he shall give written notice to the owner of his intention to do so by personal service at least 10 days or by registered mail at least 20 days before an action is commenced.¹⁶

A lien is perfected by recording with the Register of Deeds in the county where the property is located, within 90 days after all contribution is done, a construction lien describing the property, stating the amount due, the dates of the first and last contribution, and the person with which the claimant contracted.¹⁷

A lien is not lost for failure to file within 90 days except as to purchasers or encumbrancers whose rights accrue after the 90 days and before a claim is filed and against the owner, to the extent they have made payment before the recording of the lien.¹⁸ A lien may not be filed more than 3 years after the date of the first item of material is furnished.¹⁹

Upon written demand of the owner, suit must be commenced and filed with the Clerk of Court within 30 days thereafter or the lien is forfeited. No lien is valid or may be enforced unless the holder thereof asserts the same by complaint, filed with the Clerk of Court, within 3 years after the date of recording of the lien.²⁰

IV. INSURANCE COVERAGE AND ALLOCATION ISSUES

A. General Coverage Issues

The interpretation of insurance contracts follows that of contract law, which is governed by Title 9 of the Century Code. A contract for insurance is construed to give effect to the mutual intent of the parties at the time of formation.²¹ If the contract is clear on its face, there is no room for a court to construe its provisions.²²

The courts regard insurance policies as contracts of adhesion, and resolve all ambiguity against the insurer.²³ Further, “exclusions from coverage in an insurance contract must be clear and explicit and are strictly construed against the insurer.”²⁴

B. Trigger of Coverage

This is not a well-settled issue of law in North Dakota. There are two cases that have dealt with the issue of when coverage applies to a claim for damage. In *Friendship Homes v.*

American States Ins. Companies, the court held the insurance policy did not extend to liability for a fire due to negligent installation, and seemingly applied the ‘injury-in-fact’ rule, which is that coverage isn’t triggered until the actual property damage first occurs.²⁵ In *Kief Farmers v. Famland Mutual*, the court, in an apparently contradictory decision, seemed to hold that the event which triggers liability exposure should be judged on a case by case basis depending on the interpretation of each insurance contract at issue.²⁶

C. Allocation Among Insurers

There is no legislation in North Dakota regarding the allocation of risk amongst parties to a construction contract. Nor are there limitations, statutory or otherwise, on contracts for additional insurance.

V. CONTRACTUAL INDEMNIFICATION.

There are no specific statutes in North Dakota that limit the enforceability of indemnity provisions in construction contracts. However, North Dakota law generally provides that “an indemnity agreement will not be construed to indemnify a party against the consequences of its own negligence unless that interpretation is clearly intended.”²⁷

The North Dakota Supreme Court has interpreted a contract to indemnify a party against the consequences of its own negligence where the indemnity agreement contained no language of limitation or qualification and required the indemnitor to procure liability insurance, including an endorsement adding the indemnitee as an additional insured.²⁸

In *Barsness*, a construction worker was injured when he fell from a crane leased from General Diesel & Equipment Co., Inc. The trial court determined that General Diesel was entitled to contractual indemnity from Barsness’ employer, First Assembly. On appeal, the North Dakota Supreme Court reversed the trial court’s decision stating that it did “not believe that the lease agreement, when read in its entirety, reflect[ed] a clear intent that General Diesel be indemnified for its own negligence. “ Of particular significance were the following: (d) the lease did “not require indemnification for ‘any and all claims,’ but merely for ‘liability arising out of the operation’ of the crane: and (e) while there was an insurance requirement, it required insurance for damage to the crane but not for person injury damages.

Note: indemnity agreements involving ‘motor carrier contracts’ that purport to indemnify or hold harmless the promise for their own fault is void as a matter of law.²⁹

VI. CONTINGENT PAYMENT AGREEMENTS

There is no legislation on this issue as it pertains to contracts for construction. See: Title 9 of the North Dakota Century Code for the general provisions of contract law, N.D.C.C. Chapter 9-08 governs unlawful and voidable contracts generally. Further, any provision which would make the contractor liable for deficiencies in the plans and specifications is void.³⁰

VII. DAMAGES LIMITATIONS.

North Dakota does not currently have specific damages limitations applicable to the construction industry. Chapter 32-03 governs the proper measure of damages generally.

In all cases, no more than reasonable damages may be recovered.³¹ Whether a verdict is excessive does not depend on any objective measure, but is a matter of the quality of evidence on the record.³²

A. Personal Injury Damages vs. Construction Defect Damages

There is no express limitation on the recovery of damages generally in either a claim for personal injury or due to construction defect. Note, however, that the limit on damages has been held to be narrower in claims for breach of contract as opposed to tort claims.³³

Pursuant to claims for wrongful death, a plaintiff may recover for mental anguish, loss of society, comfort, and companionship.³⁴ In all other tort cases, the measure of damages is limited to the amount that would reasonably compensate the plaintiff for their loss, whether the detriment caused is anticipated or not.³⁵ The measure of damages for breach of contract, however, is a reasonable amount that will compensate the aggrieved party for that which would likely result from the breach thereof, and any damages must be clearly ascertainable.³⁶ In short, the measure of damages for breach of contract is that which will compensate for any loss the fulfillment of the contract would have prevented.³⁷

B. Attorney's Fees Shifting and Limitations on Recovery

In civil actions, upon a finding that the claim for relief was frivolous, the court shall award costs including reasonable attorneys fees to the prevailing party.³⁸

C. Consequential Damages

The provisions of North Dakota law governing damages would exclude consequential damages for any claim arising from breach of contract. As previously stated, the measure of damages in tort claims generally is that which would compensate the plaintiff for their loss, *whether that loss is anticipated or not*. However, damages for breach of contract are limited to that which would 'likely result.' However, the 'substantial performance' doctrine is alive and well in North Dakota. Under this doctrine, if defects can be repaired with necessitating substantial reconstruction, then the contract may still recover the contract price less the cost of repair. However, if substantial reconstruction is necessary, the aggrieved party may recover the value of a properly constructed project less the value of the project actually constructed.³⁹

D. Delay and Disruption Damages

Overhead costs, including those for delay and disruption, are not allowed in the calculation of damages.⁴⁰

E. Economic Loss Doctrine.

The economic loss doctrine bars tort claims when the only damage was to the defective product. Such claims must be brought in an action to recover for breach of warranty or contract.⁴¹

F. Interest.

Except where there is a dispute between a state agency and a contractor, every state agency must make payment for property or services as specified in the contract or within 45 days after receipt of the invoice.⁴² Interest shall accrue at the rate of 1¾% per month unless a different rate is specified within the contract.⁴³ Subcontractors are likewise entitled to be paid within 45 days after payment from such agency to the prime contractor. Interest accrues at the rate of 1¾% per month unless a different rate is provided in the contract.⁴⁴

On public building contracts, in the event the governing board fails or neglects to consider any estimate properly submitted, pay any estimate approved, or make final payment upon completion and acceptance for a period of more than 30 days then said estimate or final payment shall draw interest two percentage points below the Bank of North Dakota prime interest rate.⁴⁵

Interest for any legal indebtedness must be at the rate of 6% per annum unless a different rate, not exceeding the usury rate, is contracted for in writing.⁴⁶

G. Punitive Damages.

Punitive damages may not be awarded in a case arising out of breach of contract.⁴⁷ In a case not arising out of breach of contract where the defendant has been guilty by clear and convincing evidence of oppression, fraud or actual malice, punitive damages may be awarded, however, they may not be sought in the complaint. After filing of the suit, a motion to amend the pleadings to claim exemplary or punitive damages may be made and will be allowed if the court finds that there is sufficient evidence to support a finding by the trier of fact that a preponderance of evidence proves oppression, fraud or actual malice.⁴⁸

H. Other Damages Limitations

Any provision in a construction contract which would make the contractor liable for the errors or omissions of the owner or the owner's agents in the plans and specifications is against public policy and void.⁴⁹

Except for certain contracts with governmental agencies, contracts with contractors are subject to a maximum retainage of 10% of each estimate presented until such time as a project is 50% complete, after which no further retainage is allowed.⁵⁰

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- ¹ N.D.C.C. § 35-27-02.
- ² N.D.C.C. § 35-27-02.
- ³ N.D.C.C. § 35-27-09.
- ⁴ N.D.C.C. § 35-27-24.
- ⁵ N.D.C.C. § 35-27-24.
- ⁶ N.D.C.C. § 35-27-10.
- ⁷ N.D.C.C. § 35-27-19.
- ⁸ N.D.C.C. § 35-27-04.
- ⁹ N.D.C.C. § 35-27-14.
- ¹⁰ N.D.C.C. § 41-02-104(1).
- ¹¹ N.D.C.C. § 28-01-16(1).
- ¹² N.D.C.C. § 28-01-44(1).
- ¹³ N.D.C.C. § 28-01-44(2).
- ¹⁴ N.D.C.C. § 28-01-44(3).
- ¹⁵ *Hebron Public School Dist. No. 13 of Morton County v. U.S. Gypsum Co.*, 475 N.W.2d 120, 127 (N.D. 1991).
- ¹⁶ N.D.C.C. § 35-27-24.
- ¹⁷ N.D.C.C. § 35-27-13.
- ¹⁸ N.D.C.C. § 35-27-14.
- ¹⁹ N.D.C.C. § 35-27-14.
- ²⁰ N.D.C.C. § 35-27-25.
- ²¹ *K & L Homes, Inc. v. American Family Mut. Ins. Co.*, 829 N.W.2d 724 (N.D. 2013).
- ²² *Id.*
- ²³ *Id.*
- ²⁴ *Id.*
- ²⁵ *Friendship Homes, Inc. v. American States Ins. Companies*, 450 N.W. 2d 778 (N.D. 1990).
- ²⁶ *Kief Farmers Co-op Elevator Co. v. Farmland Mut. Ins. Co.*, 534 N.W.2d 28 (N.D. 1995).
- ²⁷ *Barsness v. General Diesel & Equipment Co, Inc.*, 422 N.W.2d 819, 825 (N.D. 1988) citing *Vanderhoof v. Gravel Products, Inc.*, 404 N.W.2d 485 (N.D. 1987); *Bridston v. Dover Corp.*, 352 N.W.2d 194 (N.D. 1984).
- ²⁸ *Bridston v. Dover Corp.*, 352 N.W.2d 194, 197 (N.D. 1984).
- ²⁹ N.D.C.C. § 22-02-10.
- ³⁰ N.D.C.C. § 9-08-02.1.
- ³¹ N.D.C.C. § 32-03-37.
- ³² *Miller v. Breidenbach*, 520 N.W. 2d 869 (N.D. 1994).
- ³³ *Bumann v. Maurer*, 203 N.W.2d 434 (N.D. 1972).
- ³⁴ *Hopkins v. McBane*, 427 N.W.2d 85 (N.D. 1988).
- ³⁵ N.D.C.C. § 32-03-20.
- ³⁶ N.D.C.C. § 32-03-09.
- ³⁷ *Ehrichs v. Kearney*, 730 F.2d 1170 (D.N.D. 1984), cert. denied 469 U.S. 930.
- ³⁸ N.D.C.C. § 28-26-01(2).
- ³⁹ *Curtis Const. Co., Inc. v. American Steel Span, Inc.*, 707 N.W.2d 68 (N.D. 2005).
- ⁴⁰ *Triton Corp. v. Hardrives, Inc.*, 85 F.3d 343 (8th Cir. 1996).
- ⁴¹ *Stiener v. Ford Motor Co.*, 606 N.W.2d 881, 884 (N.D. 2000).
- ⁴² N.D.C.C. § 13-01.1-01.
- ⁴³ N.D.C.C. § 13-01.1-02.
- ⁴⁴ N.D.C.C. § 13-01.1-06.
- ⁴⁵ N.D.C.C. § 48-01.2-14.
- ⁴⁶ N.D.C.C. § 47-14-05.
- ⁴⁷ N.D.C.C. § 32-03.2-11.
- ⁴⁸ N.D.C.C. § 32.03.2-11.
- ⁴⁹ N.D.C.C. § 9-08-02.1.
- ⁵⁰ N.D.C.C. § 43-07-23.

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I. MECHANIC'S LIEN BASICS

Lawyers and construction professionals dealing with Ohio's mechanic's law for the first time (and every time thereafter) must proceed with caution, for there are many traps for the unwary. Ohio's courts strictly construe the statutory lien perfection requirements because mechanic's lien rights are in derogation of the common law. Statutory requirements relating to post-perfection issues are more liberally construed, but that is no relief for a claimant that has lost its rights. Ohio law provides for mechanic's lien rights at Ohio Revised Code ("ORC") § 1311.01, *et. seq.* The purpose of mechanic's liens is to protect those whose claims accumulate daily and who have no other means to protect themselves.² Those with statutory lien rights can waive them in their written contracts. They often do so unwittingly. Thus, the analysis should begin with a review of the pertinent contract terminology.

Mechanic's liens against public property are not permitted. In lieu of that, Ohio law provides for liens (historically referred to as "attested account claims") against the project funds held by the government entity that owns the public project. Thus, there are two parallel but distinct frameworks for private project and public project liens. Furthermore, on private projects, the law distinguishes between residential projects, gas and oil projects, and other traditional commercial projects.

Practitioners and construction professionals must also be aware of distinct requirements that must be satisfied by certain deadlines. For instance, some documents must be "served" (i.e. by certified mail or otherwise) on certain defined persons, while others must be "recorded" at the County Recorder's office, and others must be "filed" at the County Courthouse. Tracking the action required is as important as tracking the deadlines for each activity.

A. Requirements

1. Notice of Commencement

For the project owner, lien-related duties commence prior to the initial project activity. Prior to commencement, an owner must prepare a Notice of Commencement ("NOC"). For private projects, the NOC must state:

To Lien Claimants and Subsequent Purchasers:

Take notice that labor or work is about to begin on or materials are about to be furnished for an improvement to the real property described in this instrument. A person having a mechanics' lien may preserve the lien by providing a notice of furnishing to the above-named designee and the above-named designee's original contractor, if any, and by timely recording an affidavit pursuant to section 1311.06 of the Revised Code.

A copy of this notice may be obtained upon making a written request by certified mail to the above-named owner, part owner, lessee, designee, or the person with whom you have contracted.³

The NOC must be recorded with the County Recorder, posted on the job site, and made available upon request.⁴ "Home construction projects" are exempted from this requirement, unless the lender elects otherwise.⁵

For public projects, the NOC must state:

- (1) The name, location, and a number, if any, used by the public authority to identify the public improvement sufficient to permit the public improvement to be identified;
- (2) The name and address of the public authority;
- (3) The name, address, and trade of all principal contractors;
- (4) The date the public authority first executed a contract with a principal contractor for the public improvement;
- (5) The name and address of the sureties for all principal contractors;
- (6) The name and address of the representative of the public authority upon whom service shall be made for the purposes of serving an affidavit pursuant to section 1311.26 of the Revised Code.⁶

It need not be recorded or posted on the site, though it must be made available on request.⁷

2. Notice of Furnishing

For contractors, subcontractors, laborers, and material and equipment suppliers, perfection requirements generally begin once a laborer, subcontractor, or supplier begins to provide services, equipment, or materials to the project. The first step involves the service of a Notice of Furnishing ("NOF").

For private projects, the NOF must state:

Please take notice that the undersigned is performing certain labor or work or furnishing certain materials to (name and address of other contracting party) in connection with the improvement to the real property located at..... The labor, work, or materials were performed or furnished first or will be performed or furnished first on (date). WARNING TO OWNER: THIS NOTICE IS REQUIRED BY THE OHIO MECHANICS' LIEN LAW. IF YOU HAVE ANY QUESTIONS ABOUT YOUR RIGHTS AND DUTIES UNDER THESE STATUTES YOU SHOULD SEEK LEGAL ASSISTANCE TO PROTECT YOU FROM THE POSSIBILITY OF PAYING TWICE FOR THE IMPROVEMENTS TO YOUR PROPERTY.⁸

Any project participant who does not have a contract with the record owner of the project must serve (i.e. certified mail) a NOF upon the owner and the original contractor in its chain of privity.⁹ If a NOC is not recorded, the NOF is not required.¹⁰

For public projects, the NOF must state:

The undersigned notifies you that the undersigned has furnished or performed or will furnish or perform (describe labor, work, or materials) for the improvement of real property identified as (property description or address) under order given by (name of subcontractor or material supplier). The labor, work, or materials were first furnished or performed or will be furnished or performed on (date).¹¹

Any project participant who does not have a contract with a prime contractor on a public project must serve a NOF upon “the principal contractor whose contract with the public authority is the contract under which the subcontractor or materialman is performing labor or work or furnishing materials.”¹²

On public or private projects, lien claimants must serve the NOF within 21 days of the date that they first provide services, labor, or materials.¹³ Lien claimants should not serve the NOF before the first day they provide services, labor, or materials. If they do, the NOF may be invalid.¹⁴ If the lien claimant serves the NOF after the 21-day deadline, their lien will only cover the value of services, labor, or materials provided during or after the 20-day period before they provided the NOF.¹⁵ Service is to be made via certified mail, or another method which provides a written evidence of receipt.¹⁶

Laborers are not required to serve a NOF, regardless of project type or privity relationship.¹⁷

3. Affidavit of Lien

On private projects, the Affidavit of Lien must be recorded with the Recorder of the county where the project is located within 60 days of the last date of work on a residential project, within 120 days of the last date of work on a gas or oil project, and within 75 days from the last date of work on other projects (including commercial projects).¹⁸ The Affidavit of Lien must be served via certified mail (or other method which provides a written evidence of receipt) on the owner's designee identified in the NOC or the owner, part owner or lessee, if no designee is identified) within 30 days of the date it was recorded.¹⁹

On public projects, the lien claimant (i.e. anyone but the prime contractor) must serve the Affidavit of Lien on the public owner of the project within 120 days of the last date of work.²⁰ The Affidavit of Lien must be served on the representative of the public authority at the address set forth in the NOC.²¹ To enhance recovery rights, the lien claimant should also record, with the Recorder of the county where the Project is located, the Affidavit of Lien within 30 days of the date of service.²²

B. Enforcement and Foreclosure

1. Public Projects

On public projects, the owner's receipt of the Affidavit of Lien starts the clock running on its obligations. The public owner must immediately escrow the disputed amount.²³ Within 5 days, the owner must provide a copy of the Affidavit to the prime contractor.²⁴ The prime contractor then has 20 days to inform the owner if it intends to dispute the claim.²⁵ If the prime contractor misses its deadline or elects not to dispute the lien, the prime contractor is deemed to have assented to the correctness of the claim, and the owner can release the funds to the claimant.²⁶ The contractor can discharge the lien by providing a bond and issuing a 60-day Notice to Commence Suit.²⁷ Either the owner or the prime contractor can independently issue a 60-day Notice to Commence Suit.²⁸ If the claimant does not file a lawsuit within that time period, the claim is waived and the funds are released.²⁹

Ohio does not provide a statute of limitations for lawsuits on public project liens where there is no Notice to Commence Suit.

If a lien discharge bond is in place, then the lien claimant will file suit against the surety on the bond. Otherwise, the lien claimant will commence suit against the public entity and may obtain an award of attorneys' fees.³⁰

2. Private Projects

On private projects, an owner or contractor may also provide a 60-day Notice to Commence Suit.³¹ Otherwise, the Affidavit of Lien will encumber the property for 6 years before it is released by operation of statute.³²

Typically, foreclosure actions must be accompanied by a title report. This requirement varies based upon the local rules of the appropriate court. Furthermore, the plaintiff/lien claimant must name as defendants all parties with an interest in the lien property. This includes the owner, lenders with secured interests, and other lien claimants.³³

C. Ability to Waive and Limitations on Lien Rights

As indicated in the introduction, claimants may waive their lien rights in their written agreements.³⁴

On residential projects, homeowners are protected from double payment. Thus, if they can show that they have paid the prime contractor for the labor, services, equipment, or materials that are the subject of the lien, then the lien claim will fail.³⁵

Ohio does not have a statutory form of lien waiver for use with progress payments. Claimants must therefore be sure that they understand what they are signing when they receive a progress payment. Lien waiver forms are characterized by the use of the terms “Conditional” or “Unconditional” and “Partial” or “Final.” “Unconditional” waivers are used where the funds are in the bank. A “Final” lien waiver is only appropriate if the funds being paid are in fact the last and final payment. Hence, an “Unconditional Final Lien Waiver” will be signed only when final payment, including retainage, is in the bank. Because of the variety of lien forms, claimants should also be careful to understand the waivers included within them, and to modify the form to reserve rights as to any pending claims.

II. STATUTES OF LIMITATION AND REPOSE

A. Statutes of Limitation and Limitations on Application of Statutes

For claims typically at issue on construction projects, Ohio provides the following limitations periods:

- (1) For a written contract, 8 years;³⁶
- (2) For an oral agreement, 6 years;³⁷
- (3) For unjust enrichment and action on an account, 6 years;³⁸
- (4) For breach of contract for sales covered by the Uniform Commercial Code (“UCC”), 4 years;³⁹
- (5) For certain torts, including the duty to perform construction work in a workmanlike manner and professional negligence (other than legal or medical malpractice claims), 4 years;⁴⁰
- (6) For personal injury or damage to personal property, 2 years;⁴¹
- (7) For foreclosure of a mechanic’s lien, 6 years;⁴²

Provisions in written agreements that shorten the applicable limitations period are typically enforced when they are between commercial entities, but may not be shortened to less than 1 year for contracts that fall under the UCC.⁴³

Typically, causes of action arising in tort accrue at the time the negligent act occurred. However, Ohio recognizes the “delayed damages” and “discovery” rules in the construction context. Under the discovery rule, a cause of action does not begin to accrue until the claimant discovers, or should have discovered, that it has been injured by the defendant's conduct.⁴⁴ The delayed damages rule provides that a cause of action for negligence is not complete, and the statute of limitations does not begin to run, until there has been an injury.⁴⁵ These rules are similar and often used interchangeably by Ohio courts, particularly in the construction setting.⁴⁶

B. Statutes of Repose and Limitations on Application of Statutes

Ohio statutory law prohibits a claimant from bringing certain causes of action against a person that designed, planned, supervised, or constructed an improvement to real property more than 10 years from the date of substantial completion of the improvement:

(A)(1) ... no cause of action to recover damages for ... an injury to real or personal property ... that arises out of a defective and unsafe condition of an improvement to real property ... shall accrue against a person who performed services for the improvement to real property or a person who furnished the design, planning, supervision of construction, or construction of the improvement to real property later than ten years from the date of substantial completion of such improvement.⁴⁷

Substantial completion is defined in the statute as the date the property is first used, or available for use.⁴⁸ If the defective or unsafe condition is first discovered within 2 years of the expiration of the 10-year period, a claimant may bring a claim within 2 years of discovery even if it is past the 10-year limit.⁴⁹

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

Ohio Revised Code Chapter 1312 – Right to Cure

During the past few years, many states, including Ohio, have enacted statutes known as “Right To Cure” statutes. The Ohio statute applies only to residential construction contracts. Chapter 1312 of the ORC sets forth the procedure under which a residential contractor may cure a defect prior to an owner commencing arbitration proceedings or a civil action. It applies only to claims for construction defects and property damages, and has no applicability to suits for personal injury.

ORC § 1312.03 requires residential contractors to provide owners with a statutory notice designed to alert the owner of the residential contractor's right to resolve any alleged construction defects before the owner pursues any legal action or arbitration. The notice must be provided to the owner at the time of contracting, either in the contract or in a separate document. The owner must provide the residential contractor with written notice of the construction defect which would form the basis of legal action or arbitration against the residential contractor at least 60 days before filing suit or arbitration.⁵⁰ The notice must

provide the residential contractor with information sufficient to respond to the notice.⁵¹ Filing a mechanic's lien, however, exempts an owner from having to provide the statutorily-required right to cure.⁵²

After receiving notice from the owner, a residential contractor has 21 days to provide the owner with a "good faith" response. This response must contain an offer to do one of the following: (1) Inspect the residential building; (2) Compromise and settle the claim without an inspection; or (3) Dispute the claim.⁵³ If the contractor fails to respond or disputes the claim, the owner is deemed to have complied with this chapter and may commence a lawsuit or arbitration without further notice to the contractor.⁵⁴ The owner is required to reject the contractor's offer, in writing, to inspect, compromise or settle the claim within 14 days, and may thereafter initiate a lawsuit or arbitration.

If, however, the owner accepts the contractor's offer to inspect the building, the owner shall notify the contractor of that acceptance within 14 days and allow the contractor reasonable access to the building during normal working hours.⁵⁵ The contractor must inspect it within 14 days of the owner's acceptance.⁵⁶ If the contractor properly performs the inspection, it must then provide the owner with one of the following within 10 days:

- (1) A written offer to remedy the defects at no cost to the owner, . . . accompanied by an inspection report, a prediction of the additional construction work necessary to remedy each defect, and a timetable for completing the work necessary to remedy the defects.
- (2) A written offer to settle the claims; or
- (3) A written statement asserting that the contractor does not intend to remedy the defects.⁵⁷

If the residential contractor fails to inspect, fails to file a written response or fails to remedy the defect within these times, the owner may commence legal action or arbitration.⁵⁸ Finally, all applicable statutes of limitation or repose are tolled from the time the owner sends a notice of defect to a contractor until the owner complies with this chapter.⁵⁹

Ohio Revised Code Chapter 1311 - Liens

ORC § 1311.11 dictates when an owner may demand that a mechanic's lienholder commence suit, and is discussed in Section I, *supra*.

IV. INSURANCE COVERAGE AND ALLOCATION ISSUES

A. General Coverage Issues

A Commercial General Liability ("CGL") policy may provide a contractor with coverage against claims alleging defective construction. In order to make out a *prima facie* case for coverage under a CGL, a policyholder must show the existence of an "occurrence" and "property damage" as those terms are defined in the policy. Some Ohio Courts held that defective work

does not constitute an “occurrence,”⁶⁰ while others have found that defective construction may potentially meet the definition of “occurrence.”⁶¹

In October 2012, the Ohio Supreme Court addressed this frequently litigated issue in *Westfield Ins. Co. v. Custom Agri Sys., Inc.*, 133 Ohio St. 3d 476 (Ohio 2012). The Court in *Westfield* held that traditional CGL policies do not protect against risk of loss on account of defective construction. The Court determined that a policy holder’s own defective work that caused damage only to the insured’s work did not constitute an occurrence.⁶² However, the Court recognized that coverage does exist for consequential damages that stem from the defective work like personal injury or damage to other property and work.⁶³ In handing down this ruling, the Ohio Supreme Court reinforced the long-standing principle that insurance does not protect against losses attributable to purely “business risks” (i.e. failing to properly perform one’s work).

In *Westfield*, a project owner sued its general contractor based upon alleged defects in the construction of a steel grain bin that was part of a feed-manufacturing plant.⁶⁴ In turn, the general contractor asserted claims against its subcontractor that constructed the bin.⁶⁵ The subcontractor tendered the claim to its insurance carrier and coverage was denied on the basis that the defective construction did not constitute an occurrence under the subcontractor’s policy.⁶⁶ The carrier then sought a declaratory judgment that it had no duty to defend or indemnify the subcontractor under its CGL policy.⁶⁷

The Court’s opinion centered on losses solely attributable to repairing one’s own defective work. According to the Court, workmanship defects do not normally satisfy the definition of an “occurrence” because they are not an “accident.”⁶⁸ Relying on prior precedent, the Court defined “accidental” as an “unintended” or “unexpected” result and concluded that the subcontractor’s defective work was not “fortuitous” and, therefore, not covered by the CGL policy.⁶⁹

In addition to demonstrating an “occurrence,” a policyholder must also establish the existence of “property damage,” which is defined as physical injury to tangible property or loss of use of property that is not physically injured. Once these elements are established, the burden of proof shifts to the insurer to show the applicability of any exclusion contained in the policy. In property damage losses, these exclusions are (i) Damage to Property, (ii) Damage to Your Work and (iii) Damage to Impaired Property or Property Not Physically Injured. If the insurer can prove the applicability of any of these exclusions, or the policyholder fails to establish the existence of an “occurrence” and “property damage” during the policy period, coverage will not be afforded under the policy.

B. Trigger of Coverage

The Ohio Supreme Court has yet to address trigger issues with respect to property damage typically covered by CGL policies. There are, however, four (4) general theories as to how occurrence-based policies are triggered: manifestation, injury-in-fact, exposure and continuous trigger.⁷⁰

Two (2) Ohio appellate courts have held that coverage for property damage is triggered when the property damage first manifests itself.⁷¹ In *Stickle, supra.*, the roof at East High School began leaking shortly after construction and continued for 13 years. The court held that where damage manifests itself immediately following completion of construction and continues unabated into a successive carrier's coverage, there is no "occurrence" under the subsequent policies. Alternatively, where resulting damage does not manifest itself until a new carrier is on the risk, the insurer on the risk when the first visible or discoverable manifestations of damage occur must pay the entire claim.

The manifestation trigger has been questioned by more recent decisions. In *Plum v. Am. Ins. Co.* (1st Dist.), 2006-Ohio-452 at ¶¶ 16-24, the court held that the application of a "continuous-coverage trigger" was more appropriate where the damage did not manifest itself until *after* the policy period at issue. The court found that all policies in effect when property damage occurred were triggered. A different Ohio appellate court reached the same decision in *Westfield Ins. Co. v. Milwaukee Ins. Co.* (12th Dist.), 2005-Ohio-4746 at ¶¶ 11-16. There, the court held "where a structure suffers damage of a continuing nature, coverage must be apportioned between the insurance carriers that insured the property during the course of the damage." Thus, in Ohio, there is support for the application of a continuous trigger for property damage claims.

C. Allocation Among Insurers

When different insurance policies are triggered for the same loss over multiple policy periods, the issue of allocation or apportionment becomes an issue. Classic examples involve environmental clean-up claims, long-term exposure toxic torts and defective construction.

In Ohio, a policyholder is permitted to pick one policy period and secure coverage under that policy up to the limits of those policies, including any excess or umbrella policies. This is called a "targeted tender." Ohio's allocation method is called the "all sums" or joint and several liability approach.⁷² This is the majority approach across the country. The minority approach is "pro rata" which requires each insurer to pay only a portion of the loss "based on the duration of the occurrence during [that insurer's] policy period in relation to the entire duration of the occurrence."⁷³ The pro rata approach divides the loss "horizontally" among all triggered policy periods, with each insurance company paying only a share of the policyholder's total damages.⁷⁴ The "all sums" approach will be used unless the policy at issue contains express language limiting the insurer's liability if the loss continues after the policy period.⁷⁵ The Court's rationale allows an insured to have reasonable expectations of adequate coverage, but allows the insurer to seek contribution from other triggered insurance policies.⁷⁶ Thus, the "all sums" approach effectively shifts the burden to the insurer to recover contribution or include express "pro rata" language in the policy.

When choosing which policy (usually a tower of policies including excess or umbrella policies) to target, a policyholder must consider the policies' limits, any bankruptcies or receiverships in the tower, exhaustion from other covered losses, deductibles or self-insured retentions, and different coverage terms between the various policies. The question then arises how the targeted carriers can seek contribution from the other non-targeted carriers. This

question was left unanswered until the Ohio Supreme Court rendered its decision in *Pa. Gen. Ins. Co. v. Park-Ohio Indus.* (2010), 126 Ohio St.3d 98, 2010-Ohio-2745.

In *Park-Ohio*, the policyholder was sued by an asbestos-claimant and tendered its defense to the targeted carrier. The targeted carrier paid its limits to settle the lawsuit. Approximately two years later, the policyholder provided the targeted carrier with information regarding its non-targeted carriers. The targeted carrier then filed suit against them for equitable contribution. The non-targeted carriers argued that Park-Ohio failed to provide timely notice of the loss in breach of the terms of the policies. The trial court agreed and dismissed the targeted carrier's claim. The Eighth District Court of Appeals, however, reversed finding that the targeted carrier's claim was not based on the non-targeted carriers' policy language, but rather on a theory of equitable contribution per the holding in *Goodyear, supra*. The Ohio Supreme Court agreed.

The critical holdings in *Park-Ohio* are: (1) a policyholder must cooperate with the targeted carrier and identify its other carriers; (2) a targeted carrier is not bound by the notice provisions in the non-targeted policies; and (3) lack of notice to a non-targeted carrier will only bar a targeted carrier's equitable contribution claim if the non-targeted carrier is prejudiced.

V. CONTRACTUAL INDEMNIFICATION

In Ohio, the validity of contractual indemnification agreements in construction contracts are governed by ORC § 2305.31, Ohio's Anti-Indemnity Statute.⁷⁷ The purpose of anti-indemnity statutes is to make construction jobsites as safe as possible by removing a parties' ability to contract away its safety responsibilities. The Ohio statute prohibits indemnity agreements in construction contracts where the promisor (subcontractor or lower-tier contractor) agrees to indemnify the promisee (general contractor or upper-tier contractor) for damages caused by or resulting from the negligence of the promisee (general contractor or upper-tier contractor), regardless of whether such negligence is sole or concurrent.⁷⁸

Ohio is somewhat unique in its application of its anti-indemnity statute. Some Ohio case law suggests that ORC § 2305.31 also prohibits an upper-tier contractor from forcing a lower-tier contractor to name the upper-tier as an additional insured on the lower-tier's commercial general liability policy.⁷⁹ This appears to be the minority position in Ohio.

VI. CONTINGENT PAYMENT AGREEMENTS

A. Enforceability

Contingent payment agreements or clauses that condition payment upon receipt of payment from the owner or another party in the contract privity chain are frequently used in construction contracts in Ohio. These provisions are valid and enforceable, provided that the contract terms are drafted clearly and enforced properly. There are two very distinct contingent payment clauses used in construction contracts, which have vastly different consequences regarding the timing of payments and the parties' collection remedies. The two provisions are commonly referred to as a "pay-when-paid" provision or a "pay-if-paid" provision.

A pay-when-paid clause allows a party, such as a general contractor, to delay payment to its subcontractor for a “reasonable time” if payment for the subcontractor’s work has not been received from the owner.⁸⁰ A typical pay-when-paid clause provides as follows: “General Contractor shall pay Subcontractor within ten days of receipt of payment for Subcontractor who work from the owner.” A pay-when-paid clause represents an unconditional promise to pay a lower tier contractor whereby “the time of payment [is] postponed until the happening of a certain event, or for a reasonable period of time if it develops that such event does not take place.”⁸¹ Thus, the risk of non-payment by the owner falls upon the general contractor. The “reasonable time” period within which a party may withhold payment pursuant to a pay-when-paid clause is not a fixed duration, and will depend on the facts and circumstances of each case. These facts and circumstances will include the efforts made to collect from the owner, the course of conduct or course of dealing between the parties, industry practices or norms regarding typical payment periods, and other relevant evidence.

A pay-if-paid clause, in contrast, allows a party such as the general contractor to avoid payment to its subcontractor if the owner fails or refuses to pay for the subcontractor’s work.

B. Requirements

The requirements for a valid pay-when-paid clause are quite simple. The parties must include a contract provision which states that payment will be made after, or within a certain time period following receipt of payment from the owner.

The requirements for an enforceable pay-if-paid provision are not as simple. In order to invoke the substantial protections of a pay-if-paid clause, at the very least, the parties’ written agreement must (1) be “undeniably clear and unambiguous” regarding the true intent and meaning of the clause, and its intent to shift the risk of non-payment by the owner to a lower tier contractor;⁸² (2) contain language stating that payment from the owner or another third party is an express condition precedent to the payor’s obligation to pay;⁸³ (3) contain language indicating that the lower tier contractor expressly accepts and assumes the risk of the owner’s non-payment.⁸⁴ This language is typically drafted very broadly to include non-payment as a result of bankruptcy, insolvency, or any other reason. In addition, some Ohio Courts have also required that an enforceable pay-if-paid clause state in plain language that a subcontractor must ultimately look to the owner of the project for payment.⁸⁵

A party may be able to challenge the enforcement of a pay-if-paid provision where the owner’s failure or refusal to pay is the direct result of the general contractor’s breach or other conduct that has effectively prevented the occurrence of this condition precedent (e.g., owner payment). The case law relating to this enforcement issue is not as well-developed in Ohio as in other jurisdictions though, so practitioners are advised that the ability to avoid enforcement of a pay-if-paid provision in Ohio is difficult.

While contingent payment clauses are valid and enforceable in Ohio, they cannot be used to prevent a party from perfecting its public or private lien rights, or its payment bond claim remedies. Pursuant to Ohio’s Fairness in Contracting Act, a party may still perfect these

remedies within the time periods set forth in the relevant statutes even if payment is not yet “due and payable” because the general contractor has not received payment from the owner.⁸⁶

VII. DAMAGE LIMITATIONS

A. Personal Injury Damages vs. Construction Defect Damages

In Ohio, the proper measure of damages for a construction defect claim against a contractor is the reasonable cost of placing the building or structure in the condition as intended by the parties at the time they entered into the contract.⁸⁷ The burden of proof is on the party seeking damages, who must prove by a preponderance of the evidence the necessary and reasonable cost to complete the building in accordance with the original contract.⁸⁸ Where the costs of repair would create “economic waste,” the court will use the fair market value test, which measures damages using the fair market value of the structure as it should have been constructed less the value of the imperfect structure.⁸⁹

Compensatory damages for construction tort claims, such as negligent workmanship and construction defects, can also be measured using the fair market value test if the damage to the property is irreparable.⁹⁰ If the damage is susceptible to repair, the landowner may recover the reasonable cost of restoration, plus the reasonable value of the loss of the use of the property.⁹¹ But where restoration of the damaged building is practicable, damages should be the reasonable cost of restoration.⁹²

Damages relating to personal injuries sustained in connection with construction work in Ohio, which are not subject to worker's compensation relief, are subject to Ohio's tort reform, which caps noneconomic damages (e.g., pain and suffering damages, mental anguish, loss of consortium) at three times the economic loss, up to \$350,000, or \$250,000, whichever is higher.⁹³

Ohio's tort reform statutes also: (a) permit judges to reduce awards they deem excessive;⁹⁴ (b) limit punitive damages to no more than double economic damages;⁹⁵ and (c) lower limits on punitive awards against small businesses, capped at double the economic damage or 10 percent of the business net worth up to a maximum of \$350,000, whichever is smaller.⁹⁶ But there are no limits applicable to compensatory damages for personal injuries, such as medical expenses and lost wages.⁹⁷

B. Attorney's Fees Shifting and Limitations on Recovery

Ohio common law typically follows the American Rule regarding recovery of legal fees, i.e. “a prevailing party may not recover attorney fees as costs of litigation in the absence of statutory authority unless the breaching party has acted in bad faith, vexatiously, wantonly, obdurately or for oppressive reasons.”⁹⁸ Ohio's Prompt Payment Act is one statute that provides authority for a claimant to recover attorney fees.⁹⁹ Ohio's Mechanic's Lien Laws includes another such statute that permits a lien claimant to recover attorney fees in a lien foreclosure action.¹⁰⁰

Attorney fee-shifting provisions in a written contract are enforceable in Ohio.¹⁰¹ While some states will permit both parties to benefit from a provision that is worded as unilateral (i.e. only one party may recover fees), Ohio does not do so.¹⁰²

C. Consequential Damages

A party can recover consequential damages in a breach of contract action, but Ohio's courts will enforce contractual provisions that waive such damages, which are typical in the standard agreements within the construction industry.¹⁰³

D. Delay and Disruption Damages

Likewise, a party can recover delay damages absent a contractual provision barring delay damages. But, under Ohio's Fairness in Contracting Act, a "no damage for delay" clause is unenforceable if the cause of the delay is the action or inaction of the party attempting to enforce it.¹⁰⁴

E. Economic Loss Doctrine

Ohio recognizes the Economic Loss Doctrine, which prohibits tort claims for economic loss only (claims that are not arising from personal injury or property damage), and will ordinarily prohibit claims between non-contracting parties that arise in tort. The Ohio Supreme Court most recently addressed the issue of tort claims in the construction area as follows:

Tort law is not designed to compensate parties for losses suffered as a result of a breach of duties assumed only by agreement. That type of compensation necessitates an analysis of the damages which were within the contemplation of the parties when framing their agreement. It remains the particular province of the law of contracts.¹⁰⁵

When construing the validity of a negligence claim against a design professional in the construction context, the Ohio Supreme Court held:

In the absence of privity of contract between two disputing parties, the general rule is there is no *** duty to exercise reasonable care to avoid intangible economic loss or losses to others that do not arise from tangible physical harm to persons and tangible things.¹⁰⁶

The Court further noted that duties on construction projects "[a]re governed by the contracts related to the construction project. While such a duty may be imposed by contract, no common law duty requires [one party] to protect [another] from purely economic loss."¹⁰⁷ Given the policy considerations underlying tort law, the Ohio Supreme Court unequivocally concluded "that recovery for economic loss is strictly a subject of contract negotiation and assignment. Consequently, in the absence of privity of contract, no cause of action exists in tort to recover economic damages against design professionals involved in drafting plans and specifications."¹⁰⁸

F. Interest

Absent a contractual provision or statute providing otherwise, claimants are entitled to the legal rate of interest established each year by the tax commissioner¹⁰⁹ for pre-judgment interest from the date the money “becomes due and payable.”¹¹⁰ The statutory rate for 2011 was 4%, and decreased in 2012 to 3%. The rate remained at 3% for 2013, and continues at 3% in 2014.¹¹¹

Ohio's Prompt Payment Act provides a penalty interest rate of 18%, which begins to accrue on the eleventh day of a general contractor's receipt of payment from the owner or subcontractor's receipt of payment from the general contractor.¹¹²

G. Punitive Damages

Punitive damages are available where there is proof of actual damages and a finding of “actual malice.”¹¹³ “The purpose of punitive damages is not to compensate a plaintiff, but to punish and deter certain conduct.”¹¹⁴ Actual malice necessary for an award of punitive damages can be found when there is either (1) a state of mind from which a person's conduct is characterized by hatred, ill will, or revenge, or (2) a conscious disregard for the rights and safety of others that has a great possibility of causing substantial harm.¹¹⁵

VIII: CASE LAW UPDATE AND LEGISLATIVE UPDATE

Statutory Updates:

Updates to Ohio Utility Protection Laws

In March 2013, Substitute House Bill 458, updating Ohio’s utility protection laws, went into effect. Codified at ORC 3781.25 *et seq.*, highlights of the updates include:

- Each utility owner that is a member of OUPS (Ohio Utility Protection Service) must participate in an automated “positive response system where, through OUPS, a utility owner is required to communicate directly to the excavator when there is a conflict between the proposed work and the utility owner’s infrastructure.” ORC §3781.26(D).
- Any excavator, contractor or utility owner that uses OUPS must be trained in underground utility protection. However, membership to OUPS or a “statewide association representing excavators” that provides training in underground utility protection sufficiently meets this requirement. ORC §3781.261.
- A utility owner has the option of either marking the utilities in the field, or providing digital or paper drawings that are drawn to scale and include locatable items, such as poles, curbs, sidewalks, etc. ORC §3781.27(C).

- If the utility owner makes no marks within 48 hours, then the utility company is deemed to have given notice that it does not have any facilities at the excavation site. ORC § 3781.29(A)(1).
- Unless a utility is uncovered or probed by the utility or excavator, any indications of the depth of the utility shall be treated as estimates only. ORC §3781.29(B).
- If the excavation will cover a large area and will progress over areas over time, the excavator must give the utility owner written notice of its work, including scheduling information. ORC §3781.28.
- Prior to calling into a request for marking, an excavator must premark the excavation area with white paint, flags, stakes or other approved methods, unless:
 - the utility can determine the precise location, direction, size and length of the proposed excavation based on info given by the excavator;
 - when the excavator and the affected utility have had an on-site pre-construction meeting for the purpose of pre-marking the excavation site;
 - the excavation involves replacing a pole that is within five feet of the location of an existing pole; and
 - pre-marking would clearly interfere with pedestrian or vehicular traffic control.

ORC § 3781.29(D).

Case Law:

Application of Governmental Immunity

In *Coleman v. Portage County Engineer*, 133 Ohio St.3d 28 (2013), the Ohio Supreme Court determined that government immunity applies to failure to upgrade an existing sewer. In reaching its decision, the court noted the difference between a failure to maintain or repair a sewer (for which a governmental entity is not immune to liability) versus a failure to upgrade a sewer (for which a governmental entity is immune). Because the homeowners could not identify any particular part of the sewer system that was broken or allegedly not maintained or repaired, government immunity did not apply. Additionally, the court found the four year statute of limitations barred the homeowners' claims.

Likewise, in *State ex rel. Rohrs v. Germann*, 2013-Ohio-2497 (3rd Dist.), the Third Appellate District extended immunity to the Henry County Engineer relative to damage caused by a failed drainage improvement project. The *Germann* court found that because the purpose of the drainage improvement project was to redesign and reconstruct the existing drainage system, and to improve the safety of a county road, the project was a "governmental function." Under Ohio law, political subdivisions are immune from liability for "governmental functions." Thus, the county engineer was not responsible for damages related to drainage failures.

Arbitration Clause Applies To All Project Claims

The Ohio Twelfth Appellate District determined that an arbitration clause contained in one project document may extend to claims arising from other documents related to the same work. In *Gaffin v. Schumacher Homes of Cincinnati, Inc.*, 2013-Ohio-992 (12th Dist.), the contract agreement (the “Agreement”) included an arbitration clause, but the contract “Scopes of Work” did not. The plaintiff sued on the “Scopes of Work” only, and asserted the arbitration provision therefore did not apply. The court disagreed. Because the parties signed both documents on the same date, because the Agreement indicated the Scopes of Work was attached (even though it actually was not), and because the Agreement repeatedly referenced the “Scope of Work” throughout, the court determined the Scopes of Work was clearly incorporated in the Agreement. Thus, the arbitration provision in the Agreement required the parties to arbitrate.

Six-Year Statute of Limitations On A Public Lien Begins When The Cause Of Action Accrues, Not When the Lien is Filed

In *Akron v. Concrete Corp. v. Board of Educ. for the Medina City Sch. Dist.*, 2012-Ohio-2917 (9th Dist.), a subcontractor filed an attested account claim (lien on public funds). The general contractor did not dispute the claim, and, indeed, consented to the subcontractor’s claim. Disputes thereafter arose between general contractor and the owner school district, which the school district settled by issuing a payment to the general contractor from the public fund. The subcontractor was not involved in the disputes, nor in the ensuing litigation and settlement, and never consented to any payment out of the public fund. At the time the school district made the settlement payment, the subcontractor’s lien still remained in place against the fund.

The subcontractor filed suit to foreclose its public lien. The school district moved to dismiss pursuant to the ORC § 2305.07 6-year statute of limitations, asserting that the limitations period commences on the date the lien is filed. The motion to dismiss was denied, and the school district appealed. The appellate court upheld the trial court’s decision by finding that the cause of action accrued when the school district violated the public lien by disbursing public to the general contractor, in violation of the subcontractor’s lien. As the disbursement fell within the 6-year statute of limitations, the subcontractor’s claim was not time-barred.

A Public Authority Has Broad Discretion In Determining a Bidder’s Responsibility

In *State of Ohio ex re. Glidepath, LLC v. Columbus Reg’l Airport Auth.*, 2012-Ohio-20 (10th Dist.), a company’s bid on a public airport project was rejected, despite being the lowest bidder. The public authority determined that the bidder was “non-responsible,” which the bidder challenged. Specifically, the public authority had concerns with the bidder’s special purpose audits, financial statements, a Dun & Bradstreet report, the proposed project manager’s lack of qualifications, and “off-the record” comments it heard about the bidder’s performance.

The court upheld the public authority’s determination, pursuant to ORC § 9.312, which permitted the public authority to reject a bid based upon financial responsibility, conduct and performance on prior contracts, and management skills. The court recognized that the bid process is based upon information that is subjective, and open to interpretation. Provided the public authority uses sound logic and reasoning within the confines of ORC § 9.312 when making a determination, a public authority has broad discretion in awarding a bid.

¹ This section of the ALFA Construction Law Compendium was prepared with the valuable assistance of Rick L. Amburgey, Jr., Daniel Bollinger, Melissa A. Jones and Allison E. Taller, associates in Frantz Ward LLP's Construction Practice Group.

² *Lee Turzillo Contracting Co. v. Cincinnati Metropolitan Housing Authority*, 10 Ohio St. 2d 5, 225 N.E.2d 255 (1967).

³ ORC § 1311.04(B)(10).

⁴ ORC § 1311.04(A)(1).

⁵ ORC § 1311.04(D).

⁶ ORC § 1311.252.

⁷ ORC § 1311.252A.

⁸ ORC § 1311.05(A).

⁹ ORC § 1311.05(H).

¹⁰ ORC § 1311.05(A).

¹¹ ORC § 1311.261.

¹² ORC § 1311.261(A)(1).

¹³ ORC § 1311.05 & ORC § 1311.261(A)(1).

¹⁴ *Halsey, Inc. v. Isbel*, 12th Dist. Warren No. CA2009-12-159, 2010-Ohio-2052 (NOF served one day prior to lien claimant's first date of project work rendered invalid, which, in turn, invalidated the mechanic's lien).

¹⁵ ORC § 1311.261(A)(2).

¹⁶ ORC § 1311.19.

¹⁷ ORC § 1311.05(G) & ORC § 1311.261(F).

¹⁸ ORC § 1311.06.

¹⁹ ORC § 1311.07.

²⁰ ORC § 1311.26.

²¹ ORC § 1311.26.

²² ORC § 1311.29; *B.F. Sturtevant Co. v. Board of Education of City School District of Cincinnati*, 51 Ohio App. 348, 1 N.E.2d 148 (1st Dist. 1935).

²³ ORC § 1311.28.

²⁴ ORC § 1311.31.

²⁵ *Id.*

²⁶ *Id.*

²⁷ ORC § 1311.311.

²⁸ *Id.*

²⁹ *Id.*

³⁰ *Id.*

³¹ ORC § 1311.11.

³² ORC § 1311.13.

³³ ORC § 1311.16.

³⁴ *Portsmouth Iron Co. v. Murray*, 38 Ohio St. 323 (1882); *J. J. Hammond Co. v. Jent Constr. Inc.*, 10th Dist. Franklin No. 74AP-19, 1974 Ohio App. LEXIS 3563 (May 28, 1974); *Steveco, Inc. v. C&G Inv. Assoc.*, 10th Dist. Franklin No 77AP-101, 1977 Ohio App. LEXIS 7341 (August 4, 1977).

³⁵ ORC § 1311.011(B)(1).

³⁶ ORC § 2305.06.

³⁷ ORC § 2305.07.

³⁸ ORC § 2305.07.

³⁹ ORC § 1302.98(A).

⁴⁰ ORC § 2305.09.

⁴¹ ORC § 2305.10.

⁴² ORC § 1311.13(C).

⁴³ ORC § 1302.98(A).

⁴⁴ *Flagstar Bank, FSB v. Airline Union's Mortgage Co.*, 128 Ohio St. 3d 529, 2011-Ohio-1961, 947 N.E.2d 672, ¶ 14; *see also* *Sexton v. City of Mason*, 117 Ohio St. 3d 275, 2008-Ohio-858, 883 N.E.2d 1013, ¶ 53.

⁴⁵ *Flagstar* at ¶ 19.

⁴⁶ *See Harris v. Liston*, 86 Ohio St.3d 203, 714 N.E.2d 377 (1999) (upholding application of discovery rule in negligence claim by subsequent homeowner against builder/developer); *Velotta v. Leo Petronzio Landscaping, Inc.*, 69 Ohio St.2d 376, 433 N.E.2d 147 (1982) (upholding application of discovery rule in negligent workmanship claim against builder).

⁴⁷ ORC § 2305.131(A)(1); *see also Tutolo v. Young*, 11th Dist. Lake No. 2010-L-118, 2012-Ohio-121.

⁴⁸ ORC § 2305.131(G).

⁴⁹ ORC § 2305.131(A)(2).

⁵⁰ ORC § 1312.04(A).

⁵¹ ORC § 1312.04(B).

⁵² ORC § 1312.04(D).

⁵³ ORC § 1312.05(A).

⁵⁴ ORC § 1312.05(B).

⁵⁵ ORC § 1312.06(A).

⁵⁶ *Id.*

⁵⁷ ORC § 1312.06(B).

⁵⁸ ORC § 1312.06(C).

⁵⁹ ORC § 1312.08(A).

⁶⁰ *Heile v. Herrmann* (Hamilton 1999), 136 Ohio App.3d 351, 736 N.E.2d 566; *Westfield Ins. Co. v. Riehle* (Williams 1996), 113 Ohio App.3d 249, 680 N.E.2d 1025; *Paramount Parks, Inc. v. Admiral Ins. Co.*, Warren App. No. CA2007-05-066, 2008-Ohio-1351; *Westfield Ins. Co. v. R.L. Diorio Custom Homes, Inc.*, Warren App. No. CA2009-09-12, 2010-Ohio-1007.

⁶¹ *Dublin Building Systems v. Selective Ins. Co. of America*, Franklin App. No. 06AP-213, 2007-Ohio-494; *Spears v. Smith* (Montgomery 1996), 117 Ohio App.3d 262, 690 N.E.2d 557; *United Steel Fabricators, Inc. v. Fid. & Guar. Ins. Underwriters, Inc.* (March 11, 1993), Franklin App. 92AP-1171, 1993 Ohio App. LEXIS 1422; *Bundy Tubing Co. v. Royal Indemn. Co.* (6th Cir. 1962), 298 F.2d 151; and *Ohio Cas. Ins. Co. v. Hanna*, Medina App. Nos. 07CA0016-M and 07CA0017-M, 2008-Ohio-3203.

⁶² *Id.* at 484.

⁶³ *Id.* at 480.

⁶⁴ *Id.* at 477.

⁶⁵ *Id.*

⁶⁶ *Id.*

⁶⁷ *Id.*

⁶⁸ *Id.* at 481.

⁶⁹ *Id.*

⁷⁰ *See GenCorp, Inc. v. AIU Ins. Co.* (N.D. Ohio 2000), 104 F.Supp.2d 740, 743-752.

⁷¹ *Cleveland Bd. of Ed. v. R.J. Stickle Int'l* (Cuyahoga 1991), 76 Ohio App.3d 432, 437; *Reynolds v. Celina Mut. Ins. Co.* (Feb. 16, 2000), 9th Dist. 98CA007268, 2000 Ohio App. LEXIS 517 at *9.

⁷² *Goodyear Tire & Rubber Company v. Aetna Casualty & Surety Company* (2002), 95 Ohio St. 3d 512, 2002-Ohio- 2842.

⁷³ *Id.*

⁷⁴ *Id.* (internal citation omitted).

⁷⁵ *Id.*

⁷⁶ *Id.*

⁷⁷ ORC § 2305.31 states: “A covenant, promise, agreement, or understanding in, or in connection with or collateral to, a contract or agreement relative to the design, planning, construction, alteration, repair, or maintenance of a building, structure, highway, road, appurtenance, and appliance, including moving, demolition, and excavating connected therewith, pursuant to which contract or agreement the promisee, or its independent contractors, agents or employees has hired the promisor to perform work, purporting to indemnify the promisee, its independent contractors, agents, employees, or indemnities against liability for damages arising out of bodily injury to persons or damage to property initiated or proximately caused by or resulting from the negligence of the promisee, its independent contractors, agents, employees, or indemnities is against public policy and is void. Nothing in this section shall prohibit any person from purchasing insurance from an insurance company authorized to do business in the state of Ohio for his own protection or from purchasing a construction bond.”

⁷⁸ *Kendall v. U.S. Dismantling Co.* (1985), 20 Ohio St.3d 61, 485 N.E.2d 1047; *Kemmeter v. McDaniel Backhoe Serv.* (2000), 89 Ohio St.3d 409, 2000-Ohio-209.

⁷⁹ *Buckeye Union Ins. Co. v. Zavarella Bros. Constr. Co.* (Cuyahoga 1997), 121 Ohio App.3d 147, discretionary appeal not allowed by 80 Ohio St.3d 1449 (requirement by contractor that subcontractor name contractor as additional insured on its insurance policy was void as violating ORC § 2305.31); *Liberty Mut. Ins. Group v. Travelers Prop. Cas.* (8th Dist.), 2002-Ohio-4280, appeal not accepted for review by 98 Ohio St.3d 1410; *Waddell v. LTV Steel Co., Inc.* (Cuyahoga 1997), 124 Ohio App.3d 350, discretionary appeal not allowed by 81 Ohio St.3d 1457; *C.J. Mahan Constr. Co. v. Mohawk Re-Bar Serv., Inc.* (5th Distr.), 2005-Ohio-5427, discretionary appeal not allowed by 108 Ohio St.3d 1489, 2006-Ohio-962; *see also J&L Specialty Steel, Inc. v. Hammond Constr., Inc.* (Aug. 11, 1997), Stark App. No. 1996CA00370, *unreported* (summary judgment granted to subcontractor affirmed where indemnity agreement purported to indemnify property owner from its sole or joint negligence); *Toledo Edison v. P & W Painting and Sandblasting Co., Inc.* (Sept. 11, 1992), Lucas App. No. L-91-412, *unreported* (as indemnity agreement was void on its face there was no need to analyze its application to the underlying facts; summary judgment affirmed) and *Toledo Edison Co. v. Henry Gurtzweiler, Inc.* (Feb. 8, 1991), Lucas App. No. L-89-366, *unreported* (same), *but cf. Danis Building Construction Co. v. Employers Fire Ins. Co.* (2nd Dist.), 2002-Ohio-6374, appeal not accepted for review by 98 Ohio St.3d 1512 and *Brzeczek v. Standard Oil Co.* (Lucas 1982), 4 Ohio App.3d 209 (requirement to name upper-tier contracting partner as an additional insured on lower-tier’s insurance policy not a violation of Ohio’s Anti-Indemnity statute).

⁸⁰ *Chapman Excavating Co., Inc. v. Fortney & Weygandt, Inc.*, 8th Dist. Cuy. County No. 84005 2004-Ohio-3867 at P23-24; *Power Pollution Serv., Inc. v. Suburban Power Piping Corp.*, 74 Ohio App. 3d 89, 91, 598 N.E.2d 89 (8th Dist. 1991); *The Thos. J. Dyer Co. v. Bishop Int'l Engineering Co.*, 303 F.2d 655, 661, 21 Ohio Op. 2d 235 (6th Cir. 1962).

⁸¹ *Id.*

⁸² *Power Pollution Serv., Inc. v. Suburban Power Piping Corp.*, 74 Ohio App. 3d 89, 91, 598 N.E.2d 89 (8th Dist. 1991); *Kalkreuth Roofing & Sheet Metal, Inc. v. Bogner Construction Co.*, 1998 Ohio App. LEXIS 4694 at *6, 1998 WL 666765 (5th Dist. 1998); *Transtar Elec. v. A.E.M. Elec. Servs. Corp.*, 6th Dist. No. L-12-1100, 2012-Ohio-5986 at P 29, 983 N.E.2d 399

⁸³ *The Thos. J. Dyer Co. v. Bishop Int'l Engineering Co.*, 303 F.2d 655, 661, 21 Ohio App. 2d 235 (6th Cir. 1962); *Transtar Elec. v. A.E.M. Elec. Servs. Corp.*, 6th Dist. No. L-12-1100, 2012-Ohio-5986 at P 30, 983 N.E.2d 399.

⁸⁴ *Transtar Elec. v. A.E.M. Elec. Servs. Corp.*, 6th Dist. No. L-12-1100, 2012-Ohio-5986 at P 29-30, 983 N.E.2d 399.

⁸⁵ *Transtar Elec. v. A.E.M. Elec. Servs. Corp.*, 6th Dist. No. L-12-1100, 2012-Ohio-5986 at P 30, 983 N.E.2d 399 The Ohio Appellate District Courts are currently split as to what requirements are necessary to construe a contingent payment agreement as a pay-if-paid provision, rather than a pay-when-paid provision. The Districts agree that an enforceable pay-if-paid clause clearly and unambiguously state that payment from the owner is a condition precedent to payment to the subcontractor and that the subcontractor assumes the risk of owner non-payment, but differ on what, if anything, beyond this is required. The Ohio Supreme Court accepted an appeal considering this issue for review on March 27, 2013. *Transtar Elec., Inc. v. A.E.M. Elec. Servs. Corp.*, 134 Ohio St. 3d 1507, 984 N.E.2d 1101, 2013-Ohio-1123.

⁸⁶ ORC §4113.62 (E).

⁸⁷ *Jones v. Honchell*, 14 Ohio App.3d 120, 470 N.E.2d 219, syll ¶3 (12th Dist. 1984).

⁸⁸ *Id.*

⁸⁹ *Stackhouse v. Logangate Property Mgmt.*, 172 Ohio App. 3d 65, 2007-Ohio-3171, 872 N.E.2d 1294, ¶53 (7th Dist.).

⁹⁰ *Id.*

⁹¹ *Id.* at ¶ 54, citing *Ohio Collieries Co. v. Cocke*, 107 Ohio St. 238, 240, 140 N.E. 356 (1923).

⁹² *Id.* at ¶ 55, citing *Northwestern Ohio Natural Gas v. First Congressional Church of Toledo*, 126 Ohio St. 140, 150, 184 N.E. 512 (1933); *see also Marsilio v. Brian Bennett Constr.*, 7th Dist. Mahoning No. 06 MA 180, 2008-Ohio-5049.

⁹³ *See* ORC § 2315.18(B) (unless the injury constitutes as “catastrophic” under the statute); *see also Faieta v. World Harvest Church*, 147 Ohio Misc. 2d 51, 2008-Ohio-3140, 891 N.E.2d 370 (C.P.).

⁹⁴ ORC § 2315.19(A).

⁹⁵ ORC § 2315.21(D)(2)(a).

⁹⁶ *Id.* at (D)(2)(b).

⁹⁷ ORC § 2315.18(B)(1).

⁹⁸ *Gahanna v. Eastgate Properties, Inc.*, 36 Ohio St. 3d 65, 66, 521 N.E.2d 814 (1988).

⁹⁹ ORC § 4113.61(B)(1).

¹⁰⁰ ORC § 1311.16.

¹⁰¹ *Nottingdale Homeowners' Assoc. v. Darby*, 33 Ohio St. 3d 32, 33, 514 N.E.2d 702 (1987); *see also Buckeye Check Casing, Inc. v. Madison*, 8th Dist. Cuyahoga No. 90861, 2008-Ohio-5124, ¶ 24.

¹⁰² *GMS Management Co. v. K & K Industries, Inc.*, 5th Dist. Stark No. CA 8279, 1991 Ohio App. LEXIS 2036 (April 29, 1991) (a unilateral attorney’s fees clause is enforceable as long as fees awarded are fair, just and reasonable).

¹⁰³ *See Nottingdale* at 36 (“persons have a fundamental right to contract freely with the expectation that the terms of the contract will be enforced”).

¹⁰⁴ ORC § 4113.62.

¹⁰⁵ *Corporex Dev.’t & Constr. Mngt., Inc. v. Shook, Inc.*, 106 Ohio St. 3d 412, 413, 2005-Ohio-5409, 835 N.E.2d 701 (owner's claims directly against subcontractor were properly dismissed due to the absence of contractual privity).

¹⁰⁶ *Floor Craft Floor Covering, Inc. v. Parma Community General Hosp. Assoc.*, 54 Ohio St. 3d 1, 3, 560 N.E.2d 206 (1990).

¹⁰⁷ *Id.* at 4.

¹⁰⁸ *Id.* at 8.

¹⁰⁹ ORC § 5703.47.

¹¹⁰ ORC § 1343.03.

¹¹¹ For a list of the current year's rate, and all rates from the year 1983 to the present, go to http://www.tax.ohio.gov/ohio_individual/individual/interest_rates.aspx.

¹¹² ORC § 4113.61.

¹¹³ *See Moskowitz v. Mt. Sinai Medical Ctr.*, 69 Ohio St. 3d 638, 635 N.E.2d 331 (1994).

¹¹⁴ *Id.* at 651.

¹¹⁵ *Preston v. Murty*, 32 Ohio St.3d 334, 512 N.E.2d 1174 (1987).

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I. MECHANIC'S & MATERIALMEN'S LIEN BASICS

Oklahoma Statute Title 42, §§ 141–154 govern the procedure to invoke and the enforceability of mechanic's and materialmen's liens filed against private property.

A. Notice for Owner Occupied Dwellings. In 2011 Oklahoma repealed its statute requiring presentment of pre-construction lien notices to homeowners.

B. Pre-Lien Statement. A pre-lien statement only has to be filed when the claimant is a sub-contractor, not an original contractor (an original contractor is someone who contracts with the property owner), and the material or services are performed on a commercial property (exception: if it is a residential property and has more than five (5) dwelling units a subcontractor must provide a pre-lien statement). A pre-lien statement is not required for a subcontractor who is performing work upon a residential property (single family or less than five (5) dwelling units) or if the aggregate claim is less than \$10,000. The pre-lien statement must contain: (1) a statement that the notice is a pre-lien notice; (2) the complete name, address, and telephone number of the claimant, or the claimant's representative; (3) the date material, services, labor, or equipment was supplied; (4) a description of the material, services, labor, or equipment; (5) the name and last-known address of the person who requested that the claimant provide the material, services, labor, or equipment; (6) the address, legal description, or location of the property to which the material, services, labor, or equipment has been supplied; (7) a statement that the dollar amount of the material, services, labor, or equipment furnished or to be furnished exceeds Ten Thousand Dollars (\$10,000.00); and (8) the signature of the claimant, or the claimant's representative.¹

C. Lien Statement. The lien statement is the document filed in order to obtain a lien. You must file a lien statement at the county clerk's office in the county where the property is located. The lien statement must set forth (1) the amount claimed; (2) the name of the property owner; (3) the name of the contractor; (4) the name of the claimant; and (5) the legal description of the

property. *The lien statement must be verified by affidavit.* The lien statement must be filed within four (4) months of the date when material or equipment was used on said land or last furnished or labor last performed if the claimant is a general contractor.² If the claimant is a subcontractor, the lien statement must be filed within 90 days of the date when material or equipment was used on said land or last furnished or labor last performed.³ The county clerk mails notice of the lien to the interested parties.⁴ When work under the original contract has been completed, the performance of repairs does not extend the time to file a lien statement.⁵

D. Foreclosure. A civil lawsuit must be brought on a mechanic's and materialmen's lien within one (1) year after the lien accrues.⁶ If not, the lien is unenforceable.

E. Sale. In all cases where judgment may be rendered in favor of any person or persons to enforce a lien, the real estate or other property shall be ordered to be sold as in other cases of sales of real estate to satisfy the judgment.⁷

II. STATUTES OF LIMITATION AND REPOSE

A statute of limitation starts to run when the cause of action occurs, i.e., the date of the injury or the date the contract is completed. A statute of limitation limits the time period whereby a person may pursue a remedy. Whereas, a statute of repose is a time period which limits the time within which a party may acquire a cause of action, i.e., the date of injury cannot be more than 10 years after the construction project was completed.

A. Statute of Limitations. The Oklahoma statute of limitations period for a construction defect based on a written breach of contract is five (5) years, or three (3) years for an oral breach of contract. The period begins to run when the home or project is completed.⁸ The Oklahoma Supreme Court, in *Jaworsky v. Frolich*, expressly rejected the argument that the statute of limitations begins to run at the time the defect is discovered.⁹ On the other hand, the Oklahoma statute of limitations period for a construction defect based on tort is two (2) years. The two (2) year statute of limitations period starts to run when the Plaintiff is vested with a cause of action, i.e., at the time the Plaintiff knows, or should know in the exercise of due diligence, of the injury.

B. Statute of Repose. The statute of repose period for a tort alleging a construction defect is ten (10) years after substantial completion of improvements on the property.¹⁰

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

In the residential property context, a contract for the construction of a new residence or for an alteration of, repair of, or addition to an existing residence may include provisions which: (1) Require a homeowner, prior to filing a lawsuit for construction defects, present to the contractor a written notice of construction defects; and (2) allow the contractor to inspect any construction defects and present to the homeowner a written response which shall include the contractor's

offer to repair the defects or compensate the homeowner for such defects within thirty (30) days after receipt of the notice of defects.

If the above mentioned provisions are included in a contract, the homeowner shall not file a lawsuit against the contractor until the conditions precedent have been fulfilled. In the event the homeowner files a lawsuit against the contractor without fulfilling the conditions precedent, the contractor shall be entitled to a stay of proceedings until such conditions have been fulfilled. If the conditions precedent have been fulfilled, the homeowner may seek remedies against the contractor as provided by law.¹¹

IV. COVERAGE AND ALLOCATION ISSUES

A commercial general liability (CGL) policy provides insurance coverage for covered perils which occur during the policy period. In certain situations, a separate professional liability policy may cover the same loss as well, *i.e.*, an error and omissions policy. Where there are multiple CGL policies covering different time frames, it must be determined which policy covers the loss. The paramount questions is: “When did the injury occur coupled with the type of policy?”

Under a “claims made” liability insurance policy, coverage is only triggered when, during the policy period, an insured becomes aware of *and* notifies his or her insurer of either claims against the insured or occurrences that might give rise to such claim.¹² Notice of a claim must be made to the insurer during the policy period. An “occurrence” liability policy allows for notice to be made after the term of the insurance contract, so long as the insurable event occurred during the term of coverage.¹³ It is very important to know what type of policy you possess. You need to make sure that your CGL policy is tailored so that it will provide you the proper coverage.

A “Completed Operations Hazard” endorsement insures a contractor against accidents which occur during the policy period, but after the completion of a project. Such a provision is important to possess if your CGL is project specific. Even under a “Completed Operations Hazard” endorsement in a policy providing coverage for a specific construction project, an insurer will restrict the coverage to occurrences during the policy period, and thus, no coverage will be afforded for a loss occurring after the policy period expires.¹⁴

V. CONTRACTUAL INDEMNIFICATION

Oklahoma does not allow indemnification in construction contracts that require an entity to indemnify another entity against liability for damage arising out of death or bodily injury to persons, or damage to property, which arise out of the negligence or fault of the indemnitee, its agents, representatives, subcontractors, or suppliers, because such indemnification is considered void and unenforceable as against public policy.¹⁵

However, a construction contract may require an entity to indemnify another entity against liability for damage arising out of death or bodily injury to persons, or damage to property, but such indemnification *shall not exceed* any amounts that are greater than that represented by the degree or percentage of negligence or fault attributable to the indemnitor, its agents, representatives, subcontractors, or suppliers.¹⁶

VI. DAMAGE LIMITATIONS

A. Attorneys' Fees. In an action brought to enforce any lien the party for whom judgment is rendered shall be entitled to recover reasonable attorneys' fees, to be fixed by the court, which shall be taxed as costs in the action.¹⁷ A prevailing party may be awarded its reasonable attorneys' fees, to be taxed as costs, for a suit predicated on breach of an express warranty and in a civil action to recover for labor or services rendered or for a contract relating to the purchase or sale of goods or merchandise.¹⁸ Moreover, an Oklahoma court will enforce a contract provision which grants the prevailing party attorneys' fees.

B. Consequential Damages. Recovery for a breach of contract is generally limited to consequential damages. Consequential damages are damages naturally flowing from the contract breach or damages that were reasonably contemplated as probable at the time the contract was executed. Such damages can include expenses due to a party's failure to perform in a workmanlike manner, costs to settle with the owner for a subcontractor's breach, excess costs, loss of use, and lost profits which are reasonably ascertainable.¹⁹

C. Delay and Disruption Damages. Delay and disruption damages are collectable and the prevailing party may be awarded actual costs, escalation costs in materials and labor, overhead, and profits.²⁰

D. Interest. A prevailing party is entitled to collect prejudgment interest on the amount of the obligation in a breach of contract suit, starting from the time he or she is vested with the right to recover.²¹ A prevailing party may collect prejudgment interest for personal injuries. In a personal injury action, the prejudgment interest starts accruing when the lawsuit is filed.²² In addition, a prevailing party may collect post judgment interest.²³ Post Judgment interest accrues from the earlier of the date the judgment is rendered or the date the judgment is filed with the court clerk. For 2012, the prejudgment interest rate was 5.25% and that post judgment interest in Oklahoma was 0.05%. For 2013, the post judgment interest rate was 5.25%. For January 1, 2013 through June 30, 2013, the pre-judgment rate is 5.25%, July 1, 2013 through October 31, 2013 is 5.25% and November 1, 2013 through the first business day of January, 2014 is 0.09%. For 2014, pre-judgment interest is 5.25% and post judgment interest is 0.05%.

E. Punitive Damages. Punitive damages are damages imposed to punish a defendant. At the very least, punitive damages are not allowed unless there is clear and convincing evidence the defendant recklessly disregarded the rights of others. "Reckless disregard" is beyond mere negligence and "clear and convincing evidence" is beyond a preponderance of the evidence, i.e., evidence which provides higher proof than more likely than not. Punitive damages, if awarded, fall into one of three categories. Category I involves "reckless disregard, and damages are

limited to the greater of \$100,000 or the amount of actual damages awarded. Category II damages involve intentional and malicious actions, and damages cannot exceed the greater of \$500,000, twice the amount of actual damages awarded, or the increased financial benefit derived by the defendant as a direct result of the conduct. Category III involves intentional, malicious and life-threatening actions, and has no limitation on the amount of punitive damages. Generally, punitive damages are not allowed in a breach of contract action.²⁴

¹ *Okla. Stat. tit. 42, § 142.6.*

² *Okla. Stat. tit. 42, § 142.*

³ *Okla. Stat. tit. 42, § 143.*

⁴ *Okla. Stat. tit. 42, § 143.1.*

⁵ *H.E. Leonhardt Lumber Co. v. Ed Wamble Distributing Co.*, 378 P.2d 771, 774 (Okla. 1963).

⁶ *Okla. Stat. tit. 42, § 149.*

⁷ *Okla. Stat. tit. 42, § 175* (Priority of mechanic's and materialmen's liens is fact specific and rather complicated, thus, priority of such is beyond the scope of this summary).

⁸ *Jaworsky v. Frolich*, 850 P.2d 1052 (Okla. 1992); *Okla. Stat. tit. 12, § 95.*

⁹ *Frolich*, 850 P.2d at 1054.

¹⁰ *Okla. Stat. tit. 12, § 109; Frolich*, 850 P.2d at 1054.

¹¹ *Okla. Stat. tit. 15, § 765.6.*

¹² *State ex rel. Crawford v. Indemnity Underwriters Ins. Co.*, 943 P.2d 1099 (OK CIV APP 1997).

¹³ *Id.*

¹⁴ *Harbour v. Mid-Continent Cas. Co.*, 752 P.2d 258 (OK CIV APP 1987).

¹⁵ *Okla. Stat. tit. 15, § 221(B).*

¹⁶ *Okla. Stat. tit. 15, § 221(C).*

¹⁷ *Okla. Stat. tit. 42, § 176.*

¹⁸ *Okla. Stat. tit. 12, § 939; Okla. Stat. tit. 12, § 936.*

¹⁹ "For the breach of an obligation arising from contract, the measure of damages, . . ., is the amount which will compensate the party aggrieved for all the detriment proximately caused thereby, or which, in the ordinary course of things, would be likely to result therefrom. No damages can be recovered for a breach of contract, which are not clearly ascertainable in both their nature and origin. *Okla. Stat. tit. 23, § 21.*

²⁰ *Ralph D. Nelson Co., Inc. v. Beil*, 671 P.2d 85 (OK CIV APP 1983).

²¹ *Okla. Stat. tit. 23, § 22.*

²² *Okla. Stat. tit. 12, § 727.1(E).*

²³ *Okla. Stat. tit. 12, § 727.1(A)(1).*

²⁴ *Okla. Stat. tit. 23, § 9.1.*

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I. CONSTRUCTION LIEN BASICS

A. Pre-Claim Notices

Oregon statutes require certain contractors to provide one or more notices to property owners prior to perfecting – or recording – a construction lien on the owner of property.

1. Notice of Right to Lien

In order to later file a lien, a contractor who works on a residential improvement, and is not hired directly by the owner of the improvement, must provide a Notice of Right to Lien to the owner.¹ The term “owner” includes lessees, as well as fee simple owners. Where multiple owners exist, a contractor should send notices to all owners to ensure its lien rights are preserved.

The notice should be sent as soon as possible after the contractor begins providing labor, materials, services or equipment. Where a Notice of Right to Lien is required, a contractor’s lien is perfected only as to those services or materials provided “after a date which is eight days, not including Saturdays, Sundays and other holidays * * *, before the notice is delivered or mailed.”² A Notice is therefore only retroactively effective as to work performed within eight days of the Notice (excluding weekends and holidays).

Under ORS 87.021, a contractor is not required to send a Notice on a commercial project, if its work falls into one of the following three categories:

- a. It provided labor only;
- b. It provided labor and materials only; or
- c. It provided rental equipment only.

If a contractor properly sends a required Notice of Right to Lien to the mortgagees on the property, the materials portion of its lien takes priority over a mortgage. In the event a contractor failed to send a Notice of Right to Lien to a mortgagee (thereby causing the contractor to lose priority as to the materials portion of its lien), the Claim of Lien should segregate the remaining balance between those outstanding amounts related to materials and non-materials (e.g. labor,

equipment, etc.). Otherwise, the court may find that it cannot determine the lien amounts which are entitled to priority over a pre-existing mortgage. In which case, it may find the entire lien to be invalid or otherwise unenforceable as to the mortgage.³

2. Information Notice to Owner

As a supplement to owners, Oregon law also requires original contractors (those who contract directly with an owner – typically the general contractor) to provide owners of residential improvements with a general notice regarding construction liens.⁴

If the contract is in writing, the notice must be provided at the signing of a written contract.⁵ An Information Notice is only required when the aggregate contract price exceeds \$2,000.⁶

B. Claim of Construction Lien

1. Written Contracts Required

Effective January 1, 2008, a written construction contract is required for residential projects exceeding \$2,000.⁷ If the price increases above \$2,000 during the course of construction, the contractor must send a written contract to the owner within 5 days. If a contractor fails to execute a written contract, it forfeits its rights to lien the property at issue. This provision applies to only “original contractors” on residential projects, i.e. those who contract directly with a residential owner.

2. Timing

A contractor claiming a construction lien must file its Claim of Lien within 75 days after that contractor has stopped providing labor, equipment, or materials on the project, or 75 days after substantial completion of the project, whichever comes first.⁸

Generally speaking, a contractor has stopped providing labor, materials, or equipment, when that contractor’s contract is substantially complete.⁹ Performance of additional work not originally contemplated in the initial contract extends the 75 day period until the completion of the additional requested work.¹⁰ Trifling work, or the repairing of a contractor’s substandard work, does not act to extend the 75-day deadline.¹¹

In determining when the contractor’s work is substantially completed, factors such as when the owner pays, and when a contractor removes tools from a construction site may be indicative.¹²

A construction project is complete when one of three things occurs: (1) the improvement is substantially complete; (2) a valid completion notice is posted and recorded as provided by ORS 87.045; or (3) the improvement is abandoned.¹³

3. Content

The Claim of Lien must contain a “true statement of demand” after deducting all just credits and offsets.¹⁴ It must also contain the name of the owner, the name of the party who hired the contractor, and a description of the property to be charged with the lien.¹⁵ Each lien claim must also be “verified by the oath of the person filing or some other person having knowledge of the facts, subject to the criminal penalties for false swearing....”¹⁶

C. Foreclosure

A suit to foreclose on a construction lien must be brought within 120 days after lien filing.¹⁷ Prior to initiating a suit to foreclose a construction lien, a lien claimant must deliver to all owners and mortgagees,¹⁸ a 10-day notice of intent to foreclose on the construction lien.¹⁹ Applicable to complaints filed after July 1, 2017, an owner may suspend a lien foreclosure suit by filing a Construction Contractors Board (CCB) complaint, where it paid the general contractor, but the subcontractor alleges it was not paid.²⁰

D. Attorney Fees

Assuming a contractor complies with all relevant statutory requirements in perfecting its lien and initiating its lien foreclosure suit, it will be entitled to recover its reasonable attorney fees if it prevails in the foreclosure suit.²¹

E. Public Works Projects

Oregon provides a separate statutory scheme related to work on publicly owned projects. The rules discussed above do not apply to such situations.

II. STATUTES OF LIMITATION AND REPOSE

A. Breach of Contract – Statute of Limitations

ORS 12.080(1) states that a breach of contract claim must be filed within six years. In *Waxman v. Waxman & Associates, Inc.*, 224 Or. App. 499, 198 P.3d 445 (2008), the Court of Appeals held that this statute of limitations does not include the discovery rule, meaning that the limitations period begins to run at the time of breach, regardless of when the breach is discovered.

B. Negligence (Property Damage) – Statute of Limitations

The statute of limitations for tort actions arising out of construction defect related property damage is in dispute. There is also some dispute as to whether accrual is when property damage begins to occur or if a discovery rule applies.

ORS 12.080(3) provides that “[a]n action . . . for interference with or injury to any interest of another in real property, excepting those mentioned in . . . ORS 12.135 . . . shall be commenced within six years.” Oregon cases confirmed this repeatedly – 6 years for claims arising out of damage to property.

However, the Oregon Supreme Court issued an opinion in a construction defect case in 2011 with the following statement included in a footnote:

“Tort claims arising out of the construction of a house must be brought within two years of the date that the cause of action accrues, but, in any event, within 10 years of the house being substantially completed. ORS 12.110; ORS 12.135. Tort claims ordinarily accrue when the plaintiff

discovers or should have discovered the injury. *Berry v. Branner*, 245 Or. 307, 311- 312, 421 P.2d 996 (1966).”

Abraham v. T. Henry Const. et al, 350 Or. 29, 34 n. 3, 249 P.3d 534 (March 10, 2011) (recon. denied, ___ Or. ___, 2011 Ore. LEXIS 433 (May 5, 2011)).

The statute of limitations was not essential to the court’s holding, because the question before the court was whether a negligence claim could proceed where the parties had a contractual relationship. The plaintiffs’ claim was brought more than six years, but less than ten years, from the date of injury. Thus, a breach of contract claim was time-barred, but the statute of ultimate repose had not expired on plaintiff’s negligence claim. The court found that plaintiff’s negligence claim was not foreclosed by the contract because its terms did not alter or eliminate the defendant’s liability for the claimed property damage. The court did not rule on the issue of when the plaintiff’s cause of action accrued. A motion for reconsideration of the subject footnote was denied by the Court.

However, Oregon judges at the trial court level have split as to their application of the 2-year statute of limitations endorsed in *Abraham*.²² Some judges ignore the footnote or dismiss it as *dicta*. Others have relied on the footnote in *Abraham* and have dismissed construction defect cases based on the plaintiff’s failure to file its claim within two years of accrual.²³

Recently, in *Rice v. Rabb*, the Oregon Supreme Court held that a claim for conversion or replevin under ORS 12.080(4) is subject to a discovery rule, regardless of whether or not the statute of limitations expressly includes it.²⁴ The ruling supports the position that accrual incorporates a discovery rule for negligent construction claims as well (which fall under a subsection of the same statute – ORS 12.080(3)), and is contrary to the claim that accrual occurs as soon as property damage occurs.

Also, in *Sunset Presbyterian Church v. Brockamp & Jaeger, Inc.*, the Oregon Supreme Court recently stated that where a contract (such as the standard AIA form) states the applicable statute of limitations runs from “substantial completion,” as “certified by the Architect,” a tort claim accrues only if and when the architect issues a certificate of substantial completion, even if the project owner has already occupied and used the property for its intended purposes.²⁵

C. Design Professionals – Statute of Limitations

ORS 12.135(3) provides a two-year statute of limitations for specialized actions against design professionals.²⁶ The action must be commenced within two years “from the date the injury or damage is first discovered or in the exercise of reasonable care should have been discovered.”²⁷ This statute of limitations applies to claims of any nature, including claims for breach of contract.²⁸

And note that any claim against a design professional requires ORS 31.300 certification that plaintiff’s attorney has “consulted a licensed construction design professional who is qualified, available and willing to testify to admissible facts and opinions sufficient to create a question of fact as to the liability of the construction design professional.”²⁹ If the statute of limitations against a design professional is about to expire the statute alternatively allows for a specific affidavit.³⁰

D. Statute of Ultimate Repose

The statute of ultimate repose applicable to actions for damages from construction, alteration or repairs to real property was amended in 2009. Many residential structures, including those that are four stories or less above grade, are still subject to a ten-year period following substantial completion. However, the statute has been reduced to six-years from substantial completion for large commercial structures.³¹ And the legislature further amended the statute in 2013 to clarify that the same six-year statute of repose period for large commercial structures applies to design professionals.³² Therefore, for causes of action arising in 2010 and later, each of the definitions should be investigated and considered.

For residential structures and small commercial structures, ORS 12.135 provides a ten year statute of ultimate repose for construction claims, whether in contract, tort or otherwise. The definition of “residential structure” includes those that contain one or more dwelling units and are four stories or less above grade. See ORS 701.005 (14). In general, a “small commercial structure” includes non-residential structures that are 10,000 square feet or less, but there are a number of other possibilities, including some non-residential rental units that are part of a larger structure. See ORS 701.005(16).

Large commercial structures are subject to a six-year statute of limitations under ORS 12.135. A “large commercial structure” is defined, by exclusion, as a “structure that is not a residential structure or small commercial structure.”³³

Recently, in *Sunset Presbyterian Church v. Brockamp & Jaeger, Inc.*, the Oregon Supreme Court clarified when the statute of repose period begins to run. Specifically, the period begins to run on the date on which the contractee accepts the construction as fully complete, as opposed to accepting the construction as sufficiently complete for its intended use or occupancy.³⁴ In other words, evidence of mere occupancy isn’t enough. There has to be an affirmation of full completion by the contractee.

In a companion case, *PIH Beaverton, LLC v. Super One, Inc.*, the Oregon Supreme Court interpreted the rule in *Sunset Presbyterian* and held that a completion notice pursuant to ORS 87.045 (construction lien) is insufficient to trigger the running of the 10-year statute of repose.³⁵ The court stated there must be evidence that, when considered in its entirety, demonstrates written consent or assent to construction as sufficiently complete for its intended use or occupancy.³⁶

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

A. Pre-Suit Notice

An owner cannot file a lawsuit or initiate arbitration against a contractor, subcontractor or supplier regarding residential construction defects without sending the contractor, subcontractor or supplier a written notice of the defects by registered mail, return receipt requested.³⁷ If the owner does not give proper notice, the contractor, subcontractor or supplier can have the lawsuit or arbitration dismissed without prejudice.³⁸ The owner must then provide proper notice before re-filing.³⁹

1. Required Content

An owner’s pre-suit notice must include:

- a. The name and mailing address of owner or the owner’s legal representative;
- b. A statement that the owner may file lawsuit or compel arbitration;

- c. The address and location of the residence affected by the defect;
- d. A description of:
 - i) Each defect;
 - ii) The remediation the owner believes is necessary; and
 - iii) Any incidental damage that cannot be remediated; and
- e. Any report or other document evidencing the existence of the defects and any incidental damage.⁴⁰

2. Secondary Notices

After receiving a notice of defect, a contractor, subcontractor, or supplier has 14 days to send by registered mail, return receipt requested, a secondary notice to any other known contractor, subcontractor, or material supplier who may be responsible for the defects.⁴¹ This secondary notice must include a copy of the owner's notice and a statement that describes why the person/entity may be responsible for some or all of the defects.⁴²

3. Right of Visual Examination / Right of Inspection

If a contractor, subcontractor or supplier wants to visually examine the residence, he must request as much in writing within 14 days of receiving the notice of defect or secondary notice.⁴³ The request must state the estimated time required for the visual examination and the owner must make his residence available during normal business hours within 20 days after receiving the written request.⁴⁴

Under ORS 701.570, if a contractor, subcontractor or supplier wants to inspect the residence, he must request as much in writing within 14 days of receiving the notice of defect or secondary notice. The request must state the nature and scope of the inspection, the testing to be performed, the estimated time required for the inspection, and the identity of those attending the inspection.⁴⁵ The owner must make his residence available during normal business hours or at a time that is mutually agreeable to the owner and the requester.⁴⁶ The party requesting the inspection must coordinate the inspection with any parties he intends to hold secondarily liable and must provide them with copies of the notice sent to the owner.⁴⁷

B. Response and Remediation

1. Timing

Unless otherwise agreed to by the owner, a contractor, subcontractor or supplier that receives a notice of defect or secondary notice must send a written response to the owner not later than 90 days after receipt.⁴⁸

2. Content

The response must be in writing, sent by registered mail, return receipt requested.⁴⁹ For each defect listed in the notice of defect, secondary notice or observed during visual examination or inspection, the response must either:

- a. Acknowledge the defect's existence, nature and extent without regard to responsibility;
- b. Describe the existence of a defect different in nature or extent from the defect described in the notice without regard to responsibility; or
- c. Deny the defect exists.⁵⁰

The response must also include copies of reports detailing the results of the inspection and any defects discovered and an offer to perform remediation within a specified time frame, an offer to pay monetary compensation, or a denial of responsibility for some or all of the defects and incidental damage.⁵¹

An owner has 30 days to accept an offer to remediate or pay.⁵² While the statute provides that any claim by an owner shall be dismissed if the notice provisions have not been complied with, it is silent on the consequence for a general contractor failing to send the secondary notice.

If an owner sends a notice before the applicable statute of limitations has expired, the statute is extended for 120 days after the contractor denies responsibility, 120 days after the owner rejects the contractor's offer, or 30 days after the contractor fails to perform the agreed repair or pay agreed damages.⁵³

IV. COVERAGE AND ALLOCATION ISSUES

A. Commercial General Liability (CGL) Policies

In general, coverage will exist under a Commercial General Liability (CGL) policy for "occurrences" that cause "bodily injury" or "property damage," which occur within the policy period, subject to exclusions contained in the policy.

1. The Insured

The definition of "insured" depends on how the named insured is shown on the policy's declarations.

2. Occurrences

Where, as typical, occurrence is defined as an "accident" the meaning is well established under Oregon case law. An injury is accidental unless the insured acted both intentionally and with an intent to cause harm. As explained in *Drake v. Mutual of Enumclaw Ins. Co.*, 167 Or. App. 475, 481, 1 P.3d 1065 (2000), a case in which our office represented the insurer, the "occurrence" requirement is satisfied unless the insured acted both deliberately and maliciously – meaning, the insured intended to commit the injury-producing act and also intended to inflict the injury.

Oregon appellate courts have held that a contract or warranty cannot be breached accidentally.⁵⁴ Thus, a breach of contract or a warranty is not an "occurrence."

3. Property Damage

Under typical policy definitions, property damage does not include consequential or intentional damage, nor does it include the insured's product when the policy excludes coverage for damage to the insured's product. Further, defective workmanship and materials, standing alone, does not qualify as "property damage."⁵⁵

4. Bodily Injury

The Oregon Court of Appeals has held that "bodily injury" coverage applies where there is an allegation of physical harm, however slight. For example, in *McLeod v. Tecorp International, Ltd.*, 117 Or. App. 499, 502, 844 P.2d 925 (1992), *modified* 199 Or. App. 442, 850 P.2d 1161, *rev'd on other grounds*, 318 Or 209 (1993), a case involving sexual harassment in the workplace, the court said that "nausea" – a physical ailment – and "pain" – presumably physical pain – constituted "bodily injury."

5. Duty to Defend

Under Oregon law, an insurer's duty to defend depends entirely on the terms of the policy and the allegations of the complaint against the insured.⁵⁶ The insurer must defend if the complaint, without amendment, alleges "facts" that reasonably can be read to state a legally cognizable claim covered by the policy.⁵⁷ It doesn't matter that the alleged "facts" are known to be untrue, based on the insurer's investigation.

B. Completed Operations Coverage

Insurance coverage for construction defect claims is generally predicated on the completed operations provision, as most construction defect damages occur after the project is completed. As a general rule, the operation is deemed complete when the work is finished.⁵⁸

C. Allocation

Oregon Courts have not addressed allocation issues. Assume a defect of 8 years, where three companies each provided coverage for two years and the subcontractor had no coverage for the two remaining years. Typically, the three companies agree to split the cost of defense and 100% of the indemnity three ways. However, without citation to Oregon precedent, an Oregon Federal District Court has opined that the three companies and the insured would each be responsible for 25% of the damage.

V. CONTRACTUAL INDEMNIFICATION AND CONTRIBUTION

A. Contractual Indemnification

If the general contractor, in the construction contract, requires the subcontractor to indemnify the general contractor for the liability it incurs as a result of the subcontractor's performance, the general contractor has an enforceable indemnity agreement. If an indemnity

clause requires a subcontractor to indemnify a contractor for the contractor's own negligence, it is overbroad⁵⁹; however, a court will still enforce such a provision, but only to the extent of the subcontractor's own negligence.⁶⁰

A contractual indemnitor has a duty to defend the indemnitee in the action if any allegation in the complaint could be covered under the contractual indemnity provision.⁶¹ The general contractor can obtain a judgment against the subcontractor for the amount of damage caused by the subcontractor. If the indemnity agreement specifically includes defense costs and attorney fees, the general contractor may be able to recover the costs of defense and attorney fees it has to pay the plaintiff.

Oregon law is not clear as to how the attorney fees will be allocated to each party in construction defect cases with multiple defendants or third-party defendants. In certain cases the courts have used a pro rata approach, i.e., if the subcontractor pays 20% of the damage judgment, the subcontractor pays 20% of the cost of defense/attorneys' fees. Courts have also divided the total defense costs by number of defendants/third-party defendants and allocated an equal share to each, regardless of that party's fault allocation.

Note, however, that the Oregon Supreme Court has determined that where a general contractor's insurer has made payments under a policy, the general contractor can only seek indemnity from a subcontractor to the extent that subcontractor's work on the project occurred during the relevant policy period.⁶² In other words, a subcontract can only be held liable for covered losses for which it could have actually been responsible.⁶³

B. Contribution

In *Lasley v. Combined Transport, Inc.*, the Oregon Supreme Court held that when alleging contribution against co-defendants, a defendant cannot rely on evidence not pled by the plaintiff to prove the fault of the co-defendant.⁶⁴ And to allocate the fault of a co-defendant in circumstances where no judgment is being sought by the defendant against the co-defendant, an affirmative defense, as opposed to a cross-claim, is the appropriate procedural vehicle for achieving allocation.⁶⁵ If the defendant is seeking a judgment against a co-defendant (by contribution, indemnity, or otherwise), a cross-claim appears to be the appropriate procedural vehicle.

Recently, in *Marton v. Ater Construction Co.*, the Oregon Court of Appeals held that a defendant's contribution claim against a co-defendant arising out of money it owed the plaintiff is subject to the economic loss doctrine.⁶⁶ However, the Court stated it was possible for a defendant to bring a claim against a co-defendant alleging it is liable instead to the plaintiff.⁶⁷

VI. DAMAGES LIMITATIONS

A. Economic Loss Doctrine

Oregon courts adhere to the rule that "a negligence claim for the recovery of economic losses caused by another must be predicated on some duty of the negligent actor to the injured party beyond the common law duty to exercise reasonable care to prevent foreseeable harm."⁶⁸ Stated another way, "one ordinarily is not liable for negligently causing a stranger's purely economic loss without injuring his person or property."⁶⁹ Some source of a duty outside the common law of negligence is required.⁷⁰ A duty outside the common law of negligence is found

when the actor and the injured party are in a “special relationship” which is a relationship in which one party undertakes to protect the economic well-being of the other. Common examples include the relationship between professionals, such as lawyers, engineers, and architects, and their clients.

In *Jones v. Emerald Pacific Homes, Inc.*, 188 Or. App. 471 (2003), it appeared the Oregon Court of Appeals held that the relationship between homebuilder and homeowner was not special and thus would not support a negligence claim. There, a homeowner sued a contractor because of allegedly poor workmanship for breach of contract and negligence. The trial court dismissed the negligence claim and the Court of Appeals affirmed the dismissal in an opinion that appeared to rely on the economic loss doctrine.

However, the economic loss doctrine did not apply where a secondary purchaser sued a builder for negligently causing damage to the property during its initial construction. *Harris v. Suniga*, 209 Or. App. 410, 149 P.3d 224 (2006), (affirmed 344 Or. 301, 180 P.3d 12 (2008)). In *Harris*, the plaintiffs purchased an apartment complex several years after it had been constructed under a contract between the defendant builder and the initial owner. Shortly after the purchase, plaintiffs allegedly discovered construction defects and damages attributable to defendants’ work. Prior to trial, summary judgment was granted in favor of defendants, who argued that plaintiffs’ negligence claim was barred by the economic loss doctrine; that is, because the damage to the apartment building was purely economic loss, a claim for negligence would not lie in the absence of a special relationship.

The Oregon Court of Appeals reversed the trial court’s decision, relying primarily on the facts and holding in *Newman v. Tualatin Development Co. Inc.*, 287 Or. 47, 597 P.2d 800 (1979). The court stated:

“In both cases, the defendants are builders of housing complexes. In both cases, the plaintiffs were not original purchasers directly from the defendants, but rather owners who purchased the homes from those who were. In both cases, the plaintiffs assert claims against the original builder for negligent construction, based on the deterioration of the physical structure of the buildings because of water damage. It seems to us necessarily to follow that the cases should be treated in similar fashion. In *Newman*, the court held that there was no impediment to the claim. The court did not explicitly refer to the economic loss doctrine, but we understand the necessary implication of its decision to be that the damage at issue was not economic loss. We do not understand why this case should be treated differently.”

The court also distinguished *Jones*, *supra*, explaining that *Jones* only dealt with the issue of whether a breach of contract could give rise to tort liability.

The Oregon Supreme Court upheld the Court of Appeals’ decision upon review, and went on to state that the concerns underlying the economic loss doctrine were not implicated when the focus of the claimed negligence is on physical damage to property.

What *Harris* means is that subsequent purchasers can sue builders and developers, and do not need to rely on a “special relationship” to maintain a claim that the builder or developer negligently caused foreseeable damages to the property. It does not matter whether the builder or developer had any contact with the plaintiff. In fact, as the Court of Appeals noted, a subsequent purchaser has greater rights against the builder/developer than does the original purchaser/client.

As noted above, if pled incorrectly, a defendant can be subject to the economic loss doctrine when alleging contribution of a co-defendant.⁷¹

B. Attorney Fees

As a general rule, attorney fees are not recoverable absent a statute or contractual agreement authorizing the award.⁷² An exception exists however, when a party's breach of contract involves the non-breaching party in litigation with a third party.⁷³ In such a case, the non-breaching party may recover attorney fees incurred in the separate action involving the third party, as consequential damages.⁷⁴

C. Delay

An owner can recover only for the period of delay that the owner proves was due solely to the contractor's fault.⁷⁵

For a residential project, the proper measure of damages for delay is the rental value of the home, even if the owner did not intend to rent the property to others.⁷⁶ For a commercial project, where an owner can demonstrate with reasonable certainty that the project would have been completed and usable absent the defendant's delay, the owner can recover either (1) the reasonable rental value of the completed project or (2) the anticipated profits lost due to the breach.⁷⁷

¹ Oregon Revised Statutes (ORS) 87.021.
² ORS 87.021(1).
³ ORS 87.025.
⁴ ORS 87.093, *et seq.*
⁵ ORS 87.093(2)(b).
⁶ ORS 87.093(4).
⁷ ORS 701.305.
⁸ ORS 87.035.
⁹ *Consolidated Electric Distributors, Inc. v. Jetson Electric Contracting, Inc.*, 272 Or. 384, 387, 537 P.2d 83 (1975).
¹⁰ *Farrell v. Lacey/Basic Builders, Inc.*, 264 Or. 505, 511-12, 507 P.2d 31 (1973).
¹¹ *See Fox & Company v. Roman Catholic Bishop*, 107 Or. 557 (1923).
¹² *See Schade v. Alton*, 61 Or. 187, 189, 121 P 898 (1912); *Dallas LBR. & Supply v. Phillips*, 249 Or. 58, 60, 436 P.2d. 739 (1968).
¹³ ORS 87.045(1).
¹⁴ ORS 87.035(3)(a).
¹⁵ ORS 87.035(3)(d).
¹⁶ ORS 87.035(4).
¹⁷ ORS 87.055.
¹⁸ Note that ORS 87.018 was recently amended to redefine “mortgagee.”
¹⁹ ORS 87.057(1).
²⁰ ORS 87.059.
²¹ ORS 87.060(5).
²² Washington County Circuit Court judges have largely followed the *Abraham* 2-year statute of limitations to date, whereas Multnomah County Circuit Court judges are more likely to disregard *Abraham* in favor of a 6-year statute of limitations.
²³ *See Liberty Oaks Homeowners Assoc. v. Liberty Oaks, LLC et al*, C096255CV, Wash. Co. Cir. Ct., (filed Oct. 15, 2009). The judgment entered by the trial court granted “[a]ll motions for summary judgment based on Plaintiff’s failure to commence the action within two years of accrual and the Supreme Court’s recent decision in *Abraham v. T. Henry Const., Inc.*, 350 Or. 29 (2011).”
²⁴ 354 Or. 721 (2014).
²⁵ CC C091601CV, 2014 WL 1641728 (Or. April 24, 2014).
²⁶ This includes architects as defined under ORS 671.010 to 671.220, landscape architects as defined in ORS 671.310 to 671.459 and engineers as defined under ORS 672.002 to 672.325.
²⁷ ORS 12.135(3)(a)(A).
²⁸ *Waxman v. Waxman & Associates, Inc.*, 224 Or. App. 499, 198 P.3d 445 (2008) (in these cases, the limitations period is determined by the identity of the defendant, not the nature of claim).
²⁹ ORS 31.300(2).
³⁰ ORS 31.300(3).
³¹ ORS 12.135(1)(c) (applies to causes of action arising after January 1, 2010).
³² ORS 12.135(3)(a)(C) (applies to causes of action arising after January 1, 2014).
³³ ORS 701.005(10).
³⁴ CC C091601CV, 2014 WL 1641728 (Or April 24, 2014).
³⁵ CC C072107CV, 2014 WL 1661341 (Or April 24, 2014).
³⁶ *Id.*
³⁷ ORS 701.565.
³⁸ ORS 701.595.
³⁹ *Id.*
⁴⁰ ORS 701.565.
⁴¹ ORS 701.570(1).
⁴² *Id.*
⁴³ ORS 701.570.
⁴⁴ *Id.*; ORS 701.575.
⁴⁵ ORS 701.570.

⁴⁶ ORS 701.575(2).
⁴⁷ ORS 701.570(4).
⁴⁸ ORS 701.570(5).
⁴⁹ *Id.*
⁵⁰ *Id.*
⁵¹ *Id.*
⁵² ORS 701.580(1).
⁵³ ORS 701.585.
⁵⁴ *Oak Crest Construction Co. v. Austin Mutual Ins. Co.*, 329 Or. 620, 998 P.2d 1254 (2000); *Kisle v. St. Paul Fire & Marine Ins.*, 262 Or. 1, 495 P.2d 1198 (1972).
⁵⁵ *See Wyoming Sawmills v. Transportation Ins. Co.*, 282 Or. 401, 578 P.2d 1253 (1978) (holding that the cost to remove and replace bad lumber used by a framer was not covered, but the cost of repairing other contractors' work which was damaged in the process of removing the bad lumber was covered).
⁵⁶ *See, e.g., Richardson v. Howard S. Wright Construction Co.*, 2007 U.S. Dist. LEXIS 37011, at 17, (D.Or. May 18, 2007) (duty to defend dependent solely on allegations in complaint and language of insurance policy).
⁵⁷ *Marleau v. Truck Ins. Exchange*, 333 Or. 82, 91, 37 P.3d 148 (2001); *Ledford v. Gutoski*, 319 Or. 397, 400-01, 877 P.2d 80 (1994).
⁵⁸ *Boyer Metal Fab v. Maryland Casualty Co.*, 90 Or. App. 103, 107; 750 P.2d 1195, rev. den. 305 Or. 672, 757 P.2d 422 (1988).
⁵⁹ ORS 30.140.
⁶⁰ *Montara Owners Ass'n v. La Noue Dev., LLC*, 259 Or. App. 657, 682; 317 P.3d 257, 272 (2013). Note that a petition for review of the *Montara* ruling was filed in March 2014.
⁶¹ *Nat'l Union Fire Ins. Co. of Pittsburgh, Pa. v. Starplex Corp.*, 220 Or. App. 560; 188 P.3d 332 (2008).
⁶² *Montara Owners Ass'n v. La Noue Dev., LLC*, 259 Or. App. 657, 675-76, 317 P.3d 257, 268-69 (2013).
⁶³ *Id.*
⁶⁴ 351 Or. 1 (2011).
⁶⁵ *Id.*
⁶⁶ 256 Or. App. 554 (2013).
⁶⁷ *Id.* at 565, n. 8 ("... the language of the comparative fault statute, ORS 31.600, demonstrates that '[t]he legislature anticipated that a defendant could file a third-party complaint against a tortfeasor who would not be liable to the defendant but who could, instead, be liable to the plaintiff.' 351 Or. at 22; 261 P.3d 1215 (emphasis added).").
⁶⁸ *Onita Pacific Corp. v. Trustees of Bronson*, 315 Or. 149, 159 (1992).
⁶⁹ *Hale v. Groce*, 304 Or. 281, 284 (1987).
⁷⁰ *Id.*
⁷¹ *Marton v. Ater Construction Co.*, 256 Or. App. 554, 565, n. 8 (2013).
⁷² *Brookshire v. Johnson*, 274 Or. 19, 21; 544 P.2d 164 (1976).
⁷³ *Raymond v. Feldmann*, 124 Or. App. 543, 546; 863 P.2d 1269 (1993).
⁷⁴ *Id.*
⁷⁵ *See Valley Inland Pac. Constructors v. Clack. Water Dist.*, 43 Or. App. 527, 537; 603 P.2d 1381 (1979).
⁷⁶ *Gregory v. Weber*, 51 Or. App. 547, 552; 626 P.2d 392 (1981).
⁷⁷ *Stubblefield v. Montgomery Ward & Co.*, 163 Or. 432; 96 P.2d 774 (1939).

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I. MECHANICS' LIEN BASICS

The Mechanics' Lien Law of 1963 ("Lien Law"), 49 P.S. § 1101 et seq., grants contractors, subcontractors and second tier subcontractors on private projects the right to file a lien against the owner's property for the payment of all debts due by the owner to the contractor or by the contractor to any subcontractors for labor and materials furnished in the erection and construction or alteration and repair of the improvement.¹ No liens are allowed where the labor or materials are provided for a purely public purpose or on leasehold premises unless the owner acknowledges in writing that the improvements are for the owner's immediate use and benefit.² Additionally, liens are prohibited where the property was conveyed for valuable consideration before a claim for alterations or repairs was filed, or where a claimant holds or has claimed a security interest under the Pennsylvania Uniform Commercial Code.³

1. **Recent Amendments to the Lien Law:** The Lien Law was significantly amended on January 1, 2007. The most significant change to the Lien Law was to expand the definition of "subcontractor" to allow second tier subcontractors to file liens.⁴ The previous version of the Lien Law also contained a widely utilized procedure wherein contractors and subcontractors could waive their right to file a lien against the property by executing a stipulation against liens, and in fact were often required to do so by owners and their lenders. Under the current Lien Law, owners are no longer able to rely on lien waivers executed by contractors, subcontractors, and sub-subcontractors prior to the receipt of payment for their work, except in limited situations.⁵ The January 1, 2007 amendments also change the requirements for filing and perfecting a mechanics' lien claim by allowing a claimant to file a claim with the prothonotary's office within six months of the completion of his work, as opposed to four month deadline in the prior version of the Lien Law, and also eliminate the requirement that a subcontractor performing alterations or repairs file a "preliminary notice" of his intent to file a lien.⁶
2. **Basic Filing Requirements:** Pennsylvania's Lien Law still contains slightly different requirements for contractors and subcontractors. In order to establish a valid claim, each subcontractor must provide formal notice to the owner of his intention to file a claim.⁷ Said notice must be given at least thirty days before the claim is filed and must include the elements set forth in 49 P.S. §1501. Prime contractors are not required to provide such notice. To perfect a lien, every claimant must file a claim with the prothonotary's office of the county where the work was done within six months after the completion of

his work, serve written notice of the filing upon the owner within one month of the filing, and file an affidavit of service of the notice, or acceptance of service, within twenty days of the service.⁸ Each mechanics' lien claim must include certain elements as set forth in 49 P.S. §1503. Pennsylvania's Courts have frequently held that strict compliance with the Lien Law is necessary in order to effect a valid claim.⁹

Finally, any action to obtain judgment upon a mechanics' lien claim must be commenced within two years from the date of filing, unless the time is extended in writing by the owner, and a verdict or judgment must be entered within five years from the date of filing the claim or the claim shall be wholly lost.¹⁰

3. **Lien Waivers:** On residential construction projects, a contractor may waive his lien rights only when the total contract price between owner and contractor is less than one million dollars.¹¹ Subcontractors may waive their lien rights only (i) when the total contract price between the contractor and owner is less than one million dollars; or (ii) if the contractor has posted a bond guaranteeing payment for the labor and materials provided by the subcontractor, in which case advance waivers by subcontractors are allowed regardless of the total price of the contract.¹²

On non-residential construction projects, the Lien Law provides that a contractor's waiver of lien rights is against public policy, and thus is unlawful and void unless given in exchange for payment for the work performed, and then only to the extent that payment is actually made.¹³ A subcontractor's waiver of lien rights is likewise void unless given in exchange for receipt of payment, unless the contractor has posted a bond guaranteeing payment for the labor and materials provided by the subcontractors.¹⁴

II. STATUTES OF LIMITATIONS AND REPOSE

A. Statute of Limitations

The statutes of limitations generally applicable to construction projects in Pennsylvania are set forth at 42 Pa.C.S.A. §5521 et seq. Pursuant to 42 Pa.C.S.A. §5523, an action upon any payment or performance bond is subject to a one-year statute of limitations. Generally, a two-year statute of limitations applies to any action based upon negligent, intentional, or otherwise tortious conduct, in accordance with 42 Pa.C.S.A. §5524. Breach of contract actions are generally controlled by the four-year statute of limitations set forth at 42 Pa.C.S.A. §5525. Pennsylvania law also provides for a residual six-year statute of limitations for actions not specifically covered by another statutory provision.

In *Gustine Uniontown v. Anthony Crane Rental*, 577 Pa. 14 (2004), the Pennsylvania Supreme Court addressed the precise issue of whether actions claiming latent defects and arising out of a written construction contract are subject to the residual six-year period of limitations or the four-year statute of limitations set forth at 42 Pa.C.S.A. §5525(a)(8). The Court noted that the issue was one of first impression, and after a thorough examination of statutory interpretation principles and public policy concerns, determined that except in circumstances where another

limitations period explicitly applies, an action upon a written contract, including a contract for the construction of real estate, is subject to the four-year period of limitations explicitly set forth at 42 Pa.C.S.A. §5525(a)(8). In determining that the four-year statute of limitations applies, the Court noted it is undisputed that there is no other specific statutory provision affording a longer period of limitations for actions upon real estate construction contracts, or latent defects in construction.¹⁵

Although the applicable statute of limitations normally begins to run from the moment there is a cause of action, Pennsylvania courts allow the Discovery Rule and Repair Doctrine to toll statutes of limitations. The Discovery Rule tolls the statute of limitations during the period the plaintiff's injury or its cause was neither known nor reasonably knowable to the plaintiff.¹⁶ The Pennsylvania Supreme Court has generally approved the Discovery Rule¹⁷, and the Pennsylvania Superior Court has specifically held that the Discovery Rule may be applied to cases involving defective construction.¹⁸

The Repair Doctrine tolls the statute of limitations where it can be shown that (1) repairs were attempted; (2) representations were made that the repairs would cure the defects; and (3) the complaining party relied upon such representations.¹⁹ While the Pennsylvania Supreme Court has not specifically accepted the Repair Doctrine, the Repair Doctrine has been adopted by the Pennsylvania Superior Court.²⁰

B. Statutes of Repose

The statute of repose for construction projects, set forth at 42 Pa.C.S.A. §5536, generally requires that any civil action brought against anyone performing design, planning, supervision or construction services, for damages relating to deficiency in the design, planning, supervision or construction, injury to persons or property, wrongful death, or contribution and indemnity in certain circumstances, must be brought within twelve years after completion of the construction. The twelve year limitation does not apply to injuries or wrongful death occurring ten to twelve years from the completion of the improvement and may not be asserted by any person in actual possession or control of the improvement at the time the deficiency constitutes the proximate cause of the actionable injury or wrongful death.²¹

Pursuant to 42 Pa.C.S.A. § 5536, a party seeking protection under the statute of repose must show (1) an improvement to real property was supplied; (2) more than twelve years have elapsed between the completion of the improvements to the real estate and the injury; and (3) the activity of the moving party must be within the class which is protected by the statute.²² The Pennsylvania Supreme Court has clarified that the statutory period begins when the entire construction project is so completed that it can be used by the general public.²³ Additionally, the Pennsylvania Supreme Court has held that application of the statute of repose is not limited to architects, engineers or contractors.²⁴ While manufacturers are not generally protected by the statute of repose, they are not specifically excluded.²⁵ Instead, the focus of the inquiry remains on whether any individual expertise has been supplied, in which case manufacturers may also be protected by the statute of repose.

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

In Pennsylvania, there is no universal statute which defines what specific adequate pre-suit notice of claim is applicable to all lawsuits arising out of construction projects. Therefore, in terms of what notice of claim is required, there are two important sources of information to consider. First, the language of any construction contract that the respective parties entered into is the first source of required pre-claim notice. However, the enforceability of such contractual pre-claim notices will vary largely depending on the language of the contract, the underlying facts of each case, and the prejudice to the party not receiving notice.

The second important consideration for pre-suit notice of claim will depend largely on the specific contracts at issue. The most common example of pre-claims process which must be followed arises in the context of contract claims against the Commonwealth. In that instance, Chapter 17 of the Commonwealth Procurement Code (62 P.S. §1701) et. seq., sets forth the pre-claim requirements, and requires that generally that a claim be submitted to the contracting officer within six months of the date the claim accrues, and further provides that a contractor has fifteen days from the date of the contracting officer's decision to file a claim with the Pennsylvania Board of Claims.

IV. COVERAGE AND ALLOCATION ISSUES

Contractors typically acquire Commercial General Liability insurance policies. Provisions of a CGL policy provide coverage if the insured's work or product actively malfunctions causing injury to an individual or damage to another's property.²⁶

An "occurrence" policy protects the policyholder from liability for any act done while the policy is in effect, whereas a "claims made" policy protects the holder only against claims made during the life of the policy.²⁷ The Pennsylvania Supreme Court recently evaluated what constitutes an occurrence in *Kvaerner Metal Division of Kvaerner U.S., Inc. v. Commercial Union Insurance Company*.²⁸ In *Kvaerner*, Kvaerner was under contract with a third party to construct a "coke oven battery," which ultimately exhibited several deficiencies. The third party filed a complaint and Kvaerner looked to Commercial Union Insurance (CUI), the CGL insurer, to defend and indemnify. CUI refused to defend or indemnify.

The Court found that the insurer's duties to defend and indemnify under the insurance policy are triggered, if at all, by the language of the complaint against the insured.²⁹ The complaint only alleged breach of contract claims based on faulty workmanship, and raised no claims for damages to other property or injury to individuals. The policy defined "occurrence" as "an accident, including continuous or repeated exposure to substantially the same or general harmful conditions."³⁰ The Court opined the plain meaning of accident implies a degree of fortuity that is not present in a claim for faulty workmanship, and thus refused to convert a CGL policy into a performance bond, holding faulty workmanship is not an "accident" and thus under this policy not an "occurrence."³¹

With respect to allocation, in Pennsylvania where multiple insurers (for example a continuous injury spanning multiple insurers) have a duty to indemnify and defend allocation of cost will largely depend on the language of the policy.³² In the absence of any other contractual language, if the policy specifies that the insurer is obligated to pay all sums which the insured becomes legally obligated to pay, then each insurer would be considered a primary insurer. In that situation, the insured could select which policy or policies under which it is to be indemnified.³³

In the alternative, if there is an "other insurance" provision within the policy, insurers may seek contribution for a share of the indemnification or defense costs from other insurers.³⁴

V. CONTRACTUAL INDEMNIFICATION

Pennsylvania law contains several limitations on the scope and enforceability of clauses which provide that one can be indemnified from his own negligence. First, by statute, certain indemnity provisions are unenforceable. Pennsylvania Law provides:

Every covenant, agreement or understanding in, or in connection with any contract or agreement made and entered into by owners, contractors, subcontractors or suppliers whereby an architect, engineer, surveyor or his agents, servants or employees shall be indemnified or held harmless for damages, claims, losses or expenses including attorneys' fees arising out of: (1) the preparation or approval by an architect, engineer, surveyor or his agents, servants, employees or invitees of maps, drawings, opinions, reports, surveys, change orders, designs or specifications, or (2) the giving of or the failure to give directions or instructions by the architect, engineer, surveyor or his agents, servants or employees provided such giving or failure to give is the primary cause of the damage, claim, loss or expense, shall be void as against public policy and wholly unenforceable.

68 P.S. § 491.

This provision therefore renders unenforceable the design professional's contract indemnity clause, when the professional's errors or omissions are the primary cause of the damages. This statute defines indemnity as against public policy, but this does not invalidate limits on liability provisions.³⁵

Additionally in Pennsylvania, indemnity, exculpatory, and hold harmless clauses are disfavored, and must meet certain conditions to be enforceable.³⁶ In order to be enforceable, the clause must not contravene public policy, the contract must relate solely to the private affairs of the contracting parties and not include a matter of public interest, and each party must be a free bargaining agent.³⁷ Further, if these requirements are satisfied, these provisions will only indemnify for losses due to the indemnitee's own negligence, if the language is clear and unequivocal and "no inference from words of general import can establish such indemnification."³⁸

One example of how Pennsylvania Courts consider indemnification issues is the case of *Ruzzi v. Butler Petroleum Company*. In *Ruzzi*, a subcontractor was injured when a used fiberglass underground storage tank exploded prior to installation because it still contained gasoline from the prior owner. The owners of the gas station and the contractor, who acquired the used storage tank for use in reconstructing the gas station, signed an agreement containing an indemnity provision. The provision purported to indemnify the contractor for injuries "caused or occasioned by any leakage, fire, explosion or other casualty occurring through any imperfection in, injury or damage to, or by reason of the installation, use, operation and/or repair of the said equipment or of the premises."³⁹ The Pennsylvania Supreme Court held these were "words of general import," not sufficiently clear, and therefore did not indemnify the contractor for his own negligence.

VI. DAMAGES LIMITATIONS

A. Attorneys' Fees

Pennsylvania follows the "American rule" that in the absence of a statute or contractual provision, each party bears his own attorneys' fees.⁴⁰ The Judicial Code, 42 Pa. C.S.A. § 2503, provides ten exceptions to this general rule, including provisions that attorneys' fees may be awarded "as a sanction against another participant for dilatory, obdurate or vexatious conduct" and when "the conduct of another party in commencing the matter or otherwise was arbitrary, or in bad faith." In addition to the exceptions under the Judicial Code, two "prompt pay" statutes also allow contractors and subcontractors to recover attorneys' fees and penalties under certain circumstances if payment for work performed is not made in a timely fashion.⁴¹ However, the standards for recovering such fees are different on public projects and private projects.

B. Consequential Damages

Like most states, the ability to collect consequential damages in Pennsylvania may depend on whether the Uniform Commercial Code applies. If the UCC applies, consequential damages are recovered through 13 Pa. C.S.A. §2-715(2) which provides that, consequential damages resulting from the seller's breach include any loss resulting from general or particular requirements and needs of which the seller at the time of contracting had reason to know and which could not reasonably be prevented by cover or otherwise.

In a non-UCC context, the non-breaching party is entitled to recover, unless the contract provides otherwise, whatever damages he suffered, provided (1) they were such as would naturally and ordinarily result from the breach, or (2) they were reasonably foreseeable and within the contemplation of the parties at the time they made the contract, and (3) they can be proved with reasonable certainty.⁴²

C. Delay and Disruption Damages

The government possesses a duty to act in a way that will not hinder or delay a contractor's performance. When this duty is violated the contractor may have a claim for damages. In order to recover for a compensable delay, a contractor must prove: (1) the extent of the delay with reasonable degree of accuracy; (2) the delay was caused solely by the government's actions; and (3) the delay caused specific, quantifiable injury to the contractor.⁴³ Evidence of damages may consist of probabilities and inferences as long as the amount is shown with reasonable certainty.⁴⁴ Further, under Pennsylvania law, "no damage for delay clauses" are enforceable, but Courts often disregard such clauses if the contractor can show that the owner "positively interfered" with project operations.⁴⁵

D. Economic Loss Doctrine

Recent caselaw has significantly curtailed the Economic Loss Doctrine as a defense to construction claims. Formerly, design professionals employed by owners to develop plans and specifications for construction projects could raise the economic loss doctrine as a defense to contractor's tort actions. The Pennsylvania Supreme Court recently created an exception to the Economic Loss Doctrine in the context of design professionals and contractors. The Court adopted Section 552 of the Restatement of Torts, entitled Negligent Misrepresentation, as the law in Pennsylvania in cases where information is negligently supplied by one in the business of supplying information, such as an architect or design professional, and where it is foreseeable that the information will be used and relied upon by third persons, even if the third parties have no direct contractual relationship with the supplier of information.⁴⁶ Since this decision in Pennsylvania, contractors may sue design professionals directly for mere economic losses without contractual privity.

E. Interest

In contract cases, a successful plaintiff is entitled to prejudgment interest at the statutory rate as a matter of right. Interest is calculated from the time that debt became due or payable, and the statute, 41 P.S. § 201, defines the "legal rate of interest" as 6 percent per annum.⁴⁷ Pennsylvania's Prompt Pay statutes, cited above, provide for other specific interest rates if a claim is brought under those Acts.

F. Punitive Damages

Generally punitive damages are not recoverable in a breach of contract claim.⁴⁸ Similarly, liquidated damages provisions within construction contracts can be rendered unenforceable if at the time the parties enter into the contract, the sum agreed to is an unreasonably high approximation of the expected loss. These unreasonably high liquidated damages are unenforceable on grounds of public policy as a penalty.⁴⁹

¹ 49 P.S. § 1301.

² 49 P.S. §1303.

³ Id.

⁴ 49 P.S. §1201.

⁵ 49 P.S. §1401.

⁶ 49 P.S. §§1501-1502.

⁷ 49 P.S. §1501.

⁸ 49 P.S. §1502.

⁹ *Flick Construction, Inc. v. Dyke*, 401 Pa. Super. 168 (1991) (internal citations omitted).

¹⁰ 49 P.S. §1701.

¹¹ 49 P.S. 1401.

¹² Id..

¹³ Id.

¹⁴ Id..

¹⁵ *Gustine Uniontown v. Anthony Crane Rental*, 577 Pa. 14, 34 (2004).

¹⁶ *Fine v. Checcio*, 582 Pa. 253 (2005).

¹⁷ *Gustine Uniontown v. Anthony Crane Rental*, 577 Pa. 14 (2004) (internal citations omitted).

¹⁸ *Amodeo v. Ryan Homes, Inc.*, 407 Pa. Super 448 (1991) (internal citations omitted).

¹⁹ *Gustine Uniontown v. Anthony Crane Rental*, 577 Pa. 14 (2004) (internal citations omitted).

²⁰ *Amodeo v. Ryan Homes, Inc.*, 407 Pa. Super 448 (1991).

²¹ 42 Pa.C.S.A. §5536.

²² *McConnaughey v. Building Components, Inc.*, 536 Pa. 95, 99 (1994).

²³ *Noll by Noll v. Harrisburg Area Y.M.C.A.*, 537 Pa. 274, 281 (1994) (internal citations omitted).

²⁴ *McCormick v. Columbus Conveyor Company*, 522 Pa. 520, 525 (1989).

²⁵ *Noll by Noll v. Harrisburg Area Y.M.C.A.*, 537 Pa. 274, 284 (1994) (internal citations omitted).

²⁶ *Snyder Heating v. Pennsylvania Manufacturers' Association Insurance Co.*, 715 A.2d 483 (Pa. Super. 1998).

²⁷ *Consulting Engineers Inc., v. Ins. Co. of North America*, 710 A.2d 82, 85 (Pa. Super. 1998).

²⁸ *Kvaerner*, 908 A.2d 888 (Pa. 2006).

²⁹ *Mutual Benefit Insurance Co. v. Haver*, 725 A.2d 743, 745 (Pa. 1999).

³⁰ *Kvaerner*, at 897.

³¹ Id., at 899.

³² See generally, *J.H. France v. Allstate Insurance Company et al.*, 626 A.2d 502 (Pa. 1993).

³³ Id., at 508.

³⁴ Id., at 509.

³⁵ *Valhal Corp. v. Sullivan Associates, Inc.*, 44 F.3d 195, 203-204 (3d Cir. 1995)(applying Pennsylvania law)

³⁶ Id., at 204; *Topp Copy Products Inc. v. Singletary*, 626 A.2d 98, 99 (Pa. 1993).

³⁷ *Topp Copy Products Inc.*, at 99 (internal citations omitted).

³⁸ *Ruzzi v. Butler Petroleum Co.*, 588 A.2d 1, 7 (Pa. 1991).

³⁹ Id., at 8.

⁴⁰ *Jones v. Muir*, 515 A.2d 855 (Pa. 1986).

⁴¹ 62 Pa. C.S. §3935; 73 P.S. §512.

⁴² *Taylor v. Kaufhold*, 84 A.2d 347 (Pa. 1951) (internal citations omitted).

⁴³ *A.G. Cullen Construction, Inc. v. State System of Higher Education*, 898 A.2d 1145, 1160-61(Pa. Cmwlt. 2006) (internal citations omitted).

⁴⁴ Id., at 1161, 1174 (affirming use of total cost method to establish damages)

⁴⁵ *Coatsville Contractors & Engineers, Inc. & Borough of Ridley*, 506A.2d 862 (Pa. 1986).

⁴⁶ *Bilt-Rite*, at 287.

⁴⁷ *Robert Wooler Co. v. Fidelity Bank*, 479 A.2d 1027 (Pa. Super. 1984).

⁴⁸ *DeLuca v. Fidelity Bank*, 422 A.2d 1159 (Pa. 1980) citing, *Hoy v. Grenoble*, 34 Pa. 9 (Pa. 1859).

⁴⁹ *A.G. Cullen Construction, Inc. v. State System of Higher Education*, 898 A.2d 1145 (Pa. Cmwlt. 2006) (internal citations omitted).

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I. MECHANICS' LIEN BASICS

Chapter 28 of Title 34 of the Rhode Island General Laws, Rhode Island's Mechanics' Lien Law, provides a statutory remedy for recovery to any person who has contributed either labor or materials used in the improvement of property upon consent of its owner.¹ The Mechanics' Lien Law is in derogation of the common law and is therefore strictly construed.² It creates a lien in favor of contractors, subcontractors, engineers, architects, and material suppliers, among others, who contribute labor or materials used in the construction or improvement of property.³ The statute also covers persons who rent or lease equipment.⁴ Liens may attach to all projects involving private property, but may not attach to public works projects.⁵

A. Requirements

A mechanics' lien attaches to the property "when the work begins or the materials are furnished."⁶ The lien, however, is not self-executing. To perfect a lien, the claimant must comply with two steps: (1) mail, within 200 days after performing the work or furnishing the materials, notice of intention to claim a mechanics' lien to the property owner; and (2) file a copy of the notice mailed to the property owner in the records of the land evidence in the city or town in which the land generally described in such notice is located.⁷ Section 34-28-4(b) lists the information required in the lien notice and also provides a model form of notice. A lien notice will cover all the value or all work performed in the 200 days preceding the lien notice's filing as well as work performed in the future.⁸ The 200-day restriction does not apply to retainage withheld.⁹ Further, contractors, engineers, and architects contracting with the owner or lessee must give notice within ten days of the commencement of work or delivery of materials for construction.¹⁰

B. Enforcement and Foreclosure

1. Enforcement

Following notice and recording, the lien-holder must take the following steps to enforce the lien. Within forty days of perfecting the lien, the lien-holder must file a complaint in the Superior Court.¹¹ The lien-holder must also file a notice of *lis pendens* in the land records office of the city or town in which the land is located.¹² Sections 34-28-13 and 34-28-11 provide forms for the complaint and *lis pendens*.

Upon filing the complaint, the clerk of the Superior Court places one advertisement in the newspaper notifying all persons who have a lien or any title, claim, lease, mortgage, attachment or other encumbrance, or any unrecorded claim on any part of the same property, to respond to the court and make their demands against the property.¹³ To dismiss the complaint and release the lien, the landowner may pay into the registry of the court, in the county in which the land is located, cash equal to the total amount noticed by the lien-holder and the accounts and demands of any person claiming a mechanics' lien as well as costs, interest and reasonable attorneys' fees.¹⁴ On proof of proper payment or deposit and upon motion by the owner of the property, any Superior Court justice can, by *ex parte* order, discharge the notice of intention and the *lis pendens* and dismiss the cause of action.¹⁵ Payment of sums deposited in the registry to lien-holders are governed by the terms of § 34-28-17.

The 2006 amendments to Rhode Island's Mechanics' Lien Law provide the landowner with additional procedural safeguards. Section 34-28-17.1 allows the landowner to petition for a "prompt" show cause hearing, at which the lien-holder has the burden of establishing the lien's validity.¹⁶

2. Foreclosure

The filing of a petition under the Mechanics' Lien Law suspends a mortgage holder's power of sale.¹⁷ Instead, following the filing of the complaint and *lis pendens* pursuant to § 34-28-10, a mortgage holder having priority over a mechanics' lien may petition, at any time, for foreclosure to exercise the power of sale after notice to all interested parties that the mortgage is valid, entitled to priority, and in default.¹⁸

For holders of mechanics' liens, the court, upon motion by any party claiming to have a lien or any encumbrance on the property, may direct that the property be sold under the direction of a special master appointed for that purpose, with the proceeds directed to all holders of interest according to their priority.¹⁹ Directing costs of the proceedings between the parties is within the discretion of the court, and the court may also allow for attorneys' fees to a prevailing party.²⁰

C. Ability to Waive and Limitations on Lien Rights

Contractual waiver of a party's right to file a mechanics' lien is expressly prohibited by statute, as such a waiver would be against public policy, and is therefore void and unenforceable.²¹

II. STATUTES OF LIMITATION AND REPOSE

A. Statute of Limitations

Section 9-1-13 of the Rhode Island General Laws provides for a ten-year statute of limitations on actions not involving personal injury.²² The limitations period of § 9-1-13 "begins to run when the evidence of injury to property, resulting from the negligent act upon which the action is based, is sufficiently significant to alert the injured party to the possibility of a defect."²³ Actions brought to enforce the implied warranties of reasonable workmanship and habitability are also subject to the ten-year statute of limitations.²⁴

Contribution and indemnity claims must be brought within one year of the accrual of the cause of action.²⁵ The limitations period begins to run “after the first payment made by a joint tortfeasor which has discharged the common liability or is more than his or her pro rata share thereof.”²⁶

B. Statute of Repose

Constructors of real property are immune from liability for causes of action brought “more than ten (10) years after substantial completion of such an improvement.”²⁷ Section 9-1-29 of the Rhode Island General Laws “provides that those who seek to recover damages for negligence from architects, professional engineers, contractors, subcontractors, or materialmen arising as a result of the design or construction of an improvement to real property must bring their action within ten years of the substantial completion of the improvement.”²⁸ The statute provides protection against certain classes of injuries arising from a workmanship deficiency, namely “injury to property, real or personal[, and] injury to the person or . . . [for] wrongful death.”²⁹ The statute also protects against suits “[f]or contribution or indemnification.”³⁰

Importantly, § 9-1-29 does not protect against those actions “sounding in contract,” even if brought more than ten years after substantial completion of the improvement.³¹ Thus, actions brought to enforce the implied warranty of habitability are not subject to the ten-year statute of repose.³²

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

For residential construction, § 5-65-12.1 of the Rhode Island General Laws provides a private cause of action against a contractor for negligent work, improper work, breach of contract, and contract disputes.³³ If successful, the plaintiff in such an action may, in addition to any judgment awarded, recover from the defendant treble damages, reasonable attorneys’ fees, and the costs of the action.³⁴ A complaint filed under § 5-65-12.1 “may be instituted in lieu of or as a supplement to the contractors’ registration board’s administrative proceedings and penalties only to the extent that the board’s final orders are insufficient to satisfy the claimant’s damages.”³⁵

The Rhode Island Supreme Court has rejected a blanket notice requirement for suits claiming a breach of the implied warranty of habitability.³⁶ In *Lacey v. Edgewood Home Builders, Inc.*, 446 A.2d 1017, 1020 (R.I. 1982), the Court considered the argument that “lack of notice may be construed as a waiver of the claim.” The Court “decline[d] to hold that a notice requirement similar to that contained in the Uniform Commercial Code is applicable to sales of real estate.”³⁷ The Court explained that “depending upon circumstances, lack of notice may affect, in greater or lesser degree, the credibility of a plaintiff’s claim.”³⁸

IV. INSURANCE COVERAGE AND ALLOCATION ISSUES

A. General Coverage Issues

Coverage under commercial general liability policies is “designed to protect the insured from losses arising out of business operations.”³⁹

B. Trigger of Coverage

Under Rhode Island law, “coverage under a general liability policy is triggered by an occurrence that takes place when property damage, which includes property loss, manifests itself or is discovered or in the exercise of reasonable diligence is discoverable.”⁴⁰ Accordingly, coverage is triggered when the property damage: (1) manifests itself; (2) is discovered; or (3) in the exercise of reasonable diligence is discoverable.⁴¹ Where a plaintiff asserts coverage based upon damage discoverable in the exercise of reasonable diligence, the plaintiff must have had some reason to discover the damage and must actually have been able to discover it in the exercise of reasonable diligence.”⁴² Finally, “continuous activity constitutes only one occurrence for purposes of an insurance policy.”⁴³

C. Allocation Among Insurers

In circumstances where there are multiple potentially applicable insurance policies containing conflicting provisions, Rhode Island law, in general, allocates coverage on a *pro rata* basis. Thus, if each policy, among the multiple policies at issue, would provide primary coverage to an insured if it were the only applicable policy, and they each contain conflicting insurance provisions, then the coverage responsibilities of all insurers are shared on a *pro rata* basis.⁴⁴ Likewise, if each policy, among the multiple policies at issue, disclaims coverage on the basis of the existence of another policy, then the coverage responsibilities of the insurers are shared on a *pro rata* basis.⁴⁵ However, “the *pro rata* rule regarding apportionment of liability [among multiple insurance policies] should be resorted to only if the * * * insurance policies at issue are *actually in conflict*.”⁴⁶

V. CONTRACTUAL INDEMNIFICATION

Rhode Island law does not permit indemnification agreements in which the general contractor attempts to contract away liability for its own negligence. Section 6-34-1 of the Rhode Island General Laws states that any indemnification contract:

“purporting to indemnify the promisee [general contractor], the promisee’s independent contractors, agents, employees, or indemnitees against liability for damages arising out of bodily injury to persons or damage to property proximately caused by or resulting from the negligence of the promisee, the promisee’s independent contractors, agents, employees, or indemnitees, is against public policy and is void.”⁴⁷

“This statute, by its express terms, invalidates any agreement in which a party seeks indemnification from another for the consequences of its own or its agent’s negligence.”⁴⁸

Section 6-34-1, however, does not prohibit indemnification agreements in which the subcontractor agrees to indemnify the general contractor against the subcontractor’s own negligence.⁴⁹ Therefore, because an indemnification agreement prohibited by § 6-34-1 may nevertheless be enforceable in part, apportionment of fault between the contractor and subcontractor is critical to determining whether and to what extent such a mixed agreement is

enforceable.⁵⁰ Finally, §6-34-1 “shall not affect the validity of any insurance contract, worker’s compensation agreement, or an agreement issued by an insurer” regarding indemnification.⁵¹

VI. CONTINGENT PAYMENT AGREEMENTS

Contingent payment agreements, or “pay-when-paid” clauses, are generally found in construction contracts and provide that a subcontractor will be paid for its work only if and when the general contractor receives payment.⁵² Although neither Rhode Island state courts nor the Rhode Island General Assembly have yet addressed “pay-when-paid” clauses, the United States District Court for the District of Rhode Island has addressed them in several cases.⁵³ Notably, the District Court has followed well-established precedent that “a pay-when-paid clause . . . does not foreclose a subcontractor’s right to bring suit for payment under the Miller Act against a general contractor and its surety.”⁵⁴ In keeping with this and other established principles of law, Rhode Island state courts would likely find that “pay-when-paid” clauses are nonetheless valid “where the language of the contract in question is clear on its face” and unambiguous.⁵⁵

VII. DAMAGE LIMITATIONS

A. Personal Injury Damages vs. Construction Defect Damages

Rhode Island courts assess personal injury damages and construction defect damages in the same manner:

“The question of the amount of damages is important, as well as that of liability, and the trial court is * * * duty bound to give it serious consideration, keeping in mind that the burden is upon the plaintiff to prove the damages by a preponderance of the evidence. A plaintiff should be compensated for all his damages of which the defendants’ negligence was the proximate cause, but no claim for damages should be allowed to stand where such claim is not supported by the required degree of proof, or is speculative, or imaginary, or is clearly attributable to other causes.”⁵⁶

B. Attorneys’ Fees Shifting and Limitations on Recovery

Under Rhode Island law, absent contractual or statutory authorization, attorneys’ fees may not be awarded.⁵⁷ Rhode Island subscribes to the “American rule,” under which attorneys’ fees are not available absent certain narrow exceptions: (1) pursuant to the “common fund” exception; (2) “as a sanction for willful disobedience of a court order”; or (3) when a party has “acted in bad faith, vexatiously, wantonly, or for oppressive reasons.”⁵⁸ If there is a basis for awarding fees, the decision of whether to do so rests in the trial judge’s discretion.⁵⁹

Pursuant to § 9-1-45 of the Rhode Island General Laws, a court “may award reasonable attorney’s fees to the prevailing party in any civil action arising from a breach of contract in which the court: (1) [f]inds that there was a complete absence of a justiciable issue of either law or fact raised by the losing party; or (2) [r]enders a default judgment against the losing party.”⁶⁰

C. Consequential Damages

Consequential damages, for a breach of contract, are not recoverable under Rhode Island law unless they are foreseeable.⁶¹ Consequential damages are damages “that do not flow directly and immediately from an injurious act but that result indirectly from the act.”⁶²

D. Delay and Disruption Damages

Rhode Island law allows for the recovery of delay and disruption damages in contract actions.⁶³ Such damages are recoverable under ordinary damages principles so long as they can be “proven with a reasonable degree of certainty,” and “the plaintiff * * * establish[es] reasonably precise figures and [does not] rely upon speculation.”⁶⁴

E. Economic Loss Doctrine

The economic loss doctrine, which Rhode Island has adopted, provides that “a plaintiff may not recover [purely economic] damages under a negligence claim when the plaintiff has suffered no personal injury or property damage.”⁶⁵ In the absence of a contract between entities, the recovery of economic damages that are proximately caused by one of the entities is unavailable.⁶⁶ The consumer exception to the economic loss doctrine provides that the doctrine only applies to disputes involving commercial entities—it does not apply when the parties are consumers.⁶⁷

F. Interest

In all civil actions in Rhode Island, a party is entitled to prejudgment interest by statute at the annual rate of twelve percent (12%), determined “from the date the cause of action accrued.”⁶⁸ No interest accrues on a judgment for punitive damages.⁶⁹ Post-judgment interest also accrues at the rate of twelve percent (12%) per annum.⁷⁰ A contract provision may provide for interest for the use of money, or it may waive interest. However, such a provision has no bearing on “interest which by legislative fiat or decisional law is added to a judgment of damages for default in the payment of money due under a contract.”⁷¹

G. Punitive Damages

In actions for breach of contract, “punitive damages should be awarded only where [the] ‘defendant’s conduct requires deterrence and punishment *over and above* that provided in an award of compensatory damages.’”⁷² “The party seeking punitive damages has the burden of producing ‘evidence of such willfulness, recklessness or wickedness, on the part of the party at fault, as amounts to criminality, which for the good of society and warning to the individual, ought to be punished.’”⁷³ Thus, punitive damages are only appropriate where there is “a showing that the defendant acted with malice or in bad faith.”⁷⁴ In the context of determining whether punitive damages are appropriate, malice is defined as “an intention to cause harm.”⁷⁵ Importantly, under Rhode Island law punitive damages are not insurable.⁷⁶

VIII. Case law and legislation update

A. Substantial Amendment to § 5-20.8-4

In 2012, the Rhode Island General Assembly substantially amended § 5-20.8-4 of the Rhode Island General Laws pursuant to Public Laws 2012 ch. 375 § 1 and 2012 ch. 394 § 1. These amendments fundamentally altered the intent and purpose of the statute. Previously, § 5-20.8-4 required that a homeowner provide a vendor or home improvement contractor with the opportunity to cure a defective condition.⁷⁷ The buyer could elect to have the seller cure a defect “prior to closing but after execution of an agreement to transfer.” Only then would the buyer provide the seller with “a report of inspection performed by a recognized and reputable inspector or inspection company.”⁷⁸ Now, § 5-20.8-4(a) requires that every real estate purchase-and-sale agreement contain a provision affording the prospective purchaser a ten-day period, exclusive of Saturdays, Sundays, and holidays, to inspect the premises for sale and all buildings thereon before he or she becomes obligated to purchase under the contract.⁷⁹ The parties to the transaction may agree to a different inspection period, while the prospective purchaser may waive this requirement in writing.⁸⁰ Under section 5-20.8-4(b), failure to include the inspection provision in the purchase-and-sale agreement does not create any defect in title to the property.⁸¹ However, failure to include the provision allows the purchaser to void the purchase-and-sale agreement, in writing, prior to the transfer of title at a closing.⁸² Like the pre-amendment version, however, the current § 5-20.8-4 only applies to vacant land or real property containing one to four dwelling units.⁸³

B. *GSM Industrial, Inc. v. Grinnell Fire Protection Systems Co., Inc.*, 47 A.3d 264 (R.I. 2012)

In *GSM Industrial, Inc. v. Grinnell Fire Protection Systems Co., Inc.*, 47 A.3d 264 (R.I. 2012), the Rhode Island Supreme Court clarified the meaning and nature of the requirement in § 34-28-4(b) that every notice of intention to enforce a mechanics’ lien be “executed under oath.” In that case, the plaintiff subcontractor filed a mechanics’ lien to recover overdue payment for the installation of an air pollution control system on the defendant’s property.⁸⁴ The plaintiff’s notice of intention to enforce the lien was notarized by a licensed notary public, but did not contain an affirmation that it was “signed and sworn” by the plaintiff.⁸⁵ The trial court ruled that the lien was wholly lost for failure to comply with the mandatory “oath” requirement of § 34-28-4(b), determining that the notarization was merely an “acknowledgement,” not an “oath” within the meaning of the statute.⁸⁶ The Supreme Court affirmed. It recognized the degree of difference between an “acknowledgement” and an “oath” and found that a mere acknowledgement was insufficient to satisfy § 34-28-4(b) because, unlike an oath, it failed “to militate against [a] meritless claim[.]”⁸⁷ Further, the Court agreed with the trial judge that the “under oath” requirement was a mandatory, not directory, requirement, the absence of which wholly voided the plaintiff’s lien.⁸⁸

C. *Rhode Island Construction Services, Inc. v. Harris Mill, LLC*, 68 A.3d 450 (R.I. 2013)

The Rhode Island Supreme Court continues to literally construe the requirements of Rhode Island’s Mechanics’ Lien Law. For example, in *Rhode Island Construction Services, Inc.*

v. Harris Mill, LLC, 68 A.3d 450 (R.I. 2013), a mortgage assignee's statement of claim on a mechanics' lien filed by an architect on the property encumbered by the mortgage was dismissed for failure to adhere to the statutory timing requirements. In *Rhode Island Construction Services, Inc.*, the assignee obtained an interest in the mortgage months after the filing of the mechanics' lien on the encumbered property.⁸⁹ Although § 34-28-16(a) requires "claimants with an interest in property" to file claims on mechanics' liens within twenty days of the return date provided for in the mechanics' lien citation, the trial court allowed the assignee to bring an untimely claim under the doctrine of "excusable neglect" because it acted swiftly to vindicate its claim once it obtained the mortgage.⁹⁰ The Supreme Court reversed and voided the claim, finding that a reasonably prudent purchaser in the assignee's position would have discovered the pendency of the mechanics' lien (and accompanying expiration of the period in which to file a statement of claim) before purchasing the mortgage and, thus, the doctrine of "excusable neglect" was inapplicable to validate its untimely filing.⁹¹

¹ R.I. GEN. LAWS § 34-28-1 (WEST through Chap. 534 of 2013 Reg. Sess.).

² *Frank N. Gustafson & Sons v. Walek*, 599 A.2d 730, 732 (R.I. 1991).

³ §§ 34-28-1 through 34-28-3.1.

⁴ § 34-28-1.

⁵ § 34-28-31.

⁶ *Gem Plumbing & Heating Co., Inc. v. Rossi*, 867 A.2d 796, 803 (R.I. 2005).

⁷ § 34-28-4(a).

⁸ *Id.*; § 34-28-10.

⁹ *See J.D. Cement Works, Inc. v. SBER Royal Mills, LLC*, 2010 WL 331966 (R.I. Super. January 22, 2010).

Retainage is the portion of a contract's final payment withheld by the principal until the project is complete, satisfies all contract terms, and all mechanic's liens have either been released or have expired.

¹⁰ §§ 34-28-4.1, 34-28-7.

¹¹ § 34-28-10; *see also Gem Plumbing & Heating Co., Inc.*, 867 A.2d at 804.

¹² § 34-28-10.

¹³ § 34-28-14.

¹⁴ § 34-28-17.

¹⁵ *Id.*

¹⁶ *Gem Plumbing & Heating Co., Inc.*, 867 A.2d at 812.

¹⁷ § 34-28-10(b).

¹⁸ § 34-28-16.1.

¹⁹ § 34-28-21. Priority is determined pursuant to § 34-28-25.

²⁰ § 34-28-19.

²¹ § 34-28-1(b).

²² R.I. GEN. LAWS § 9-1-13 (WEST through Chap. 534 of 2013 Reg. Sess.). For claims involving personal injury, Rhode Island has a three year statute of limitation pursuant to § 9-1-14(b).

²³ *Boghossian v. Ferland Corp.*, 600 A.2d 288, 290 (R.I. 1991) (*quoting Lee v. Morin*, 469 A.2d 358, 360 (R.I. 1983)).

²⁴ *Boghossian*, 600 A.2d at 290.

²⁵ R.I. GEN. LAWS § 10-6-4 (WEST through Chap. 534 of 2013 Reg. Sess.).

²⁶ *Id.*

²⁷ § 9-1-29; *see also Boghossian*, 600 A.2d at 290.

²⁸ *Leeper v. Hillier Group, Architects Planners, P.A.*, 543 A.2d 258, 259 (R.I. 1988); *see also Boghossian*, 600 A.2d at 290.

²⁹ §§ 9-1-29(1)-(2).

³⁰ § 9-1-29(3).

³¹ *Boghossian*, 600 A.2d at 290; *Nichols v. R.R. Beaufort & Associates*, 727 A.2d 174, 176-81 (R.I. 1999).

³² *Id.*

³³ R.I. GEN. LAWS § 5-65-11 (WEST through Chap. 534 of 2013 Reg. Sess.).

³⁴ § 5-65-12(e).

³⁵ The Rhode Island General Assembly created a private right of action under § 5-65-12.1 as an *alternative* to an administrative procedure. The Contractors' Registration Board, created by statute, is an administrative body whose purpose is to address discretionary claims brought by a homeowner against a registered contractor. *See Butera v. Bucher*, 798 A.2d 340, 354 (R.I. 2002). The Board is empowered to hear certain claims and issue orders against a contractor, including orders requiring corrective work. *See* §§ 5-65-12, 5-65-16(f)(2). Any claims are subject to the notice requirements of § 5-65-12. Additional administrative regulations and forms are available at <http://www.crb.ri.gov/docs/rules.pdf>.

³⁶ *Lacey v. Edgewood Home Builders, Inc.*, 446 A.2d 1017, 1020 (R.I. 1982).

³⁷ *Id.*

³⁸ *Id.*

³⁹ *Industrial Water Park Co. v. National Fire Ins. Co.*, 2005 WL 372298 at *4 (R.I. Super. February 9, 2005).

⁴⁰ *CPC International v. Northbrook Excess & Surplus Ins. Co.*, 668 A.2d 647, 650 (R.I. 1995).

⁴¹ *Textron, Inc. v. Aetna Casualty & Surety Co.*, 723 A.2d 1138, 1142 (R.I. 1999).

⁴² *Id.* at 1144.

⁴³ *Truk-Away of R.I., Inc. v. Aetna Casualty & Surety Co.*, 723 A.2d 309, 313 (R.I. 1999).

⁴⁴ *See Hindson v. Allstate Ins. Co.*, 694 A.2d 682 (R.I. 1997). *See also Irene Realty Corp. v. Travelers Property Casualty Co. of Am.*, 973 A.2d 1118 (R.I. 2009); *Ferreira v. Mello*, 811 A.2d 1175 (R.I. 2002).

⁴⁵ *Ryan v. Knoller*, 695 A.2d 990, 995 (R.I. 1997).

⁴⁶ *Irene Realty Corp.*, 973 A.2d at 1123 (emphasis in original).

⁴⁷ R.I. GEN. LAWS § 6-34-1 (WEST through Chap. 534 of 2013 Reg. Sess.); *see also Rodrigues v. DePasquale Building & Realty Co.*, 926 A.2d 616, 622-23 (R.I. 2007).

⁴⁸ *A.F. Lusi Construction, Inc. v. Peerless Ins. Co.*, 847 A.2d 254, 265 (R.I. 2004).

⁴⁹ *Consentino v. A.F. Lusi Const. Co., Inc.*, 485 A.2d 105, 107 (R.I. 1984).

⁵⁰ *See id.* (remanding for apportionment of negligence).

⁵¹ § 6-34-1.

⁵² *See Allstate Interiors & Exteriors, Inc. v. Stonestreet Construction, LLC*, 907 F. Supp. 2d 216, 226 (D.R.I. 2012); *ADP Marshall, Inc. v. Noresco, LLC*, 710 F. Supp. 2d 197, 207 (D.R.I. 2010).

⁵³ *See id.*

⁵⁴ *See United States ex rel. J.H. Lynch & Sons, Inc. v. Travelers Casualty & Surety Co.*, 783 F. Supp. 2d 294, 298 (D.R.I. 2011).

⁵⁵ *Universal Concrete Products Corp. v. Turner Construction Co.*, 595 F.3d 527, 529-30 (4th Cir. 2010) (applying Virginia law). For a detailed analysis of how other jurisdictions have handled “pay-when-paid” clauses, see 3 PHILIP L. BRUNER & PATRICK J. O’CONNOR, JR., CONSTRUCTION LAW §§ 8:48, 8:49 (2002).

⁵⁶ *Perrotti v. Gonicberg*, 877 A.2d 631, 636 (R.I. 2005) (citations omitted).

⁵⁷ *Pearson v. Pearson*, 11 A.3d 103, 108-09 (R.I. 2011); *Blue Cross & Blue Shield of R.I. v. Najarian*, 911 A.2d 706, 710 (R.I. 2006).

⁵⁸ *Najarian*, 911 A.2d at 711 (citations and internal quotation marks omitted).

⁵⁹ *Id.* at 710.

⁶⁰ § 9-1-45.

⁶¹ *Carter v. Nassif*, 2000 WL 1910047 at *3 (R.I. Super. December 8, 2000); *Mellow v. Medical Malpractice Joint Underwriting Association of R.I.*, 1991 WL 789775 at *2-*3 (R.I. Super. April 5 1991) (citing *Hadley v. Baxendale*, 9 Exch. 341, 156 Eng. Rep. 145 (1854)); *see also Greene v. Creighton*, 7 R.I. 1, 10-12 (1861).

⁶² *Riley v. Stafford*, 896 A.2d 701, 703 (R.I. 2006) (citing BLACK’S LAW DICTIONARY 416 (8th ed. 2004)).

⁶³ *See Clark-Fitzpatrick, Inc./Franki Foundation Co. v. Gill*, 652 A.2d 440 (R.I. 1994).

⁶⁴ *National Chain Co. v. Campbell*, 487 A.2d 132, 134 (R.I. 1985).

⁶⁵ *Franklin Grove Corp. v. Drexel*, 936 A.2d 1272, 1275 (R.I. 2007).

⁶⁶ *Id.*

⁶⁷ *Id.* at 1276-77.

⁶⁸ R.I. GEN. LAWS § 9-21-10 (WEST through Chap. 534 of 2013 Reg. Sess.).

⁶⁹ *De Leo v. Anthony A. Nunes, Inc.*, 546 A.2d 1344, 1348 (R.I. 1988).

⁷⁰ R.I. GEN. LAWS § 6-26-1 (WEST through Chap. 534 of 2013 Reg. Sess.).

⁷¹ *Villa v. Hedge*, 96 R.I. 52, 59, 188 A.2d 904, 908 (1963).

⁷² *Cady v. IMC Mortgage Co.*, 862 A.2d 202, 220 (R.I. 2004) (quoting *Palmisano v. Toth*, 624 A.2d 314, 318 (R.I. 1993)) (emphasis in original).

⁷³ *Palmisano*, 624 A.2d at 318 (R.I. 1993) (quoting *Sherman v. McDermott*, 114 R.I. 107, 109, 329 A.2d 195, 196 (1974)).

⁷⁴ *Id.* (citing *Morin v. Aetna Casualty & Surety Co.*, 478 A.2d 964, 967 (R.I. 1984)).

⁷⁵ *Wilson Auto Enterprises, Inc. v. Mobil Oil Corp.*, 778 F. Supp. 101, 107 (D.R.I. 1991).

⁷⁶ *See Allen v. Simmons*, 533 A.2d 541, 542-44 (R.I. 1987).

⁷⁷ R.I. GEN. LAWS § 5-20.8-4 (since amended).

⁷⁸ § 5-20.8-4(b)(2) (since amended).

⁷⁹ R.I. GEN. LAWS § 5-20.8-4(a) (WEST through Chap. 534 of 2013 Reg. Sess.).

⁸⁰ *Id.*

⁸¹ § 5-20.8-4(b).

⁸² § 5-20.8-4(c).

⁸³ § 5-20.8-1(6).

⁸⁴ *GSM Industrial, Inc. v. Grinnell Fire Protection Systems Co., Inc.*, 47 A.3d 264, 266-67 (R.I. 2012).

⁸⁵ *Id.* at 267.

⁸⁶ *Id.*

⁸⁷ *Id.* at 268-69.

⁸⁸ *Id.* at 270-71.

⁸⁹ *Rhode Island Construction Services, Inc. v. Harris Mill, LLC*, 68 A.3d 450, 452-53 (R.I. 2013).

⁹⁰ *Id.* at 453-54.

⁹¹ *Id.* at 454-57.

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I. MECHANICS' LIEN BASICS

A. Requirements

S.C. Code Ann. Sections 29-5-10 to 5-430 provide for and govern mechanics' liens on private projects in South Carolina. A mechanics' lien may be filed by a contractor, subcontractor, or supplier who, *with the owner's consent*, performs work to improve buildings or structures on real property. This right has been statutorily extended to surveyors, real estate professionals and those providing landscape services.¹ The purpose of the lien is to allow such a contractor, subcontractor, or supplier to obtain a security interest on the improved property, and to force the sale of the property in order to secure payment for the improvements. The failure to perfect a mechanic's lien does not preclude an action on the debt.²

The right to a lien “arises inchoate,” which is to say that the right exists but the lien has not been perfected.³ In order to perfect a mechanics' lien, a contractor who has contracted directly with the owner must:

- (1) Serve on the owner or person in possession and file with the register of deeds or clerk of court a notice or certificate of lien containing the loan amount and a description of the real property.⁴ As only licensed or registered contractors may file a mechanics' lien, the contractor must record his contractor license or registration number on the lien document when it is filed.⁵ These documents must be filed within ninety days after the contractor ceases to labor or furnish labor or materials.⁶
- (2) Commence a lawsuit seeking to enforce the lien within six months after ceasing to provide labor or materials for such real property; and

¹ See S.C. Code Ann. §§ 29-5-21 and 29-5-26.

² *Butler Contracting, Inc. v. Court Street, LLC*, 369 S.C. 121, 631 S.E.2d 252 (S.C. 2006).

³ *Id.*

⁴ *Id.*

⁵ S.C. Code Ann. § 29-5-15(A).

⁶ S.C. Code Ann. § 29-5-90.

- (3) File a notice of the pending action (lis pendens) within six months after ceasing to provide labor or materials for such real property.⁷

A subcontractor or supplier who has not contracted directly with the owner must also send to the general contractor and owner,⁸ via registered or certified mail, a Notice of Mechanics' lien that provides the following information:

- (1) the name of the subcontractor or supplier who claims payment;
- (2) the name of the person with whom the claimant contracted or by whom he was employed;
- (3) a description of the labor, services, or materials furnished and the contract price or value thereof;
- (4) a description of the project where labor services, or materials were used sufficient for identification;
- (5) the date when the first and last item of labor or service or materials was actually furnished or scheduled to be furnished; and
- (6) any amount claimed to be due, if any.⁹

After properly providing notice, a subcontractor is entitled to be paid in preference to the contractor "at whose instance the labor was performed or material furnished and no payment by the owner to the contractor thereafter shall operate to lessen the amount recoverable by the person so giving the notice."¹⁰ "In other words, 'payment by the owner to the general contractor after the owner has received notice of the lien is made at the owner's peril, as it will not effect [sic] the amount recoverable by the party with the mechanics' lien.'"¹¹

B. Enforcement

Foreclosure of a mechanics lien is an action at law.¹² The suit must be filed in the Court of Common Pleas of the County in which the property is located, and must consist of a Summons, a Notice of Lis Pendens, and a Complaint. The Complaint must include a statement of the amount due, a description of the premises, and a prayer for relief requesting sale of the premises and distribution of the proceeds. Failure to timely file a foreclosure action can result in dissolution of the lien but only if it is formally dismissed through Court order, affidavit of the bondholder's attorney or defendant's attorney.¹³

⁷ *Butler Contracting, Inc.*, 369 S.C. at 129.

⁸ S.C.Code Ann. § 29-5-40; *Ferguson Fire and Fabrication, Inc. v. Preferred Fire Protection, LLC*, 397 S.C. 379, 725 S.E.2d 495 (Ct.App. 2012)("When the person claiming the lien was employed by someone other than the owner, he must notify the owner of the furnishing of labor or material in order for the lien to attach to the property").

⁹ S.C. Code Ann. § 29-5-20.

¹⁰ S.C. Code Ann. § 29-5-50.

¹¹ *Action Concrete Contractors, Inc. v. Chappellear*, 404 S.C. 312, 745 S.E.2d 77 (2013) (quoting *Maddux Supply Co. v. Safhi, Inc.*, 316 S.C. 404, 412, 450 S.E.2d 101, 106 (Ct.App.1994)).

¹² *Cohen's Drywall Co. Inc. v. Sea Spray Homes, LLC*, 374 S.C. 195, 648 S.E.2d 598 (2007).

¹³ See S.C. Code Ann. § 29-5-120.

A party who files suit to enforce a mechanics' lien is entitled to a jury trial. If a lien is established in such an action, the party is entitled to sell the real property to which the lien attaches. The sale may be subject to, and inferior to, prior liens and properly recorded mortgages.¹⁴ However, if the lien is perfected by a subcontractor or supplier, the amount which may be recovered from the owner is limited to the amount owed by the owner to the contractor.¹⁵ While the subcontractor and supplier's liens have preference over those of a contractor¹⁶, if the amount owed to the contractor is insufficient to pay all perfected liens, the lienholders will be required to pro-rate their recovery.¹⁷

The prevailing party in an action to enforce a mechanics' lien is entitled to recover attorneys' fees. The determination of the prevailing party is established in S.C. Code Ann. § 29-5-10 and 20 and is based on the exchange of offers and demands prior to trial. However, the amount of the fee may not exceed the amount of the lien.

Note for Public Projects: A contractor who contracts directly with the government cannot file a mechanics' lien against property owned by the government. However, such a contractor can sue a governmental entity for breach of contract if the government entity wrongfully withholds payment. Subcontractors and others who do not contract directly with the government can seek payment through payment bonds which general contractors typically are required to provide for state and federal projects.

C. Waiver and Limitation on Lien Rights

To date, the South Carolina courts have not directly addressed the issue of prospective waivers of liens. The Court of Appeals has referred in passing, however, to “conditional waivers.”¹⁸ In other settings, the courts have allowed a waiver of future rights provided the waiver is knowingly given, supported by consideration and bargained for.

II. STATUTES OF LIMITATION AND REPOSE

The statutes of limitation that commonly apply in construction related litigation are the following:

A. Statutes of Limitations

1. Contract for Sale (UCC) - 6 years.¹⁹

This does not alter the law of tolling of statute of limitations nor does it apply to causes of action which have accrued before the act became effective.

¹⁴ See S.C. Code Ann. § 29-5-70.

¹⁵ See S.C. Code Ann. § 29-5-60.

¹⁶ S.C. Code Ann. § 29-5-50.

¹⁷ S.C. Code Ann. § 29-5-60.

¹⁸ *Taylor, Cotton & Ridley, Inc. v. Okatie Hotel Group, LLC*, 372 S.C. 89, 99 641 S.E.2d 459 (Ct.App. 2007).

¹⁹ S.C. Code Ann. §36-2-725.

2. Contract action, obligation, or liability (express or implied) – 3 years.²⁰

This 3 year statute of limitations applies to all contractual obligations other than (a) an action upon a bond or other written contract secured by a mortgage on real property; or (b) an action upon a sealed instrument. The statute of limitations for these actions is the twenty (20) year period set forth in §15-3-520.

3. Actions for trespass upon or damage to real property – 3 years.²¹
4. Actions for injury to the person, property or rights of another (negligence) – 3 years.²²

The "discovery rule" is applicable to actions under each of these provisions.²³ Under the discovery rule, the statute runs from the date the injury resulting from the wrongful conduct either is discovered or may be discovered by the exercise of reasonable diligence.²⁴ "The exercise of reasonable diligence means an injured party must act with some promptness where the facts and circumstances of an injury would put a person of common knowledge and experience on notice that some right . . . has been invaded or that some claim against another party might exist."²⁵

B. Statute of Repose

No actions to recover damages based upon or arising out of the defective or unsafe condition of an improvement to real property may be brought more than 8 years after substantial completion of the improvement.²⁶ An action based upon or arising out of the defective or unsafe condition of an improvement to real property includes:

1. an action to recover damages for breach of a contract to construct or repair an improvement to real property;
2. an action to recover damages for the negligent construction or repair of an improvement to real property;
3. an action to recover damages for personal injury, death, or damage to property;

²⁰ S.C. Code Ann. § 15-3-530(1).

²¹ S.C. Code Ann. §15-3-530 (3).

²² S.C. Code Ann. § 15-3-530(5)

²³ S.C. Code Ann. § 15-3-535 (all actions, initiated under § 15-3-530(5) must be commenced within 3 years after a person knew or by exercise of reasonable diligence should have known that he had a cause of action).

²⁴ *McClain v. Jarrad*, 354 S.C. 218, 580 S.E.2d 763 (Ct. App. 2003).

²⁵ *Id.*, citing *Snell v. Columbia Gun Exchange, Inc.*, 276 S.C. 301, 278 S.E.2d 333 (1981).

²⁶ S.C. Code Ann. § 15-3-640.

4. an action to recover damages for economic or monetary loss;
5. an action in contract or in tort or otherwise;
6. an action for contribution or indemnification for damages sustained on account of an action described in this section;
7. an action against a surety or guarantor of a defendant described in this section;
8. an action brought against any current or prior owner of the real property or improvement, or against any other person having a current or prior interest in the real property or improvement;
9. an action against owners or manufacturers of components, or against any person furnishing materials, or against any person who develops real property, or who performs or furnishes the design, plans, specifications, surveying, planning, supervision, testing, or observation of construction, or construction of an improvement to real property, or a repair to an improvement to real property.²⁷

"Substantial completion" means "that degree of completion of a project, improvement, or a specified area or portion thereof (in accordance with the contract documents, as modified by any change orders agreed to by the parties) upon attainment of which the owner can use the same for the purpose for which it was intended; the date of substantial completion may be established by written agreement between the contractor and owner."²⁸

Unless the contractor and owner, by written agreement, establish a different date of substantial completion of an improvement, a certificate of occupancy issued by a county or municipality, in the case of new construction, or completion of a final inspection by the responsible building official in the case of improvements to existing improvements, shall constitute proof of substantial completion.²⁹

Normal statutes of limitations continue to run within this 8 year statute of repose.³⁰

This statute of repose does not in any way preclude a person from entering into a contractual agreement prior to the substantial completion of the improvement which extends any guarantee of a structure or component being free from defective or unsafe conditions beyond 8 years after substantial completion of the improvement or component.³¹

²⁷ *Id.*

²⁸ S.C. Code Ann. § 15-3-630.

²⁹ S.C. Code Ann. § 15-3-640.

³⁰ *Id.*

³¹ *Id.*

A building permit for the construction of an improvement to real property must contain in bold type notice to the owner or possessor of the property of his rights to contract for a guarantee of the structure being free from defective or unsafe conditions beyond 8 years after substantial completion of the improvement.³²

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

A. Non-Residential Construction Defects

The claimant must serve a written notice of claim on the contractor, subcontractor, supplier, or design professional. The notice of claim must contain the following:

1. a statement that the claimant asserts a construction defect;
2. a description of the claim or claims in reasonable detail sufficient to determine the general nature of the construction defect; and
3. a description of the results of the defect, if known.

Within 15 days of receiving the claim, the contractor, subcontractor, supplier, or design professional must advise the claimant if the description of the claim or claims is not sufficiently stated and shall request clarification.³³

The contractor, subcontractor, supplier, or design professional has 60 days from service of the initial notice of claim to inspect, offer to remedy, offer to settle with the claimant, or deny, in whole or in part, the claim regarding the defects. Within 60 days from the service of the initial notice of claim, the contractor, subcontractor, supplier, or design professional shall serve written notice on the claimant of the contractor's, supplier's, or design professional's election pursuant to this section. The claimant shall allow inspection of the construction defect at an agreeable time, during normal business hours, to any party, if requested. The claimant shall give the contractor, subcontractor, supplier, or design professional reasonable access to the property for inspection and if repairs have been agreed to by the parties, reasonable access to effect repairs. Failure to respond within 60 days is considered a denial of the claim.³⁴

The claimant shall serve a response to the contractor's, subcontractor's, supplier's, or design professional's offer within 10 days of receipt of the offer.³⁵ If the parties cannot agree to settle the dispute pursuant to this article within 90 days after service of the initial notice of claim on the contractor, subcontractor, supplier, or design professional, the claim is considered denied and the claimant may proceed with a civil action or other remedy provided by contract or by law.³⁶

³² *Id.*

³³ S.C. Code Ann. § 40-11-530.

³⁴ S.C. Code Ann. § 40-11-540.

³⁵ *Id.*

³⁶ *Id.*

If the claimant files a civil action or initiates an arbitration before first complying with the requirements of this article, on motion of a party to the action, the court or arbitrator shall stay the action until the claimant has complied with the requirements of this article.³⁷

The claimant's written notice tolls the applicable statute of limitations and statute of repose pursuant to Title 15, Chapter 3, and an applicable warranty period for 120 days after the date the written notice is served upon the contractor, subcontractor, supplier, or design professional.³⁸ The protections afforded by these notice provisions do not limit the ability of a person to file and perfect a mechanic's lien, as discussed in Section I, above.³⁹

B. Residential Construction Defects

In an action brought against a contractor or subcontractor arising out of the construction of a dwelling, the claimant must, no later than 90 days before filing the action, serve a written notice of claim on the contractor.⁴⁰ The notice of claim must contain the following:

1. a statement that the claimant asserts a construction defect;
2. a description of the claim or claims in reasonable detail sufficient to determine the general nature of the construction defect; and
3. a description of any results of the defect, if known.

The contractor or subcontractor shall advise the claimant within 15 days of receipt of the claim if the construction defect is not sufficiently stated and shall request clarification.⁴¹

The contractor or subcontractor has 30 days from service of the notice to inspect, offer to remedy, offer to settle with the claimant, or deny the claim regarding the defects. The claimant shall receive written notice of the contractor's or subcontractor's, as applicable, election under this section. The claimant shall allow inspection of the construction defect at an agreeable time to both parties, if requested under this section. The claimant shall give the contractor and any subcontractors reasonable access to the dwelling for inspection and if repairs have been agreed to by the parties, reasonable access to affect repairs. Failure to respond within 30 days is deemed a denial of the claim.⁴²

The claimant shall serve a response to the contractor's offer, if any, within 10 days of receipt of the offer. If the parties cannot settle the dispute pursuant to this article, the claimant may proceed with a civil action or other remedy provided by contract or by law.⁴³

³⁷ S.C Code Ann. § 40-11-520.

³⁸ S.C. Code Ann. § 40-11-570.

³⁹ S.C. Code Ann. § 40-11-560.

⁴⁰ S.C. Code Ann. § 40-59-840.

⁴¹ S.C. Code Ann. § 40-59-840.

⁴² S.C. Code Ann. § 40-59-850.

⁴³ *Id.*

If the claimant files an action in court before first complying with the requirements of this article, on motion of a party to the action, the court shall stay the action until the claimant has complied with the requirements of this article.⁴⁴

IV. COVERAGE AND ALLOCATION ISSUES

In a recent opinion, the South Carolina Supreme Court modified its analysis as to how coverage should be determined under a CGL policy in a progressive damage situation. Prior to this opinion, the South Carolina Supreme Court focused exclusively on the definition of “occurrence” under the CGL policy.⁴⁵ However, the *Crossmann* opinion found the definition of “occurrence” was ambiguous and “elected to clarify the applicable legal framework for determining whether coverage is triggered” under a CGL policy.⁴⁶ The Court shifted the focus to “property damage” as the initial coverage trigger.⁴⁷ The Court held that any coverage analysis must begin with a determination as to whether the damage falls within the meaning of “property damage” set forth in the policy.⁴⁸ Only if that threshold question is answered in the affirmative, should a South Carolina court then consider whether there has been an “occurrence” pursuant to the policy definition.⁴⁹ Analyzing the damages through the lens of “property damage” and “occurrence,” the Court concluded that the negligent or defective workmanship itself cannot constitute “property damage” as defined in the policy.⁵⁰ The Court further found the definition of “property damage” was limited to damage to “other non-defective” elements of the construction caused by the negligent or defective workmanship.⁵¹ The South Carolina Supreme Court has also held that diminution in value is not property damage, and therefore does not give rise to an occurrence.⁵² However, the Court specifically noted that the *Crossmann* opinion did not address the impact the exclusions or exceptions contained in the CGL may have on the coverage issue.⁵³

The South Carolina Supreme Court also altered the test applicable to the allocation of progressive damages when successive CGL policies cover the property. The Court adopted the pro rata/“time on the risk” approach for this allocation analysis, overruling its prior allocation

⁴⁴ S.C. Code Ann. § 40-59-830.

⁴⁵ See *Auto Owners v. Newman*, 385 S.C. 187, 684 S.E.2d 541 (2009).

⁴⁶ *Crossmann*, Op. No. 26909 at 21-22.

⁴⁷ *Id.* at 22 (“We believe a more complete understanding of the coverage issue in this kind of progressive property damage case should involve the term ‘property damage.’”)

⁴⁸ *Id.*

⁴⁹ *Id.* at 23

⁵⁰ *Id.* (“[W]e clarify that the costs to replace the negligently constructed stucco did not constitute ‘property damage’ under the terms of the policy However, the damage to the remainder of the project caused by water penetration due to the negligently installed stucco did constitute ‘property damage.’”) See also *Stroup Sheetmetal Work, Inc. v. Aetna Casualty & Surety Co.*, 268 S.C. 203, 232 S.E.2d 885 (1977) (nothing in the policy warrants the conclusion Aetna is obligated to pay for faulty workmanship); *C.D. Walters Construction Co. v. Fireman’s Ins. Co. of Newark, N.J.*, 281 S.C. 593, 316 S.E.2d 709 (Ct. App. 1984).

⁵¹ *Id.* at 24.

⁵² See *Auto-Owners Ins. Co. v. Carl Brazell Builders, Inc.* 356 S.C. 156, 588 S.E.2d 112 (2003) (The court held that under the unambiguous language of the policies, diminution in value did not fall within the definition of property damage, and therefore, there is no coverage.).

⁵³ *Id.* (“Because the parties stipulated not to raise the issue, we do not address any policy exclusions or exceptions.”)

precedent.⁵⁴ The Court recognized that the “time on the risk” approach “best conforms to the terms of a standard CGL policy and the parties’ objectively reasonable expectations” under the policy.⁵⁵ This new approach mandates that each insurer is only responsible for a pro rata portion of the damages corresponding with the time the insurer insured the risk.⁵⁶ The Court provided a default formula to assist in calculating the share for each party, but the Court acknowledged that the trial court may have to adapt this formula to ensure that each insurer is responsible for only that portion of the property damage occurring during that party’s policy period.⁵⁷ The Court clarified that the insured would be responsible for a pro rata share of the damages for any period that the insured failed to have sufficient CGL coverage or failed to insure the property at all.⁵⁸

IV. CONTRACTUAL INDEMNIFICATION

In South Carolina, a party engaged in a construction related activity cannot contract for indemnification from its own negligence. Any attempt to do so is against public policy and is unenforceable. S.C. Code. Ann § 32-2-10 (1976) provides that:

Notwithstanding any other provision of law, a promise or agreement in connection with the design, planning, construction, alteration, repair or maintenance of a building, structure, highway, road, appurtenance or appliance, including moving, demolition and excavating, purporting to indemnify the promisee, its independent contractors, agents, employees, or indemnitees against liability for damages arising out of bodily injury or property damage proximately caused by or resulting from the sole negligence of the promisee, its independent contractors, agents, employees, or indemnitees is against public policy and unenforceable. Nothing contained in this section shall affect a promise or agreement whereby the promisor shall indemnify or hold harmless promisee or the promisee’s independent contractors, agents, employees or indemnitees against liability for damages resulting from the negligence, in whole or in part, of the promisor, its agents or employees. The provisions of this section shall not affect any insurance contract or workers’ compensation agreements; nor shall it apply to any electric utility, electric cooperative, common carriers by rail and their corporate affiliates or the South Carolina Public Service Authority.

This language has not been addressed by a South Carolina appellate court. However, it should be noted that this language is unique to construction-related entities. The South Carolina courts have upheld a party’s ability to contractually indemnify itself from its own negligence, if the language is clear and explicit.⁵⁹

⁵⁴ *Id.* (expressly overruling *Century Indemnity Co. v. Golden Hills Builders, Inc.*, 348 S.C. 559, 561 S.E.2d 355 (2002)).

⁵⁵ *Id.*

⁵⁶ *Id.* at 27 & 36.

⁵⁷ *Id.* at 41.

⁵⁸ *Id.* at 41, n. 15.

⁵⁹ In *Federal Pacific Electric v. Carolina Production Enterprises*, 298 S.C. 23, 378 S.E.2d 56 (Ct. App. 1989) the South Carolina Court of Appeals held that a party can contract for indemnification from its own negligence, but that the provision must be clear and explicit.

A contract of indemnity will be construed in accordance with the rules for the construction of contracts generally. *Longi v. Raymond-Commerce Corp.*, 34 N.J.Super. 593, 113 A.2d 69 (1955). Because it is somewhat unusual for an indemnitor to indemnify the indemnitee for losses resulting from the indemnitee’s own negligence, a contract containing an indemnity provision that purports

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to relieve an indemnitee from the consequences of its own negligence will be strictly construed. Annot., 4 A.L.R.4th 798 at 801 (1981). Indeed, most courts agree with the basic rule that a contract of indemnity will not be construed to indemnify the indemnitee against losses resulting from its own negligent acts unless such intention is expressed in clear and unequivocal terms."

Id. at 26. Courts have applied three different tests to interpret the phrase "clear and unequivocal." The court noted:

Some courts hold that the "clear and unequivocal terms" requirement is satisfied only by a specific reference in the indemnity clause to the indemnitee's negligence. Other courts take the view that words of general import are sufficient to satisfy the "clear and unequivocal terms" requirement and that a specific reference to the indemnitee's negligence is therefore not necessary. Still other courts look at the entire contract and any other factors manifesting the intention of the parties to determine whether they "clearly and unequivocally" expressed the intent to indemnify the indemnitee for its own negligence."

Id. at 27. The court found that the South Carolina Supreme Court had not specifically stated what view applied, but found that the Supreme Court had "hinted at its choice in *Murray v. The Texas Co.*, 172 S.C. 399, 402, 174 S.E. 231, 232 (1934)" *Id.*

The general rule with reference to such contract is laid down in 6 R. C. L. 727, as follows: 'It is, of course, clear that a person cannot by contract relieve himself from a duty which he owes to the public independently of the contract. Whether he can relieve himself from the duties to the other contracting party attaching as a matter of law to the relation created by the contract is more difficult to determine.'

Murray, at 232. In that case, the contract had failed to specifically state that the provision was relieving the party of all negligence, and therefore was not sufficient.

[T]he provision of a contract relieving one of the parties thereto from liability for his or its own negligence should be clear and explicit. While it is true that the language used in the quoted provision of the contract before us, that the agent shall hold the company "harmless from all claims, suits, and liabilities of every character whatsoever and howsoever arising from the existence or use of the equipment at said station," is broad and comprehensive, it is, as stated by the court below, provocative of some doubt. The defendant itself wrote the provision into the contract for its own benefit. It could have plainly stated, if such was the understanding of the parties, that the plaintiff agreed to relieve it in the matter from all liability for its own negligence. As it did not do so, we resolve all doubt, as we should, in favor of the plaintiff, and hold that it was not the intent of the parties to give to the contract as written the effect claimed by the company.

Id. The *Federal Pacific* court used this analysis in determining that the provision in question did not clearly and unequivocally indemnify the party for its own negligence. The court held that:

[r]esolving the doubt concerning the language used by the indemnity provision in Carolina Production's favor, we therefore hold that the use of the general terms "indemnify ... against any damage suffered or liability incurred ... or any loss or damage of any kind in connection with the Leased Premises during the term of [the] lease" does not disclose an intention to indemnify for consequences arising from Federal Pacific's own negligence.

This opinion was confirmed by the Supreme Court in *Laurens Emergency Medical Specialists v. M.S. Bailey & Sons Bankers*, 355 S.C. 104, 584 S.E.2d 375 (2003).

A. Attorneys' Fees

Attorney's fees generally are available only if specified in a contract, or if available by statute.⁶⁰ As noted above, the prevailing party in an action to enforce a mechanics' lien is entitled to attorneys' fees. Likewise, under S.C. Code Ann. § 27-1-15, a contractor, laborer, design professional and others may send a demand to the owner or the contractor for payment. If the party receiving the demand fails to investigate and pay the amounts due, the demanding party will be entitled to recover his attorney's fees if his claim is proven.⁶¹

B. Construction Contracts

When a builder is wrongfully prohibited from performing the contract by the owner, the builder may recover profits anticipated under the contract.⁶² Generally, when the owner has breached the contract after the builder has partially performed, the builder may recover under one of three formulae: (1) the contract price less the cost to finish the job; (2) the profits expected from the entire job plus any expenses incurred in the partial performance; or (3) the percentage of the contract price for the completed work plus the profits on the uncompleted work.⁶³ The builder is not limited to the contract price if that would not fully compensate for the work performed.⁶⁴ However, an unlicensed contractor may not recover either under contract or in equity for any work performed.⁶⁵

Damages can include the cost of labor and materials;⁶⁶ supervisory costs (including the value of the owner's time);⁶⁷ and use of tools, equipment, and overhead and operating expenses.⁶⁸

When the breach involves defective construction, damages may be measured by (1) the cost to repair or replace the defect; or (2) if repair is too expensive, the difference in value as constructed and as contracted.⁶⁹

C. Delay and Disruption Damages

The general damages for delay in completing construction are measured by the rental value of the completed building. Special damages may include the loss of any "specific

⁶⁰ *United States Rubber Co. v. White Tire Co.*, 231 S.C. 84, 97 S.E.2d 403 (1956).

⁶¹ See also S.C. Code Ann. § 29-6-50.

⁶² *Jenkins v. Charleston S.R. Co.*, 58 S.C. 373, 36 S.E. 703 (1900).

⁶³ See *Feaster v. Richland Cotton Mills*, 51 S.C. 143, 28 S.E.301 (1897); C. McCormick, *Handbook of the Law of Damages*, §§ 164, 166 (1935).

⁶⁴ See *id.*

⁶⁵ See *Skiba v. Gessner*, 374 S.C. 208, 648 S.E.2d 605 (2002).

⁶⁶ *W.F. Magann Corp. v. Diamong Mfg. Co.*, 580 F. Supp. 1299 (D.S.C. 1984), *aff'd* in part, *rev'd* in part, 775 F.2d 1202 (4th Cir. 1985).

⁶⁷ *Jowers v. Dysard Constr. Co.*, 113 S.C. 84, 100 S.E. 892 (1919).

⁶⁸ C. McCormick, *Handbook of the Law of Damages*, § 165; see also *W.F. Magann Corp.*, 580 F. Supp. 1299 (D.S.C. 1984).

⁶⁹ C. McCormick, *Handbook of the Law of Damages*, §§ 168 (1935); see also *Scott v. Fort Roofing and Sheetmetal Works, Inc.*, 385 S.E.2d 826, 299 S.C. 449 (1989); *Roland v. Palmetto Hills*, 308 S.C. 283, 417 S.E.2d 626 (App. 1992); *Joyner v. St. Mathews Builders*, 263 S.C. 136, 208 S.E.2d 48 (1974).

opportunity" to rent the building or to earn profits, provided the owner had notice of these special damages at the time of the contract.⁷⁰

A contractor may be liable for delay damages regardless of whether time was of the essence of the contract.⁷¹ Where a contract sets no date for performance, time is not of the essence of the contract and it must be performed within a reasonable time.⁷²

D. Unjust Enrichment

South Carolina follows the rule in many states that sub-contractor's claims of unjust enrichment will usually be denied where the owner in fact has paid on its contract with the general.⁷³

E. Builder's Personal Liability for Negligent Construction

The Residential Home Builders Act does not create a legal duty for a residential builder license holder that can serve as the basis for a negligent construction claim.⁷⁴

F. Economic Loss Rule

South Carolina law generally follows the economic loss rule, which limits a plaintiff to contract remedies if the plaintiff has suffered only an economic loss with no personal injury or property loss.⁷⁵ However, the South Carolina Supreme Court has refused to apply this restrictive rule to a builder who violated building codes in such a way that he knew or should have known the violations posed a risk of physical harm.⁷⁶

In 2008, the South Carolina Supreme Court partially extended this exception to commercial construction matters, holding that, when there is a breach of a legal duty owed, accompanied by a clear, serious and unreasonable risk of bodily injury or death, the user of a defective product can recover in tort even though only the product itself has been injured.⁷⁷

G. Interest

In all cases of accounts stated and in all cases wherein any sum or sums of money shall be ascertained and, being due, shall draw interest according to law, the legal interest shall be at

⁷⁰ *Id.* § 70.

⁷¹ *See Drews Co. v. Ledwith-Wolfe Associates, Inc.*, 296 S.C. 207, 212 (S.C. 1988), *citing* 17A C.J.S. Contracts § 502(4)(a) (1963).

⁷² *Id.*, *citing General Sprinkler Corp. v. Loris Industrial Developers, Inc.*, 271 F. Supp. 551, 557 (D.S.C. 1967).

⁷³ *See Columbia Wholesale v. Scudder May, N.V.*, 312 S.C. 259, 440 S.E.2d 129 (1994).

⁷⁴ *16 Jade Street, LLC v. R. Design Const. Co., LLC.*, 405 S.C. 384, 747 S.E.2d 770 (2013).

⁷⁵ *See Sapp v. Ford Motor Co.*, 386 S.C. 143, 687 S.E.2d 47 (2009).

⁷⁶ *Kennedy v. Columbia Lumber & Mfg. Co.*, 299 S.C. 335, 384 S.E.2d 730 (1989),

⁷⁷ *Colleton Preparatory Academy, Inc. v. Hoover Universal, Inc.*, 379 S.C. 181, 666 S.E.2d 247 (2008), *overruled on other grounds by Sapp v. Ford Motor Co.*, 386 S.C. 143, 687 S.E.2d 47 (2009).

the rate of 8.75% per annum.⁷⁸ Interest may also be awarded if an owner or contractor fails to timely make periodic or final payment of properly submitted invoices.⁷⁹ However, this provision does not apply to residential builders or persons making improvements to residential property consisting of 16 or fewer units.⁸⁰

H. Punitive Damages

Punitive damages will not generally be awarded for breach of contract, unless the breach is accompanied by a fraudulent act independent of the act constituting the breach. However, a builder may be liable in punitive damages for gross negligence.⁸¹

⁷⁸ S.C. Code Ann. § 34-31-20. See also S.C. Code Ann. § 27-1-15 (interest allowed if a proper demand is not investigated and paid); *Hardaway Concrete Co., Inc. v. Hall Contracting Corp.*, 374 S.C. 216, 647 S.E.2d 488, (Ct. App. 2007).

⁷⁹ S.C. Code Ann. § 29-6-50.

⁸⁰ S.C. Code Ann. § 29-6-60.

⁸¹ *Kennedy*, 299 S.C. at 350, 384 S.E.2d at 737.

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I. MECHANIC'S LIENS BASICS

The following is a brief summary of the relevant sections of the South Dakota Codified Laws Chapter 44-9 which govern the filing and perfection of mechanics' liens. However, it is important to note that § 44-9-49 provides that failure to comply with this Chapter does not bar the owner of a claim from bringing the claim as an "ordinary civil action."¹

A. Requirements

Notice. As against the owner of the property, a mechanic's lien shall attach and take effect from the time the first item of material or labor is furnished upon the premises by the lien claimant, and shall be preferred to any mortgage or other encumbrance not then of record, unless the lien holder had actual notice thereof.² As against a bona fide purchaser, mortgagee, or encumbrancer without notice, no lien shall attach prior to the actual and visible beginning of the improvement on the ground, but a person having a contract for the furnishing of labor, skill, material, or machinery for such improvement, may file with the register of deeds of the county within which the premises are situated or of the county to which such county is attached for judicial purposes, or if claimed under subdivision 44-9-1(2), with the Secretary of State, a brief statement of the nature of such contract, which shall be notice of his lien for the contract price or value of all contributions to such improvement thereafter made by him or at his instance.³

Mechanic's Lien Statement. At the end of 120 days after doing the last of such work or after furnishing the last item of such skill, services, material or machinery, the lien shall cease within such period unless a statement of the claim is filed with the register of deeds of the county in which the improved premises are situated or of the county to which such county is attached for judicial purposes,⁴ or if the claim be under the provision of subdivision 44-9-1-(2), with the Secretary of State. Such statement shall be made by or at the instance of the lien claimant, shall be verified by the oath of some person shown by such verification to have knowledge of the facts stated, and shall set forth:

- (1) A notice of intention to claim and hold a lien, and the amount thereof;
- (2) That such amount is due and owing to the claimant for labor performed, or for skill, services, material, or machinery furnished, and for what improvement the same was done or supplied;

(3) The names and post office address of the claimant, and of the person for or to whom performed or furnished;

(4) The dates when the first and last items of the claimant's contribution were made;

(5) A description of the property to be charged, identifying the same with reasonable certainty;

(6) The name and address of the owner at the time the statement is made, according to the claimant's best information at the time; and

(7) An itemized statement of the account upon which the lien is claimed.⁵

Before filing the lien statement, the claimant must mail to the property owner at his or her last known address a copy of such lien statement by registered or certified mail. The receipt for such mailing shall be attached to the lien statement and filed in the office of the register of deeds.⁶

B. Enforcement and Foreclosure.

The lien may be enforced by action in the circuit court of the county in which the improved premises or some part thereof are situated, or of the county to which such county is attached for judicial purposes.⁷ Upon written demand of the owner, the owner's agent, or contractor, served on any person holding a lien, requiring the person to commence suit to enforce such lien, such suit shall be commenced within thirty days after such service, or the lien shall be forfeited.⁸

At the time the action is commenced, the claimant must file notice of the pending claim with the register of deeds of the county in which the action is pending and of the several counties into which the utility extends, if the lien is claimed under subdivision 44-9-1(2).⁹

No lien shall be enforced in any case unless the holder asserts the same, either by complaint or answer, within six years after the date of the last item of his claim as set forth in the lien statement; nor shall any person be bound by judgment unless he is made a party within six years.¹⁰

C. Ability to Waive and Limitations on Lien Rights

Liens for materials, supplies, equipment, and services furnished under construction contracts to contractors or subcontractors may be expressly waived upon the execution of a joint check wherein the payees include the contractor or subcontractor and the person or corporation furnishing the materials, supplies, equipment, and services. The joint check must make reference to a separate written agreement of waiver in a conspicuous manner on the reverse side.¹¹

Further, in order to enforce a mechanics' lien generally, the lien-holder must comply with the provisions of Chapter 44-9. Note: failure to comply with Chapter 44-9 does not limit the right to recover in an ordinary civil action, even if the lien is deemed waived for failure to comply.¹²

II. STATUTES OF LIMITATIONS AND REPOSE

A. Statutes of Limitation and Limitations on Application of Statutes

The following is a brief summary of the relevant sections of the South Dakota Codified Laws Chapter 15-2, which govern limitation periods for general claims of breach of contract, § 44-9-24, which provides the limitation for foreclosing liens specifically, and 15-2A, which specifically addresses the limitation periods relating to claims for construction deficiency.

Limitation of Actions Generally

An action upon contract, obligation or liability express or implied, can be commenced only within six years after the cause of action shall have accrued.¹³

Limitation on Enforcement of Liens

An action foreclosing an lien must be commenced within six years after the date of the last item of the claim as set forth in the lien statement. No person shall be bound by a judgment under this Chapter unless he is made a party within six years.¹⁴

B. Statutes of Repose and Limitations on Application of Statutes

No action to recover damages for any injury to real or personal property, for personal injury or death arising out of any deficiency in the design, planning, supervision, inspection, and observation of construction, of an improvement to real property, nor any action for contribution or indemnity for damages sustained on account of such injury or death, may be brought against any person performing or furnishing the design, planning, supervision, inspection, and observation of construction, or construction, of such an improvement more than ten years after substantial completion of such construction. The date of substantial completion shall be determined by the date when construction is sufficiently completed so that the owner or his representative can occupy or use the improvement for the use it was intended.¹⁵

The Eight Circuit has concluded that South Dakota would follow the standard rule adopted by many states in defining the phrase “improvement to real property” for the purposes of interpreting its limitation statutes. “Generally, in determining whether a modification of or addition to real property is an improvement, courts have adopted a commonsense interpretation of the word ‘improvement.’...Among the factors considered are whether the modification or addition enhances the use of the property, involves the expenditure of labor or money, is more than mere repair or replacement, adds to the value of the property, and is permanent in nature.”¹⁶

The statute may not be asserted by way of defense by any person in actual possession and control as owner, tenant or otherwise, of the improvement at the time any deficiency constitutes the proximate cause of an injury or death for which it is proposed to bring an action.¹⁷

For injuries occurring during the tenth year after substantial completion of the construction, an action may be brought within one year after the date on which such injury occurred, but not later than eleven years after the substantial completion of construction of such improvement.¹⁸

The statute may not be asserted as a defense by any person guilty of fraud, fraudulent concealment, fraudulent misrepresentations or willful or wanton misconduct in furnishing the design, planning, supervision, inspection and observation of construction, or construction, of improvements to real property.¹⁹

The statute does not prohibit any action against a defendant who has expressly warranted or guaranteed the improvement to real property for a longer period from being brought within that period.²⁰

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

Any person furnishing any of the items for which a lien may be claimed under the provisions of § 44-9-1 may serve upon the property owner a sworn account and notice of his claim showing the items and amounts and the dates that the same were furnished. The owner is then entitled to withhold payment from the contractor as may be necessary to meet the claims of persons who have served such notice.²¹

Before filing a lien statement as required prior to filing a claim to enforce a lien, the person claiming the lien shall mail the property owner by registered or certified mail, a copy of the lien statement. The post office receipt for the mailing shall be attached to the lien statement and filed in the office of register of deeds.²² The property owner is obliged to provide a copy of any claim to the contractor, and if the contract does not give written notice that he intends to dispute within 15 days, then the contractor is deemed to assent to the claim.²³

The right of redemption for all estates to be foreclosed other than leaseholds shall be the same as upon execution sales.²⁴

Whenever a lien is claimed, and subsequently satisfied by payment, foreclosure, compromise, or another method, such satisfaction shall be executed and delivered to the owner of the property. The satisfaction is to be executed before two witnesses or acknowledged by a notary before being filed with the register of deeds.²⁵ If the lien-holder fails to execute the satisfaction as provided in § 44-9-21 within ten days after written demand by the property owner, then the lien-holder becomes liable to the owner for all damages, costs, and expenses including attorneys' fees, and a one hundred dollar penalty.²⁶

IV. INSURANCE COVERAGE AND ALLOCATION ISSUES

A. General Coverage Issues

An insurance contract will be interpreted according to its plain and ordinary meaning.²⁷ The scope of coverage of insurance policy is determined by intent and the objectives of the

parties as expressed in the contract.²⁸ If an insurance contract is ambiguous, the contract will be construed liberally in favor of the insured, and strictly against the insurer.²⁹

B. Trigger of Coverage

The trigger of insurance coverage will be determined by the contract between the parties. There are no specific statutory provisions regarding this issue in South Dakota.

C. Allocation Among Insurers

South Dakota does have an anti-indemnity statute for the liability for negligence in construction, repair, or maintenance of a structure or equipment.³⁰ However, there is no bar against contracting to add another as an additional insured, thus effectively allocating risk of liability as if one was indemnifying the other.

V. CONTRACTUAL INDEMNIFICATION

Construction contracts, plans and specifications which contain indemnification provisions shall include the following provisions:

The obligations of the contractor shall not extend to the liability of the architect or engineer, his agents or employees arising out of:

- (1) The preparation or approval of maps, drawings, opinions, reports, surveys, change orders, designs or specifications, or
- (2) The giving of or the failure to give directions or instructions by the architect, or engineer, his agents or employees provided such giving or failure to give is the primary cause of the injury or damage.³¹

Any indemnification provision in a construction contract in conflict with § 56-3-16 shall be unlawful and unenforceable.³²

A covenant, promise, agreement or understanding in, or in connection with, or collateral to, a contract or agreement relative to the construction, alteration, repair or maintenance of a building, structure, appurtenance and appliance, including moving, demolition and excavating connected therewith, purporting to indemnify the promise against liability for damages arising out of bodily injury to persons or damage to property caused by or resulting from the sole negligence of the promise, his agents or employees, or indemnitee, is against the policy of the law and is void and unenforceable.³³

VI. CONTINGENT PAYMENT AGREEMENTS

A. Enforceability

No case or statutory law on the subject. Note, however that penalties imposed by contract for the nonperformance of the same are void, unless those provisions are commonly used, wherein the penal clause will be all that is void.³⁴

B. Requirements

No case or statutory law on the subject.

VII. DAMAGE LIMITATIONS

A. Personal Injury Damages vs. Construction Defect Damages

For the breach of an obligation not arising from contract, the measure of damages is the amount which will compensate for all detriment proximately caused thereby, unless otherwise provided for.³⁵

There is no further limitation on damages, or tort reform legislation, concerning claims that may arise from claims for personal injury or construction defect.

B. Attorney's Fees Shifting and Limitations on Recovery

Attorney fees must be provided for in contract, or by statute, to be recoverable.³⁶ There are no further limitations, other than general provisions governing unlawful contracts in Chapter 53-9.

C. Consequential Damages

The measure of damages for breach of contract is for clearly ascertainable damages that are reasonably likely to occur, thereby preempting any claim for consequential damages.³⁷ The measure of damages for tort, however, do not require foreseeability.³⁸ There being no other applicable limitation on damages, a claim arising from tort as opposed to breach of contract would appear to allow for consequential damages.

D. Delay and Disruption Damages

No specific limitations for delay or disruption damages beyond those noted previously, and in Economic Loss Doctrine, along with more general provisions in Chapters 21-2 and 21-3.

E. Economic Loss Doctrine

A Plaintiff may not recover on a claim for damages in tort for economic loss alone. Damages for breach of contract must not be uncertain.³⁹

F. Interest

Unless otherwise established, there is no maximum interest rate or charge, or usury rate restriction between any persons or entities so long as the rate is established by written agreement.⁴⁰ If the period of time is not specified, it is presumed an annual rate.⁴¹

G. Punitive Damages

A jury may award punitive damages for breach of any obligation not arising from contract when the defendant is guilty of oppression, fraud, malice, actual or presumed, committed intentionally or by willful and wanton misconduct.⁴²

Negligence alone is not sufficient for punitive damages.⁴³

H. Other Damage Limitations

No other damage limitations created by statute or provided by case law.

¹ S.D. CODIFIED LAWS § 44-9-49.

² S.D. CODIFIED LAWS § 44-9-7.

³ S.D. CODIFIED LAWS § 44-9-8.

⁴ S.D. CODIFIED LAWS § 44-9-15.

⁵ S.D. CODIFIED LAWS § 44-9-16.

⁶ S.D. CODIFIED LAWS § 44-9-17.

⁷ S.D. CODIFIED LAWS § 44-9-23.

⁸ S.D. CODIFIED LAWS § 44-9-26.

⁹ S.D. CODIFIED LAWS § 44-9-28.

¹⁰ S.D. CODIFIED LAWS § 44-9-24.

¹¹ S.D. CODIFIED LAWS § 44-9A-1 *et seq.*

¹² S.D. CODIFIED LAWS § 44-9-49.

¹³ S.D. CODIFIED LAWS § 15-2-13(1).

¹⁴ S.D. CODIFIED LAWS § 44-9-24.

¹⁵ S.D. CODIFIED LAWS § 15-2A-3.

¹⁶ *Van Den Hul v. Baltic Farmers Elevator Co.*, 716 F.2d 504, 508 (8th Cir. 1983)(citations omitted).

¹⁷ S.D. CODIFIED LAWS § 15-2A-4.

¹⁸ S.D. CODIFIED LAWS § 15-2A-5.

¹⁹ S.D. CODIFIED LAWS § 15-2A-7.

²⁰ S.D. CODIFIED LAWS § 15-2A-8.

²¹ S.D. CODIFIED LAWS § 44-9-10.

²² S.D. CODIFIED LAWS § 44-9-17.

²³ S.D. CODIFIED LAWS § 44-9-11.

²⁴ S.D. CODIFIED LAWS § 44-9-45.

²⁵ S.D. CODIFIED LAWS § 44-9-21.

²⁶ S.D. CODIFIED LAWS § 44-9-22.

²⁷ *St. Paul Fire and Marine Ins. Co. v. Schilling*, 520 N.W.2d 884 (S.D. 1994).

²⁸ *Id.*

²⁹ *Id.*

³⁰ S.D. CODIFIED LAWS § 56-3-18.

³¹ S.D. CODIFIED LAWS § 56-3-16; *see Hennigan, Durham & Richardson, Inc. v. Swift Brothers Construction Co.*, 739 F.2d 1341 (8th Cir. 1984).

³² S.D. CODIFIED LAWS § 56-3-17.

³³ S.D. CODIFIED LAWS § 56-3-18.

³⁴ S.D. CODIFIED LAWS § 53-9-4.

³⁵ S.D. CODIFIED LAWS § 21-3-1.

³⁶ *Lord v. Hy-Vee Food Stores*, 720 N.W.2d 443 (S.D. 2006).

³⁷ S.D. CODIFIED LAWS § 21-2-1.

³⁸ S.D. CODIFIED LAWS § 21-3-1.

³⁹ S.D. CODIFIED LAWS § 21-2-1.

⁴⁰ S.D. CODIFIED LAWS § 54-3-1.1.

⁴¹ S.D. CODIFIED LAWS § 54-3-3.

⁴² S.D. CODIFIED LAWS § 21-3-2.

⁴³ *Grynberg v. Citation Oil & Gas Corp.*, 573 N.W.2d 493, 506 (S.D. 1997).

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I. MECHANIC'S LIEN

The purpose of Tennessee's materialman lien statute, T.C.A. § 66-11-101 et seq., is to provide owners, general contractors, subcontractors, or other suppliers with sufficient notice that a subcontractor has not been paid. More importantly, it provides the subcontractor an opportunity to obtain a security interest in the real property for which they have improved.

There are two ways in which to perfect a mechanic's lien that hinge on whether the claimant has a direct contract with the owner or whether the claimant has no contract (i.e. subcontractor) with the owner of the property. In order to perfect a mechanic's lien in Tennessee, you should consider the following:

A. Direct Contract

In order to preserve a lien where the claimant has a direct contract with the owner, a suit must be filed within one (1) year. Pursuant to T.C.A. § 66-11-106, there is an automatic lien that runs from the completion of the project for a period of one year, including the time it takes to include any lawsuit for enforcement brought within the one year time period.

B. No Direct Contract

1. Notice

T.C.A. § 66-11-115 provides that every journeyman or other person contracted with or employed to work on the buildings, fixtures, machinery, or improvements, or to furnish materials for the same must send a notice of nonpayment within 90 days after the demolition and/or building or improvement is completed, or the contract of such laborer, mechanic, furnisher, or other person shall expire, or such person is discharged, such person shall notify, in writing, the owner of the property on which the building is being erected or the improvement is being made, or the owner's agent or attorney, if the owner resides out of the county, that the lien is claimed. If this notice is not provided, any lien will be invalid.

2. Mechanic's Lien Statement of Nonpayment

T.C.A. § 66-11-145 provides that a person seeking to enforce a mechanic's lien shall provide, within ninety (90) days of the last day of the month within the work, services or materials were provided, a notice of nonpayment for such work, services or materials to the owner and contractor contracting with the owner if its account is unpaid. The notice shall be served by registered or certified mail, return receipt requested; hand delivery with sworn statement, properly notarized, confirming delivery of written notice; or any other commercial delivery service which can confirm delivery of the notice. It should contain the following information:

- (1) The name of the subcontractor, laborer or materialman and the address to which the owner and the contractor contracting with the owner may send communications to the subcontractor, laborer or materialman;
- (2) A general description of the work, services or materials provided;
- (3) A statement of the last date the claimant performed work and/or provided services or materials in connection with the improvements; and
- (4) A description sufficient to identify the real property against which a lien may be claimed.

3. Statute of Limitations on Mechanic's Lien

Pursuant to T.C.A. § 66-11-115(c), the lien will continue in favor of the claimant for ninety (90) days from the date of notice (*as described in section I. (B) (1) above*). If the lien remains unsatisfied and the claimant fails to file suit within this time, the claim is forfeited. Thus, the claimant must file suit in order to retain a lien within ninety (90) days from the date notice is served.

4. Enforcement of Mechanic's Lien

Pursuant to T.C.A. § 66-11-126, enforcement of a mechanic's lien will be by attachment in court of law or equity or before a court of general sessions upon petition at law or bill in equity, filed under oath, setting forth the facts, describing the property, and making the necessary parties defendant. The writ of attachment should be accompanied by a warrant for the sum

claimed, to be served upon the owner and may within the discretion of the claimant be served upon the contractor, or subcontractor in any degree, with whom the claimant is in contractual relation. Nevertheless, the owner shall have the right to make the contractor or subcontractor a defendant by cross-action or cross-bill.

5. Effect of Filing of Notice of Completion

Where an owner wishes to file a notice of completion in order to be protected from lien claims which have not previously been registered, the owner must send all contractors, subcontractors, and material suppliers a copy of the notice. If the claimant has waited until after receiving the notice of completion to make a claim and the notice of completion is filed before the claimant provides notice of the lien claim, then the claimant has thirty (30) days from the date of filing of the notice of completion to file a claim for a mechanic's lien.

6. Contracting Without a License, and Loss of Lien Rights

Contracting, including offering to contract, without a license, or doing so above the limit of one's license, bars the contractor from asserting any lien rights. The statute, and Tennessee case law in this regard, is unforgiving. If deemed in violation of the statute, the contractor can recover only actual documented expenses as shown by clear and convincing evidence. Beginning January 1, 2014, the Contractor's Licensing Board has discretion to, in effect, waive a contractor's violation of the licensing limit provision, but contractors would be well-advised not to rely on such discretion.

62-6-103. License requirement – Recovery of expenses by unlicensed contractor.
[Effective on January 1, 2014.]

(a) (1) Any person, firm or corporation engaged in contracting in this state . . . shall be licensed as provided in this part. It is unlawful . . . to engage in or offer to engage in contracting . . . unless . . . duly licensed with a monetary limitation sufficient to allow the person, firm, or corporation to engage in or offer to engage in such contracting project.

The board for licensing contractors shall have the authority to grant or allow an exception, in an amount not to exceed ten percent (10%), to the monetary limitation of such license provided in this subdivision (a)(1).

(b) Any contractor . . . in violation of this part . . . shall not be permitted to recover any damages in any court other than actual documented expenses that can be shown by clear and convincing proof.

II. STATUTES OF LIMITATION AND REPOSE

A. Statute of Limitations

Tennessee has a one-year statute of limitation for personal injury actions (T.C.A. §28-3-104(a)(1)) and a three-year statute of limitations for property damage claims (T.C.A. §28-3-105(1)).

Both the personal injury and property damage statutes begin to run when the cause of action accrues. Under Tennessee law, a cause of action accrues when a plaintiff knew or reasonably should have known that a cause of action existed. *Stone v. Hines*, 541 S.W.2d 598 (1976).

Although Tennessee has a general six (6) year statute of limitations for breach of contract actions, it is clear that under Tennessee law an action for defective construction is subject to the three (3) year statute of limitations as opposed to the six (6) year breach of contract statute (T.C.A. §28-3-109(a)(3)). In addition, Tennessee courts consistently look to the “gravamen” of the complaint and not to what the plaintiff calls its cause of action (i.e. either “contract” or “tort”) in determining the applicable statute of limitations. *Keller v. Colgems-EMI Music, Inc.*, 924 S.W.2d 357 (1996).

B. Statute of Repose

T.C.A. §28-3-202 provides:

All actions to recover damages for any deficiency in the design, planning, supervision, observation of construction, or construction of an improvement to real property, for injury to property, real or personal, arising out of any such deficiency, or for injury to the person or for wrongful death arising out of any such deficiency, shall be brought against any person performing or furnishing the design, planning, supervision, observation of construction, construction of, or land surveying in connection with, such an improvement within four (4) years after substantial completion of such an improvement.

The term “substantial completion” is defined by statute to mean “that degree of completion of a project, improvement or a specified improvement, or a specified area or portion thereof (in accordance with the contract documents, as modified by any change orders agreed to by the parties) upon attainment of which the owner can use the same for the purpose for which it was intended; the date of substantial completion may be established by written agreement between the contractor and the owner.” T.C.A. §28-3-201(2).

Notwithstanding the above, T.C.A. §28-3-203 provides that if the injury to property or person occurs during the fourth (4th) year after substantial completion, then the action may be brought within one (1) year after the date on which such injury occurred, but in no event may it be brought more than five (5) years after the substantial completion of any such improvement.

It is clear that under Tennessee law, the above statute of limitation does not extend either the one (1) or three (3) year periods for filing actions based upon personal injuries and property damages. In other words, if a person is injured as the result of a construction deficiency, then that suit must still be brought within one (1) year of the date of injury. If that personal injury occurs

outside of the time period set forth in the statute of repose, then the claim is barred. The same result holds for property damage claims.

There are a couple of exceptions to the above statute of repose, however. First, if the alleged negligent party is in actual possession or control of the improvement (as owner, tenant, or otherwise) at the time the deficiency causes the injury in question, then that party cannot rely upon the statute of repose. For example, this would prevent a developer who maintains control and operation of an apartment complex from relying upon the four (4) year statute of repose if a tenant is injured as the result of a construction defect.

In addition, T.C.A. §28-3-205(b) provides that the statute of repose cannot be used as a shield by a person who has “been guilty of fraud in performing or furnishing the design, planning, supervision, observation of construction, construction of, or land surveying, in connection with any such improvement, or to any person who shall wrongfully conceal any such cause of action.” This is obviously a public policy exception to the running of the statute of repose.

Not unexpectedly, plaintiffs’ attorneys have sought innovative ways to get around the statute of repose. For example, in construction defect cases involving homeowners, claims are often raised under the Tennessee Consumer Protection Act, which like most states’ consumer statutes, offers a broad range of remedies for various acts and omissions.

In a recent decision of the Tennessee Eastern Section Court of Appeals, it was held that the statute of repose did in fact bar a Tennessee Consumer Protection Act claim relating to alleged defective construction. In *Cunha v. Cecil*, 2007 WL 273753 (Tenn. Ct. App.), the plaintiffs claimed that the statute of repose should not apply because the defendant made a series of promises to correct the deficiency but never followed through with those repairs. Plaintiffs argued that as such, their claims were proper under the Tennessee Consumer Protection Act and did not fall within the scope of the statute of repose. The Trial Court had disagreed and granted summary judgment based upon the statute of limitations, and the Court of Appeals affirmed.

This decision is even broader because the defendant was the seller of the home that had partnered with a builder in the housing development. Plaintiffs argued that since the defendant was merely a “vendor”, it did not come within the scope of the statute of repose to begin with.

The Court, finding that the seller was involved in a joint venture with the builder, held that it was entitled to protection under the statute of repose.

Plaintiffs further argued that the defendant should be estopped from claiming the benefit of the statute of repose because of its alleged repeated promises to make repairs that were not completed. The Trial Court held that there was insufficient evidence to establish an estoppel, and the Appellate Court did not disturb that finding.

In sum, the Tennessee statute of repose provides a clear outer limit for liability to all parties to the construction process save and except for an owner that maintains control and possession of the property. This is true regardless of whether or not the injury is one for property

damage, personal injury or even wrongful death.

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

In 2004, Tennessee enacted legislation requiring commercial property owners to give pre-suit notice of a construction defect, and to allow any notified and allegedly responsible parties access to the project to inspect the alleged conditions and an opportunity to cure the defects. The Act applies to all claims for construction defects accruing on or after May 24, 2004. T.C.A. §66-36-101 *et seq.* For the unacquainted, the Act can be easily miscomprehended without careful review of the definitions section, T.C.A. §66-36-101, and the procedural steps for giving notice and responding set out in T.C.A. §66-36-1031. For example, the limitation of the Act to commercial projects arises from the definition of “action”:

“any civil action for damages or indemnity asserting a claim for damage to or loss of commercial property caused by an alleged construction defect, but does not include any civil action or arbitration proceeding asserting a claim for alleged personal injuries arising out of an alleged construction defect.”

Under the Act, a "construction defect" is defined as “a deficiency in, or a deficiency arising out of, the design, specifications, surveying, planning, supervision, observation of construction, or construction or remodeling of a structure resulting from:

- (A) Defective material, products, or components used in the construction or remodeling;
- (B) A violation of the applicable codes in effect at the time of construction or remodeling;
- (C) A failure of the design of a structure to meet the applicable professional standards of care at the time of governmental approval, construction or remodeling; or
- (D) A failure to construct or remodel a structure in accordance with accepted trade standards for good and workmanlike construction at the time of construction or remodeling; T.C.A. §66-36-101(1).

Another key definition is “contractor”, which is defined as any person, firm, partnership, corporation, association, or other organization that is legally engaged in the business of designing, developing, constructing, manufacturing, selling, or remodeling structures or appurtenances to structures. T.C.A. §66-36-101(4).

T.C.A. §66-36-103 sets forth the pre-suit notice procedure, and response duties and timeline for responding to the notice. In brief, the Act generally provides that a commercial property owner must forward written notice of the defect to the last known address of the

contractor, subcontractor, supplier or design professional within 15 days of discovery, but failure to give notice within 15 days does not bar the action.

The Act contemplates that all potentially responsible parties will receive notice and have an opportunity to inspect the conditions. By way of example, upon the contractor's receipt of the notice, the contractor must, within 10 days of receipt of the notice, notify all subcontractors, suppliers, or designers that may be responsible for the defects. Those parties are then afforded 10 days from that notice to likewise inspect the defects. Within 30 days of receipt of notice, every notified party must provide the claimant with a written response in which the responding party may: (1) offer to cure the defect, including a timetable for completing the work; (2) settle the claim by monetary payment; or (3), dispute the claim.

Importantly, any offer to cure or settle a claim must be rejected in writing, and must specifically state "rejected" on the rejection. T.C.A. §66-36-103(h). While no Tennessee case has so held, it would seem plausible under this provision of the Act that a contractor's offer to cure or settle, if not properly rejected, constitutes a claimant's acceptance.

Finally, T.C.A. §66-36-103(l) provides that a claimant's written notice tolls the applicable statute of limitations until the later of:

- (1) One hundred eighty (180) days after the contractor, subcontractor, supplier, or design professional receives the notice; or
- (2) Ninety (90) days after the end of the correction or repair period stated in the offer, if the claimant has accepted the offer. By stipulation of the parties, the period may be extended and the statute of limitations is tolled during the extension.

Aside from the statutory notice and cure provisions of Tenn. Code Ann. § 66-36-101 *et seq.*, Tennessee common law imposes a general duty to give notice of a construction defect and to allow the defaulting party to repair the defective work, to reduce the damages, to avoid additional defective performance and to promote settlements of disputes. *McClain v. Kimbrough Constr. Co., Inc.*, 806 S.W.2d 194, 198 (Tenn. Ct. App. 1990).

In *McClain*, the Court imposed upon a contractor a duty to give its subcontractor notice and an opportunity to cure alleged defects prior to terminating a contract for a commercial construction project. *Id.* at 198-99. The rule requiring giving notice and an opportunity to cure has also been extended to cases involving residential construction. *E.g., Greeter Const. Co. v. Tice*, 11 S.W.3d 907, 910-11 (Tenn. Ct. App. 1999); *Lavy v. Carroll*, No. M2006-00805-COAR3-CV, 2007 Tenn. App. LEXIS 809, at **9-10 (Tenn. Ct. App. Dec. 26, 2007), *Rule 11 appl. perm. appeal denied May 27, 2008*; and *Custom Built Homes by Ed Harris v. McNamara*, No. M2004-02703-COA-R3-CV, 2006 Tenn. App. LEXIS 781, at 14-15 (Tenn. Ct. App. Dec. 11, 2006), *no appl. perm. appeal filed*.

IV. INSURANCE COVERAGE AND ALLOCATION ISSUES

A. Coverage Issues

Under Tennessee law, a liability insurer's duty to defend is determined by comparing the allegations of the complaint filed against the insured with the terms of the insurance policy. *Drexel Chem Co. v. Bituminous Ins. Co.*, 933 S.W.2d 471, 480 (Tenn. App. 1996). If the allegations of the complaint against the insured are potentially within the coverage of the insurance policy, the insurer has a duty to defend. *Id.* An insurer's duty to indemnify its insured, by contrast, is based upon the "actual facts", rather than the complaint allegations. *St. Paul Fire & Marine Ins. Co. v. Torpoco*, 879 S.W.2d 831, 834 (Tenn. 1994). Where the allegations in the complaint against the insured are ambiguous and there is doubt whether they trigger coverage, the doubt should be resolved in favor of the insured. *Dempster Bros., Inc. v. U.S. Fidelity & Guar. Co.*, 388 S.W.2d 153, 156 (Tenn. 1964).

Under Tennessee law, an unambiguous exclusionary clause precludes coverage and the courts should give the words and exclusionary clauses their ordinary meaning. *Blaine Const. Corp. v. Insurance Co. of North America*, 171 F.3d 343 (6th Cir. 1999). Tennessee follows the general insurance law rule that "exceptions, exclusions and limitations in policies of insurance are to be most strongly construed against the insurer." *Travelers Ins. Co. v. Aetna Cas. & Surety Co.*, 491 S.W.2d 363, 367 (Tenn. 1973).

In a typical "all risk" policy, coverage extends to risks not usually contemplated, and recovery under the policy will generally be allowed at least for all losses of a fortuitous nature in the absence of fraud or other intentional misconduct of the insured unless the policy contains a specific provision expressly excluding the loss from coverage. *HCA, Inc. v. American Protection Ins. Co.*, 174 S.W.3d 184 (Tenn. App. 2005).

As in most states, many disputes arise over the issue of what is or is not covered by "faulty workmanship". Generally, damage to the insured's property caused by faulty workmanship is an insured risk under a general liability policy unless expressly eliminated by an exclusion provision. The defective work itself, however, is not covered. In 2007, with its decision in *Travelers Indem. Co. of America v. Moore & Associates, Inc.*, 216 S.W.3d 302 (Tenn. 2007), the Tennessee Supreme Court joined with a growing minority of states in finding that defective workmanship may constitute an "occurrence" and that damage caused by faulty workmanship is "property damage."

Commercial general liability (CGL) insurance policies cover risks that the insured's product or work will cause bodily injury or damage to property other than the work itself for which the insured may be found liable. *Standard Fire Ins. Co. v. Chester O'Donley & Associates, Inc.*, 972 S.W.2d 1 (Tenn. App. 1998).

B. Allocation Issues

The allocation of a loss depends initially whether or not the policy is a "claims-made" or "occurrence" policy. An "occurrence" policy protects the insured against incidents that occur while the policy is in force, even if the claim that arises from that incident is not filed until after the policy expires or is terminated. *Pope v. Leut & Heath, PLLC*, 87 S.W.3d 89 (Tenn. App.

2002). On the other hand, a “claims-made” policy protects an insured against claims that are filed while the policy is in force, even if the incident giving rise to the claim occurred before the policy was executed. *Id.*

C. Trigger of Coverage

Although there is a scarcity of case law in Tennessee on the issue, it appears that Tennessee follows the continuous trigger theory, i.e. where a progressive injury existed over multiple policy periods. In *State Farm Fire & Cas. Co. v. McGowan*, 421 F.3d 433, (6th Cir. 2005), a claim was made relating to a rotting tree that was left standing adjacent to an insured apartment building. The insured (on whose property the rotten tree was situated) made a claim against its insurer for the time period that the tree was rotting. The tree later fell and killed someone after the subject policy had expired. Nonetheless, the court held that because the language of the applicable coverage period and definitions were ambiguous, there was potentially an “accident” and thus an “occurrence” under the policy.

In another unreported case, *State Auto Mutual Ins. Co. v. Shelby Mut. Ins. Co.*, 1988 WL 67155 (Tenn. Ct. App.1988), the Tennessee Court of Appeals held that an insured cannot “enjoy completed operations coverage indefinitely” after the coverage period. If a complaint alleges injury from a continuous exposure over a specific time, however, there will probably be coverage even though the continuous exposure extends past the policy period. The expiration of the policy should not bar pro rata responsibility on a prior carrier in a continuous exposure situation. The prior carrier would receive an undue windfall if the subsequent carrier were charged with the entire loss.

Under a continuous trigger situation, it is likely that the Tennessee courts would apply a pro rata approach in allocating the loss among the various carriers that afforded coverage to the insured during the applicable time periods. This is the general rule from other jurisdictions, specifically including most states within the Sixth Circuit of which Tennessee is a part.

V. CONTRACTUAL INDEMNIFICATION

Tennessee law does not permit contractual provisions in connection with or collateral to an agreement to improve a structure or real estate which indemnify the promisee for negligence caused solely by such promisee. T.C.A. § 62-6-123 states that:

A covenant promise, agreement or understanding in or in connection with or collateral to a contract or agreement relative to the construction, alteration, repair or maintenance of a building, structure, appurtenance and appliance, including moving, demolition and excavating connected therewith, purporting to indemnify or hold harmless the promisee against liability for damages arising out of bodily injury to persons or damage to property caused by or resulting from the sole negligence of the promisee, the promisee’s agents or employees, or indemnitee, is against public policy and is void and unenforceable.

The scope of this statute, however, is not limited to construction contracts *per se*. T.C.A. § 62-6-123 broadly covers agreements and contracts between all parties regarding the construction or improvement to real property. *Elliot Crane Servs., Inc. v. H.G. Hill Stores, Inc.*, 840 S.W.2d 376, 379 (Tenn. Ct. App. 1992). In *Elliot Crane*, the plaintiff insisted that Elliot Crane Service was not a “contractor” under the language of § 62-6-123 because it was merely in the business of furnishing cranes to further construction. This argument did not persuade the Tennessee Court of Appeals which held that a company operating a crane designed to be used in constructing a building cannot logically claim that the company was unaware of the construction use of the crane. *Elliot Crane*, 840 S.W.2d at 379-80 (citing *Am. Pecco Corp. v. Concrete Building Sys[s]., Co.*, 392 F.Supp. 789, 793 (N.D. Ill. 1975)). The Court of Appeals of Tennessee also dealt with the scope of § 62-6-123 in *Corroum v. Dover Elevator Co.*, when it stated that “there is no language limiting [T.C.A. § 62-6-123]’s applicability solely to construction contracts.” *Corroum v. Dover Elevator Co.*, 806 S.W.2d 777, 779 (Tenn. Ct. App. 1990). The *Corroum* court interpreted the statute to “include any agreement relative to the construction of a building.” *Id.* at 780. Thus, the Court of Appeals held, “a contract to provide certain services relative to a building under construction under a separate contract would be included under [the statute] and any provision purporting to indemnify . . . the promisee . . . is void and unenforceable.” *Id.* at 780.

VI. CONTINGENT PAYMENT AGREEMENTS

A. Enforceability

Contingent payment agreements are not favored in Tennessee, but are likely enforceable if the contract clearly conveys that the general contractor’s receipt of payment is an express condition precedent to its obligation to pay lower tier contractors. The only recent case addressing these contract payment terms is *Koch v. Construction Technology, Inc.*, 924 S.W.2d 68 (Tenn. 1996). In *Koch*, the Tennessee Supreme Court held that conditions precedent are not favored in contract law, and will not be upheld unless there is clear language to support them.

Koch involved a painting subcontractor’s claim for payment against the general contractor and its surety. The contract contained a payment term which provided: “[p]atrial payments subject to all applicable provisions of the Contract shall be made when and as payments are received by the Contractor.” The Court held that this term did not condition the obligation of payment upon the general contractor’s receipt of payment, but instead merely established the timing of payment. The Court further noted that the contract impliedly obligated the general contractor to make payment within a reasonable time of the subcontractor’s application for payment.

B. Requirements

There is no reported decision in Tennessee in which the terminology of an enforceable contingent payment agreement has been upheld. However, the *Koch* case establishes that to be enforceable, contingent payment terms must plainly and unambiguously state that the general contractor’s obligation of payment is *expressly conditioned* upon its own receipt of payment

from the owner, and that the general contractor's receipt of payment from the owner is an express condition precedent to its obligation of payment to a subcontractor.

VII. MEASURE AND TYPES OF DAMAGES

Under Tennessee law, the awarding of damages for a breach of contract action is both a question of law and fact. *GSB Contractors, Inc. v. Hess*, 179 S.W.3d 535, 541 (Tenn. Ct. App. 2005). However, there are different standards for the award of each type of damages.

A. Personal Injury Damages vs. Construction Defect Damages

A party sustaining personal injuries as a result of a construction defect can recover for past and future pain and suffering, past and future medical expenses, loss of earning capacity and loss of enjoyment of life; provided, however, that any future damages are established by competent medical testimony within a reasonable degree of medical certainty.

Tennessee has two (2) methods of recovery for damage to real property. The first method concerns permanent damage. For permanent damage, the court will award the difference between the property's value before the damage and the value after the damage. *Cathcart v. Malone*, 229 S.W.2d 157 (Tenn. Ct. App. 1950). One common example is the cutting of a tree on someone else's property. Such was the case in *Cathcart*, where the court deemed the loss of a tree permanent and thus awarded the difference in value of the property before and after the cutting of the tree. *Id.* at 159.

The second method concerns damage that is only temporary in nature. For temporary damage a court will award either the reasonable cost of repair or the diminution in value of the property. *Jones v. Johnson*, 2003 WL 21278282 *1 (Tenn. Ct. App. 2003). The court determines which to award based on which is amount is less. *Id.*

B. Attorney's Fees Shifting and Limitations of Recovery

Tennessee does not permit the collection of attorneys' fees unless there is a statute or the parties have contracted for attorneys' fees in the event of litigation. *Elec. Controls v. Ponderosa Fibres of Am.*, 19 S.W.3d 222 (Tenn. Ct. App. 1999). However, the Tennessee Supreme Court has found attorneys' fees recoverable without statute when the dispute involves indemnity. *Pullman Standard, Inc. v. Abex Corp.*, 693 S.W.2d 336 (Tenn. 1985). Resultantly, the indemnitee may recover attorneys' fees in an indemnity relationship.

C. Consequential Damages

Consequential damages are damages a court awards to put the injured party in the position they would have been had a breached contract been performed fully. However, such damages must be reasonable and necessary for a court to award. In *Custom Built Homes by Ed Harris v. McNamara*, 2006 WL 3613583 *7 (Tenn. Ct. App. 2006), the court would not award the plaintiff's entire damage request as the plaintiff could not show that the repairs they made on their home were needed. Even though a homeowner may make repairs, repairs that are beyond

the scope of the original contract, such as upgrades, are not consequential as they are not foreseeable. *Id.*

D. Delay & Disruption Damages

To recover delay damages, the items for which a party is attempting to recover must have been part of the contract. *White's Elec. v Lewis Constr.*, 1999 WL 605654 *14 (Tenn. Ct. App. 1999). These damages can be in the form of increased operating expenses, late service charges, and miscellaneous costs. *Id.* at *4. It naturally follows from these examples that a court may consider increased labor costs as well. *McClain v. Kimbrough Constr. Co., Inc.*, 806 S.W.2d 194, 201 (Tenn. Ct. App. 1990).

E. Economic Loss Doctrine

The “economic loss doctrine” mandates that when there is only an economic loss underlying an action the proper action is not one for negligence. *Ritter v. Custom Chemicides, Inc.*, 912 S.W.2d 128, 133 (Tenn. 1955). Moreover, when dealing only with economic loss, the rights of the parties are governed exclusively by the contract. *Messer Griesheim v. Eastman Chem.*, 194 S.W.3d 466 (Tenn. Ct. App. 2005).

F. Interest

From the entry of judgment in a breach of contract action, interest runs at a rate of five point two five percent (5.25%). T.C.A. § 47-14-103. But, according to T.C.A. § 47-14-109, pre-judgment interest begins accumulation from the time the contract is due. The rate is either the contract rate or four (4) points above the prime rate. T.C.A. § 47-14-103(2).

G. Punitive Damages

Tennessee does not normally allow punitive damages when there is a breach of contract. *Hodges v. S.C. Toof & Co.*, 833 S.W.2d 896 (Tenn. 1992). However, this is not always true; and thus, there is a two-step process for awarding punitive damages. In the first step, the fact finder must determine whether punitive damages should even be awarded. *Id.* at 901. The fact finder must find by “clear and convincing evidence” that a party acted (1) intentionally, (2) fraudulently, (3) maliciously, or (4) in a reckless manner. *Id.* at 900-01.

If there is a determination that punitive damages are proper, then there is a second step where the fact finder determines the necessary amount to award. *Id.* at 901. In reaching a determination, the fact finder considers many factors which essentially amount to a standard of “totality of the circumstances”. *Id.* at 901-02. Use of such a standard allows the consideration of all factors and the assignment of a value to each factor or consideration.

VIII. CASE LAW AND LEGISLATION UPDATE

In January 2013, the 6th Circuit issued an opinion in *Forrest Construction v. Cincinnati Insurance Company*, 703 F.3d 359 (6th Cir. Jan. 11, 2013), a decision involving judicial interpretation “property damage”, the “your work”, and the subcontractor exception. The decision underscores the minimal pleading requirements necessary to trigger the duty to defend in a construction defect case. Forrest was a residential contractor in middle Tennessee, who after having sued to collect unpaid invoices, was counter-sued for construction defects. Forrest had in place a commercial general liability policy issued by Cincinnati Insurance Company. The homeowners had alleged “Forrest recklessly constructed the foundation, *or recklessly caused to be constructed the foundation*.” Cincinnati denied coverage and refused to defend, citing the “your work” exclusion. The district court and 6th Circuit both found that the complaint clearly conveyed allegations of faulty work potentially caused by a subcontractor, i.e. constructed . . . *or caused to be constructed* . . . faulty work. This case tracks a growing trend among courts to side with insured contractors in finding that a construction defect claim constitutes an occurrence under a CGL policies.

In 2011, the Tennessee Legislature passed two pieces of legislation effecting construction litigants. First, the Legislature enacted a statute changing the summary judgment procedure in all state courts. The purpose of the legislation was to overrule a decision of the Tennessee Supreme Court handed down in October, 2008 which essentially shifted the burden to a defendant to negate an essential element of a plaintiff’s claim in order to be entitled to summary judgment. *Hannan v. Alltel Publishing Company*, 270 S.W. 3d 1 (Tenn. 2008). Subsequent to the *Hannan* decision, the Courts of Appeal reversed numerous summary judgments granted in trial courts across Tennessee. As a result, trial courts became extremely reluctant to grant summary judgment motions.

The new legislation basically codified the prior summary judgment standard and applies essentially the same standard in Tennessee state courts as is applied in federal courts. Now, as before *Hannan*, a plaintiff must come forward with affirmative proof that there is a genuine issue of fact to defeat a properly-filed summary judgment motion.

The second important legislative change was the enactment of a comprehensive tort reform bill titled “The Tennessee Civil Justice Act of 2011”. This new legislation covers several areas of the law (medical malpractice, products liability, etc.), but there are three areas of particular importance to construction law cases. The first is a cap on non-economic damages (physical and emotional pain and suffering, disfigurement, loss of enjoyment of life, etc.), which is now capped at \$750,000.00 per each injured Plaintiff. [Note: There are a few exceptions where the cap is increased to \$1,000,000.00 for catastrophic loss and injury.] The second important provision is the cap on punitive damages which now limits them to the greater of two (2) times the total amount of compensatory damages or \$500,000.00, *whichever is less*. The third significant change was limitation on the scope of the private right of action under the Tennessee Consumer Protection Act. Prior to the 2011 amendments, the TCPA enabled a private right of action by “[a]ny person who suffers an ascertainable loss . . . as a result of the use or employment by another person of an unfair or deceptive act or practice.” The 2011 amendments, however, added language limiting the private right of action to actions under subsection (b), for violations of one of the list of identified unfair or deceptive acts or practices. The amendments also cut off any private right of action under the most commonly deployed “catch-all” theory of liability -

“[e]ngaging in any other act or practice which is deceptive to the consumer or to any other person.” The TCPA still includes this catch-all provision, but the 2011 amendments make it enforceable only by the attorney general.

The new summary judgment statute became effective July 1, 2011, and the new tort reform bill applies to causes of action that accrue on or after October 1, 2011.

TEXAS

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I. MECHANIC'S LIEN BASICS

Texas law recognizes two types of mechanic's and materialman's liens—statutory and constitutional.¹ This section is intended to provide basic information regarding the requirements for perfecting a lien both as to timing of and the information to be contained in lien notices and affidavits, when applicable.

A. Constitutional Liens

Article XVI, § 37 of the Texas Constitution grants to mechanics, artisans and materialmen of every class a lien on the buildings and articles made or repaired by them for the value of their labor performed or material furnished, and requires that the Legislature provide by law for the speedy and efficient enforcement of such liens.² Constitutional mechanic's liens are self-executing as between the original contractor and the owner; that is, no notice or filing requirements must be met for the lien to attach, and the lien exists independently and apart from any legislative act.³ Subcontractors and material suppliers not contracting directly with the property owner do not have constitutional liens.⁴ However, a subcontractor will be deemed to be in a direct contractual relationship with the property owner if it can be shown that original contractor acquired his status by virtue of a sham relationship with the owner.⁵ The constitutional lien is not self-enforcing.⁶ Thus, the Constitution further requires that the Legislature provide for the enforcement of mechanic's liens.⁷ Pursuant to this constitutional mandate, Chapter 53 of the Texas Property Code sets forth the procedure for enforcing constitutional and statutory mechanic's liens.⁸

¹ *Strang v. Pray*, 35 S.W. 1054 (Tex. 1896); *Apex Fin. Corp. v. Brown*, 7 S.W.3d 820, 830 (Tex. App.—Texarkana 1999, no writ) (“[a] statutory lien exists through compliance with the applicable statutes, while a constitutional lien arises by virtue of the Constitution without the aid of the statutes.”) (citations omitted).

² TEX. CONST. art. XVI, § 37.

³ *Id.*

⁴ *Id.* See also *Gibson v. Bostick Roofing & Sheet Metal Co.*, 148 S.W.3d 482, 493 (Tex. App.—El Paso 2004, no pet.).

⁵ See TEX. PROP. CODE § 53.026; *Da-Col Paint Mfg. Co. v. American Indemnity Co.*, 517 S.W.2d 270, 271–274 (Tex. 1974)⁵ *CVN Group, Inc. v. Delgado*, 95 S.W.3d 234, 246 (Tex. 2002).

⁶ TEX. CONST. art. XVI, § 37.

⁷ TEX. CONST. art. XVI, § 37.

⁸ TEX. PROP. CODE ANN. § 53.051 et seq. (Vernon 2007).

B. Statutory Liens

Anyone who provides labor or materials, including specially fabricated materials, for the construction or repair of real property is afforded protection by statutory mechanics' liens.⁹ The Texas Property Code's statutory mechanics' lien may be asserted by general contractors, subcontractors, materialmen, mechanics, laborers, or artisans.¹⁰ Consequently, lower-tier derivative claimants have lien rights in the event of nonpayment; however, the notice requirements are more extensive for these claimants than for the original contractor.¹¹ All lien claimants other than the original contractor (the contractor that has a direct contract with the owner) are defined as derivative claimants. Derivative claimants must give notice and take other steps not required for original contractors. If these rules are not strictly followed, the subcontractor will lose any lien claim rights.¹²

1. Notice Requirements

An original contractor must complete two steps to establish his or her lien on the owner's property. First, the original contractor must file a lien affidavit with the county clerk of the county in which the property is located. The deadline for filing the lien affidavit is the 15th day of the fourth calendar month from the day on which the indebtedness accrues, which is always the last day of the month in which the project was completed, except when the original contractor leaves the job before completing it.¹³ Second, the original contractor must send a copy of the lien affidavit to the owner by certified mail no later than five business days after the affidavit is filed.¹⁴

By contrast, a claimant whose contract is not with the owner (a subcontractor or lower-tier claimant) must send periodic notices of the unpaid balance of the claim to the owner in order to perfect its statutory lien. Unlike the lien affidavit, these notices must be given periodically and not merely upon completion of work. These notices of nonpayment are preconditions to the validity of the lien, and if not provided there cannot be a valid lien, even though the lien affidavit itself may be timely filed.¹⁵ Contractually agreed retainage is considered an unpaid amount for the purposes of the statute and must be noticed in the same manner as amounts due and unpaid, unless notice of a retainage agreement is provided to the owner in the early stages of the project.¹⁶

The notices required to be delivered to the owner must be given to the owner and copied to the original contractor no later than the 15th day of the third month following each month in which the claimant performed all or part of its work.¹⁷ Notices must be sent by certified or registered mail, return receipt requested.¹⁸

⁹ TEX. PROP. CODE ANN. § 53.021 (Vernon 2007).

¹⁰ *Id.*

¹¹ *See* TEX. PROP. CODE ANN. § 53.056(b).

¹² *See id.*

¹³ *Id.* § 53.052.

¹⁴ *Id.* § 53.055.

¹⁵ *Id.* § 53.056.

¹⁶ *Id.* § 53.057.

¹⁷ *Id.* § 53.056(b).

¹⁸ *Id.* § 53.056(e).

If the claimant's contract is not with the original contractor (sub-subcontractors or other lower-tier claimants), notice must be given to the original contractor and the owner.¹⁹ Sub-subcontractors and other lower-tier claimants not in a direct contractual relationship with the original contractor must give notice to the original contractor no later than the 15th day of the second month following each month in which the claimant performed all or part of its work.²⁰

2. Lien Affidavit

Any lien claimant, whether original contractor, subcontractor, or lower-tier claimant, must file a lien affidavit with the county clerk in the county in which the property is located in order to enforce or perfect its lien.²¹ The affidavit must be signed by the claimant or by another person on the claimant's behalf and must contain : (1) a sworn statement of the amount of the claim; (2) the name and last known address of the owner or reputed owner; (3) a general statement of the kind of work done and materials furnished by the claimant and, for a claimant other than an original contractor, a statement of each month in which the work was completed and materials furnished for which payment is requested; (4) the name and last known address of the person by whom the claimant was employed or to whom the claimant furnished materials or labor; (5) the name and last known address of the original contractor; (6) a description, legally sufficient for identification, of the property sought to be charged with the lien; (7) the claimant's name, mailing address, and, if different, physical address; and (8) for a claimant other than the original contractor, a statement identifying the date each notice of the claim was sent to the owner and the method by which the notice was sent.²²

The lien claimant must file the affidavit on the earlier of the 30th day after the actual completion of the construction project, or the 15th day of the fourth calendar month after the day on which the indebtedness accrues.²³ A person claiming a lien arising from a residential construction project must file an affidavit no later than the 15th day of the third calendar month after the day on which the indebtedness accrues.²² A proper determination of the date the indebtedness accrues depends on the category of lien claimant. The owner's debt to the original contractor accrues on the last day of the month in which (1) the original contract is completed, finally settled or abandoned, or (2) either the owner or contractor receives from the other a written notice of contract termination.²³ A debt owed to a subcontractor or any party other than the original contractor or one furnishing specially fabricated materials, accrues on the last day of the last month in which the claimant performed labor or furnished materials.²⁴

A copy of the lien affidavit must be sent by registered or certified mail to the owner and original contractor no later than the fifth day after the date the affidavit is filed with the county clerk.²⁵ If the person claiming the lien is not an original contractor, he or she must also send a copy of the affidavit to the original contractor.²⁶

¹⁹ *Id.* § 53.056(b).

²⁰ *Id.*

²¹ Tex. Prop. Code Ann. § 53.055(a).

²² *Id.* § 53.054(a).

²³ *Id.* § 53.052(a).

²⁴ *Id.* § 53.052(b).

²⁵ *Id.* § 53.053(b).

²⁶ *Id.* § 53.053(c).

3. Action on the Lien

The deadline for bringing suit to foreclose the lien is the later of: (1) two years from the last day for the claimant to file its lien affidavit; or (2) one year after completion, abandonment, or termination of the original contract.²⁷ For residential construction, the limitations period is one year from the later of: (1) the last day for filing the affidavit; or (2) completion, abandonment, or termination of the original contract.²⁸

4. The Right to Waive Liens

Texas courts have held that the right to assert a mechanic's or materialman's lien may be waived.²⁹

Waiver of these liens in Texas has traditionally been analyzed under case law, with courts finding waiver where there existed either an express agreement or an implication of waiver resulting from acts inconsistent with the continued existence of rights under the lien.³⁰ But there is no intentional waiver unless such intent has been made "very plain and clear." The presumption is always against waiver.³¹

However, in 2011 the Texas Legislature enacted new statutory language specifically addressing waiver of mechanic's and materialman's liens. For contracts entered into after January 1, 2012, purported waivers of mechanic's and materialman's liens are unenforceable unless a waiver and release is executed in accordance with Chapter 53 of the Texas Property Code.³² This chapter provides that a waiver and release releases the owner, the owner's property, the contractor, and the surety on a payment bond from claims and liens only if: 1) the waiver and release substantially comply with the forms in Texas Property Code § 53.284; 2) the waiver and release is signed by the claimant or the claimant's authorized agent and notarized; and 3) in the case of a conditional release, evidence of payment to the claimant exists.³³

Additionally, statements purporting to waive liens are only enforceable if: (1) the claimant has actually received payment in good and sufficient funds in full for the lien; (2) the statement is in a written original contract or subcontract for land development related to, or the construction, remodel, or repair of a single-family house, townhouse, or duplex, *and* the statement is made before labor or materials are provided under the original contract or subcontract; or (3) the statement is in writing and substantially complies with Texas Property Code § 53.284.³⁴

Texas Property Code § 53.284 provides form language to be used to execute: a conditional waiver and release in exchange for or to induce the payment of a progress payment;

²⁷ *Id.* § 53.055(a).

²⁸ *Id.* § 53.055(b).

²⁹ See, e.g., *Shirley-Self Motor Co. v. Simpson*, 195 S.W.2d 951 (Tex. Civ. App.—Fort Worth 1946, no writ); [*San Antonio Bank & Trust Co. v. Anel, Inc.*, 613 S.W.2d 55, 59 \(Tex. Civ. App.—Texarkana 1981, writ ref'd n.r.e.\)](#).

³⁰ *McBride v. Beakley*, 203 S.W. 1137, 1138 (Tex. Civ. App.—Amarillo 1918, no writ); see, e.g., *El Paso Dev. Co. v. Berryman*, 769 S.W.2d 584, 589.

³¹ *Milburn v. Athans*, 190 S.W.2d 388, 392 (Tex. Civ. App.—Fort Worth 1945, writ dismissed).

³² Tex. Prop. Code § 53.281.

³³ *Id.*

³⁴ Tex. Prop. Code § 53.282. ³⁴ *Id.* § 53.284.

an unconditional waiver and release to prove the receipt of good and sufficient funds for a progress payment; a conditional waiver and release in exchange for or to induce the payment of a final payment; and an unconditional waiver and release to prove the receipt of good and sufficient funds for a final payment.³⁵

These conditions on enforceability do not apply to “written agreements to subordinate, release, waive, or satisfy all or part of a lien or bond claim in: (1) an accord and satisfaction of an identified dispute; (2) an agreement concerning an action pending in any court or arbitration proceeding; or (3) an agreement that is executed after an affidavit claiming the lien has been filed.”³⁶

II. STATUTES OF LIMITATION AND REPOSE

The statutes of limitation and repose applicable to construction defect claims are contained in various general statutes of limitations and some specific statutes of repose related to construction projects and construction professionals. This section provides a brief overview of the statutes and highlights some of the case law interpreting these provisions as it applies to causes of action typically seen in construction defect cases.

A. Statute of Limitations

1. Breach of Contract

The limitations period for an action for breach of contract is four years after the day the cause of action accrues.³⁷

2. Tort

The statute of limitations for negligence,³⁸ professional negligence,³⁹ and negligent misrepresentation⁴⁰ is two years.

3. Fraud

The statute of limitations for fraud is four years from the date of accrual of the cause of action.⁴¹

4. Deceptive Trade Practices Act

An action must be commenced within two years after the date on which the false, misleading, or deceptive act or practice occurred or within two years after the consumer

³⁵ Tex. Prop. Code § 53.287.

³⁶ TEX. CIV. PRAC. & REM. CODE ANN. § 16.004 (Vernon 2007).

³⁷ TEX. CIV. PRAC. & REM. CODE ANN. § 16.004 (Vernon 2007).

³⁸ *Id.* § 16.003(a).

³⁹ *Ryan v. Morgan Spear Assocs., Inc.*, 546 S.W.2d 678 (Tex. App.—Corpus Christi 1977, writ ref’d n.r.e.).

⁴⁰ *Hendricks v. Thornton*, 973 S.W.2d 348 (Tex. App.—Beaumont 1998, pet. denied).

⁴¹ TEX. CIV. PRAC. & REM. CODE ANN. § 16.004(a)(4).

discovered, or in the exercise of reasonable diligence should have discovered, the occurrence of the false, misleading, or deceptive act or practice. The limitation period is extended by 180 days if the plaintiff proves that its failure to commence the action timely was caused by the defendant's conduct that was calculated to induce the plaintiff to refrain from or postpone the commencement of the action.⁴² The plaintiff does not need to know the full extent of the injury for limitations to begin to run.⁴³

5. Breach of Implied Warranty

Generally, the limitations period on a breach of implied warranty ends four years from the date of the breach that results in the legal injury.⁴⁴ The application of the discovery rule has not yet been determined by Texas courts. It is not available for breach of implied warranty cases under the Uniform Commercial Code (UCC).⁴⁵ Further, there is no implied warranty for breach of professional services.⁴⁶

6. Discovery Rule

The discovery rule defers the accrual of a cause of action's accrual until the plaintiff knows, or by the exercise of reasonable diligence should know, of the wrongful act and resulting injury.⁴⁷ For the discovery rule to apply, the plaintiff must prove the injury was inherently undiscoverable and objectively verifiable.⁴⁸ The limitations period accrues when the plaintiff discovers or should have discovered the damage and that it was likely caused by the wrongful acts of another—it is unnecessary for the plaintiff to know the exact identity of the wrongdoer.⁴⁹ The Texas Supreme Court has held that once a plaintiff learns of a wrongful injury, the statute of limitations begins to run even if plaintiff does not yet know the cause of injury, the responsible party, or the full extent of damages.⁵⁰ The discovery rule has been applied to construction defect cases.⁵¹ It is specifically applicable to a cause of action under the Texas Deceptive Trade Practices Act.⁵² It is undetermined, however, whether the discovery rule applies to a breach of implied warranty to perform services in a good and workmanlike manner.

B. Statutes of Repose

1. Contractors and Subcontractors

A claimant must bring suit for damages for personal injury, property damage, wrongful death, contribution or indemnity against a person who constructs or repairs an improvement to

⁴² TEX. BUS. & COM. CODE ANN. § 17.565 (Vernon 2007).

⁴³ See *Murphy v. Campbell*, 964 S.W.2d 265 (Tex. 1997).

⁴⁴ See *Certain-Teed Products Corp. v. Bell*, 422 S.W.2d 719, 722 (Tex. 1968).

⁴⁵ *Am. Tobacco Co. v. Grinnell*, 951 S.W.2d 420 (Tex. 1997).

⁴⁶ *Murphy v. Campbell*, 964 S.W.2d 265 (Tex. 1997).

⁴⁷ *Wagner & Brown v. Horwood*, 58 S.W.3d 732, 734 (Tex. 2001); *S.V. v. R.V.*, 933 S.W.2d 1, 4 (Tex. 1996).

⁴⁸ *Wagner & Brown*, 58 S.W.3d at 734; *S.V.*, 933 S.W.2d at 6.

⁴⁹ *Childs v. Haussecker*, 974 S.W.2d 31 (Tex. 1998).

⁵⁰ *PPG Indus., Inc. v. JMB/Houston Ctrs.*, 146 S.W.3d 79 (Tex. 2004).

⁵¹ See, e.g., *Cornerstone Mun. Util. Dist. v. Monsanto Co.*, 889 S.W.2d 570 (Tex. App.—Houston [14th Dist.] 1994, writ denied); *Bayou Bend Council of Co-Owners v. Manhattan Constr. Co.*, 866 S.W.2d 790 (Tex. App.—Houston [14th Dist.] 1993, writ denied).

⁵² TEX. BUS. & COM. CODE ANN. § 17.565.

real property within ten years after the substantial completion of the improvement in an action arising out the defective or unsafe condition of the real property or deficiency in the construction or repair of the improvement.⁵³ If the claimant presents a written claim for damages, contribution, or indemnity to such a person during the ten-year limitations period, the period is extended for two years from the date of presentment.⁵⁴ Further, if the damage, injury, or death occurs during the 10th year of the limitations period, the claimant has two years after the date the cause of action accrues to bring the claim.⁵⁵

2. Design Professionals

A person must bring a suit for damage to real or personal property, personal injury, death, contribution, or indemnity against a registered or licensed architect, engineer, interior designer, or landscape architect who designs, plans, or inspects the construction of an improvement to real property or equipment attached to real property no later than ten years after (a) the substantial completion of the improvement or (b) the beginning of operation of the equipment in an action arising out of a defective or unsafe condition of the real property, the improvement, or the equipment.⁵⁶ If a written claim for such damages is brought against these persons within the ten-year limitations period, the period is extended for two years from the date the claim is presented.⁵⁷

3. Surveyors

A person must bring suit for damages arising from an injury or loss caused by an error in a survey conducted by a registered public surveyor or a licensed state land surveyor not later than ten years after the date the survey is completed.⁵⁸ If a written claim for damages to the surveyor is presented during the ten-year limitations period, the period is extended for two years from the date the claim is presented.⁵⁹

4. Exception to Limitations and Statutes of Repose

In Texas, there is a process whereby a defendant may designate a person as a “responsible third party” without formally adding that person to the lawsuit as a party.⁶⁰ The plaintiff is not barred by limitations from seeking to join a person designated as a responsible third party, even though joinder would otherwise be barred by limitations, as long as the claimant seeks joinder within sixty days of the designation.⁶¹ The application of this section includes only “limitations,” not statutes of repose.⁶²

⁵³ TEX. CIV. PRAC. & REM. CODE ANN. § 16.009(a)-(b).

⁵⁴ *Id.* § 16.009(c).

⁵⁵ *Id.* § 16.009(d).

⁵⁶ *Id.* § 16.008(a)-(b).

⁵⁷ *Id.* § 16.008(c).

⁵⁸ *Id.* § 16.011(a).

⁵⁹ *Id.* § 16.011(b).

⁶⁰ *Id.* § 33.004(a).

⁶¹ *Id.* § 33.004(e).

⁶² *Galbraith Eng'g Consultants, Inc. v. Pochucha*, 290 S.W.3d 863, 869 (Tex. 2009).

III. PRE-SUIT NOTICE OF CLAIM

Generally, in construction defect cases, there is no requirement to provide pre-suit notice of claim or to provide an opportunity to cure, except in certain statutory instances.

A. Breach of Contract

There is no requirement for pre-suit notice of claim. However, if the claimant intends to seek statutorily allowed attorney's fees, the claimant must present the claim to the opposing party and allow thirty days for payment of the claim, prior to filing suit.⁶³

B. Texas Deceptive Trade Practices Act

A consumer must give written notice to the proposed defendant at least sixty days before filing a DTPA claim.⁶⁴ The notice must provide in reasonable detail the specific complaints and amount of economic damages, damages for mental anguish, and expenses, including attorney's fees reasonably incurred in asserting the claim against the proposed defendant.⁶⁵ During this sixty-day period, a written request to inspect in a reasonable manner and reasonable time and place may be presented to the consumer.⁶⁶ If this sixty-day notice requirement is not met, the person against whom the lawsuit is subsequently filed may file a plea in abatement no later than thirty days after the answer is filed.⁶⁷ The court must abate the lawsuit and the abatement continues until the 60th day after the date that written notice is served in compliance with this statute.⁶⁸ Notice is not required if it is impracticable because the statute of limitations is about to run or if the plaintiff's claim is brought as a counterclaim.⁶⁹

C. Residential Construction Defects

An action to recover damages or other relief arising from a construction defect, except a claim for personal injury, survival, or wrongful death or for damage to goods, is governed by the Residential Construction Liability Act (RCLA).⁷⁰ A claimant seeking damages under the RCLA must give written notice to the contractor at least sixty days before the date the claimant files an action.⁷¹ However, if this claim is a counterclaim or asserted to avoid limitations, the notice requirement is excused. If notice is not provided, the contractor can abate the lawsuit or arbitration if the homeowner fails to (1) provide the required notice to the contractor of the RCLA proceeding; (2) permit inspection of the property; or (3) follow the procedures applicable to the contractor's settlement and repair offers.⁷²

⁶³ TEX. CIV. PRAC. & REM. CODE ANN. § 38.002.

⁶⁴ TEX. BUS. & COM. CODE § 17.505(a).

⁶⁵ *Id.*

⁶⁶ *Id.*

⁶⁷ *Id.* § 17.505(c).

⁶⁸ *Id.* § 17.505(e).

⁶⁹ *Id.* § 17.505(b).

⁷⁰ *Id.*

⁷¹ TEX. PROP. CODE § 27.002.

⁷² *Id.* § 27.001(1).

⁷³ *Id.* § 27.004(d).

Within forty-five days of receiving notice, the contractor may make a written settlement offer to the claimant, which may include an agreement to repair the defect or have it repaired by an independent contractor at the contractor's expense.⁷³ A claimant who rejects a reasonable settlement offer or who does not permit a reasonable opportunity to inspect or repair the defect after accepting the offer may not recover more than the fair market value of the contractor's last settlement offer or a reasonable settlement amount.⁷⁴ If the contractor fails to make a reasonable settlement offer, the contractor loses all defenses to liability and the protections of damages limitations provided by the RCLA.⁷⁵

IV. COVERAGE AND ALLOCATION ISSUES

A. Occurrence/Property Damage

Texas state and federal courts are divided on the applicability of commercial general liability ("CGL") coverage for defective construction, especially on the issue of whether a contractor's negligence can constitute an "occurrence" or "property damage." In *Lamar Homes, Inc. v. Mid-Continent Casualty Company*, the Texas Supreme Court addressed this issue on the following certified questions from the Fifth Circuit Court of Appeals:

1. When a homebuyer sues his general contractor for construction defects and alleges only damage to or loss of use of the home itself, do such allegations allege an "accident" or "occurrence" sufficient to trigger the duty to defend or indemnify under a CGL policy?
2. Do such allegations allege "property damage" sufficient to trigger the duty to defend or indemnify under a CGL policy?⁷⁶

The Texas Supreme Court answered these questions in the affirmative, but it did not reach the question of duty to indemnify.⁷⁷

In *Lamar Homes*, homebuyers purchased a new home from Lamar Homes and subsequently encountered problems that they attributed to defects in the home's foundation.⁷⁸ The homebuyers sued Lamar Homes and its subcontractor and Lamar Homes, in turn, forwarded the lawsuit to Mid-Continent Casualty Company ("Mid-Continent") seeking defense and indemnification under a CGL insurance policy.⁷⁹ When Mid-Continent refused to defend, Lamar sought a declaration of its rights under the CGL policy.⁸⁰ On cross motions, the federal district

⁷³ *Id.* § 27.004(b).

⁷⁴ *Id.* § 27.004(e).

⁷⁵ *Homes v. Alwattari*, 33 S.W.3d 376 (Tex. App.—Fort Worth 2000).

⁷⁶ *Lamar Homes, Inc. v. Mid-Continent Casualty Company*, 242 S.W.3d 1, 4 (Tex. 2007). The Fifth Circuit also certified a third question to the Texas Supreme Court: (3) If the answers to certified questions 1 and 2 are answered in the affirmative, does Article 21.55 of the Texas Insurance Code [the Prompt Payment of Claims statute] apply to a CGL insurer's breach of the duty to defend? The Court answered yes.

⁷⁷ *Id.* at 4-5.

⁷⁸ *Id.* at 5.

⁷⁹ *Id.*

⁸⁰ *Id.*

court granted summary judgment for Mid-Continent, holding it had no duty to defend Lamar Homes for construction errors that harmed only Lamar Homes' own project.⁸¹ In view of the inconsistent authority concerning this issue, the Fifth Circuit asked the Texas Supreme Court to resolve the conflict.⁸²

The Texas Supreme Court first analyzed whether defective construction or faulty workmanship damaging only the insured's work is an "occurrence."⁸³ Noting the CGL policy's definition of "occurrence" as "an accident, including continuous or repeated exposure to substantially the same general harmful conditions," the Court explained that "the determination of whether an insured's faulty workmanship was intended or accidental is dependent on the facts and circumstances of the particular case," and that for purposes of the duty to defend, the eight-corners rule applies.⁸⁴ Because the complaint alleged that the defective construction was a product of the builder's negligence, the Court found no allegation of intentional conduct.⁸⁵

The Court then analyzed whether the contractor's negligence constituted "property damage" and noted the definition of "property damage" as "[p]hysical injury to tangible property, including all resulting loss of use of that property."⁸⁶ The Supreme Court stated that, on its face, this definition did not eliminate the work performed by Lamar Homes.⁸⁷ Mid-Continent disagreed and argued that CGL coverage does not apply to defective construction that injures only the work of the contractor because the policy's purpose is to protect from tort liability, not claims of defective performance under a contract, and that defective work is not an occurrence because it is not accidental.⁸⁸ The carrier also urged that damage to the insured's own work was a contractual economic loss, not "property damage."⁸⁹ In response, the Court emphasized that "the proper inquiry is whether an 'occurrence' has caused 'property damage,' not whether the ultimate remedy for that claim lies in contract or in tort."⁹⁰ Thus, the Court held that "claims for damage caused by an insured's defective performance or faulty workmanship" may constitute an 'occurrence' when 'property damage' results from 'unexpected, unforeseen or undesigned happening or consequence' of the insured's negligent behavior."⁹¹

B. Actual Injury, Manifestation or Exposure Rule

Another split among Texas courts concerns the proper rule to determine when property damage "occurs" under a CGL policy. In *Don's Building Supply, Inc. v. OneBeacon Insurance Company*, the Texas Supreme Court resolved this issue on the following certified questions from the Fifth Circuit Court of Appeals:

⁸¹ *Id.*

⁸² *Id.*

⁸³ *Id.* at 7.

⁸⁴ *Id.* at 9.

⁸⁵ *Id.*

⁸⁶ *Id.* at 10.

⁸⁷ *Id.*

⁸⁸ *Id.* at 8.

⁸⁹ *Id.*

⁹⁰ *Id.* at 16.

⁹¹ *Id.* See also *Homeowners Mgmt. Enters, Inc. v. Mid-Continent Cas. Co.*, 294 Fed. Appx. 814 (5th Cir. 2008) (insurer conceded its duty to defend in light of *Lamar Homes*); *Rotella v. Mid-Continent Cas. Co.*, No. 3:08-CV-0486-G, 2008 WL 2694754 (N.D. Tex. 2008) (In light of the eight-corner rule and the holding in *Lamar Homes*, "the pleadings in the underlying action allege[d] facts stating a cause of action potentially falling within the scope of coverage sufficient to trigger the insurer's duty to defend.").

1. When not specified by the relevant policy, what is the proper rule under Texas law for determining the time at which property damage occurs for purposes of an occurrence-based commercial general liability insurance policy?
2. Under the rule identified in the answer to the first question, have the pleadings in lawsuits against an insured alleged that property damage occurred within the policy period of an occurrence-based commercial general liability insurance policy, such that the insurer's duty to defend and indemnify the insured is triggered, when the pleadings allege that actual damage was continuing and progressing during the policy period, but remained undiscoverable and not readily apparent for purposes of the discovery rule until after the policy period ended because the internal damage was hidden from view by an undamaged exterior surface?⁹²

The Texas Supreme Court held that, at least with respect to the CGL policy at issue, “property damage” occurred when actual physical damage occurred and that the duty to defend was triggered when the property damage occurred, which was within the policy period.⁹³

In *Don's Building Supply*, various Texas homeowners filed lawsuits against Don's Building Supply (“DBS”) from 2003 to 2005, alleging that a certain siding system installed in their homes between 1993 and 1996 was defective.⁹⁴ During that period DBS was covered by CGL policies issued by OneBeacon Insurance Company (“OneBeacon”).⁹⁵ The homeowners argued that their injuries “‘actually began to occur on the occasion of the first penetration of moisture behind [the siding system],’ which they say was ‘within six months to one year after the application of the [siding system].’”⁹⁶ The homeowners sought to avoid limitations problems for their claims by pleading the discovery rule, arguing that the home damage was “‘hidden from view’ by the siding’s undamaged exterior” and “not discoverable or readily apparent to someone looking at that surface until after the policy period ended.”⁹⁷ OneBeacon filed for a declaratory judgment action in federal district court seeking a ruling that it had no duty to defend or indemnify under the CGL policies.⁹⁸ The district court agreed with OneBeacon and held that the duty did not arise until the damage became identifiable.⁹⁹ DBS appealed to the Fifth Circuit, which certified the above questions to the Texas Supreme Court.¹⁰⁰

With respect to the first question, the Court first considered the definition of “property damage” provided in the CGL policy and held that “property damage” under this policy occurred when actual physical damage was inflicted.¹⁰¹ As such, property damage to one of the homes at issue occurred when the home suffered wood rot or other physical damage. The Court further stated that “the date the physical damage is or could have been discovered is irrelevant under the

⁹² *Don's Bldg. Supply, Inc. v. OneBeacon Ins. Co.*, 267 S.W.3d 20 (Tex. 2008).

⁹³ *Id.* at 22.

⁹⁴ *Id.*

⁹⁵ *Id.*

⁹⁶ *Id.*

⁹⁷ *Id.* at 23.

⁹⁸ *Id.*

⁹⁹ *Id.*

¹⁰⁰ *Id.*

¹⁰¹ *Id.* at 24.

policy.”¹⁰² After a thorough examination of case law regarding various approaches courts have taken in determining when “property damage” occurs, the Court adopted the actual injury rule, as opposed to the manifestation or exposure rules.¹⁰³ The Court reasoned as follows:

The policy in straightforward wording provides coverage if the property damage ‘occurs during the policy period,’ and further provides that property damage means ‘[p]hysical injury to tangible property.’ Whatever practical advantages a manifestation rule would offer to the insured or the insurer, the controlling policy language does not provide that the insurer’s duty is triggered only when the injury manifests itself during the policy term, or that coverage is limited to claims where the damage was discovered or discoverable during the policy period.

Similarly, the policy’s language does not support adoption of an exposure rule, at least not where there is ‘physical injury to tangible property’ as alleged in this case. Again, the policy provides coverage if the “‘property damage’ occurs during the policy period.” The policy does not state that coverage is available if property is, during the policy period, exposed to a process, event, or substance that later results in bodily injury or physical injury to tangible property.

We therefore decline to recognize a manifestation rule or exposure rule for the property damage claims alleged under this policy. (Citation omitted). This policy links coverage to damage, not damage detection. Engrafting a manifestation rule to limit coverage—by conditioning coverage on the observations of a third-party claimant would blur the distinction between this occurrence-based policy and a claims-made policy.¹⁰⁴

The Court further emphasized that it did not endeavor to create a “universally applicable ‘rule’ for determining when an insurer’s duty to defend a claim is triggered under an insurance policy,” but rather that “determinations should be driven by the contract language-language that obviously may vary from policy to policy.”¹⁰⁵

In answering the second certified question, the Court relied on the eight-corners rule in holding that the insurer’s duty to defend DBS depends on whether the homeowners’ pleadings allege property damage that occurred during the policy term:

Under the actual-injury rule applicable to this policy, a plaintiff’s claim against DBS that any amount of physical injury to tangible

¹⁰² *Id.*

¹⁰³ *Id.* at 25.

¹⁰⁴ *Id.* at 29.

¹⁰⁵ *Id.* at 30.

property occurred during the policy period and was caused by DBS's allegedly defective product triggers OneBeacon's duty to defend. This duty is not diminished because the property damage was undiscoverable, or not readily apparent or "manifest," until after the policy period ended. Nor does it depend on whether DBS has a valid limitations defense. The parties could have conditioned coverage on identifiability, but the contract imposes no such limitation.¹⁰⁶

The Court stressed that its holding was directed only to the specific questions posed by the Fifth Circuit and was limited to the specific language of the CGL policy at issue concerning property damage in the construction defect context.¹⁰⁷

C. Scope of Duty to Defend Where Property Damage Occurs Over Multiple Policy Periods

In cases where property damage occurs over the course of two or more policy periods, Texas law is clear that an insurer's duty to defend its insured "is not reduced pro rata by the insurer's 'time on the risk' or by any other formula."¹⁰⁸ On the contrary, "the insurer's duty is to provide its insured with a complete defense."¹⁰⁹

D. Additional Insurance

Traditionally, Texas law has allowed construction contracts to require the general contractor and subcontractors to name the owner and/or the general contractor as "additional insureds" under their liability policies.¹¹⁰

However, for construction contracts entered into after January 1, 2012, additional insurance requirements designed to protect an owner or general contractor from the consequences of their own negligence are voided. This is a consequence of recently enacted Texas Anti-Indemnity Act, which includes anti-indemnification language designed to prevent owners and general contractors on construction projects from shifting the risk of their own negligence or breach of contract to subcontractors.¹¹¹

V. CONTRACTUAL INDEMNIFICATION

A. Contracts entered into Prior to January 1, 2012

The Texas Anti-Indemnity Act significantly changed contractual indemnification in the context of construction contracts. Its anti-indemnification provisions are effective for contracts

¹⁰⁶ *Id.* at 31-32.

¹⁰⁷ *Id.* at 32.

¹⁰⁸ *Tex. Prop. & Cas. Ins. Guar. Ass'n v. Sw. Aggregates, Inc.*, 982 S.W.2d 600, 606-07 (Tex. App.—Austin 1998, no pet.).

¹⁰⁹ *Id.*

¹¹⁰ *See, e.g., Atofina Petrochemicals, Inc. v. Cont'l Cas. Co.*, 185 S.W.3d 440, 444 (Tex. 2005) (per curiam).

¹¹¹ TEX. INS. CODE § 151.102.

entered into after January 1, 2012.¹¹² For contracts entered into before January 1, 2012, normal rules of contract construction will govern the enforceability of indemnification provisions, with the primary goal of determining the intent of the parties.¹¹³ However, even prior to the new law's enactment, the Texas Supreme Court recognized the extraordinary risk shifting associated with indemnifying a party for its own negligence and required that indemnity clauses satisfy the express negligence test and the conspicuousness requirements.¹¹⁴ Whether an indemnity clause complies with these fair notice requirements is a question for the court, and a clause which fails to satisfy either of the fair notice requirements when they are imposed is unenforceable as a matter of law.¹¹⁵

1. The Express Negligence Doctrine

The express negligence doctrine is set out in *Ethyl Corp. v. Daniel Const. Co.*¹¹⁶ The purpose of the express negligence test is to require a party who attempts to indemnify itself from its own negligence to express that intent in specific terms.¹¹⁷ The intent of the parties must be specifically stated within the four corners of the contract.¹¹⁸

The Texas Supreme Court adopted the express negligence test in an attempt to stem the tide of litigation resulting from ambiguous indemnity agreements.¹¹⁹ The Court sought to thwart the efforts of drafters to “indemnify the indemnitee for its negligence, yet be just ambiguous enough to conceal that intent from the indemnitor.”¹²⁰ The courts have recognized that indemnifying a party for its own negligence involves a dramatic shifting of risks.¹²¹ The express negligence test was designed to guard against the unfairness that results when one party is unaware that it has assumed responsibility for another's negligence.¹²² Requiring such an indemnity provision to be clearly and unambiguously drafted ensures that the indemnitor is well aware that he is assuming this extra burden.¹²³

In *Ethyl*, an employee of the contractor, Daniel Construction, was injured while working on a construction project for the owner, Ethyl. The employee sued the owner, who in turn sued the contractor for indemnification based upon the following indemnification clause in the contract between the owner and the contractor: “Contractor shall indemnify and hold Owner harmless against any loss or damage to persons or property as a result of operations growing out of the performance of this contract and caused by the negligence or carelessness of Contractor, Contractor's employees, Subcontractors and agents or licensees.”¹²⁴ Ethyl argued that the words “any loss” and “as a result of operations” showed an intent by the contractor to indemnify Ethyl

¹¹² 2011 Tex. HB 2093.

¹¹³ *Assoc. Indem. Corp. v. CAT Contracting, Inc.*, 964 S.W.2d 276, 284 (Tex. 1998).

¹¹⁴ *Dresser Indus., Inc. v. Page Petroleum*, 853 S.W.2d 505, 508 (Tex. 1993).

¹¹⁵ *Id.* at 509; *Storage & Processors, Inc. v. Reyes*, 134 S.W.3d 190, 192 (Tex. 2004).

¹¹⁶ *Ethyl Corp. v. Daniel Const. Co.* 725 S.W.2d 705, 708 (Tex. 1987).

¹¹⁷ *Ethyl*, 725 S.W.2d at 708; *Storage*, 134 S.W.3d at 192.

¹¹⁸ *Ethyl*, 725 S.W.2d. at 708.

¹¹⁹ *Id.*

¹²⁰ *Id.* at 707-08.

¹²¹ *Dresser Indus., Inc.*, 853 S.W.2d at 508.

¹²² *Houston Lighting & Power Co. v. Atchison, Topeka & Santa Fe Ry. Co.*, 890 S.W.2d 455, 458 (Tex. 1994).

¹²³ *Id.*

¹²⁴ *Ethyl*, 725 S.W.2d at 707.

for Ethyl's own negligence.¹²⁵ The Court disagreed and held that the indemnity provision did not meet the express negligence test.¹²⁶

Another example of an indemnity agreement that failed to meet the express negligence test occurred in *Robert H. Smith, Inc. v. Tennessee Tile, Inc.*¹²⁷ The contract in *Smith* provided that the subcontractor, Tennessee Tile, would indemnify the contractor, Robert H. Smith, for "any negligent act or omission of Tennessee Tile, arising out of or resulting from the performance of the Subcontractor's Work ... regardless of whether it is caused in part by a party indemnified hereunder."¹²⁸ That court held the subcontractor did not, by that language, indemnify the contractor for the contractor's own negligence.¹²⁹

The Supreme Court of Texas has also found that the express negligence doctrine was satisfied in a number of cases involving indemnity agreements. In *Enserch Corp. v. Parker*,¹³⁰ the contract stated that Christie, the indemnitor, "assumes entire responsibility for any claim ... regardless of whether such claims ... are founded in whole or in part upon alleged negligence of [Enserch], [Enserch's] representative, or the employees, agents, invitees, or licensees thereof."¹³¹ The Court held that this contract sufficiently showed that Christie expressly agreed to indemnify Enserch for the consequences of Enserch's own negligence.¹³²

One Texas appellate court has applied *Enserch* to find that the express negligence requirement may be met when an indemnity agreement is comprised from multiple separate provisions of the contract.¹³³ The Houston Court of Appeals read *Enserch* as supporting the conclusion that the agreement need not be confined to one paragraph, and that the contract should be read as a whole to divine the parties' intent.¹³⁴ Taking the multiple indemnity paragraphs together, the court found that the contract as a whole met the express negligence test.¹³⁵

2. The Conspicuousness Requirement

In *Dresser Industries*, the Texas Supreme Court adopted the UCC standard for conspicuousness.¹³⁶ The UCC provides: A term or clause is conspicuous when it is so written that a reasonable person against whom it is to operate ought to have noticed it. A printed heading in capitals (as: NON-NEGOTIABLE BILL OF LADING) is conspicuous. Language in the body

¹²⁵ *Id.* at 708.

¹²⁶ *Id.*

¹²⁷ *Robert H. Smith, Inc. v. Tennessee Tile, Inc.*, 719 S.W.2d 385 (Tex. App.—Houston [1st Dist.] 1986, no writ).

¹²⁸ *Id.* at 387 (emphasis omitted).

¹²⁹ *Id.* at 388.

¹³⁰ *Enserch Corp. v. Parker*, 794 S.W.2d. 2 (Tex. 1990).

¹³¹ *Id.* at 6-7 (emphasis omitted).

¹³² *Id.* at 8.

¹³³ *Ayres Welding Co., Inc. v. Conoco, Inc.*, 243 S.W.3d 177 (Tex. App.—Houston [14th Dist.] 2007, pet. denied). Paragraph 14.1 of the contract at issue contained the express negligence language, while paragraph 14.4 required that Ayres indemnify Conoco for any loss or liability arising from any claim made by Ayres' employees. *Id.* at 180.

¹³⁴ *Id.* at 182.

¹³⁵ *Id.*

¹³⁶ *Dresser Indus.*, 853 S.W.2d at 511.

of a form is “conspicuous” if it is in larger or other contrasting type or color. But in a telegram, any term is “conspicuous.”¹³⁷

At least one Texas court of appeals has applied *Dresser* in holding that a capitalized heading and text of the indemnity clause rendered the indemnity clause conspicuous, even when part of the clause was on a subsequent page and not capitalized.¹³⁸ The indemnification clause in the service contract began with the capitalized heading “INDEMNIFICATIONS,” and the main body of the clause was also capitalized, including an indicator that examples were to follow (“...INCLUDING BUT NOT LIMITED TO:...”).¹³⁹ On the next page of the contract, the clause continued with numbered paragraphs in regular, uncapitalized text.¹⁴⁰ The court found that the capitalization of the initial indemnification paragraph was sufficient to attract the attention of a reasonable person to both the main clause, and the subsequent, uncapitalized portions of the agreement.¹⁴¹

B. Contracts Entered into After January 1, 2012

The Texas Anti-Indemnity Act, which became effective January 1, 2012, did away with the express negligence and conspicuousness considerations discussed above for contracts entered into after January 1, 2012.¹⁴² The Act added anti-indemnification language designed to prevent owners and general contractors on construction projects from shifting the risk of their own negligence or breach of contract to subcontractors.¹⁴³

In particular, Section 151.102 of the Texas Insurance Code now provides that “a provision in a construction contract ... is void and unenforceable ... to the extent that it requires an indemnitor to indemnify, hold harmless, or defend a party, including a third party, against a claim caused by the negligence or fault ... of the indemnitee, its agent or employee, or any third party under the control or supervision of the indemnitee ...”¹⁴⁴

The new provisions of the Texas Insurance Code contain exceptions, including claims brought by an employee of a subcontractor.¹⁴⁵ This will allow a general contractor to continue to protect against claims brought by injured persons who are barred from suing their own employer. Other exceptions include such things as homebuilders, municipal projects, oil and gas projects and railroad work.¹⁴⁶ These groups already have laws in effect, however, which may achieve similar purposes.

C. Indemnity with Respect to Architects and Engineers

¹³⁷ *Id.* at 510 (citing TEX. BUS. & COM. CODE ANN. § 1.201(10) (Vernon Supp. 2004-05)).

¹³⁸ *Amtech Elevator Serv. Co. v. CSFB 1998-1 Buffalo Speedway Office Ltd. P’ship*, 248 S.W.3d 373, 378 (Tex.App.—Houston [1st Dist.] 2007, no pet.).

¹³⁹ *Id.*

¹⁴⁰ *Id.*

¹⁴¹ *Id.* at 379.

¹⁴² 2011 Tex. H.B. 2093.

¹⁴³ TEX. INS. CODE § 151.102.

¹⁴⁴ *Id.*

¹⁴⁵ *Id.* § 151.103.

¹⁴⁶ *Id.* § 151.105.

Section 130.002 of the Texas Civil Practice & Remedies Code states that any provision in a construction contract which attempts to require a contractor to indemnify or hold harmless a registered architect or licensed engineer, or an agent, servant, or employee of a registered architect or licensed engineer from liability for damage caused by defects in plans, specifications, or other design documents, or the negligence of the architect or engineer in his professional duties arising out of the construction design documents, is void and unenforceable.¹⁴⁷

At least one Texas court has narrowly construed this statute. In *Foster, Henry, Henry & Thorpe, Inc. v. J.T. Constr. Co.*,¹⁴⁸ after a jury apportioned 0% fault to the architect, the architect sought to enforce its contractual indemnity clause against the contractor in order to recover attorney's fees and court costs.¹⁴⁹ The *Foster* court concluded that Section 130.002 did not apply, as Plaintiff's claimed damages were the result of the contractor's, not the architect's, negligence, and as Section 130.005 of the Code specifically states that the chapter does not apply where the indemnity is for the negligent acts of the contractor. Accordingly, the court reversed the contractor's take nothing judgment against the architect.¹⁵⁰

VI. CONTINGENT PAYMENT AGREEMENTS

A. Contingent Payment Clauses Generally

The Texas Legislature has set parameters on the use and enforceability of contingent payment clauses, also known as "pay when paid" and "pay if paid" clauses, in construction contracts. A contingent payment clause is defined by statute as "a contract for construction management, or for the construction of improvements to real property or the furnishing of materials for the construction, that provides that the contingent payor's receipt of payment from another is contingent precedent to the obligation of the contingent payor to make payment to the contingent payee for work performed or materials furnished."¹⁵¹ Assertion of a contingent payment clause is an affirmative defense in a civil action for payment under a contract.¹⁵² Obligors—those persons obligated to make payments to the contingent payor for the improvement, and primary obligors—the owners of the real property to be improved or repaired under the contract—may not prohibit contingent payors from allocating risk by means of contingent payment clauses.¹⁵³

B. Restrictions on Enforceability

Such clauses are unenforceable to the extent that the obligor's nonpayment to the contingent payor is the result of the contingent payor's failure to meet the contractual

¹⁴⁷ Tex. Civ. Prac. & Rem. Code § 130.002.

¹⁴⁸ *Foster, Henry, Henry & Thorpe, Inc. v. J.T. Constr. Co.*, 808 S.W.2d 139, 140 (Tex. App.—El Paso 1991, writ denied).

¹⁴⁹ *Foster*, 808 S.W.2d at 141.

¹⁵⁰ *Foster*, 808 S.W.2d at 141.

¹⁵¹ TEX. BUS. & COM. CODE § 56.001(2) (2011).¹⁵¹ *Id.* § 56.056.

¹⁵² *Id.* § 56.057.

¹⁵³ *Id.* § 56.051.

obligations, unless the nonpayment is the result of the contingent payee's failure to meet the contingent payee's contractual requirements.¹⁵⁴

Contingent payment clauses may not be enforced if the contingent payor is in a "sham relationship" with the obligor, or if the enforcement would be unconscionable.¹⁵⁵

A contingent payor or its surety may not enforce a contingent payment clause as to work performed or materials delivered after the contingent payor receives written notice from the contingent payee objecting to the further enforceability of the clause, and such written notice becomes effective.¹⁵⁶ The written notice may be sent only after the 45th day after the date the contingent payee submits a written request for payment to the contingent payor that is in a form substantially in accordance with the contingent payee's contract requirements for the contents of a regular progress payment request or an invoice.¹⁵⁷ As detailed in Chapter 56 of the Texas Business and Commerce Code, the date the written notice becomes effective is dependent upon the type of project.¹⁵⁸

In addition, a contingent payment clause may not be used to invalidate the enforceability or perfection of a mechanic's lien.¹⁵⁹

C. Exceptions to Enforceability Restrictions

The statutory restrictions on enforceability do not apply to contracts that are solely for: design services; construction or maintenance of a road, highway, street, bridge, utility, water supply project, water plant, wastewater plant, water and wastewater distribution or conveyance facility, wharf, dock, airport runway or taxiway, drainage project, or related type of project associated with civil engineering construction; or improvements to or the construction of a detached single-family residence, duplex, triplex, or quadruplex.¹⁶⁰

These provisions do not affect a contract provision concerning the timing of a payment in a contract for construction management or for the construction of improvements to real property if the payment is to be made within a "reasonable period."¹⁶¹

D. Waiver Prohibition

These statutory provisions may not be waived, and any purported waiver is void.¹⁶²

VII. DAMAGES LIMITATIONS

A. Measures of Damages Generally

The goal of a damages award for breach of contract is to provide just compensation for the loss actually sustained, awarding the complaining party neither less nor more than the party's

¹⁵⁴ *Id.* §§ 56.053, 56.054.

¹⁵⁵ *Id.* §§ 56.053, 56.054.

¹⁵⁶ *Id.* § 56.052(a).

¹⁵⁷ *Id.*

¹⁵⁸ *Id.* § 56.052(b).

¹⁵⁹ *Id.* § 56.055.

¹⁶⁰ *Id.* § 56.002.

¹⁶¹ *Id.* § 56.003.

¹⁶² *Id.* § 56.004.

actual loss.¹⁶³ In contract cases, the measure normally employed to determine direct damages, whether prescribed by statute or case law, seeks to put the party in as good a position as if the other contracting party had performed as promised by giving the complaining party what was reasonably expected under the contract.¹⁶⁴ The traditional measure of expectancy damages is referred to as the “benefit-of-the-bargain” rule. If it is not feasible to measure a party’s damages by expectancy (as if the contract had been performed), the law may call for a measure that tends to restore the parties to the position they would have been in had the contract never been made. This measure is often referred to as the “out-of-pocket” rule, allowing recovery of damages necessary to restore the status quo.

B. Liquidated Damages vs. Improper Penalty Provisions

In lieu of both the above-mentioned measures, and subject to certain limitations, the parties may agree that damages for a specific breach are “liquidated,” that is, will be assessed as a certain amount or calculated by a set formula. The general rule in Texas is that parties are bound by their agreed-to measure of damages for a breach of contract, unless the agreed-to measure is shown to be an improper penalty provision.¹⁶⁵

The Texas Supreme Court has fashioned a two-part test for the enforceability of a liquidated damages provision, applicable in cases not governed by the UCC. A liquidated damages clause is enforceable if (1) the harm caused by the breach was impossible or difficult to estimate at the time the contract was made and (2) the amount of liquidated damages was a reasonable forecast of just compensation.¹⁶⁶ This is referred to as the *Stewart* test.

Construction contracts often contain liquidated damages clauses, especially with reference to unexcused delays in completion. The results of applying the *Stewart* test to these clauses vary. For example, one court of appeals upheld a clause providing for damages of \$100 per day of delay in the construction of a school gymnasium on the grounds that it would have been difficult to ascertain damages under the circumstances.¹⁶⁷ However, another court of appeals found that \$250 a day for delayed usage of a football stadium was an improper penalty.¹⁶⁸

C. Consequential Damages

Section 2-719 of the U.C.C. allows parties to limit or exclude consequential damages in their contracts.¹⁶⁹ This is codified in Texas Business and Commerce Code § 2.719(c) as follows: “Consequential damages may be limited or excluded unless the limitation or exclusion is unconscionable. Limitation of consequential damages for injury to the person in the case of

¹⁶³ *Phillips*, 820 S.W.2d at 788; *U.S. Rest. Props. v. Motel Enters.*, 104 S.W.3d 284, 291 (Tex. App.—Beaumont 2003, pet. denied).

¹⁶⁴ *R.G. McClung Cotton Co. v. Cotton Concentration Co.*, 479 S.W.2d 733, 738 (Tex. App.—Dallas 1972, writ ref. n.r.e.).

¹⁶⁵ *See Phillips*, 820 S.W.2d at 788.

¹⁶⁶ *Stewart v. Basey*, 245 S.W.2d 484, 485-86 (Tex. 1952).

¹⁶⁷ *Commercial Union Ins. v. La Villa Sch. Dist.*, 779 S.W.2d 102, 107 (Tex. App.—Corpus Christi 1989, no writ).

¹⁶⁸ *Loggins Constr. Co. v. Steven F. Austin State Univ.*, 543 S.W.2d 682, 685-86 (Tex. Civ. App.—Tyler 1976, writ ref. n.r.e.).

¹⁶⁹ U.C.C. § 2-719.

consumer goods is *prima facie* unconscionable but limitation of damages where the loss is commercial is not.”¹⁷⁰

D. Mental Anguish and Exemplary Damages

The general rule in Texas is that mental anguish and exemplary damages are unavailable for breach of contract.¹⁷¹ Exemplary damages are not recoverable unless the contractor pleads and proves a tort, regardless of whether the breach is malicious.¹⁷²

E. Attorney’s Fees

1. Generally

For more than a century, Texas law has refused to allow the recovery of attorney’s fees in tort actions or suits on contract unless such fees are specifically authorized by statute or contract.¹⁷³ Trial courts are not permitted to require a losing party to pay the prevailing party’s fees without such statutory or contractual authorization.¹⁷⁴ This is known as the traditional “American Rule.” The opposite rule, known as the “loser pays” or “English Rule,” is common in many other countries and allows a court to award attorney’s fees to the prevailing party.¹⁷⁵

2. Statutory Authorization

For certain actions, the Texas Legislature has provided statutory authorization for the award of attorney’s fees. For example, an award of attorney’s fees in contract cases is provided by Chapter 38 of the Texas Civil Practice and Remedies Code, which authorizes the recovery of fees for any claim on an “oral or written contract,” provided that the claimant actually retains an attorney, presents the written claim to the opposing party, and allows the opposing party at least thirty days to tender payment of the contract damages.¹⁷⁶ This statute also allows for fee recovery associated with claims for performed labor and furnished material, amongst other claims.¹⁷⁷

In 2011, the Texas Legislature expanded opportunities for fee recovery by adopting a limited version of the English Rule. Chapter 30 of the Civil Practices and Remedies Code now provides that, “on a trial court’s granting or denial, in whole or in part, of a motion to dismiss” of a cause of action that has a basis in law or fact on motion and without evidence, the court shall award attorney’s fees to the prevailing party.¹⁷⁸ However, this legislation does not apply to

¹⁷⁰ Tex. Bus. & Com. Code § 2.719(c).

¹⁷¹ See *Stewart Title Guar. Co. v. Aiello*, 941 S.W.2d 68, 72 (Tex. 1997).

¹⁷² See *Jim Walter Homes, Inc. v. Reed*, 711 S.W.2d 617, 618 (Tex. 1986).

¹⁷³ E.g., *Tony Gullo Motors I, L.P. v. Chapa*, 212 S.W.3d 299, 310 (Tex. 2006).

¹⁷⁴ *Id.*

¹⁷⁵ See, e.g., *1/2 Price Checks Cashed v. United Auto. Ins. Co.*, 344 S.W.3d 378, 382 n.8 (Tex. 2011).

¹⁷⁶ TEX. CIV. PRAC. & REM. CODE §38.001 (Vernon 2007).

¹⁷⁷ TEX. CIV. PRAC. & REM. CODE § 38.001.

¹⁷⁸ TEX. CIV. PRAC. & REM. CODE § 30.021 (2011).

actions by or against the state, other governmental entities, or public officials acting in their official capacity or under color of law.¹⁷⁹

3. Contractual Authorization

Many contracts include “fee-shifting” provisions stating that attorney’s fees may be recoverable by the prevailing party in a dispute related to the contract. The contract may specify a particular amount or provide for the recovery of “reasonable” attorney’s fees. In Texas, these provisions are generally enforceable, and the language of the contract governs, even if attorney’s fees would have been available under statute.¹⁸⁰

F. Personal Injury Damages vs. Construction Defect Damages

A plaintiff’s available damages arising from a construction project are dependent upon whether the claim is a personal injury claim brought under tort law or a claim for construction defects brought under theories of general contract law or certain statutes.

1. Personal Injury Damages

In a personal injury suit, tort principles apply, which entitle a plaintiff to his actual damages. Actual damages may include both economic and non-economic damages, such as medical expenses (economic) and compensation for physical and mental pain and suffering (non-economic).¹⁸¹ By statute, exemplary damages are only available if the harm results from: a) fraud, b) malice, c) gross negligence, or d) specified circumstances or culpable mental states set out in particular statutes.¹⁸² The claimant must prove the elements of exemplary damages by clear and convincing proof.¹⁸³ Attorney’s fees are not generally available in personal injury suits.

2. Construction Defect Damages

i. Standard Breach of Contract

Construction defect claims may be brought in several different ways, each with its own damage limitations. In a standard breach of contract suit for the construction defect, the claimant is entitled to his expectancy damages.¹⁸⁴ Exemplary damages are not generally recoverable in breach of contract cases.¹⁸⁵ Attorney’s fees may be allowed under Chapter 38 of the Texas Civil Practices and Remedies Code, which permits recovery of attorney’s fees for breach of oral or written contracts.¹⁸⁶ Attorney’s fees may also be recovered if the contract contains provides for such recovery.¹⁸⁷ If a direct contractual relationship does not exist, a claimant may rely on the

¹⁷⁹ *Id.*

¹⁸⁰ *Intercontinental Group P'ship v. KB Home Lone Star L.P.*, 295 S.W.3d 650, 653 (Tex. 2009).

¹⁸¹ *Firestone Tire & Rubber Co. v. Battle*, 745 S.W.2d 909, 917 (Tex. App.—Houston [1st Dist.] 1988, writ denied).

¹⁸² TEX. CIV. PRAC. & REM. CODE § 41.003(a).

¹⁸³ *Id.* § 41.003(b).

¹⁸⁴ *R.G. McClung Cotton Co. v. Cotton Concentration Co.*, 479 S.W.2d 733, 738 (Tex. App.—Dallas 1972, writ ref. n.r.e.).

¹⁸⁵ *Title Guar. Co. v. Aiello*, 941 S.W.2d 68, 72 (Tex. 1997).

¹⁸⁶ TEX. CIV. PRAC. & REM. CODE § 38.001.

¹⁸⁷ *E.g., Tony Gullo Motors I, L.P.*, 212 S.W.3d at 310.

statutory attorney's fees provisions applicable to suits for rendered services, performed labor, or furnished material.¹⁸⁸

ii. Residential Construction Liability Act

If the claim relates to a construction defect in residential property and is brought under the Residential Construction Liability Act, the claimant may recover only the following economic damages: 1) the reasonable cost of repairs necessary to cure any construction defect; 2) the reasonable and necessary cost for the replacement or repair of any damaged goods in the residence; 3) reasonable and necessary engineering and consulting fees; 4) the reasonable expenses of temporary housing reasonably necessary during the repair period; 5) the reduction in current market value, if any, after the construction defect is repaired, if the construction defect is a structural failure; and 6) reasonable and necessary attorney's fees.¹⁸⁹

iii. Deceptive Trade Practices Act

Additionally, if a claimant brings suit under the Deceptive Trade Practices Act for breach of express or implied warranty, the claimant may recover economic damages and attorney's fees. If the trier of fact finds that the breach was committed knowingly or intentionally, the court may award mental anguish and exemplary damages.¹⁹⁰

G. Liability for Acts of Independent Contractors

Under Texas Civil Practice and Remedies Code § 95.003, a person or entity that owns real property primarily used for commercial or business purposes ("property owner") is not liable for personal injury, death, or property damage ("claim") to a contractor, subcontractor, or an employee thereof who constructs, repairs, renovates, or modifies an improvement to real property, including claims arising from the failure to provide a safe workplace, unless both (1) the property owner exercises or retains some control over the manner in which the work is performed, other than the rights to order the work to start and stop, to inspect progress, or to receive reports; and (2) the property owner had actual knowledge of the danger or condition resulting in the claim and failed to adequately warn.¹⁹¹

¹⁸⁸ TEX. CIV. PRAC. & REM. CODE § 38.001(1).

¹⁸⁹ TEX. PROP. CODE § 27.004(g).

¹⁹⁰ TEX. BUS. & COM. CODE § 17.50

¹⁹¹ TEX. CIV. PRAC. & REM. CODE § 95.003.

UTAH

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I. MECHANICS' LIEN BASICS

A. Requirements.

Utah law requires that several documents be filed in order for a mechanics' lien to be created. Each of these filings is to be made with the State Construction Registry, which accepts filings online at <https://secure.utah.gov/scr/guide/contractors.html>.

1. **Notice of Preconstruction Service.** A person performing preconstruction services must file a notice of preconstruction service within 20 days of commencing providing the services; failure to do so will prevent claim of a valid lien.¹ One notice must be filed for each anticipated improvement and for each original contract under which services are rendered.²
2. **Preliminary Notice.** A person providing construction services must file a preliminary notice within 20 days of commencing providing those services.³ If no preliminary notice is filed, no lien may be created.⁴ A late notice may be filed if it is not filed more than 10 days after filing the notice of completion.⁵ Only one notice must be filed for each project, unless construction is being performed under multiple contracts; in that case, one notice must be filed for each contract.⁶
3. **Notice of Construction Loan and Notice of Default.** A notice of construction loan must be filed "promptly, in conjunction with the closing of the construction loan," after the mortgage or trust deed is recorded.⁷ A construction lender must file a notice of construction loan default within five business days after a notice of default is filed in the county recorder's office.⁸
4. **Notice of Intent to Obtain Final Completion.** An owner or original contractor of a nonresidential construction project that is registered with the registry must file a notice of intent to obtain final completion under certain conditions: namely, if the original contract specifies a performance time longer than 120 days, if the total price under the contract exceeds \$500,000, and if no payment bond has been obtained.⁹ This notice must be filed at least 45 days before final construction is completed or when the

notice of completion could have been filed.¹⁰ Anyone providing construction work to the owner or original contractor must then file an amended preliminary notice within 20 days of the filing of the notice of intent.¹¹

5. **Notice of Completion.** Notice of completion should be filed with the registry once a project is completed.¹² An owner, original contractor, lender, surety, or title company involved with the project may file the notice, which must include the date of completion and method used to determine final completion.¹³
6. **Government Project Filings.** Government projects require a special set of additional filings. If the construction work at issue is being done at a government construction site, a notice of commencement must be filed within 15 days of the commencement of construction.¹⁴ This notice applies only to goods and services provided after it is filed.¹⁵ A subcontractor on a government project must then file a preliminary notice within either 20 days of commencing work or 20 days of the filing of a notice of commencement, whichever is later.¹⁶ Failure to file precludes any claim for compensation other than under a contract; late filings take effect five days after they are filed and apply only to work done after they take effect.¹⁷ The preliminary notice requirements described above apply to government projects also.¹⁸

B. **Enforcement and Foreclosure.**

1. **Notice of Claim.** A notice of claim based on nonpayment for preconstruction services must be filed with the applicable county recorder within 90 days after the services are completed.¹⁹ A copy of this notice must be sent to the owner of the real property within 30 days; failure to do so precludes the lienholder from recovering attorney's fees in any action to enforce the lien.²⁰ Similarly, a person claiming a construction service lien must file a notice of claim with the county recorder within 90 days after a notice of completion is filed, or, if no notice of completion is filed, within 180 days of completion.²¹ Again, notice must be sent within 30 days or the lienholder may not recover attorney's fees.²² If a subcontractor performs substantial work after a certificate of occupancy is issued or a required final inspection is completed then that subcontractor must submit a notice of construction lien within 180 days after the subcontractor's work is finished.²³
2. **Bringing an Action.** An action to enforce a lien must be filed within 180 days of the filing of a notice of claim unless the owner files for bankruptcy within the 180-day period; in that case, the action must be filed within 90 days after the bankruptcy court's automatic stay is lifted or expires.²⁴ The lien is voided if an action is not filed within this time period.²⁵ A notice of

pendency of the action must be filed with the applicable county recorder within the same time period; if this is not filed, the lien becomes void except as to parties to the action and persons with actual knowledge of the action.²⁶ When serving a complaint on the residence's owner, the lienholder must include with the complaint a statement of the owner's rights to avoid a lien; failure to do so will void the lien.²⁷

3. **Residence Lien Restriction and Lien Recovery Fund Act.** In order to enforce a lien on a residence, the owner of the residence must be served with (1) instructions under Title 38, Chapter 11, Residence Lien Restriction and Lien Recovery Fund Act (Act) and (2) a form for the owner to list the grounds for enforcement of rights under Title 38, Chapter 11.²⁸ The court is required to give the owner reasonable time to establish compliance with the Act and obtain a certificate or denial of compliance.²⁹

C. **Ability to Waive or Limit Lien Rights.**

1. **Waiver.** A lien claimant can only waive rights via a signed express agreement to that effect or via a signed restrictive endorsement on a check.³⁰ Utah Code Ann. § 38-1a-802 contains waiver forms.³¹ Unless this section is followed, "A right or privilege under this chapter may not be waived or limited by contract," and any contractual provision that purports to do so is void.³²
2. **Limitations.** In Utah, mechanics' liens may not be obtained on certain types of construction. First, government projects are governed by § 38-1b-102, and not by the general Preconstruction and Construction Leins rules.³³ In addition, a mechanics' lien may not be obtained against an owner-occupied residence if the owner meets the conditions of § 38-11-204(4)(a) and (b), or the owner has subsequently sold the property.³⁴ Similarly, a subcontractor may not place a lien on an owner-occupied residence if the general contract under which the subcontractor was working was for \$5,000 or less.³⁵ Owners must be informed of these rights via written contract with the original contractor or real estate developer.³⁶

If a subcontractor has already begun to perform services that could give rise to a lien, the subcontractor's lien is not affected by a payment from the owner to the general contractor.³⁷ This is true even if the payment was made prior to when it was due.³⁸ Similarly, a lien is not affected by alteration of a construction contract.³⁹ Raw materials furnished for use in construction and about to be applied to that construction cannot be attached or executed to satisfy a debt unless the debt was for the purchase money of those materials.⁴⁰

II. **STATUTES OF LIMITATION AND REPOSE**

Where an action is based on improvements to real property, Utah law allows parties to lengthen or shorten the statutory limitations period via contract.⁴¹ In addition, none of the provisions discussed below apply to an action for the death of or bodily injury to an individual while working on a project,⁴² nor to an action against an owner, tenant, or other person in control at the time of the defective or unsafe condition.⁴³

- A. **Statutes of Limitation and Limitations on Application of Statutes.** Actions based in contract or warranty must be commenced within six years of the date of completion.⁴⁴ However, in these cases a different time limit may be selected by the parties via express contract or warranty.⁴⁵ All other actions must be brought within two years of the date that the cause of action was or should have been discovered, unless the cause of action was discovered prior to completion, in which case the action must be brought within two years of completion.⁴⁶ A person unable to bring an action during the limitations period due to minority or incompetency may bring an action within two years of the date that disability is removed.⁴⁷
- B. **Statutes of Repose and Limitations on Application of Statutes.** Generally, no action may be brought more than nine years after a project's completion.⁴⁸ However, if the cause of action is discovered or should reasonably be discovered within the eighth or ninth year of the nine-year period, the person possessing the cause of action has two years from the date of discovery to bring the action.⁴⁹ In addition, the nine-year limit does not apply where the provider has engaged in fraudulent, willful, or intentional wrongdoing.⁵⁰ Finally, as with the statute of limitations, the statute of repose makes a two-year exception for persons unable to bring an action during the applicable time period due to minority or incompetency.⁵¹

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

Unless parties agree otherwise through contract, there is no pre-suit notice requirement specific to Utah construction law. For example, a homeowner is not required to give a vendor pre-suit notification or an opportunity to cure in any action, including actions for breach of warranty, unless the homeowner has contracted to do so. Of course, the Uniform Commercial Code, which Utah has adopted, requires that an opportunity to cure be given where goods are concerned.⁵² However, this requirement does not apply to services such as the construction itself. The UCC has limited application in the construction arena—for example, where raw materials to be used in construction are being purchased or sold.⁵³

A general pre-suit notice of claim requirement does exist where a vendor wishes to sue a governmental entity.⁵⁴ In such cases, notice of claim must be filed within one year of the event giving rise to the claim.⁵⁵

IV. INSURANCE COVERAGE AND ALLOCATION ISSUES

- A. **General Coverage Issues.** The policy most usually applicable in the construction context is a standard commercial general liability (CGL) policy. A duty to defend under a CGL policy arises “when the insurer ascertains facts giving rise to potential liability under the insurance policy.”⁵⁶
- B. **Trigger of Coverage.** Under Utah law, an “occurrence” triggering coverage under a CGL policy happens when “the occurrence causing the injury or death is not a *natural and probable* result of the victim's own acts.”⁵⁷ Utah courts have interpreted this rule to hold that a breach of warranty is not an “occurrence” and is not covered by a CGL policy.⁵⁸ Similarly, negligent misrepresentations made by a developer or contractor do not give rise to coverage.⁵⁹ In addition, Utah’s federal district court has held that Utah law precludes coverage under a CGL policy for claims arising out of an insured’s negligent construction.⁶⁰ However, Utah’s federal district court has also held that faulty work by a subcontractor constitutes an “occurrence” under a CGL policy from the standpoint of an insured general contractor.⁶¹
- C. **Allocation Among Insurers.** Where a continuing injury is alleged, Utah uses a modified “time on the risk” method to determine allocation between multiple CGL insurers. Allocation is determined by multiplying the affected policy limits by the years of coverage, taking into account periods during which the insured was uninsured or self-insured.⁶² When two insurers are involved, defense costs are apportioned by the modified time on the risk method and not based on “other insurance” clauses.⁶³

V. CONTRACTUAL INDEMNIFICATION

Under Utah law, contractual indemnification agreements in construction contracts which force a person (such as a subcontractor) to indemnify another (such as a general contractor) for the other’s own negligence are void and unenforceable if the damages arise out of bodily injury, damage to property, or economic loss.⁶⁴ If an indemnification provision was contracted for between an owner and a vendor, the fault of the owner will be apportioned among all the vendors involved in the construction if the damages were caused in part by the owner and the damage did not occur while the owner was acting in the capacity of a vendor.⁶⁵

Utah courts have held that a contractual requirement that a vendor (such as a subcontractor) procure liability insurance and name another (such as a general contractor) as an additional insured is lawful and enforceable so long as the contract does not require the vendor to personally insure or indemnify the other for liability arising out of the other’s own negligence.⁶⁶

VI. CONTINGENT PAYMENT AGREEMENTS

Utah law provides that “[a] party to a construction contract shall make all scheduled payments under the terms of the construction contract.”⁶⁷ However, this provision does not prevent the creation of a contingent payment contract, since “scheduled payments” under such contracts may be structured on a contingent basis.

- A. **Enforceability.** Utah law treats contingent payment contracts differently based on the type of construction being undertaken. Generally, a contingent payment contract is not a defense to enforcement of a mechanics' lien.⁶⁸ However, an exception is made for private residential construction work where the property at issue has four units or fewer.⁶⁹
- B. **Requirements.** A subcontractor entering into a contingent payment contract has the right to request and receive from the contractor any financial information the contractor has been given regarding the project's financing or the party paying the contractor.⁷⁰ This information, if requested, must be given to the subcontractor prior to the time the construction contract is signed.⁷¹

VII. DAMAGE LIMITATIONS

- A. **Personal Injury Damages vs. Construction Defect Damages.** Damages in tort are measured by the amount necessary to "place the plaintiff in the same position he would have occupied had the tort not been committed."⁷² Damages for breach of a construction contract, on the other hand, are determined by either "the reasonable cost of construction and completion in accordance with the contract" or, if completion of the contract would be wasteful, the diminution in value of the property.⁷³
- B. **Attorney's Fees Shifting and Limitations on Recovery.**
 - 1. **Awards of Attorney's Fees.** Under Utah law, "attorney fees are awardable only if authorized by statute or by contract."⁷⁴ In all cases, attorney's fees may be awarded if the action or defense at issue "was without merit and not brought or asserted in good faith"⁷⁵ In addition, numerous Utah statutes provide for awards of attorney's fees in the construction context. For example, a contractor who fails to pay his subcontractors and suppliers within 30 days of being paid himself must pay "reasonable costs of any collection and attorney's fees."⁷⁶ Similarly, attorney's fees are awarded to the successful party in any dispute over withholding of retention proceeds,⁷⁷ or a dispute over whether adequate funds exist to ensure the completion of a project.⁷⁸ Likewise, actions made upon payment bonds,⁷⁹ or based on the failure to obtain a payment bond,⁸⁰ may give rise to awards of attorney fees. Subcontractors are automatically awarded their costs and attorney's fees relating to the preparation of a notice of claim.⁸¹

A successful party in an action to enforce a lien is entitled to attorney's fees unless the lien was wrongful.⁸² However, a party defending an action to enforce a lien may alter the application of this rule by making an offer of judgment pursuant to Rule 68 of the Utah Rules of Civil Procedure. If an offer is made and rejected, and the subsequent judgment obtained is

less than the offer made, the party enforcing the lien must pay any attorney's fees and costs incurred after the offer was made.⁸³

A condemnee who prevails on a motion to set aside a condemnation is entitled to attorney's fees if the condemnor is found not to have commenced or completed construction within a time specified by the court.⁸⁴ Attorney's fees are also awarded in any enforcement action regarding violation of the Utah Construction Trades Licensing Act.⁸⁵

2. **Limitations on Fee Awards.** A lien claimant who has filed a mechanics' lien or a foreclosure proceeding can avoid being required to pay the other party's attorney's fees if the claimant removes the lien within 15 days of the issuance of a certificate of compliance on behalf of the property owner.⁸⁶ In a foreclosure proceeding, a plaintiff's attorney's fee must be "fixed by the court" and must be limited to "the sum which shall appear by the evidence to be actually charged by and to be paid to the attorney for the plaintiff."⁸⁷ The fee must also be limited to "the amount to be retained by the attorney or attorneys" if there is some sort of contingent or other agreement between the attorney and the plaintiff or another party to divide fees.⁸⁸ If a judgment results in a payment from the Residence Lien Recovery Fund, the amount of attorney's fees paid may not exceed 15% of qualified services.⁸⁹

- C. **Consequential Damages.** Consequential damages are available in breach of contract cases.⁹⁰ "To recover consequential damages, a nonbreaching party must prove (1) that consequential damages were caused by the contract breach; (2) that consequential damages ought to be allowed because they were foreseeable at the time the parties contracted; and (3) the amount of consequential damages within a reasonable certainty."⁹¹ "[T]he foreseeability of any such damages will always hinge upon the nature and language of the contract and the reasonable expectations of the parties."⁹²
- D. **Delay and Disruption Damages.** Damages for delay and disruption are generally recoverable,⁹³ although Utah courts have held that contractual provisions barring the pursuit of delay damages are enforceable.⁹⁴ However, even if there is a "no damages" provision in the contract, a party may recover delay damages if the other party's "interference is direct, active, or willful"⁹⁵
- E. **Economic Loss Doctrine.** The economic loss rule prevents plaintiffs from claiming economic damages in negligence actions unless there was physical property damage or bodily injury.⁹⁶ Examples of economic damages include "[d]amages for inadequate value, costs of repair and replacement, or consequent loss of profits"⁹⁷ However, the economic loss rule does not apply to claims that arise out of "a duty [that] exists independent of any contractual obligations between the parties."⁹⁸

- F. **Interest.** “Prejudgment interest may be awarded in a case where the loss is fixed as of a particular time and the amount of the loss can be calculated with mathematical accuracy.”⁹⁹ In personal injury cases, prejudgment interest is calculated from the date of the actual act giving rise to the cause of action.¹⁰⁰ In contract cases, prejudgment interest is calculated from the date of the breach.¹⁰¹
- G. **Punitive Damages.** Punitive damages may be awarded “only if compensatory or general damages are awarded and it is established by clear and convincing evidence that the acts or omissions of the tortfeasor are the result of willful and malicious or intentionally fraudulent conduct, or conduct that manifests a knowing and reckless indifference toward, and a disregard of, the rights of others.”¹⁰²

¹ Utah Code Ann. § 38-1a-401(1)(a–b).

² *Id.* § 38-1a-401(1)(c–d).

³ *Id.* § 38-a1-501(1)(a).

⁴ *Id.* § 38-1a-501(1)(e).

⁵ *Id.* § 38-1a-501(1)(c–d).

⁶ *Id.* § 38-1a-501(1)(b).

⁷ *Id.* § 38-1a-601(1).

⁸ *Id.* § 38-1a-602(1).

⁹ *Id.* § 38-1a-506(1)(a–c).

¹⁰ *Id.* § 38-1a-506(2).

¹¹ *Id.* § 38-1a-506(3)(a–b).

¹² *Id.* § 38-1a-507(1)(a).

¹³ *Id.* § 38-a1-507(1)(a)(i–v) and (b)(v–vi).

¹⁴ *Id.* § 38-1b-201(1).

¹⁵ *Id.* § 38-1b-201(5).

¹⁶ *Id.* § 38-1b-202(1)(i–ii).

¹⁷ *Id.* § 38-1b-202(5).

¹⁸ *Id.* § 38-1b-202(2).

¹⁹ *Id.* § 38-1a-402(1).

²⁰ *Id.* § 38-1a-402(5)(a–c).

²¹ *Id.* § 38-1a-502(1)(a)(i–ii).

²² *Id.* § 38-1a-502(4)(a–c).

²³ *Id.* § 38-1a-502(1)(b).

²⁴ *Id.* § 38-1a-701(2)(a–b).

²⁵ *Id.* § 38-1a-701(4)(a).

²⁶ *Id.* § 38-1a-701(3)(a)(i–ii).

²⁷ *Id.* § 38-1a-701(6)(c).

²⁸ *Id.* § 38-1a-701(6)(a)(i–ii).

²⁹ *Id.* § 38-1a-701(6)(d)(i–ii).

³⁰ *Id.* § 38-1a-802(2)(a–b).

³¹ *Id.* § 38-1a-802(4)(a–b).

³² *Id.* § 38-1a-105(1–2).

³³ *Id.* § 38-1a-103.

³⁴ *Id.* § 38-11-107(1)(a–b).

³⁵ *Id.* § 38-11-107(1)(b)(ii)(A).

³⁶ *Id.* § 38-11-108(1).

³⁷ *Id.* § 38-1a-303(1–3).

³⁸ *Id.* § 38-1a-303(2).

³⁹ *Id.* § 38-1a-303(1–3).
⁴⁰ *Id.* § 38-1a-505(1).
⁴¹ *Id.* § 78B-2-225(9).
⁴² *Id.* § 78B-2-225(7).
⁴³ *Id.* § 78B-2-225(8).
⁴⁴ *Id.* § 78B-2-225(3)(a).
⁴⁵ *Id.*
⁴⁶ *Id.* § 78B-2-225(3)(b).
⁴⁷ *Id.* § 78B-2-225(6).
⁴⁸ *Id.* § 78B-2-225(4).
⁴⁹ *Id.*
⁵⁰ *Id.* § 78B-2-225(5).
⁵¹ *Id.* § 78B-2-225(6).
⁵² *Id.* § 70A-2-508.
⁵³ See *id.* § 70A-2-105(1) (“‘Goods’ means all things (including specially manufactured goods) which are movable at the time of identification to the contract for sale . . .”).
⁵⁴ *Id.* § 63G-7-401(2).
⁵⁵ *Id.* § 63G-7-402.
⁵⁶ *Basic Research, LLC v. Admiral Ins. Co.*, 2013 UT 6 (quoting *Sharon Steel Corp. v. Aetna Cas. & Sur.*, 931 P.2d 127, 133 (Utah 1997)).
⁵⁷ *Hoffman v. Life Ins. Co. of N. Am.*, 669 P.2d 410, 416 (Utah 1983).
⁵⁸ *Green v. State Farm Fire & Cas. Co.*, 2005 UT App 564, ¶ 28, 127 P.3d 1279, 1284 (Utah Ct. App. 2005).
⁵⁹ *Nova Cas. Co. v. Able Constr., Inc.*, 983 P.2d 575, 580 (Utah 1999).
⁶⁰ *H.E. Davis & Sons, Inc. v. N. Pac. Ins. Co.*, 248 F.Supp.2d 1079, 1084 (D. Utah 2002).
⁶¹ *Great Am. Ins. Co. v. Woodside Homes Corp.*, 448 F. Supp. 2d 1275, 1283 (D. Utah 2006).
⁶² *Sharon Steel*, 931 P.2d at 140–41; see also *Ohio Cas. Ins. Co. v. Unigard Ins. Co.*, 2012 UT 1.
⁶³ *Ohio Cas. Ins. Co.*, 2012 UT 1 at ¶¶ 2, 14.
⁶⁴ Utah Code Ann. § 13-8-1(2).
⁶⁵ *Id.* § 13-8-1(3).
⁶⁶ See *Blaisdell v. Dentrux Dental Sys.*, 2012 UT 37, ¶¶ 9–10 (analyzing *Meadow Valley Contractors, Inc. v. Transcontinental Ins. Co.*, 27 P.3d 594, 598 (Utah Ct. App. 2001)).
⁶⁷ Utah Code Ann. § 13-8-4(2).
⁶⁸ *Id.* § 13-8-4(3)(a).
⁶⁹ *Id.* § 13-8-4(3)(b).
⁷⁰ *Id.* § 13-8-4(4)(a).
⁷¹ *Id.* § 13-8-4(4)(b).
⁷² *Firkins v. Ruegner*, 213 P.3d 895, 899 (Utah Ct. App. 2009) (quoting *Mahana v. Onyx Acceptance Corp.*, 96 P.3d 893, 899 (Utah 2004)).
⁷³ *Rex T. Fuhrman, Inc. v. Jarrell*, 445 P.2d 136, 139 (Utah 1968) (quoting *Restatement of Contracts* § 346(1) (1933)).
⁷⁴ *Jones v. Riche*, 2009 UT App 196, ¶ 1.
⁷⁵ Utah Code Ann. § 78B-5-825(1).
⁷⁶ *Id.* § 58-55-603(2).
⁷⁷ *Id.* § 13-8-5(10)(a)(i).
⁷⁸ *Id.* § 38-1a-506(7).
⁷⁹ *Id.* § 14-2-1. It is unclear from the statute whether an award of attorney fees is mandatory or discretionary. Subsection (5)(d) states, “In any action upon a payment bond under this section, the court *may* award reasonable attorneys’ fees to the prevailing party,” *id.* § 14-2-1(5)(d) (emphasis added), while subsection (7) states that “the court *shall* award reasonable attorneys’ fees to the prevailing party,” *id.* § 14-2-1(7) (emphasis added). The apparent conflict between these two provisions has not been resolved by Utah courts.
⁸⁰ *Id.* § 14-2-2(3).
⁸¹ *Id.* § 38-1a-706(2)(a–b).
⁸² *Id.* § 38-1a-707(1–2).
⁸³ *Id.* § 38-1a-707(3)(a–b).
⁸⁴ *Id.* § 78B-6-520(2).

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- ⁸⁵ *Id.* § 58-55-503(5)(d).
- ⁸⁶ *Id.* § 38-11-107(3).
- ⁸⁷ *Id.* § 78B-6-908(1).
- ⁸⁸ *Id.* § 78B-6-908(2).
- ⁸⁹ *Id.* § 38-11-203(3)(f).
- ⁹⁰ *See Mahmood v. Ross*, 990 P.2d 933, 937 (Utah 1999).
- ⁹¹ *Id.* (quoting *Castillo v. Atlanta Cas. Co.*, 939 P.2d 1204, 1209 (Utah Ct. App. 1997)).
- ⁹² *Berube v. Fashion Centre, Ltd.*, 771 P.2d 1033, 1050 (Utah 1989) (quoting *Beck v. Farmers Ins. Exch.*, 701 P.2d 795, 801 (Utah 1985)).
- ⁹³ *See Higgins v. City of Fillmore*, 639 P.2d 192, 194 (Utah 1981).
- ⁹⁴ *Allen-Howe Specialties Corp. v. U. S. Constr., Inc.*, 611 P.2d 705, 709 (Utah 1980).
- ⁹⁵ *Id.*
- ⁹⁶ *Davencourt at Pilgrim's Landing Homeowners Ass'n v. Davencourt at Pilgrim's Landing, LC*, 221 P.3d 234, 242 (Utah 2009).
- ⁹⁷ *Id.* (quoting *Am. Towers Owners Ass'n v. CCI Mech., Inc.*, 930 P.2d 1182, 1189 (Utah 1996)).
- ⁹⁸ *Id.* (quoting *Hermansen v. Tasulis*, 48 P.3d 235, 240 (Utah 2002)); *see also id.* at 247 ("This limited fiduciary duty does not permit any and all tort claims to be brought. Instead, only those tort claims that stem from this independent, limited fiduciary duty are permitted.").
- ⁹⁹ *Ellsworth Paulsen Constr. Co. v. 51-SPR, LLC*, 2006 UT App 353, ¶ 42 (quoting *Jorgensen v. John Clay & Co.*, 660 P.2d 229, 233 (Utah 1983)).
- ¹⁰⁰ Utah Code Ann. § 78B-5-824(1).
- ¹⁰¹ *See Orlob v. Wasatch Med. Mgmt.*, 124 P.3d 269, 277–78 (Utah Ct. App. 2005)
- ¹⁰² Utah Code Ann. § 78B-8-201(1)(a).

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I. MECHANIC'S LIEN BASICS

Contractors' liens, which include Mechanics' and Material Suppliers' liens, are governed by 9 V.S.A. § 1921-28. In general, to secure payment, a person providing labor or materials pursuant to a contract for erecting, repairing, moving, or altering improvements to real property or for furnishing labor or material to a property, shall have a lien on the labor or materials to secure the payment for the work.¹ There are several requirements for perfection of the lien that could become "minefields" for the unwary practitioner. The necessity of strict compliance with the statute's procedures has been long recognized in Vermont.²

A. Requirements

1. Pre-lien Notice

Any person claiming a lien must give notice in writing to the owner of the property that he or she shall claim a lien for the labor or material. The notice shall include the date that payment is due, if known. The lien extends to the portions of the contract price remaining unpaid at the time the notice is received by the owner.³

The lien remains in force for only 180 days from the time when payment became due for the last labor performed or materials furnished unless a Notice of Lien is recorded in the land records maintained by the town clerk's office.⁴ The pre-lien notice does not put the world on notice – only owners, who are liable in tort if they alienate the property so as to defeat the lien.⁵ Note that the statute does not prescribe a "waiting period" between the contractor's giving written notice and the filing of the lien in the land records. In many cases, the best practice may be to give notice to the owner at the same time that the lien is recorded.

2. Recording

To perfect a lien, a person must first file a notice of lien in the office of the town clerk within 180 days from the time when payment became due for the last of such labor performed or materials furnished on the property.⁶ The notice is in the form of a written memorandum, signed

by the person claiming the lien, asserting his claim, describing the real estate and/or building into which the labor and materials went and disclosing the amount claimed. The memorandum must also state the person to whom it is due and from whom it is due, and that the person from whom it is due is the owner of the property.⁷ The real estate is then charged with the lien as of the visible commencement of work or delivery of material.⁸ If there are several contractors' liens, and the sum due from the owner is not sufficient to pay them all in full, the liens shall be paid pro rata.⁹

B. Enforcement and Foreclosure

1. Enforcement

Within 180 days from the time of filing the memorandum or, if payment is not yet due at the time of filing within 180 days from the time such payment becomes due, the person asserting the lien may commence an action for the payment due and cause the real estate or other property to be attached. If judgment is obtained in the action, the record of such judgment shall contain a brief statement of the contract upon which the action is founded.¹⁰

2. Foreclosure

Within five months after the date of a judgment, a person may cause a certified copy of the judgment to be recorded in the office of the clerk of the town in which the real estate is situated.¹¹ The United States District Court for the District of Vermont, on appeal from the Bankruptcy Court, has held that the failure to strictly comply with the five month window to record the judgment causes the contractor's lien to expire.¹²

The effect of recording the judgment is to encumber the attached property for the amount due on such judgment as if it had been mortgaged for the payment thereof.¹³ Then, and only then, shall a contractor have the right to foreclose the lien, obtaining possession and foreclosing the defendant's equity of redemption as if it were a mortgage.¹⁴

C. Ability to Waive and Limitations on Lien Rights

1. Waiver not possible

A contractor's lien may not be waived in advance of the time such labor is performed or materials are furnished, and any provision calling for such advance waiver shall not be enforceable.¹⁵

2. Other Limitations on Lien Rights

The lien shall not take precedence over a deed or other conveyance to a good faith purchaser to the extent the purchase was made before the lien was recorded.¹⁶ The lien does not take precedence over a mortgage given by the owner as security for the payment of money loaned and to be used by such owner in payment of the expenses of the property, if such mortgage is recorded before the contractor's lien is filed in the town clerk's office.¹⁷ However, if the mortgagee receives written notice of any contractors' lien, the lien shall take precedence over the mortgage as to all advances made after the mortgagee has notice of the lien, except such

advances as the mortgagee may show were actually expended in completing such improvements to real property.¹⁸

II. STATUTES OF LIMITATIONS AND REPOSE

A. Statutes of Limitations

Vermont has no statute of limitations that specifically relates to the construction industry. Statutes of limitations limit only court proceedings; arbitration is not barred by the running of a statute of limitations.¹⁹ Vermont law prohibits contractual waiver of the statute of limitations.²⁰

Generally in Vermont as discussed below, the nature of harm done rather than the nature of the cause of action governs which statute of limitations applies.²¹

1. General Statute of Limitations – Six Years

The general statute of limitations is six years.²² This statute provides that, “A civil action, except one brought upon the judgment or decree of a court of record of the United States or of this or some other state, and except as otherwise provided, shall be commenced within six years after the cause of action accrues and not thereafter.”²³

Even though the general statute contains no explicit discovery rule, the court ruled in a case involving delayed discovery of asbestos fireproofing that a cause of action governed by the general statute “accrues” when plaintiff discovers the injury, or through reasonable diligence should have discovered the injury.²⁴

This general statute of limitations applies to all civil actions that are not covered by another specific statute. Claims against builders and architects for physical harm to real property are governed by this six-year statute of limitations.²⁵ Indemnity claims by contractors against designers resulting from defective flooring in condominiums are governed by the six-year statute of limitations.²⁶ Claims against engineers for a defective survey resulting in lost opportunities and diminution in value of real estate are governed by the six-year statute of limitations.²⁷

2. Statute of Limitations for Injuries to Persons or Personal Property – Three Years

The statute for injuries to the person, including emotional distress, and for damage to personal property runs three years from discovery of the injury.²⁸

An injury is “discovered” when the plaintiff knows or should have known both the fact of injury and the fact that it *may* have been caused by a *particular* defendant’s negligence or other breach of duty.²⁹ The case law requires no more than the discovery of facts sufficient to put a person of ordinary intelligence and prudence on inquiry which, if pursued, would lead to the discovery.³⁰

3. Death and Survival Claims – Two Years

Death and survival claims have a two-year statute, running from discovery of the death or from appointment of the representative, respectively.³¹

4. UCC Breach of Warranty Claims – Four Years

One exception to the “nature of the harm” rule is that a U.C.C. breach of warranty claim runs four years from “tender of delivery.”³²

5. Burden of Proof

The burden of pleading and proving that claim is barred by the statute of limitations rests on the party asserting the defense.³³

6. Which Statute of Limitations Applies?

A complaint may include claims for damage to both personal property and real estate, or may include UCC warranty claims among a number of legal theories. Which statute applies?

Sometimes the court dismisses claims for harm subject to a shorter period of limitations that has run, while permitting the suit to proceed on claims, such as claims for economic loss, that are within the longer general statute.³⁴ Other times the court looks to the “gravamen or essence” of the claim and decides whether the whole matter “predominantly or essentially relates” to the time-barred claim.³⁵

B. Statute of Repose

Vermont’s statutes of limitations can be indefinite because they generally run from discovery of the legal injury. In contrast, a “statute of repose” establishes a maximum length of time within which a plaintiff must commence suit, even if the cause of action is not discovered and not barred by any applicable statute of limitations.³⁶

Vermont’s only statute of repose relevant the construction industry places an outside time limit of twenty years from the last occurrence to which the injury is attributed. This statute applies in cases involving “noxious agents medically recognized as having a prolonged latent development.”³⁷ This might apply, for example, in a radon, formaldehyde or asbestos case.

Because of the long, twenty-year period the statute has been used or attempted to be used more by claimants than defendants.³⁸ Any usefulness of the statute to the defense is limited by an interpretation that the “last occurrence” can refer, not to the defendant’s last negligent act, but to a later triggering event.³⁹

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

To the extent Article 2 of the U.C.C. applies, Vermont requires that a buyer notify the seller of any alleged breach of warranty in order to provide the seller with an opportunity to cure. Once a buyer accepts tender, “The buyer must within a reasonable time after he discovers or

should have discovered any breach notify the seller of breach or be barred from any remedy.”⁴⁰ This notice requirement affords the seller the opportunity to cure the claimed defects or minimize the buyer’s losses.⁴¹ The right to cure has limits. The buyer is not bound to permit the seller to tinker with an item indefinitely and hope that it may ultimately be made to comply with the warranty. The timeliness of notice of a breach of contract is a question for the trier of fact.⁴² There is no specified time limit with regard to what constitutes “a reasonable time” as identified in the statute.

IV. INSURANCE COVERAGE AND ALLOCATION ISSUES

A. Trigger of Coverage

The Vermont Supreme Court has not considered the appropriate “trigger” of insurance coverage for construction defect claims. The court has, however, decided trigger issues in pollution and toxic tort cases.

Under the “continuous-trigger” theory coverage is triggered under all policies on the risk from the time of first exposure to the time the damage first becomes apparent.⁴³

The court adopted the “continuous-trigger” theory in a groundwater contamination case where a waste hauler had dumped waste over a period of fifteen years. Continuous exposure to contamination during the policy period was sufficient to trigger coverage under an old policy, though the contamination was not discovered until after the policy had expired. Because in this case environmental injury in fact occurred during the policy period the court left open whether exposure alone, without any actual injury, was a sufficient initial triggering event.⁴⁴

In an earlier case, the court implied that actual injury is necessary to support the “continuous-trigger” theory. Evidence that wastes had been spilled at the State prison during the 1940s and 1950s and that contamination was discovered in the 1990s was insufficient to trigger policies issued to the State in the 1960s and 1970s. The court said there must be evidence that the property damage was continuing or progressively deteriorating during the policy period.⁴⁵

Exposure alone, however, was sufficient to trigger defense obligations in a toxic tort case. Where claimants alleged they suffered serious increased health risks from exposure to urea formaldehyde in a home sold by defendant and that the formaldehyde insulation diminished the fair market value of their house, the court held these allegations were sufficient “bodily injury” and “property damage” to trigger defense obligation under the defendant’s homeowner’s policy.⁴⁶

B. Allocation

The problem of allocation arises in different contexts with, perhaps, different solutions. Different rules may apply where two or more insurers cover different risks or successive risks, than where two or more insurers cover concurrent risks. Rules that govern allocation among insurers may not necessarily apply where part of the risk is uninsured. If a party presents evidence showing some logical and fair basis for apportionment, the court may follow it.

The Vermont case law is sparse generally and nonexistent in cases involving construction defects or specialized contractors' liability policies. The comments that follow are general in nature.

Where "other insurance" clauses of insurance policies are mutually repugnant, each is deemed void and the rule is to prorate the loss between insurers.⁴⁷ Where "other insurance" clauses are not mutually repugnant but competing, Vermont courts will reconcile the clauses to give effect to the parties' intent as long as that reconciliation does not violate public policy or compromise coverage for the insured.⁴⁸ If policies provide for a consistent method of apportioning loss, the court will honor that method.⁴⁹

A recent Vermont case prorates the settlement amount and defense costs between concurrent insurers in proportion to limits, based both on the consistent terms of the "other insurance" clauses of the two policies, and the settled common law precedent.⁵⁰ In another case the court determined that one company's coverage was primary, and the other's was excess, based on language in one policy (omitted in the other) that said the policy was "excess over *any* other liability insurance available to *any* insured."⁵¹

In the environmental area, where a continuous trigger rule applies and exposure tends to span multiple policy periods, the court has apportioned defense and indemnity costs between an insurer and its insured who was uninsured for certain periods, based on the percentage of time spent on the risk.⁵² In another case, however, the court ruled it proper to allocate costs in proportion to the amount of gasoline that had leaked out of the insured's underground tanks in separate spills during the insurers' respective policy periods.⁵³

In a partial coverage situation, the court has not required an insurer to bear full indemnity costs where the insurer cannot prove what part of the verdict was based on uncovered claims.⁵⁴ Similarly the insurer must bear full defense costs, even though only part of the claim was covered, where the insurer cannot clearly distinguish the specific defense costs for non-covered claims from those costs necessarily incurred for covered claims.⁵⁵

V. CONTRACTUAL INDEMNITY

Contractual indemnity is a risk allocation device by which the parties to a contract apportion or shift responsibility for future third-party claims. Indemnity provisions in commercial transactions are routinely upheld by the Vermont Supreme Court. Vermont does not agree with those jurisdictions that say an indemnification clause cannot cover liability for the indemnitee's own negligence, or cannot cover such negligence unless it expressly so states.⁵⁶

Vermont law does not protect contractors from unfavorable terms in their contracts. Under Vermont law indemnity contracts are valid and enforceable according to their terms, so long as the meaning is clear. It is permissible for a commercial party to receive indemnification against its own negligent conduct, even if the contract does not expressly refer to negligence.⁵⁷ Further, it is no defense to indemnification under an express agreement that the indemnitee has breached the contract.⁵⁸ No Vermont statute restricts the enforceability of such indemnity provisions in construction contracts.

In one leading case the court enforced a broad indemnification clause against a contractor, despite the owner's negligence.⁵⁹ A security guard injured on a faulty stair while working as an employee of a contractor brought a negligence action against the owner of the facility where he was posted. The facility's owner brought a third-party action against the contractor, claiming that the contractor was required to indemnify it under their contract, even if the damaged stair was caused by the owner's own negligence. The contract at issue stated that the contractor, agreed to:

assume all risk of injury to persons, including himself, his employees and agents, and or damage to property in any manner resulting from or arising out of or in any manner connected with [the indemnitor's] operations hereunder, and [the indemnitor] agrees to indemnify and save [the indemnitee] harmless from any and all loss caused by or resulting from any such injury or damage.⁶⁰

The Court enforced the indemnity clause as written in recognition that parties to arms-length business deals will divide certain risks and responsibilities, and that an indemnification clause does no more than allocate the cost of purchasing insurance.⁶¹

VI. CONTINGENT PAYMENT AGREEMENTS

Contingent payment agreement in construction contracts are used in contracts between a general contractor and a subcontractor, and typically state that payment to the subcontractor will not be made until the general contractor is paid by the owner. They are commonly referred to as "pay-if-paid" or "pay-when-paid" clauses. In the absence of caselaw on the topic, arguments are available to both the general contractor looking to enforce the agreement and the subcontractor seeking to be relieved of its provisions.

Vermont's construction prompt payments law⁶² does not, on its face, rule out contingent payment agreements. Payments made by an owner to a contractor are held in a statutory "express trust" for payment of materials furnished or construction services rendered.⁶³ A subcontractor must be paid "the full or proportional amount received for [its] work and materials ..." within the later of seven days after receipt of each progress or final payment or seven days after receipt of the subcontractor's invoice.⁶⁴ This appears to imply that if a general contractor receives less than the full amount from the owner, the general contractor may pay the subcontractor the proportional amount that it received from the owner.

While there is no reported caselaw in Vermont construing contingent payment provisions, there is an argument that, if tested, they will be found to violate public policy. Since a "pay-if-paid" clause makes the subcontractor's right to payment contingent upon the uncertain event of payment to the general contractor by the owner; and, since a subcontractor cannot enforce its mechanic's lien until after the payments become due⁶⁵, a "pay-if-paid" clause would operate as a waiver of the subcontractor's rights to enforce its mechanic's lien. That result would conflict with the Vermont's Contractor's Lien statute, which prohibits waiver of mechanics' and material suppliers' lien rights and makes "any provision calling for such advance waiver unenforceable."⁶⁶

VII. DAMAGES LIMITATIONS

A. Personal Injury Damages vs. Construction Defect Damages

In a personal injury case recoverable damages include economic damages such as medical expenses and lost wages, as well as non-economic damages such as pain & suffering, that are not generally recoverable in a construction defect case. In construction defect cases, when loss in value to plaintiff cannot be calculated with sufficient certainty, the measure of damages is either the cost of repair or diminution in the market price of the property. If damages are to be measured by diminution in value of the property, and more than one contractor has committed a breach that affects that value, the diminution in value may be allocated to the contractors in relation to their impact on the diminution.⁶⁷ Also, see sections on consequential damages and economic loss doctrine.

B. Attorney's Fees Shifting and Limitations on Recovery

Generally, Vermont applies the "American rule" on attorneys' fees, which means that the parties must bear their own attorney's fees absent a statutory or contractual provision authorizing fee shifting. However, where a party to the action behaves in bad faith or with vexatious intent, the court may award attorneys' fees.⁶⁸

Vermont has enacted statutes that specifically apply to construction contracts. 9 V.S.A. §§ 4001 – 4009. 9 V.S.A. § 4007 creates an exception to the "American rule", providing that:

Notwithstanding any contrary agreement, the substantially prevailing party in any proceeding to recover any payment within the scope of this Chapter [construction contracts] shall be awarded reasonable attorney's fees in an amount to be determined by the court or arbitrator, together with expenses.

The statute provides that reimbursement of attorneys' fees are mandatory to a substantially prevailing party, but the question of whether any party to a lawsuit substantially prevailed is left to the trial court's discretion and does not flow automatically from the calculation of the net victor (as where the owner and contractor prevail on counterclaims against each other).⁶⁹

C. Consequential Damages

In a breach of contract case, there are two types of damages: direct damages and consequential damages.⁷⁰ Direct damages are damages that naturally and usually flow from the breach itself. Consequential damages must pass the test of causation, certainty, and foreseeability, and must have been in the contemplation of the parties at the time the parties entered into the contract.⁷¹

D. Delay and Disruption Damages

Unless the terms of a construction contract provide otherwise, when an owner's delay prevents a contractor from completing work called for by a construction contract, resulting in the contractor's termination of performance, a proper measure of the contractor's damages is contract price minus cost of completion and other costs avoided, plus damages incurred as a result of owner's delay.⁷²

E. Economic Loss Doctrine

Vermont follows the Economic Loss Doctrine which generally allows claims for purely economic losses only in contract actions, and not in tort actions. Purely economic losses are not recoverable in tort actions. Purely economic losses are recoverable under contract law.⁷³ "The underlying premise of the economic loss rule is that negligence actions are best suited for resolving claims involving unanticipated physical injury, particularly those arising out of an accident. Contract principles, on the other hand, are generally more appropriate for determining claims for consequential damage that the parties have, or could have, addressed in their agreement."⁷⁴

Vermont has not expressly recognized an exception to the Economic Loss Doctrine for claims related to the provision of "professional services." In one case, the Vermont Supreme Court acknowledged that other states recognize such an exception when the parties had a "special relationship" where one party undertakes a "special duty" distinct from contractual duties, but the Court found it unnecessary to decide in that case whether it would recognize the exception.⁷⁵ In another case, again without expressly deciding whether to adopt a professional services exception, the Court ruled that a construction contractor was not liable for negligent design or negligent construction because it held itself out as a contractor, not as a provider of specialized professional services, nor did the owner rely on the contractor as such.⁷⁶

F. Interest

Vermont's Prompt Pay Act⁷⁷ governs the interest recoverable for an overdue payment under a "construction contract," which the Act defines broadly as any agreement, whether written or oral, to perform work on any real property located within the state of Vermont."⁷⁸

If any progress or final payment to a contractor is delayed beyond the due date, whether set by statute or by the parties' agreement,⁷⁹ the owner must pay the contractor interest, beginning on the 21st day, at an interest rate equal to that established by the judgment lien statute,⁸⁰ which is 12 percent per annum, on such unpaid balance as may be due.⁸¹ The parties may agree to a different interest rate.⁸²

If any progress or final payment to a subcontractor is delayed beyond the due date, the contractor or subcontractor must pay its subcontractor interest, beginning on the next day, at the judgment lien interest rate, 12 percent per annum, on such unpaid balance as may be due. The parties may not agree to a different interest rate.⁸³

Improper withholding of retainage also subjects the withholder to 12 percent interest.⁸⁴

On claims not governed by the Prompt Pay Act, such as tort liability, prejudgment interest accrues at a rate of 12 percent per annum.⁸⁵

G. Punitive Damages

Punitive damages are compensable in Vermont only upon a showing of wrongful conduct that is outrageously reprehensible and malice.⁸⁶ Malice is defined variously as bad motive, ill will, personal spite or hatred, reckless disregard, and the like.⁸⁷ Punitive damages are generally not available in breach of contract actions. However, Vermont recognizes an exception to this general rule for cases in which the breach has the character of a willful and wanton or fraudulent tort, and when the evidence indicates that the breaching party acted with actual malice.⁸⁸ The purpose of punitive damages is to punish conduct that is "morally culpable" and "truly reprehensible", so the Vermont court has set a high bar for plaintiffs seeking such damages. Punitive damages are available only to punish and deter defendants who acted with actual malice.⁸⁹

¹ 9 V.S.A. § 1921 (a).

² See, e.g., *Piper v. Hoyt*, 61 Vt. 539, 17 A. 798, 798 (Vt. 1889) (requiring strict adherence because "the [statute] provides a special remedy in favor of a particular person . . .").

³ 9 V.S.A. § 1921(b).

⁴ 9 V.S.A. § 1921(c).

⁵ *Haigh Lumber Co. v. Drinkwine*, 130 Vt. 120, 287 A.2d 560 (1972); see 14 V.S.A. § 1922.

⁶ 9 V.S.A. § 1921(c).

⁷ 9 V.S.A. § 1921(c); 9 V.S.A. § 1923; see *Baldwin v. Spear Brothers*, 79 Vt. 43, 64 A. 235 (1906).

⁸ 9 V.S.A. § 1923.

⁹ *Id.*

¹⁰ 9 V.S.A. § 1924.

¹¹ 9 V.S.A. § 1925.

¹² *Naylor v. Cusson (In re Cusson)*, 412 B.R. 646 (D. Vt. 2009).

¹³ *Id.*; 9 V.S.A. § 1925.

¹⁴ *Id.*

¹⁵ 9 V.S.A. § 1921(f).

¹⁶ 9 V.S.A. § 1921(d).

¹⁷ *Id.*

¹⁸ *Id.*

¹⁹ *Clayton v. Unsworth*, 2010 VT 84, ¶ 26, 8 A.3d 1066.

²⁰ Vt. Stat. Ann. tit. 12, § 465 ("Except as otherwise provided by statute, any provision in a contract which limits the time in which an action may be brought under the contract or which waives the statute of limitations shall be null and void.").

²¹ E.g. *Eaton v. Prior*, 2012 Vt. 54, 192 Vt. 249, 58 A.3d 200 (2012); *Kinney v. Goodyear Tire & Rubber Co.* 134 Vt. 571, 367 A.2d 677 (1976) (not necessary to categorize strict product liability action as either tort or contract).

²² Vt. Stat. Ann. tit. 12, § 511.

²³ *Id.*

²⁴ *Univ. of Vermont v. W.R. Grace & Co.*, 152 Vt. 287, 290, 565 A.2d 1354, 1357 (1989).

²⁵ *Congdon v. Taggart Bros., Inc.*, 153 Vt. 324, 325, 571 A.2d 656, 657 (1989) (§ 511 governs action against builder for damages resulting from fire allegedly caused by negligent design and construction of building); *Union Sch. Dist. No. 20 v. Lench*, 134 Vt. 424, 425, 365 A.2d 508, 509 (1976) (§ 511 governs claim against architect for economic loss resulting from negligent repair of roof).

²⁶ *Inv. Props., Inc. v. Lyttle*, 169 Vt. 487, 739 A.2d 1222, 1228 (1999) (same limitation period applies to an indemnity action as would apply to the underlying action).

²⁷ *Bull v. Pinkham Eng'g Assocs. Inc.*, 170 Vt. 450, 455, 752 A.2d 26, 30-31 (2000) (§ 511 governs where the harm is economic loss, including lost profit and diminution of value of real property).

²⁸ Vt. Stat. Ann. tit. 12, § 512(4)-(5); *Politi v. Tyler*, 170 Vt. 428, 751 A.2d 788 (2000) (suit barred under three-year statute as to emotional distress claim).

²⁹ *Rodrigue v. VALCO Enters.*, 169 Vt. 539, 726 A.2d 61, 63 (1999) (mem.); *Earle v. State*, 170 Vt. 183, 193, 743 A.2d 1101, 1108 (1999).

³⁰ *Soutiere v. Betzdearborn, Inc.*, 189 F. Supp. 2d 183, 191 (D. Vt. 2002).

³¹ Vt. Stat. Ann., tit. 14, §§ 1492 & 1451.

³² Vt. Stat. Ann. tit. 9A, § 2-725 (1994); *Gus' Catering, Inc. v. Menusoft Sys.*, 171 Vt. 556, 762 A.2d 804 (2000) (software warranty claim was time barred four years after tender of delivery, notwithstanding argument that additional warranties arose during time when seller unsuccessfully attempted to fix problem); *Paquette v. Deere & Co.*, 168 Vt. 258, 260, 719 A.2d 410, 411-12 (1998); *Aube v. O'Brien*, 140 Vt. 1, 433 A.2d 298 (1981).

³³ V.R.C.P. 8(c) (statute of limitations is affirmative defense); *Bull v. Pinkham Eng'g Assocs. Inc.*, 170 Vt. 450, 456, 752 A.2d 26, 31 (2000) (defendant has burden of establishing statute-of-limitations defense).

³⁴ *Egri v. U.S. Airways, Inc.* 174 Vt. 443, 804 A.2d 766 (2002) (mem.) (three-year statute of limitation governs claim for emotional distress and six-year statute governs a claim for lost income and benefits resulting from single wrongful act); *Fitzgerald v. Congleton*, 155 Vt. 283, 288, 583 A.2d 595, 598 (1990) (claim for damages resulting from emotional distress is an "injury to the person" and must be commenced within three years after the cause of action accrues; whereas claim for economic losses do not constitute personal injuries and fall under the six-year limitations).

³⁵ *Lamell Lumber Corp. v. Newstress Int'l, Inc.*, 2007 VT 83, ¶ 12, 182 Vt. 282, 938 A.2d 1215 (where transaction contains elements of both sales and service, applicability of UCC four-year statute of limitations depends on whether transaction predominantly or essentially relates to goods or to services); *Rennie v. State*, 171 Vt. 584, 762 A.2d 1272 (2000) (claim barred under the three-year statute of limitations even though economic losses alleged, where "gravamen or essence" of the claim was physical and emotional harm).

³⁶ *Cavanaugh v. Abbott Labs.*, 145 Vt. 516, 528, 496 A.2d 154, 161-62 (1985).

³⁷ Vt. Stat. Ann. tit. 12, § 518(a).

³⁸ *Campbell v. Stafford*, 2011 VT 11 (mem.) (holding that cancer is not "noxious agent" that extends the statute of limitations to twenty years).

³⁹ *Cavanaugh*, 145 Vt. at 528-30, 496 A.2d at 162-63 (statute of repose did not bar DES case brought by a daughter who developed cancer 22 years after her pregnant mother injected the drug because the last occurrence to which the injury was attributed was the onset of menarche at puberty).

⁴⁰ 9A VSA § 2-607 (2006).

⁴¹ *Wilk Paving, Inc. v. Southworth-Milton, Inc.*, 162 Vt. 552, 649 A.2d 778 (1994).

⁴² *Agway, Inc. v. Teitscheib*, 144 Vt. 76, 472 A.2d 1250 (1984).

⁴³ *Morrisville Water & Light Dept. v. USF&G, CO.*, 775 F. Supp. 718, 730-731 (D. Vt. 1991) (outlining five different rules used by courts to determine if an "occurrence" was triggered during the policy period in cases involving exposure to toxic substances).

⁴⁴ *Towns v. N. Sec. Ins. Co.*, 2008 VT 98, 184 Vt. 322, 964 A.2d 1150.

⁴⁵ *State v. CNA Ins. Cos.*, 172 Vt. 318, 779 A.2d 662 (2001).

⁴⁶ *Am. Prot. Ins. Co. v. McMahan*, 151 Vt. 520, 522, 562 A.2d 462, 466 (1989).

⁴⁷ *Fireman's Fund Ins. Co. v. CNA Ins. Co.*, 2004 VT 93 ¶ 22 (citing *State Farm Mut. Auto Ins. Co. v. Powers*, 169 Vt. 230, 237, 732 A.2d 730, 735 (1999); *Champlain Cas. Co. v. Agency Rent-A-Car, Inc.*, 168 Vt. 91, 97-98, 716 A.2d 810, 814 (1998)).

⁴⁸ *Id.* at ¶ 23 (citing *Powers*, 169 Vt. at 235).

⁴⁹ *Champlain CAS. Co.*, 168 Vt. 91, 98 n.1., 716 A.2d 810, 814 (1998).

⁵⁰ *Hathaway v. Tucker*, 2010 VT 114.

⁵¹ *Fireman's Fund Ins. Co.*, 2004 VT 93 ¶ 21.

⁵² *Towns v. N. Sec. Ins. Co.*, 2008 VT 98.

⁵³ *Agency of Natural Res. v. Glens Falls Ins. Co.*, 169 Vt. 426, 736 A.2d 768 (1999).

⁵⁴ *Pharmacists Mut. Ins. Co. v. Myer*, 2010 VT 10, 993 A.2d 413.

⁵⁵ *City of Burlington v. Associated Elec. & Gas Ins. Servs., Ltd.*, 170 Vt. 358, 363, 751 A.2d 284, 292 (2000) (citing *Burlington Drug Co. v. Royal Globe Ins. Co.*, 616 F. Supp. 481, 483 (D. Vt. 1985) (where covered and non-covered claims cannot be so distinguished, the insurer will be liable for all fees expended) (affirming allocation of certain defense costs to the insured because they can "clearly be distinguished from the covered claims").

⁵⁶ *Southwick v. City of Rutland*, 2011 VT 53; *Hamelin v. Simpson Paper (Vermont) Co.*, 167 Vt. 17, 702 A.2d 86 (1997); *Furlon v. Haystack Mountain Ski Area, Inc.*, 136 Vt. 266, 269-70, 388 A.2d 403, 405 (1978). The court has stated, “[t]he issue in Vermont is not whether commercial parties may allocate liability among themselves, including indemnification of one party for its own negligence, but under what circumstances the agreement has to expressly disclose that fact.” *Stamp Tech, Inc. v. Lydall/Thermal Acoustical, Inc.*, 2009 VT 91, ¶ 22, 186 Vt. 369, 987 A.2d 292.

⁵⁷ The “most effective way” for parties to express an intention to release one party from liability flowing from that party’s own negligence is “to provide explicitly that claims based in negligence are included in the release.” *Colgan v. Agway, Inc.*, 150 Vt. 373, 376, 553 A.2d 143, 146 (1988). Nevertheless, Vermont agrees with the Restatement that parties need not incant specific words, provided they state their intention to protect the indemnitee against its own negligence in clear and unequivocal terms. *Provoncha v. Vermont Motocross Ass’n, Inc.*, 2009 VT 29, ¶ 13; *Restatement 3d of Torts: Apportionment of Liability*, § 22 comment f.

⁵⁸ In *Hart v. Amour*, 172 Vt. 588, 590, 776 A.2d 420, 424 (2001), a worker on leased commercial premises brought a negligence action against lessor for damages for severe injuries sustained in a fall from a loft storage area, through a suspended ceiling, to a floor below. Under the lease, the lessor was entitled to indemnification from the tenant, notwithstanding the tenant’s claim that the lessor breached the lease by failing to maintain the premises.

⁵⁹ *Hamelin*, 167 Vt. 17, 702 A.2d 86 (1997).

⁶⁰ *Id.* at 19.

⁶¹ *Id.* Cf. *Colgan*, 150 Vt. at 377, 553 A.2d at 146 (the court held that a waiver in the parties’ construction contract did not cover claims for the builder’s negligence. The exculpatory clause disclaimed all warranties and “any other obligations or liability on the part of the contractor” but did not make any specific reference to negligence or tort liability and therefore did not waive the owner’s ability to sue on a negligence theory when a wall of the storage facility collapsed.).

⁶² 9 V.S.A. § 4001-4009.

⁶³ 9 V.S.A. § 4005a.

⁶⁴ 9 V.S.A. § 4003(c).

⁶⁵ 9 V.S.A. § 1923.

⁶⁶ 12 V.S.A. § 1921(f).

⁶⁷ *Winey v. William E. Dailey, Inc.*, 161 Vt. 129, 636 A.2d 744 (1993).

⁶⁸ *Agway, Inc. v. Brooks*, 173 Vt. 259, 790 A.2d 438 (2001).

⁶⁹ *Fletcher Hill, Inc. v. Crosbie*, 178 Vt. 77, 872 A.2d 292 (2005).

⁷⁰ *Waterbury Feed Company, LLC v. O’Neil*, 2006 VT 126, 181 Vt. 535, 915 A.2d 759.

⁷¹ *Id.*

⁷² *McGee Constr. Co. v. Neshobe Dev.*, 156 Vt. 550, 594 A.2d 415 (1991); Restatement (Second) of Contracts § 347 (1981).

⁷³ *Hamill v. Pawtucket Mut. Ins. Co.*, 179 Vt. 250, 892 A.2d 226 (2005).

⁷⁴ *Springfield Hydroelectric Co. v. Copp*, 172 Vt. 311, 779 A.2d 67 (2001) (citations and quotations omitted); *Hunt Const. Grp., Inc. v. Brennan Beer Gorman/Architects, P.C.*, 607 F.3d 10 (2d Cir. 2010) (construing Vermont law).

⁷⁵ *Id.*

⁷⁶ *EBWS, LLC v. Britly Corp.*, 2007 VT 37, 181 Vt. 513, 928 A.2d 497.

⁷⁷ 9 V.S.A. §§ 4001 – 4007.

⁷⁸ 9 V.S.A. § 4001(5).

⁷⁹ 9 V.S.A. § 4002(c).

⁸⁰ 12 V.S.A. § 2903(c).

⁸¹ 9 V.S.A. § 4002(d).

⁸² *Id.*

⁸³ 9 V.S.A. § 4003(d).

⁸⁴ 9 V.S.A. § 4005(d).

⁸⁵ 9 V.S.A. § 41a.

⁸⁶ *Fly Fish Vt., Inc. v. Chapin Hill Estates, Inc.*, 2010 VT 33, ¶ 18, 187 Vt. 541, 996 A.2d 1167.

⁸⁷ *Id.*

⁸⁸ *Monahan v. GMAC Mortg. Corp.*, 2005 VT 110, 179 Vt. 167, 893 A.2d 298.

⁸⁹ *Id.*

VIRGINIA

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I. MECHANIC'S LIEN BASICS.

Portions of Virginia Code Title 43, as amended, govern mechanic's liens on private projects located in the Commonwealth of Virginia. Mechanic's liens provide a vehicle by which general contractors, subcontractors and certain suppliers can obtain a security interest in real property they improved, and ultimately compel the sale of the property in order to pay for the improvements they provided. A mechanic's lien is in derogation of the common law and the statutes dealing with the existence and perfection of a mechanic's lien are strictly construed.¹ The basic steps and rules governing perfection of a mechanic's lien are:

A. Requirements.

1. Memorandum of Mechanic's Lien.

Filing a "memorandum of mechanic's lien" is the first step a claimant must take to perfect its mechanic's lien. The memorandum is filed in the clerk's office in the county or city in which the building, structure or railroad, or any part thereof is located.² The memorandum must, at a minimum, include (1) the name and address of the owner and claimant, (2) type of materials furnished by the claimant, (3) amount of the claim, (4) type of structure upon which the work was performed, (5) brief description of the property, (6) date from which interest is claimed, (7) a statement declaring the claimant's intention to claim the benefit of the lien, (8) the name, if any, of the general contractor, and (9) the claimant's Virginia contractor license number, date of issuance and date of expiration.³

The content of the memorandum will differ depending on whether the claimant is the general contractor or a subcontractor/supplier for the project.⁴ Additionally, a lien claimant who is a general contractor must also file a certification of mailing of a copy of the memorandum of lien on the owner of the property at the owner's last known address with the memorandum.⁵

2. Affidavit.

The memorandum must be verified by the oath of the claimant or the claimant's authorized agent. The affidavit is filed along with the filing of the memorandum. The affidavit must be notarized.⁶

3. Notice to Owner.

Any lien claimant that is not a general contractor must provide written notice to the owner or the owner's agent of the amount and character of the lien claimant's claim.⁷

B. Enforcement.

A mechanic's lien may be enforced in a court of equity by a Complaint filed in the county or city wherein the building, structure, or railroad, or some part thereof is situated, or wherein the owner, or if there be more than one, any of them, resides.⁸ The lien claimant must file the Complaint within six (6) months of the filing date the memorandum, or after sixty days from the time the building, structure or railroad was completed or the work thereon otherwise terminated, whichever time shall last occur.⁹ Along with the Complaint, the lien claimant must file an itemized statement of his account, showing the amount and character of the work done or materials furnished, the prices charged therefor, the payments made, if any, the balance due, and the time from which interest is claimed thereon, the correctness of which account shall be verified by the affidavit of himself, or his agent.¹⁰ Absent an "issue out of chancery," the enforcement action is tried to a judge. In Virginia, the lien enforcement statutes are to be construed liberally while the perfection statutes are to be construed strictly.¹¹ Both perfection and enforcement must be timely for a claimant to recover under the mechanic's lien statutes.¹² An action to enforce a mechanic's lien must name all necessary parties with an interest in the lien action, to include the owner of the property, trustees and beneficiaries of deeds of trust, and any other lien holder, to exclude subsequently filed mechanic's liens.¹³ A claimant cannot amend its suit to add a necessary party after the 6-month limitation period has expired.¹⁴

C. Ability to Waive and Limitations on Lien Rights.

Any right to file or enforce a mechanic's lien may be waived in whole or in part at any time by any person entitled to such a lien.¹⁵ A waiver of a mechanic's lien must be express or, if it is implied, it must be established by clear and convincing evidence.¹⁶ In Virginia, the general rule is that any agreement to waive or release a mechanic's lien must be supported by consideration to be valid and binding.¹⁷

The memorandum for mechanic's lien shall be filed not later than 90 days from the last day of the month in which the claimant last performs labor or furnishes material, and in no event later than 90 days from the time the building, structure, or railroad is completed, or the work thereon otherwise terminated.¹⁸ The memorandum cannot include sums due for labor or materials furnished more than 150 days prior to the last day on which labor was performed or material furnished to the job preceding the filing of such memorandum (unless those amounts are for retainage).¹⁹ Including any amounts due for labor or materials provided prior to this 150-day period invalidates the entire lien.²⁰ Claimants can file "any number of [lien] memoranda" to guard against falling violating the 150 day rule.²¹

D. Note for Public Projects.

On a public project, there should be a payment bond in place for the protection of the subcontractors.²² Public projects are not subject to mechanic's liens.

II. STATUTES OF LIMITATION AND REPOSE

A. Statutes of Limitation and Limitations on Applicable Statutes.

1. Actions Concerning Contracts.

In Virginia, the limitations period for any action based on contract is governed by Va. Code Ann. § 8.01-246.²³ An action brought on an oral/parol contract or for unjust enrichment must be brought within three years from the date the right of action accrues.²⁴ An action brought on a written contract signed by the party against whom the plaintiff seeks to enforce the contract must be brought within five years of the date the right of action accrued.²⁵

2. Uniform Commercial Code.

If the action is for breach of a contract for the sale of goods, the four year Uniform Commercial Code limitations period set forth in Va. Code Ann § 8.2-725 applies by pursuant to the language of Va. Code Ann. § 8.01-246.

3. Personal Injury.

Any action for personal injury or wrongful death must be brought within two years after the cause of action accrues.²⁶

4. Damage to Property.

An action for damage to personal property must be brought within five years of the date the cause of action accrues.²⁷

6. Fraud.

Actions for damages due to fraud or mistake, and actions for rescission of a contract due to undue influence begin to accrue from the date of discovery by the plaintiff. The applicable limitations period is two years.²⁸

7. Discovery of Injury.

Pursuant to Va. Code Ann. § 8.02-243(C)(2), if fraud, concealment or intentional misrepresentation prevented discovery of the injury within the two-year limitation period, the plaintiff may bring an action within one year from the date the injury is discovered or by the exercise of due diligence, should have been discovered.

8. The Date the Limitations Period Begins.

The limitations period begins to run when the cause of action accrues.²⁹ Pursuant to Va Code Ann. §8.01-230 accrual of a cause of action takes place when an injury is sustained in a personal injury, property damage context; or from the breach in a contract action. Pursuant to Va. Code Ann. §8.01-229(D) if a defendant obstructs the plaintiff's ability to file an action, the applicable limitations period shall be tolled for the time period the obstruction existed.³⁰

B. Statutes of Repose and Limitations on Application of Statutes.

1. Damages Related to Defective or Unsafe Improvements to Real Property.

Pursuant to Va. Code Ann. §8.01-250, a five year statute of repose applies to actions for injuries to real or personal property, personal injury or wrongful death arising out to the defective and unsafe condition of an improvement to real property brought against persons performing or furnishing the design, surveying, or construction of such improvement.

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

Virginia Code Section 55-70.1, as amended, governs the statutory rights and obligations of a vendor and vendee for a new residence. Before a claim for breach of statutory warranty(ies) may be brought the vendor is entitled to written notice of the claim, and is given an "reasonable" period of time, not to exceed six months, to cure the alleged defect.³¹

A. The Warranty.

The warranty applies only to the sale of a new dwelling as defined in the statute.³² In such contracts, the vendor warrants to the vendee that, at the time of the transfer of record title or the vendee's taking possession, whichever occurs first, the dwelling with all its fixtures is, to the best of the actual knowledge of the vendor or his agents, sufficiently (i) free from structural defects, so as to pass without objection in the trade, and (ii) constructed in a workmanlike manner, so as to pass without objection in the trade.³³ A vendor that is in the business of building or selling such dwellings also warrants to the vendee that, at the time of transfer of record title or the vendee's taking possession, whichever occurs first, the dwelling is fit for habitation.³⁴

The warranties are held to survive the transfer of title.³⁵ The warranties are in addition to any other express or implied warranties pertaining to the dwelling, its materials or fixtures.³⁶

B. Waiver of Warranty.

A contract for sale may waive, modify or exclude any or all express and implied warranties and sell a new home "as is" only if the words used to waive, modify or exclude such warranties are conspicuous as defined by statute, set forth on the face of such contract in capital letters which are at least two points larger than the other type in the contract and only if the words used to waive, modify or exclude the warranties state with specificity the warranty or warranties that are being waived, modified or excluded.³⁷ If all warranties are waived or excluded, a contract must

specifically set forth in capital letters which are at least two points larger than the other type in the contract that the dwelling is being sold "as is".³⁸

C. Notice.

Virginia requires a homeowner seeking damages against the vendor to first provide the vendor with written notice of an alleged defect.³⁹ For any defect discovered after July 1, 2002, the vendee shall first provide the vendor, by registered or certified mail at the vendor's last known address, or by hand delivery, a written notice stating the nature of the warranty claim.⁴⁰ After such notice, the vendor shall have a reasonable period of time, not to exceed six months, to cure the defect that is the subject of the warranty claim.⁴¹

D. Deadlines.

If there is a breach of the statutory warranty, the vendee, or his heirs or personal representatives in case of his death, shall have a cause of action against the vendor for damages.⁴² The warranty extends for a period of one year from the date of transfer of record title or the vendee's taking possession, whichever occurs first.⁴³ The warranty for the foundation of new dwellings extends for a period of five years from the date of transfer of record title or the vendee's taking possession, whichever occurs first.⁴⁴

A homeowner's claim for breach of the statute must be brought within two (2) years after the breach.⁴⁵ For all warranty claims arising after January 1, 2009, sending the written notice required by the statute tolls the limitations period for six months.⁴⁶

IV. INSURANCE COVERAGE AND ALLOCATION ISSUES

A. General Coverage Issues.

Virginia courts remain relatively conservative in interpreting the applicability of commercial general liability (CGL) insurance policies to claims for defective construction work. In general terms, Virginia courts adhere to the approach that personal injury or damage to property other than the insured's work is covered by the CGL policy, but that the performance of faulty work, in and of itself, is not covered. Beyond these general concepts, there are a number of issues that arise, some of which have been resolved by Virginia courts, and some of which remain open for debate.

B. Trigger of Coverage.

What approach do Virginia courts apply to determine what liability policy or policies have been "triggered?" There is no clear answer to this question under Virginia law in terms of construction defect claims. One federal district court in Virginia has recently predicted that Virginia's Supreme Court would likely follow the "sensible general rule . . . that `coverage is triggered at the time of an injury-in-fact and continuously thereafter to allow coverage under all policies in effect from the time of injury-in-fact during the progressive damage.'"⁴⁷

1. Does defective work of the insured, without other damage, amount to covered “property damage?”

Again, this is an issue that has not been directly addressed by the Supreme Court of Virginia. One federal district court that has examined it in Virginia has concluded that such defective work would not alone amount to “property damage” because it has not been constructed properly originally.⁴⁸

2. Is defective construction work considered to be an “occurrence” under Virginia law?

Though this issue has not been directly addressed by the Supreme Court of Virginia, most of the federal and state circuit courts that have addressed this issue have concluded, in general, that poor workmanship or defective performance under a contract is not an “occurrence” and is thus not covered by a CGL policy.⁴⁹

3. Does the “your work” exclusion of the standard CGL policy determine whether there is coverage for defective construction?

When the damage at issue comes within the definition of “your work” under the CGL policy, a Virginia court is likely to apply that language to find against coverage.⁵⁰

4. What about the existence of the “subcontractor” exception to the “your work” exclusions – does that modify the result under Virginia law?

The two courts in Virginia that have directly addressed this issue have concluded that, if coverage did not exist in the “insuring agreement” of the policy, then the “subcontractor” exception to the “your work” exclusion did not grant or extend coverage.⁵¹

V. CONTRACTUAL INDEMNIFICATION

By statute, there is some limitation on the ability to obtain or provide indemnification under construction-related contract in Virginia. Under Virginia Code Section 11-4.1, any provision in a construction contract that would indemnify a party to the contract for personal injury or damage to property “caused by or resulting solely from the negligence of such other party or his agents or employees, is against public policy and is void and unenforceable.” The Supreme Court of Virginia has applied this prohibition when the contractual language at issue obligated the indemnitor to indemnify the indemnitee whether or not the claim was based upon the negligence of the indemnitor.⁵²

In full, this statute provides as follows:

11-4.1. Certain indemnification provisions in construction contracts declared void.

Any provision contained in any contract relating to the construction, alteration, repair or maintenance of a building, structure or appurtenance thereto, including moving, demolition and excavation connected therewith, or any provision contained in any contract relating to the construction of projects other than buildings by which the contractor performing such work purports to indemnify or hold harmless another party to the contract against liability for damage arising out of bodily injury to persons or damage to property suffered in the course of performance of the contract, caused by or resulting solely from the negligence of such other party or his agents or employees, is against public policy and is void and unenforceable. This section applies to such contracts between contractors and any public body, as defined in § 2.2-4301.

This section shall not affect the validity of any insurance contract, workers' compensation, or any agreement issued by an admitted insurer.

This same limitation applies to contracts involving the “planning or design” for a construction project, as follows:

11-4.4. Certain indemnification provisions in contracts with design professionals declared void.

Any provision contained in any contract relating to the planning or design of a building, structure or appurtenance thereto, including moving, demolition or excavation connected therewith, or any provision contained in any contract relating to the planning or design of construction projects other than buildings by which the architect or professional engineer performing such work purports to indemnify or hold harmless another party to the contract against liability for damage arising out of bodily injury to persons or damage to property suffered in the course of the performance of the contract, caused by or resulting solely from the negligence of such other party, his agents or employees, is against public policy and is void and unenforceable.

This section shall apply to such contracts between an architect or professional engineer and any public body as defined in § 2.2-4301. Every provision contained in a contract between an architect or professional engineer and a public body relating to the planning or design of a building, structure or appurtenance thereto, including moving, demolition or excavation connected therewith, or relating to the planning or design of construction projects other than buildings by which the architect or professional engineer performing such work purports to indemnify or hold harmless the public body against liability is against public policy and is void and unenforceable. This section shall not be construed to alter or affect any provision in such a contract that purports to indemnify or hold

harmless the public body against liability for damage arising out of the negligent acts, errors or omissions, recklessness or intentionally wrongful conduct of the architect or professional engineer in performance of the contract.

This section shall not affect the validity of any insurance contract, workers' compensation, or any agreement issued by an admitted insurer.

Any other contractual indemnification provision should be enforceable under Virginia law and the cause of action for it would accrue pursuant Virginia Code Section 8.01-249(5), which provides that:

5. In actions for contribution or for indemnification, when the contributee or the indemnitee has paid or discharged the obligation. A third-party claim permitted by subsection A of § 8.01-281 and the Rules of Court may be asserted before such cause of action is deemed to accrue hereunder

In terms of indemnification for personal injury or property damage, attention should also be given to Virginia's statute of repose, Virginia Code Section 8.01-250.

VI. CONTINGENT PAYMENT AGREEMENTS

A. Enforceability.

Virginia courts have recognized and enforced "pay-if-paid" clauses and "pay-when-paid" clauses in construction contracts. A clause that addresses the timing of payment is a pay-when-paid clause.⁵³ A pay-when-paid clause does not shift the risk of non-payment to the subcontractor. However, if a clause unequivocally states that payment by the owner to the contractor is a condition precedent of payment by the contractor to the subcontractor, it is an enforceable pay-if-paid clause.⁵⁴

B. Requirements.

Virginia courts will enforce pay-if-paid and pay-when-paid clauses that unambiguously express the intent of the parties.⁵⁵ However, Virginia courts will not enforce a pay-when-paid or pay-if-paid clauses that are ambiguous in meaning or intent.⁵⁶

VII. DAMAGES LIMITATIONS

A. Attorneys' Fees Shifting and Limitations on Recovery.

In Virginia a prevailing party may recover its attorney's fees from the losing party only when such fees are fixed by statute.⁵⁷ Under exceptional circumstances, attorney's fees may be awarded to the prevailing party in certain equitable suits.⁵⁸ In a construction dispute, attorney's fees are not ordinarily recoverable.⁵⁹ The parties may contractually agree that should a dispute arise, the losing party will be obligated to pay the prevailing party's attorney's fee.

B. Consequential Damages.

Consequential damages are defined as, “Such damage, loss or injury as does not flow directly and immediately from the act of the party, but only from some of the consequences or results of such act.”⁶⁰ In a tort action, consequential damages are recoverable if the consequential injury is proximately caused by the defendant’s tortious conduct.⁶¹ In a contract action, consequential damages are recoverable if the circumstances leading to the injury were contemplated by the parties at the time of contracting.⁶²

C. Delay and Disruption Damages.

Unless contractually limited or waived, a contractor may recover damages for delay or disruption in performance, provided that the delay and/or disruption was not caused by the contractor.⁶³ The Supreme Court of Virginia has held that “[w]hen a breach by one party imposes a delay on the ability of the other party to perform its obligations under a contract, ‘the damages are to be measured by the direct cost of all labor and material . . . plus fair and reasonable overhead expenses properly chargeable . . . during the reasonable time required’ to complete performance”.⁶⁴ The Eichleay formula is an approved method (not the exclusive method) for calculating unabsorbed overhead damages in Virginia Construction disputes where the plaintiff seeks delay damages.⁶⁵

D. Economic Loss Doctrine.

Virginia recognizes the Economic Loss doctrine, which provides that an injured party cannot sue in tort on a cause of action arising from the breach of a duty imposed by contract unless privity of contract exists between the defendant and the plaintiff.⁶⁶ A party cannot sue in tort for damages which are purely economic in nature, i.e. disappointed economic expectations.⁶⁷ Virginia courts have held economic losses to include diminution in value, cost of repair and replacement, as well as lost profits and income.⁶⁸

E. Interest.

It is well settled Virginia law that parties may contract for interest to be payable in an agreement for the payment of money.⁶⁹ The Virginia Supreme Court has held when there is no express contract to pay interest; there is an implied contract to do so.⁷⁰ Where one has use of another’s money, he must pay interest upon the sum held from the date he receives it until the date he repays it.⁷¹ The parties to an agreement may contractually agree that interest on a debt is not recoverable.⁷² Pursuant to Va. Code Ann. § 8.01-382, a Court may include pre and/or post-judgment interest in its verdict. If no date is set by the verdict, interest on a judgement will begin to accrue from the date of the judgment.⁷³

Va. Code Ann. § 6.2-302 sets the judgement rate of interest at six percent (6 %) per annum, or the rate of interest specified in the parties agreement if the interest is charged pursuant to a valid contract.⁷⁴ If the parties have not contractually agreed to the rate of interest, the court shall apply a rate of six percent (6%) per annum to any pre and/or post-judgment interest awarded.⁷⁵ Interest cannot be collected on costs expended in litigation.⁷⁶ The contractual rate of interest cannot exceed twelve percent (12%) per annum, with limited exceptions.⁷⁷

F. Punitive Damages.

Punitive damages may be recovered in tort actions, when the tort is committed under aggravation circumstances.⁷⁸ Generally, Punitive damages may not be recovered in actions for breach of contract.⁷⁹ However, in certain cases where the breach is so malicious it amounts to an independent tort, punitive damages are recoverable if the plaintiff alleges malice, wantonness or oppression.⁸⁰

VII. CASE LAW AND LEGISLATION UPDATE

A. Important Mechanic's Lien Case.

The Supreme Court of Virginia recently issued an opinion in the matter of *Glasser and Glasser, PLC, v. Jack Bays, Inc.*, et al. In its opinion, the Court considered the validity of several mechanic's liens filed under Virginia Code §43-4. The Court's opinion addressed a number of issues common to most mechanic's lien enforcement actions. This is the most comprehensive opinion concerning the application of the Virginia mechanic's lien statutes.

This case arose out of a church construction project in Woodbridge, Virginia. Jack Bays, Inc. ("Jack Bays") was the general contractor for the project. Jack Bays hired a number of subcontractors to complete trade work. The project owner obtained financing from a number of lenders. The appellant, Glasser & Glasser, PLC ("Glasser & Glasser"), was listed on the deed of trust as a "Lender," and was also designated as a "Trustee" for "First Mortgage Bond Holders, 2006 Series."

As is the story in many failed projects that result in mechanic's lien claims, when the owner exhausted all funding for the project, the owner stopped paying Jack Bays. The owner attempted, but ultimately failed, to obtain additional financing for the project. Jack Bays ceased work on the project on September 28, 2007. At that time, Jack Bays sent a memorandum to its subcontractors directing them to immediately cease work and begin demobilization. Although Jack Bays began demobilization in late September 2007, several subcontractors continued work in October 2007.

On December 28, 2007, Jack Bays recorded a mechanic's lien against the property. Subcontractors recorded mechanic's liens from December 20, 2007 through January 29, 2008. All lien claimants timely filed suits to enforce their respective mechanic's liens. The parties tried the consolidated lien enforcement actions before a Commissioner in Chancery. The Commissioner filed a report with the Circuit Court wherein he concluded that Jack Bays and the subcontractors complied with the perfection and enforcement provisions of the Mechanic's Lien Act, and that these mechanic's liens took priority over the lenders' liens. Glasser & Glasser filed exceptions to the Commissioner's report. The Circuit Court issued a letter opinion and final order adopting the Commissioner's findings and conclusions and ordered that the property be sold at auction. Glasser & Glasser appealed to the Supreme Court of Virginia, raising fourteen assignments of error.

In its opinion, the Supreme Court of Virginia addressed a multitude of issues, including:

- A. Whether the lien claimants named all necessary parties (specifically, whether the claimants failure to specifically name the individual bondholders was fatal to their claims);
- B. The application of the ninety-day rule (use of the “last day of the month” vs. “otherwise terminated”);
- C. The application of the 150-day rule;
- D. Whether the 150-day rule sets a unitary date range for all contractors;
- E. The propriety of the September 28, 2007 end date;
- F. The propriety of fees included in Jack Bays’ lien;
- G. Jack Bays’ duty to mitigate its damages;
- H. Whether the subcontractors’ liens were timely filed;
- I. The priority of the mechanic’s liens over a lien secured by a deed of trust recorded after Jack Bays began its work on the project (applying Virginia Code §§ 43-21 and 43-23); and
- J. Whether the Circuit Court should have ordered the sale of the entire parcel.

The Supreme Court of Virginia affirmed the Circuit Court on all of these issues, except the sale of the land. The Supreme Court of Virginia upheld the mechanic’s liens claimed by Jack Bays and its subcontractors, and gave those liens priority over the lenders’ liens. The Supreme Court of Virginia Court remanded the case to the Circuit Court for a determination of what portion of the property is necessary for the use and enjoyment of the land.

This opinion presents an interesting and fact specific application of the ninety-day rule, the 150-day rule, and the lien priority provisions of Virginia Code Ann. § 43-3.

¹ See *American Std. Homes Corp. v. Reinecke*, 245 Va. 111, 4245 S.E.2d 515 (1993).

² Va. Code Ann. § 43-4.

³ Va. Code Ann. §§ 43-4, 43-5, 43-8 and 43-10 (2014).

⁴ Va. Code Ann. §§ 43-4, 43-5, 43-7, 43-8, 43-9, and 43-10 (2014).

⁵ Va. Code Ann. §§ 43-4 and 43-5 (2014).

⁶ Va. Code Ann. §§ 43-4, 43-5, 43-7, 43-8, 43-9, and 43-10 (2014).

⁷ Va. Code Ann. §§ 43-7, 43-8, 43-9, and 43-10 (2014).

⁸ Va. Code Ann. § 43-22 (2014).

⁹ Va. Code Ann. § 43-17 (2014).

¹⁰ Va. Code Ann. § 43-22 (2014).

¹¹ See *American Std. Homes Corp. v. Reinecke*, 245 Va. 111, 4245 S.E.2d 515 (1993).

¹² See *Donohoe Constr. Co. v. Mount Vernon Assocs.*, 235 Va. 531, 369 S.E.2d 857 (1988).

¹³ See *Ads. Constr., Inc. v. Bacon Cosntr., Co.*, 2102 Va. Cir. LEXIS 89 (Loudon County, October 18, 2012).
See also *Monk v. Exposition Deepwater Pier Corp.*, 111 Va. 121 68 S.E. 280 (1910).

¹⁴ See *Ads. Constr., Inc. v. Bacon Cosntr., Co.*, 2102 Va. Cir. LEXIS 89 (Loudon County, October 18, 2012). See also *Johnson Controls v. Norair Eng'g Corp.*, 2013 Va. Circ. LEXIS 3 (Fairfax County, January 10, 2013). See also *Walt Robins, Inc. v. Damon Corp.*, 232 Va. 43, 348 S.E.2d 223 (1986).

¹⁵ Va. Code Ann. § 43-3(C) (2014).

¹⁶ See *First Am. Bank v. J.S.C. Concrete Constr., Inc.*, 259 Va. 60, 523 S.E.2d 496 (2000).

¹⁷ See *United Masonry, Inc. v. Riggs Nat'l Bank*, 233 Va. 476, 357 S.E.2d 509 (1987).

¹⁸ Va. Code Ann. § 43-4 (2014).

¹⁹ *Id.*

²⁰ See *Carolina Builders Corp. v. Cenit Equity Co.*, 257 Va. 405 512 S.E.2d 550 (1999).

²¹ Va. Code Ann. § 43-3 (2014). See also *Carolina Builders Corp. v. Cenit Equity Co.*, 257 Va. 405 512 S.E.2d 550 (1999).

²² Va. Code Ann. § 2.2-4337 (2014).

²³ See Michie's Jurisprudence of Virginia and West Virginia, LIMITATION OF ACTIONS, § 13.

²⁴ Va. Code Ann. § 8.01-246 (2014); *Liberty Savings Bank v. Otterview Land Co.*, 96 Va. 352, 31 S.E. 511 (1898).

²⁵ Va. Code Ann. § 8.01-246 (2014).

²⁶ Va. Code Ann. §§ 8.01-243 and 244 (2014).

²⁷ Va. Code Ann. § 8.01-243(B) (2014).

²⁸ Va. Code Ann. § 8.01-248 (2014). See *STB Mktg. Corp. v. Zolfaghari*, 240 Va. 140, 393 S.E.2d 394 (1990); *Parker-Smith v. Sto Corp.*, 262 Va. 432, 551 S.E.2d 615 (2001).

²⁹ See Michie's Jurisprudence of Virginia and West Virginia, LIMITATION OF ACTIONS, § 23.

³⁰ See *Grimes v. Suzukawa*, 262 Va. 330, 551 S.E.2d 644 (2001).

³¹ Va. Code Ann. § 55-70.1 (D) (2014).

³² Va. Code Ann. § 55-70.1 (E) (2014).

³³ Va. Code Ann. § 55-70.1 (A) (2014).

³⁴ Va. Code Ann. § 55-70.1 (B) (2014).

³⁵ Va. Code Ann. § 55-70.1 (C) (2014).

³⁶ *Id.*

³⁷ *Id.*

³⁸ *Id.*

³⁹ Va. Code Ann. § 55-70.1 (D) (2014).

⁴⁰ *Id.*

⁴¹ *Id.*

⁴² *Id.*

⁴³ Va. Code Ann. § 55-70.1 (E) (2014).

⁴⁴ *Id.*

⁴⁵ *Id.*

⁴⁶ *Id.*

⁴⁷ See *Morrow Corp. v. Harleysville Mutual Ins. Co.*, 101 F. Supp.2d 422, 428 (E.D. Va. 2000) (citing *Spartan Petroleum v. Federated Mut. Ins. Co.*, 162 F.3d 805, 8080 (4th Cir. 1998) (applying South Carolina law)).

⁴⁸ See *Travelers Indemnity Co of America v. Miller Bldg. Corp.*, 2003 WL 23512080, 2003 U.S. Dist. LEXIS 24300 (E.D. Va. 2003), *rev'd on other grounds*, 142 Fed. Appx. 147, 2005 WL 1690552 (4th Cir. 2005) (unpublished).

⁴⁹ See, e.g., *Miller Bldg. Corp.*, *supra*, 142 Fed. Appx. 147, 2005 WL 1690552 (4th Cir. 2005) (unpublished); *Hotel Roanoke v. Cincinnati Ins. Co.*, 303 F. Supp. 2d 784 (W.D. Va. 2004); *Pulte Home Corp. v. Fidelity & Guar. Ins. Co.*, 80 Va. Cir. 160, 2004 Va. Cir. LEXIS 381, 2004 WL 516216 (Fairfax County Cir. Ct. 2004).

⁵⁰ See, e.g., *Nationwide Mut. Ins. Co. v. Wenger*, 222 Va. 263, 278 S.E.2d 874 (1981).

⁵¹ See, *Miller Bldg. Corp.*, *supra*, 142 Fed. Appx. 147, 2005 WL 1690552 (4th Cir. 2005) (unpublished); *RML Corp. v. Assurance Co. of Am.*, 60 Va. Cir. 269, 2002 Va. Cir. LEXIS 392 (Cir. Ct. City of Norfolk 2002).

⁵² See *Uniwest Constr., Inc. v. Amtech Elevator Servs.*, 280 Va. 428, 669 S.E.2d 233, 2010 Va. LEXIS 234 (2010).

53 *See Galloway Corp. v. S.B. Ballard Constr. Co.*, 259 Va. 493, 464 S.E.2d 349 (1995).

54 *See Id.*

55 *See Universal Concrete Prods. Corp. v. Turner Constr. Co.*, 595 F.3d 527 (4th Cir. 2010) (*citing Galloway Corp. v. S.B. Ballard Constr. Co.*, 259 Va. 493, 464 S.E.2d 349 (1995)).

56 *See Id.*

57 *See Wallace Process Piping Co. v. Martin-Marietta Corp.*, 251 F. Supp. 411 (ED Va. 1954)

58 *See Id.* (*citing Vaughan v. Atkinson*, 369 U.S. 527, 82 S. Ct. 997, 8 L. Ed. 2d 88 (1962); *Bell v. School Board of Powhatan County, Virginia*, 321 F.2d 494 (4th Cir. 1963); *Rolax v. Atlantic Coast Line R. Co.*, 186 F.2d 473 (4th Cir. 1951)).

59 *See Michie's Jurisprudence of Virginia and West Virginia*, BUILDING CONTRACTS, § 30.

60 *Richmond Redevelopment and Housing Authority v. Laburnum Construction Corporation* 195 Va. 827, 836; 80 S.E.2d 574, 580 (1954) (*citing Black's Law Dictionary*, 3rd ed.)

61 *See Michie's Jurisprudence of Virginia and West Virginia*, DAMAGES, § 11.

62 *See Michie's Jurisprudence of Virginia and West Virginia*, DAMAGES, § 12 (*citing Roanoke Hosp. Ass'n v. Doyle & Russell, Inc.*, 215 Va. 796, 214 S.E.2d 155 (1975)).

63 *See Fairfax County Redevelopment & Hous. Auth. v. Worcester Bros. Co.*, 257 Va. 382, 514 S.E.2d 147 (1999).

64 *Id.* at 388, 514 S.E.2d 147 at 151 (*quoting E.I. duPont de Nemours & Co. v. Universal Moulded Prod.*, 191 Va. 525, 581, 62 S.E.2d 233, 259 (1950)).

65 *See Id.*

66 *See Sensenbrenner v. Rust, Orling & Neale, Architects, Inc.*, 236 Va. 419, 374 S.E.2d 55 (1988).

67 *See Id.*

68 *See Id.*

69 *See McVeigh v. Howard*, 87 Va. 599, 13 S.E. 31 (1891).

70 *See Michie's Jurisprudence of Virginia and West Virginia*, Interest, § 4 (*citing Roberts v. Cocke*, 69 Va. (28 Gratt.) 207 (1877); *Cecil v. Deyerle*, 69 Va. (28 Gratt.) 775 (1877); *Kent v. Kent*, 69 Va. (28 Gratt.) 840 (1877); *Cecil v. Hicks*, 70 Va. (29 Gratt.) 1 (1877); *McVeigh v. Howard*, 87 Va. 599, 13 S.E. 31 (1891); *Bennett v. Federal Coal & Coke Co.*, 70 W. Va. 456, 74 S.E. 418 (1912); and *Chapman v. Shepherd*, 65 Va. (24 Gratt.) 377 (1874)).

71 *See Michie's Jurisprudence of Virginia and West Virginia*, Interest, § 5 (*citing Craufurd v. Smith*, 93 Va. 623, 23 S.E. 235 (1896); *Southern Ry. Co. v. Glenn*, 102 Va. 529, 46 S.E. 776 (1904); *Vashon v. Barrett*, 105 Va. 490, 54 S.E. 705 (1906); *Lee v. Laprade*, 106 Va. 594, 56 S.E. 719 (1907); *Hall v. Graham*, 112 Va. 560, 72 S.E. 105 (1911)).

72 *See Id.*

73 *See Michie's Jurisprudence of Virginia and West Virginia*, Interest, § 6 (*citing Tazewell v. Saunders*, 54 Va. (13 Gratt.) 354 (1856); *Fry v. Leslie*, 87 Va. 269, 12 S.E. 671 (1891)).

74 Va. Code Ann. § 6.2-302 (2014).

75 *Id.*

76 *See Michie's Jurisprudence of Virginia and West Virginia*, Interest, § 4 (*citing Scott v. Doughty*, 130 Va. 523, 107 S.E. 729 (1921)).

77 Va. Code Ann. § 6.2-303 (2014).

78 *See Michie's Jurisprudence of Virginia and West Virginia*, Damages, § 65; *Giant of Va., Inc. v. Pigg*, 207 Va. 679, 152 S.E.2d 271 (1967).

79 *See Michie's Jurisprudence of Virginia and West Virginia*, Damages, § 65; *Norfolk & W.R. Co. v. Wysor*, 82 Va. 250 (1886).

80 *See Goodstein v. Weinberg*, 219 Va. 105, 245 S.E.2d 140 (1978); *Kamlar Corp. v. Haley*, 224 Va. 699, 299 S.E.2d 514 (1983).

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I. MECHANIC'S LIEN BASICS

RCW 60.04 creates a lien upon property in favor of those who provide labor and materials on the property, when the labor and materials were provided at the request of the property owner or his/her agent. These "mechanic's" or "materialmen's" liens are typically enforced against real property, but, in some cases, may be enforced against specific personal property.

In Washington, mechanic's and materialmen's liens are entirely statutory. Because the statutes are in derogation of the common law, they are strictly construed.

The procedure necessary to enforce a lien is detailed; therefore, a complete review of the code must be completed before proceeding with a claim under a mechanics' lien. The necessity of exact as opposed to substantial compliance with the verification and authentication requirements was recently affirmed in *Williams v. Athletic Field, Inc.*, 155 Wn. App. 434; 228 P.3d 1297, rev. granted, 169 Wn.2d 1021 (2010). On appeal to the Washington Supreme Court, these exacting standards were ameliorated somewhat. The Supreme Court of Washington disagreed and held that a claim of lien in the sample form was valid despite the absence of a proper acknowledgment. In this unique instance, given that both parties reasonably interpreted the ambiguous acknowledgment requirement in Wash. Rev. Code § 60.04.091(2), it was inequitable for one party alone to bear the costly burden of this litigation. In the interest of justice, the court declined to award attorney fees to either party for the trial or appellate proceedings. *Williams v. Athletic Field, Inc.*, 172 Wn.2d 683; 261 P.3d 109 (2011).

Although the appellate court's strict reading of the verification and authentication requirement were somewhat less unforgiving, a savvy practitioner would be well served by following both the letter and intent of the law in this area. A claimant must clearly demonstrate satisfaction of all the statutory lien claim requirements in order to have a valid and enforceable lien. The following is intended only to provide a general overview of the steps necessary to establish a lien. The code itself must be consulted in detail to ensure strict compliance with the statutory requirements for perfection of a mechanics lien.

A. Persons Entitled to Lien.

Any person who furnishes labor, professional services, materials, or equipment for the improvement of real property has the right to claim a lien on the improvement. RCW 60.04.021.

The lien covers the contract price of labor, professional services, materials, or equipment that was provided at the instance of the owner or the owner's agent.

B. Pre-Claim Notice.

Those entitled to a lien must give the owner of the property, and the prime contractor, if any, written notice of the right to claim a lien. RCW 60.04.031. The notice may be given at any time. However, for general construction providing notice only protects the right to claim a lien for materials, services, or equipment furnished within 60 days preceding the date the notice is given. For new construction of a single-family residence, the notice only covers 10 days preceding the date notice is given.

Certain categories of persons are exempt from the general notice requirements. These include: (1) persons who contract directly with an owner or the owner's common law agent; (2) laborers, and (3) subcontractors who contract directly with the prime contractor.

C. Claim of Lien – Contents, Form, and Recording.

A claim of lien must be filed within 90 days from the date of cessation of the performance of labor, the furnishing of materials, the supplying of equipment, or from the date the contributions to any type of employee benefit plan were due. The claim of lien must include specific information set forth in the statute, including an identification of the claimant, lien property, and dates of services, and lien amount. RCW 60.04.091. The claim of lien should be recorded with the county auditor for the county where the property is located. Failure to record the lien makes it subordinate to the interest of any subsequent mortgagee and invalid as to the interest of any subsequent purchaser.

II. STATUTES OF LIMITATION AND REPOSE

In Washington, the statute of repose sets a strict limit on the time in which a plaintiff's claim must accrue in actions arising from construction projects. The statutes of limitations, applicable to all contract actions, set a limit on when an action can be brought. Accrual marks the date of commencement of the applicable statute of limitations. The statutes of limitations and statutes of repose applicable to construction claims have been the subject of much confusion and some seemingly conflicting case law, but recent legislative and judicial clarifications have provided better guidance

A. Statutes of Limitation.

In Washington, the statute of limitations for breach of an oral contract is three years. RCW 4.16.080. For written contracts, the statute of limitations is six years. RCW 4.16.020. An additional, less frequently discussed, statute of limitations governs actions for taking, detaining or injuring personal property; it provides that those actions must be commenced within three years. RCW 4.16.080. The Washington Condominium Act, RCW 64.34, must be consulted in detail for any construction litigation involving condominiums in the state. Among other things,

it creates warranties of suitability and quality, which are subject to a four year statute of limitations. RCW 64.34.452(1).

Because Washington arguably does not currently recognize a claim for negligent construction, *see, e.g., Atherton Condo. Apartment-Owners Ass'n Bd. of Dirs. v. Blume Dev. Co.*, 115 Wn.2d 506, 799 P.2d 250 (1990), but *see Donatelli v. D.R. Strong Consulting Engineers, Inc.*, 2013 WL 6022171, 312 P.3d 620 Wash. (2013), the vast majority of construction defect claims are brought as, or at least involve, breach of contract claims.¹ The statute of limitations begins to run on these claims, either at termination of services or at “substantial completion” of the project, whichever is later.² RCW 4.16.310.

B. The Statute of Repose.

In addition to the statute of limitations, the practitioner must be aware that Washington has a six-year statute of repose, running from the date of substantial completion of construction or the termination of services, whichever is later. RCW 4.16.310. Like other jurisdictions, Washington distinguishes between the two as follows: “A statute of limitation bars plaintiff from bringing an already accrued claim after a specific period of time. A statute of repose terminates a right of action after a specific time, even if the injury has not yet occurred.” *Rice v. Dow Chem. Co.*, 124 Wn.2d 205, 875 P.2d 1213 (1994) (internal citations omitted).

C. The Interplay Between the Statutes of Limitation and Repose.

Applying the statute of limitations and statute of repose involves a two-step analysis. First, the practitioner must be certain that the cause of action accrued within six years of substantial completion. If it did not, the claim is barred by the statute of repose. *1000 Virginia L.P. v. Vertecs Corp.*, 158 Wn.2d 566, 146 P.3d 423 (2006). Second, the plaintiff must have filed suit within the applicable statute of limitations. *1000 Virginia L.P. v. Vertecs Corp.*, 158 Wn.2d 566, 146 P.3d 423 (2006). The statute of limitations, however, only begins to run once the cause of action has accrued. RCW 4.16.005.

¹ The accuracy of this longstanding idiom has been called into question recently in the recent case of *Affiliated v. LTK Consulting*, 170 Wn.2d 521, 243 P.3d 531 (2010), where the court recognized an “independent duty” owed in certain circumstances that is separate and actionable in tort. This new wrinkle in the longstanding economic loss rule will likely create a new cause of action in certain relationships such as those with architects and engineers based on the expectations created by their “professional” status. It is likely that any such cause of action, where allowed would be subject to the 3 year statute of limitations applicable to claims for negligence. RCW 4.16.080.

² Substantial completion is statutorily defined as “the state of completion reached when an improvement upon real property may be used or occupied for its intended use.” RCW 4.16.310. In practice, this is typically construed as the date the certificate of occupancy was issued.

A simple example of the interplay between the statute of limitations and statute of repose involves a personal injury action, arising out of construction, where the injury occurred in the fifth year following substantial completion. The first step is to determine whether the plaintiff's cause of action accrued within the six-year statute of repose. In this hypothetical it did, and therefore the claim is not barred by that statute.

The second step is to determine if the claim is barred by the statute of limitations, which began running upon accrual (in this example, upon injury). Therefore, to determine whether plaintiff's claim is barred by the three year personal injury statute of limitations, the practitioner must ask him/herself whether more than three years have lapsed since plaintiff's injury.

In determining running of the statutes of repose and limitations, a practitioner must be cognizant of the triggering of each statute. RCW 4.16.310 is clear that the time begins to run upon substantial completion of a project. Thus, the commencement of the period is measured from the latter of termination of services or date of substantial completion. Substantial completion runs from the point when an improvement "may be used;" actual use or occupancy is not required for construction to be substantially complete. [*Lakeview Blvd. Condominium Ass'n v. Apartment Sales Corp.*, 144 Wn. 2d 570, 29 P.3d 1249 \(2001\)](#). A claim that accrues before substantial completion of the improvement starts the running of the statute of limitations. RCW 4.16.040(1); RCW 4.16.080(3). See also, [*Phillips v. King County*, 87 Wn. App. 468, 943 P.2d 306 \(1997\)](#).

D. The Discovery Rule in Construction Defect.

To properly analyze the application of the statute of limitations and statute of repose in the context of construction defect claims, the practitioner until a few years ago needed to be cognizant that the discovery rule sometimes applied in construction defect cases. The application of the discovery rule is now much more limited.

The Supreme Court adopted the discovery in all construction defect cases in *Architechtonics Constr. Management, Inc. v. Khorram*, 111 Wn. App. 725, 737, 45 P.3d 1142 (2002), *rev. denied*, 148 Wn.2d 1005, 60 P.3d 1212 (2003). In response to the *Architechtonics* decision, the Washington Legislature enacted RCW 4.16.326(1)(g), which specifically rejected the discovery rule in the context of written construction contracts, but which is silent as to oral contracts.

Following the *Architechtonics* decision and the adoption of RCW 4.16.326(1)(g), there was considerable confusion in Washington as to precisely how the discovery rule applied to construction defect claims. The Supreme Court clarified the situation in *1000 Virginia L.P. v. Vertecs Corp.*, 158 Wn.2d 566, 146 P.3d 423 (2006). In construction defect claims, RCW 4.16.310 is a statute of repose that terminates an action for construction defects that does not accrue within six years from the time of substantial completion of construction or termination of services, whichever is later. RCW 4.16.310. Under RCW 4.16.040, an action upon a contract in writing must be commenced within six years. Generally, a statute of limitation runs from the time a claim accrues; a claim accrues when a party has the right to apply to a court for relief, which may be at the time the claim is discovered. *1000 Virginia*, 158 Wn.2d at 575-76. But in July 2003, RCW 4.16.326(1)(g) went into effect, requiring that construction defect claims be

filed within six years of substantial completion of construction or termination of services, whichever is later, regardless of when the claim was discovered. RCW 4.16.326(1)(g).

There, the Supreme Court criticized the *Architectonics* decision, but went on to hold that the discovery rule was appropriate in construction defect cases involving latent defects that the plaintiff would be unable to detect at the time of the breach. This holding and reasoning was recently affirmed in *Cambridge Townhomes, LLC v. Pac. Star Roofing, Inc.*, 166 Wn.2d 475, 209 P.3d 863 (2009).

At the same time, the Supreme Court was bound by the adoption of RCW 4.16.326(1)(g). Thus, it ultimately held that if there is a latent defect, a plaintiff may take advantage of the discovery rule in the context of oral contracts. *Id.* With respect to written contracts, it is essential for defendants to plead RCW 4.16.326(1)(g) in order to receive its benefits. If a defendant fails to plead RCW 4.16.326(1)(g) as an affirmative defense, the Supreme Court held that the discovery rule may also be applied to the statute of limitations for written contracts. Finally, the Supreme Court held that RCW 4.16.326(1)(g) will not apply retroactively.

Any attorney practicing construction defect law who wants to understand the pertinent Washington statutes of limitations and repose must carefully read RCW 4.16.326, *1000 Virginia* and *Cambridge* decisions and their progeny. As a practical matter the statutes and case law in this area leave room to advocate a variety of positions and arguments extending or limiting the time within which an action may be brought based on the precise facts of the case. Trial courts have reached inconsistent result given the rather perplexing guidance from the appellate courts and legislature.

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

On June 13, 2002, Washington's statutory scheme for pre-suit notice of claim and opportunity to cure in construction defect cases became effective. Prior to that date, such requirements existed only to the extent they were required by the parties' contract. Currently, the requirements are found at RCW 64.50.

A. Notice of Claim.

The claimant must serve a written notice of claim on construction professional 45 days before filing an action. RCW 64.50.020(1). The notice must state the general nature of the defect with sufficient detail.

B. Response.

Within 21 days after receiving a notice of claim, the construction professional must serve a written response with the following:

1. A proposal to inspect the residence within a specified time frame. Or, a statement based upon the inspection with an offer to remedy, compromise by payment or dispute;
2. An offer to compromise and settle by payment without inspection. This may include offer to purchase and pay relocation costs; or
3. A statement that the construction professional disputes the claim and will neither remedy nor settle.

RCW 64.50.020(2).

C. Inspection.

If a claimant allows an inspection as set forth in a construction professional's proposal, the claimant is required to allow reasonable access during normal working hours.

Within 14 days of an inspection, the construction professional must serve on the claimant:

1. A written offer to remedy at no cost, with a report on the scope of inspection, findings and results, a description of additional construction necessary to remedy the defect(s) described in the claim, and a timetable for completion;
2. A written offer to compromise and settle; or
3. A written statement that the construction professional will not further remedy the claimed defect(s).

RCW 64.50.020(4).

D. Filing of Action.

1. After the Initial Notice of Claim:

If the construction professional disputes the claim or makes no response, the claimant can file a lawsuit without further notice.

If the construction professional makes a proposal, and the claimant rejects that proposal, the claimant must provide written notice of the rejection prior to filing suit.

If there is no acceptance or rejection by claimant within 30 days, the construction professional may terminate the proposal or offer by serving written notice; if that happens, the claimant can then commence suit.

2. After an Inspection has been Completed:

If the construction professional does not proceed to remedy within the agreed timetable, or fails to comply with these requirements, the claimant can file action without further notice.

If the claimant rejects the offer to remedy or settle, the claimant must serve written notice. Following the written notice, the claimant can file the lawsuit.

If the construction professional does not receive rejection or acceptance within 30 days, he/she may terminate offer by written notice.

If the claimant accepts the proposal, the claimant must provide written notice of acceptance within reasonable time after receipt of offer, not later than 30 days. The claimant is required to provide access during normal working hours to perform and complete the construction within the timetable.

RCW 64.50.020(3), (4).

E. Noncompliance.

The general rule is that any action commenced without complying with this statute shall be dismissed without prejudice. The claimant may not recommence the action until he/she is in compliance. RCW 64.50.020(6). However, one of the first cases interpreting RCW 64.50, *Lakemont Ridge Homeowners Ass'n v. Lakemont Ridge L.P.*, 156 Wn.2d 696, 131 P.3d 905 (2006), reminded practitioners that the construction professional has his/her own notice requirements under RCW 64.50.050. That section of the code requires the construction professional to give notice to the claimant of the pre-suit notice and opportunity to cure requirements at the time that the parties enter into a contract.

The Supreme Court explained that the two notice provisions operated together to give effect to the legislature's dual goals of reducing potentially burdensome and expensive construction defect litigation and preserving rights and remedies for property owners. Reading the statutory scheme as an integrated whole and in light of these purposes, the Supreme Court held that, if the construction professional did not provide notice pursuant to RCW 64.50.050, then the claimant was excused from the pre-suit notice and opportunity to cure requirements of RCW 64.50. These statutes were authoritatively construed in *Lakemont Ridge Homeowners Ass'n v. Lakemont Ridge Limited Partnership*, 156 Wn.2d 696, 131 P.3d 905 (2006). There the court determined that a builder could not assert the statutory notice bar of subsection .020 without first having complied with the notice requirements of subsection .050. *Id.* at 703. The decision reversed the Court of Appeals' opinion in the same case that had enforced the purchaser's prelitigation notice requirement even though the builder had not given the statutory notice. 156 Wn.2d at 698.

IV. COVERAGE AND ALLOCATION ISSUES

A. How a Coverage Determination is Made.

In order to determine whether insurance coverage exists, Washington Courts engage in a two-step process. *Graff v. Allstate Ins. Co.*, 113 Wn. App. 799 (2002). First, the insured must demonstrate that the loss falls within the scope of the policy's insured losses. *Id.* Second, if the insured has successfully established that such coverage does potentially exist, in order to defeat coverage, the burden shifts to the insurer to show that a specific exclusion applies. *Id.*

When a construction defect claim is made, most contractors tender the claim to the insurance company that issued their commercial general liability policy or “CGL” policy. Speaking generally, CGL policies provide broad coverage for claims of “property damage.” Again, speaking very generally, three things that are required to trigger coverage under the standard CGL insuring agreement are: (1) physical injury to tangible property (or loss of use of tangible property); (2) that takes place during the policy period, and (3) is caused by an “occurrence” (or sometimes by an “event”). See *Yakima Cement Prods. Co. v. Great Am. Ins. Co.*, 93 Wn.2d 210, 608 P.2d 254 (1980); *Gruol Construction Co. of North America*, 11 Wn. App 635, 524 P.2d 427 (1974).

While these guidelines above are generally accurate, like all contracts, insurance contract analysis is specific to the language of the contract (i.e., the policy); this in turn means that when a policy defines its terms, the policy’s definitions apply. *Getz v. Progressive Specialty Ins. Co.*, 106 Wn. App 184, 187, 22 P.3d 835 (2001). Often, in determining whether there is coverage for a construction defect claim under a CGL policy, the policy’s definition of “property damage” and “occurrence” will be central to the analysis.

Thus, the question often becomes, does the claim or complaint allege “property damage” resulting from an “occurrence” during the policy period, as those terms are defined in the policy.

B. The Relevant Policy Period.

Most contractors’ CGL policies are occurrence policies, rather than claims made policies. Under an occurrence policy, the insurer’s obligations are triggered if the covered event took place during the policy period. See *Wellbrock v. Assurance Co. of America*, 90 Wn. App. 234, 951 P.2d 367, *review denied*, 136 Wn.2d 1005, 966 P.2d 902 (1998).³

Continuous and progressive damage can trigger coverage under multiple insurance policies. As a matter of law, once coverage is triggered, the insurer will be liable for an entire loss, including portions that took place outside its policy period. See *American Nat’l Fire Ins. Co. v. B & L Trucking and Constr. Co.*, 134 Wn.2d 413, 428, 951 P.2d 250 (1998). Conversely, if there is no damage during the policy period, there is no coverage regardless of any other issue. *Wellbrock*, *supra*. See also *Villella v. Pub. Employees Mut. Ins. Co.*, 106 Wn.2d 806, 725 P.2d 957 (1986).⁴

³ In contrast, claims made policies provide coverage for a (covered) claim if the claim is made during the policy period, without regard to when the actions giving rise to the claim occurred.

⁴ That said, as a practical matter, insurers often share in the payment of a settlement or judgment in the case based upon their time on the risk after substantial completion.

C. Additional Insured Requirements.

Construction contracts often contain requirements that prime contractor and subcontractors obtain “additional insured” coverage for the developer and/or contractor for whom the work is being performed. Some CGL policies contain “blanket additional insured” endorsements that automatically extend additional coverage if required by a written contract entered into by the named insured. More often, CGL policies extend coverage to additional insureds only if specifically requested, with appropriate paperwork completed.

In Washington, a contractor’s failure to obtain coverage when required by contract may be deemed a breach of contract. If a contractor is successfully pursued for such a breach, the breaching contractor is essentially required to take on the role of the developer’s or general contractor’s insurer. *U.S. Oil & Refining Co. v. Lee & Eastes Tank Line, Inc.*, 104 Wn. App. 823, 16 P.3d 1278 (2001).

V. CONTRACTUAL INDEMNIFICATION

Absent an express warranty, in Washington, implied indemnity (often mistakenly called “equitable indemnity”) is normally not available in the context of construction contracts, although some trial courts have been known to interpret the concept broadly for remedial purposes. *Urban Dev., Inc. v. Evergreen Bldg. Prods., L.L.C.*, 114 Wn. App. 639, 59 P.3d 112, *aff’d sub nom. on other grounds, Fortune View Condominium Assoc. v. Fortune Star Dev. Co.*, 151 Wn.2d 534, 90 P.3d 1062 (2003). However, the parties are free to, and often do, bargain for and include indemnity provisions in their contracts.

Historically, there has been some dispute as to whether a contractor’s indemnity rights applied to both defective work and to tort claims, or if they were limited to only tort claims. There had been no appellate court guidance on the subject until recently, when the Court of Appeals issued its decision in *MacLean Townhomes, L.L.C. v. P.J. Interprize, Inc.*, 133 Wn. App. 828 (2006).

In *MacLean*, a general contractor had sued its subcontractor, seeking, among other things, to enforce an indemnity clause in the subcontract. The indemnity clause required the subcontractor to defend and indemnify the general contractor for “any and all claims” arising from the subcontract. The subcontractor moved for partial summary judgment, arguing that the indemnity clause applied only to tort-based claims and not to construction defect claims. The clause at issue was a fairly standard indemnity provision, which stated:

SUBCONTRACTOR shall defend, indemnify, and hold CONTRACTOR harmless from *any and all claims, demands, losses and liabilities to or by third parties arising from, resulting from, or connected with, services performed or to be performed under this Subcontract* by SUBCONTRACTOR or SUBCONTRACTOR'S agents, employees, subtier Subcontractors, and suppliers *to the fullest extent permitted by law and subject to the limitations provided below:*

The limiting clauses barred indemnity for bodily injury or property damage arising from the prime contractor's sole negligence. The clauses also stated that in the case of concurrent negligence, the subcontractor would be liable only for damages caused by its own negligence. Additionally, the subcontractor expressly waived its immunity under RCW Title 51.⁵

The basis for the argument that indemnity provisions such as these apply only to tort-based claims had historically been the inclusion of the language pertaining to negligence, and the fact that there is no viable cause of action in Washington for negligent construction. Prior to *MacLean*, this argument met with varying levels of success in the trial courts.

The Court of Appeals made clear, however, that indemnity provisions in contracts are construed in accordance with general rules of contract construction. *MacLean Townhomes, L.L.C.*, 133 Wn. App. at 831. Thus, the court would not construe the contract in such a manner as to make any term absurd or meaningless. *Id.* (citing *Seattle-First Nat'l Bank v. Westlake Park Assocs.*, 42 Wn. App. 269, 274, 711 P.2d 361 (1985)). It would not read the term "all claims" out of the contract. *Id.* at 832. A better drafted indemnity agreement could conceivably limit that risk appropriately.

Ultimately, the Court ruled that the contract was properly read to include specific limitations *on* tort actions, but not to limit the indemnification obligations *to* tort actions. *Id.* at 833. Thus, the indemnity obligations applied to construction defect actions as well. *Id.* The *MacLean* decision provided much needed guidance in interpreting similar clauses; however, each indemnity agreement will need to be interpreted and applied based on the language agreed to by the parties.

The Washington Supreme Court affirmed the reasoning and holding in *Cambridge Townhomes, LLC v. Pac. Star Roofing, Inc.*, 166 Wn.2d 475; 209 P.3d 863 (2009). Specifically, the court held that a standard indemnity provision that refers to "any and all claims, demands, losses and liabilities to or by third parties arising from, resulting from, or connected with services performed or to be performed" under the contract and that does not specifically limit indemnifiable claims to tort claims does not prohibit the indemnitee from seeking indemnification for nontort claims. Additional language limiting the indemnitor's liability when the underlying claim is due to the indemnitee's sole negligence or fault does not operate to restrict the indemnity provision to tort claims only.

VI. DAMAGES LIMITATIONS

A. General Construction Defect Claims.

Washington does not currently recognize a claim for negligent construction. Thus, construction defect claim damages are primarily governed by contractual damages principles. In *Eastlake Constr. Co., Inc. v. Hess*, 102 Wn.2d 30, 686 P.2d 465 (1984), the Supreme Court discussed

⁵ Pursuant to Title 51 RCW, Washington's workers compensation system exempts an employer from liability for its own worker's injuries absent the employer's intent to injure the worker.

construction contract damages at length and adopted the Restatement (Second) of Contracts § 348, which provides for the following measures of damages:

- (1) If a breach delays the use of property and the loss in value to the injured party is not proved with reasonable certainty, he may recover damages based on the rental value of the property or on interest on the value of the property.
- (2) If a breach results in defective or unfinished construction and the loss in value to the injured party is not proved with sufficient certainty, he may recover damages based on
 - (a) the diminution in the market price of the property caused by the breach, or
 - (b) the reasonable cost of completing performance or of remedying the defects if that cost is not clearly disproportionate to the probable loss in value to him.

B. Attorney Fees and Costs.

The general rule regarding the availability of attorney fees and costs in Washington is that each party to a civil action bears its own fees and costs absent modification by contract, statute, or a recognized ground in equity. *City of Seattle v. McCready*, 131 Wn.2d 266, 274, 931 P.2d 156 (1997).⁶

In a pre-sale or spec home arrangement, there will often be an attorney fees provision contained the Purchase and Sale Agreement, particularly if the parties have used a Multiple Listing Service form agreement. It is unusual, but not unheard of, for other forms of construction contracts to include an attorney fees provisions as well. Thus, it is important to review the contract when litigating these claims to determine the potential exposure.

Additionally, the Washington Condominium Act (the “WCA”) makes attorney fees and costs available to any person or class of persons who must sue to enforce their rights under the WCA. RCW 64.34.455

C. Punitive Damages.

The general rule is that punitive damages are not available in Washington, except when expressly authorized by statute, because they are considered violative of public policy. *Barr v. Interbay Citizens Bank*, 96 Wn.2d 692, 699 (1981).

⁶ RCW 4.84.080 does provide for \$200 in statutory attorneys fees to the prevailing party. Certain limited costs are also taxed to the losing party under RCW 4.84.

VII. ECONOMIC LOSS RULE IN CONSTRUCTION CLAIMS

Historically, Washington courts have applied the economic loss rule to hold parties to their contract remedies when a loss potentially gives rise to both tort and contract relief. The rule prohibits plaintiff from recovering in tort economic losses to which their entitlement flows only from a contract because tort law is not intended to compensate parties for losses suffered as a result of breach of duties assumed only by agreement. Where economic losses occur, recovery is confined to contract to ensure that the allocation of risk and the determination of potential future liability is based on what the parties bargained for in the contract. *See generally Stuart v. Coldwell Banker*, 109 Wn.2d 406, 745 P.2d 1284 (1987), and *Atherton Condo. Apartment-Owners Ass'n v. Blume Development Co.*, 115 Wn.2d 506, 799 P.2d 250 (1990) (Washington Supreme Court declined to recognize any tort cause of action for “negligent construction.”).

The continued application of the economic loss rule in Washington was recently revisited by the Washington State Supreme Court in *Affiliated v. LTK Consulting Servs., Inc.*, 170 Wn.2d 442, 243 P.3d 521 (2010), where the court recognized that in some instances there may be an “independent duty” owed that is separate and apart from the contract. In that case the court seemed to draw a distinction between a construction contract and contracts for professional services with architects and engineers. Specifically, expectations associated with those professions give rise to duties independent of the terms of the contract. *Id.* Although the court in *Affiliated* focused on design professionals, the independent duty rule has not been explicitly limited to those relationships.

The continued viability of the economic loss rule was further called into question in the recent case of *Donatelli v. D.R. Strong Consulting Engineers, Inc.*, 2013 WL 6022171, 312 P.3 629 (Wash 2013). D.R. Strong was a professional engineering company hired by the Donatellis to provide the engineering plans to develop two plats of land. Because of case overruns, the developer did not complete the project and the plats were foreclosed upon the unbuilt houses. This seems to be consistent with Washington court’s decisions to apply the independent duty doctrine to licensed design professionals such as engineers and architects. It remains to be seen if the independent duty doctrine will be deemed to apply to general contractors or other providers of labor as opposed to design expertise. If a line is to be drawn, that would be the most logical delineation.

An attorney representing a design professional should also review *Michaels v. CH2M Hill, Inc.*, 171 Wn.2d 587 (2011), where the independent duty of licensed engineers in certain circumstances was affirmed.

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I. MECHANIC'S LIEN BASICS

The statutory provisions of W.Va. Code §§ 38-2-1 et seq. govern mechanic's liens in West Virginia, and establish the lien rights and procedures applicable to: general contractors; all levels of subordinate contractors ("subcontractors"); materialmen (whether furnishing to the owner or to contractors and/or subcontractors); mechanics or laborers (whether furnishing to the owner or to contractors and/or subcontractors); and, architects, surveyors, engineers and landscape architects.

A. Requirements

1. Notice of Mechanic's Lien

Mechanic's lien rights are initially perfected and preserved by a Notice of Mechanic's Lien.

2. Recordation & Service

A Notice of Mechanic's Lien must be recorded in the office of the clerk of the county commission of the county where the property subject to the lien is situated, within one hundred (100) days of the: (i) completion of the contract, (ii) last day of work, or (iii) last day of furnishing of supplies, as applicable. In most cases, the Notice of Mechanic's Lien must also be served upon the property owner¹ (by any means provided by law for the service of a legal notice or summons) within the same one hundred (100) day period. It is recommended that, in all cases, the Notice of Mechanic's Lien be recorded with the county and served upon the owner, applicable tenant(s), record lienholders, superior contractors and any other party to whom the lienholder is providing goods or services in connection with the improvement of the property to which the lien applies.

3. Form of Notice

The Notice of Mechanic's Lien must be in writing, and the statute provides recommended forms to use. Unlike many other states, West Virginia law requires that the description of the property in the Notice of Mechanic's Lien be an "adequate," "definite" and "ascertainable" description. It is therefore recommended that a legal description be placed in the Notice of Mechanic's Lien and not simply a street address. A description of the building or improvement for which the lienholder performed or provided labor or materials is also required. Finally, a dollar amount of the claim (together with a list of invoices or other detail) is also to be included

in the Notice of Mechanic's Lien.

B. Enforcement and Foreclosure

Suit; Remedies. A lienholder must file suit to enforce the lien (perfected by the Notice of Mechanic's Lien) within six (6) months after the filing of such Notice in the county clerk's office. Failure to file suit timely will result in the discharge of the lien.² The remedy sought by the suit is to have the court order the sale of the property (or a portion thereof) to satisfy valid liens unless the liens are first paid.³

C. Ability to Waive and Limitations on Lien Rights

1. Release of Lien

When a debt secured by a mechanic's lien is fully paid, a release or discharge of the lien must be recorded in the county clerk's office.⁴

2. Public Property

In West Virginia, mechanic's liens cannot be filed against public buildings or structures.⁵ Typically, however, a payment bond must be posted with respect to public projects.

3. Tenant Leases

When work is performed for a tenant and not the property owner, special care must be taken to determine what ownership interest (i.e. the owner's fee interest, the tenant's leasehold interest, or both) is properly subject to the lien. Improper attachment of a lien may subject the lienholder to a claim of slander of title.⁶

4. Owner's Ability to Limit Liability

The owner may limit liability with respect to potential mechanic's liens against property to the sum agreed to be paid under the applicable construction contract if, prior to the beginning of construction, the owner records such contract with the clerk of the county commission of the county in which the property is located together with a payment bond (in a penal amount equal to the contract price) given by the applicable contractor. W.Va. Code §38-2-22. If the owner does not so record his contract and bond, then the owner shall be liable and subject to all perfected liens, even if the aggregate amount of the liens exceed the owner's contract price.

II. STATUTES OF LIMITATION AND REPOSE

A. Statutes of Limitation and Limitation on Application of Statutes

There is a two-year statute of limitations applicable to a cause of action involving tort liability, as more specifically set forth in W.Va. Code §55-2-12:⁷

Every personal action for which no limitation is otherwise prescribed shall be brought: (a) within two years next after the right to bring the same shall have accrued, if it be for damage to property; (b) within two years next after the right to bring the same shall have accrued if

it be for damages for personal injuries; and (c) within one year next after the right to bring the same shall have accrued if it be for any other matter of such nature that, in case a party die, it could not have been brought at common law by or against his personal representative.

With respect to contract claims, West Virginia recognizes limitation periods of ten years for actions arising out of a written contract, and five years for other contracts. W.Va. Code §55-2-6.⁸

The applicable statute of limitations in actions for breach of the warranties of merchantability and fitness for a particular purpose is set forth in W.Va. Code §46-2-725. An action must be commenced within four (4) years after the sale of the subject goods. However, the Supreme Court of Appeals of West Virginia has held that W. Va. Code §46-2-725 is, in essence, a statute of repose, because the limitation period begins to run when the product is delivered-- regardless of when the damages are incurred.⁹

In *Taylor v. Ford Motor Co.*, the Supreme Court of Appeals of West Virginia ruled that “where a person suffers personal injuries as a result of a defective product and seeks to recover damages for these personal injuries based on a breach of express or implied warranties, the applicable statute of limitations is the two-year provision contained in W. Va. Code §55-2-12, rather than the four-year provision contained in our Uniform Commercial Code, W.Va. Code §46-2-725.”¹⁰

Finally, where a cause of action is based upon tort or on a claim of fraud, the statute of limitations does not begin to run until the injured person knows, or by the exercise of reasonable diligence should know, of the nature of his injury, and determining that point in time is a question of fact to be answered by the jury.¹¹

B. Statutes of Repose and Limitation on Application of Statutes

In West Virginia, the statute of repose for improvements to real property is set forth in W. Va. Code § 55-2-6a. This statute provides that “[n]o action, whether in contract or in tort . . . to recover damages for any deficiency in the planning, design, surveying, observation or supervision of any construction or the actual construction of any improvement to real property . . . may be brought more than ten years after the performance or furnishing of such services or construction. . . .” Moreover, the period of limitation commences when the real property has been occupied or accepted by the owner, whichever event occurs first (W.Va. Code § 55-2-6a). It should be noted that the Supreme Court of Appeals of West Virginia has specifically held the statute of repose to be constitutional.¹²

The Supreme Court of Appeals of West Virginia has also held that this code section only protects those named therein. It does not protect all defendants who perform the services listed in the statute.¹³ In *Stone v. United Engineering, Inc.*, the court held that “our statute of repose contains the following critical language which indicates that it is not intended to protect *every* defendant that performs or furnishes the activities listed [in the statute]: ‘The period of limitation provided in this section shall not commence until the improvement to the real property in question *has been occupied or accepted by the owner of real property, whichever occurs first.*’”¹⁴

The court in *Stone* also explained how a trial court should determine whether an

improvement has taken place: “when determining whether an item is an improvement to real property . . . a court must consider the enhanced value created when the item is put to its intended use, the level of integration of the item within any manufacturing system, whether the item is an essential component of the system, and the item’s permanence. These factors should be considered in making the case by case determination of whether an item is an improvement to real property. . . .”¹⁵

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

Under current West Virginia law, the owner, claiming breach of warranty or defective workmanship in any given project, is not required to give a contractor or material supplier a notice of claim or an opportunity to cure the alleged defects prior to initiating litigation.

IV. INSURANCE COVERAGE AND ALLOCATION ISSUES

A. General Coverage Issues

In West Virginia a standard commercial general liability (“CGL”) policy covers those amounts the insured is liable to pay because of property damage that occurs during the policy period.

B. Trigger of Coverage

In 2013, the Supreme Court of Appeals of West Virginia significantly revised what a CGL policy does and does not cover. In *Cherrington v. Erie Insurance Property and Casualty Company*, the Court held that “defective workmanship causing bodily injury or property damage is an ‘occurrence’ under a policy of commercial general liability insurance.”¹⁶ Prior to its decision in *Cherrington*, the Court did not recognize CGL policies as covering poor workmanship.¹⁷

C. Allocation Among Insurers

In *State v. Janicki*, the Supreme Court of Appeals of West Virginia resolved a dispute between two insurance carriers as to their respective liability for a physician’s malpractice. The Court noted that “other insurance” clauses in insurance policies are only implicated when the policies cover the same risk. Ambiguity is resolved in favor of the insured, whose reasonable expectations determine the carriers’ liability.¹⁸

D. Issues with Additional Insurance

The Supreme Court of Appeals of West Virginia addressed additional insurance in *Gauze v. Reed*. The Court determined that

when an insurance company (a) issues a primary liability insurance policy; and (b) has contracted for and received a premium for a risk as though it were a primary insurer; but (c) the insurance company has become a secondary insurer by operation of an “other insurance” clause in the policy and the existence of another primary insurance carrier, then if that other insurance carrier is declared insolvent, the insurance company is responsible for coverage of the loss as though it were the sole primary liability insurer.¹⁹

V. CONTRACTUAL INDEMNIFICATION

West Virginia recognizes the rights of parties to enter into express indemnity agreements.²⁰ However, W.Va. Code § 55-8-14 precludes agreements

relative to the construction, alteration, repair, addition to, subtraction from, improvement to or maintenance of any building, highway, road, railroad, water, sewer, electrical or gas distribution system, excavation or other structure project, development or improvement attached to real estate, including any moving and demolition in connection therewith which purport to indemnify against liability for damages arising out of injury to person or property caused by or resulting from the sole negligence of the indemnitee, his agents or employees²¹

Such agreements are “contrary to public policy and are void and unenforceable.”²²

The Supreme Court of Appeals of West Virginia clarified the application of W.Va. Code § 55-8-14 in *Dalton v. Childress Service Corporation*,²³ holding that the statute requires a court to void an indemnity agreement only if (1) the indemnitee is found by the trier-of-fact to be solely, i.e., 100% negligent in causing the accident and (2) it cannot be inferred from the contract at issue that the parties had agreed to purchase insurance for the benefit of all concerned.²⁴

VI. CONTINGENT PAYMENT AGREEMENTS

A. Enforceability

The Supreme Court of Appeals of West Virginia has found contingent payment agreements enforceable as between contractors and subcontractors in public construction projects: “[I]n a public construction project, a pay-if paid condition precedent clause in a contract between a subcontractor and a contractor does not violate [West Virginia] public policy . . . found in the public bond statute, W.V. Code § 38-2-39 (2004).”²⁵

B. Requirements

In *Wellington Power Corp.* the Court did not set out specific requirements for the enforceability of contingent payment agreements. However, the Court mentioned three particular factors that informed its ruling: that (1) “commercial entities” (2) “voluntarily agreed” (3) “to a clear, unambiguous pay-if-paid condition precedent.”²⁶

VII. DAMAGE LIMITATIONS

A. Personal Injury Damages vs. Construction Defect Damages

Damages for personal injury are measured by fair compensation for the injury suffered, but their amount is left to the discretion of a jury.²⁷ Regarding damages for construction defects, “the proper measure of damages . . . is the cost of repairing the defects or completing the work and placing the construction in the condition it should have been if properly done under the agreement contained in the building contract.”²⁸

B. Attorney’s Fees Shifting and Limitations on Recovery

Attorney's fees are recoverable only where a plaintiff shows by clear and convincing evidence that a defendant has engaged in fraudulent conduct.²⁹

C. Consequential Damages

In addition to direct damages, a plaintiff may recover consequential damages for a breach of contract action only when it can be shown that the parties, at the time of the contract, could reasonably have anticipated that these damages would be a probable result of a breach.³⁰

D. Delay and Disruption Damages

Specific penalties, such as delay and disruption damages, may be provided for in construction contracts in West Virginia.³¹

E. Economic Loss Doctrine

Absent some special relationship, which will vary and must be reviewed on a case-by-case basis, there is no duty under West Virginia law to prevent purely economic loss.³² The Supreme Court of Appeals of West Virginia has articulated certain factors that inform what constitutes a special relationship. These include: "the extent to which the particular plaintiff is affected differently from society in general";³³ "the defendant's knowledge or specific reason to know of the potential consequences of the wrongdoing";³⁴ "evidence of foreseeability of the nature of the harm to be suffered by the particular plaintiff or an identifiable class";³⁵ and "contractual privity or other close nexus."³⁶

The Court has considered whether special relationships exist in two particular areas of construction law:³⁷ in interactions between contractors and design professionals³⁸ and in interactions between certain lenders (banks) and certain borrowers (homeowners or those having houses built).³⁹ In *Eastern Steel Constructors, Inc. v. City of Salem*, the Court determined that a special relationship may exist between a design professional and a contractor.⁴⁰ In interactions between lending banks and borrowing homeowners (or those who are having houses built) the Court has also reached the conclusion that a special relationship may exist between the bank and the borrower. However, a special relationship will not exist between every lending bank and borrowing homeowner, but when the bank "maintain[s] oversight of, or interven[es] in, the construction process"⁴¹

F. Interest

Plaintiffs who are awarded compensatory damages at trial are entitled to pre-judgment interest as a matter of law.⁴² Post-judgment interest accrues from the date the judgment is entered and the rate is calculated at "three percentage points above the Fifth Federal Reserve District secondary discount rate in effect on the second day of January of the year in which the judgment or decree is entered."⁴³

G. Punitive Damages

Generally, absent an independent, intentional tort committed by the defendant, punitive damages are not available in an action for breach of contract.⁴⁴

H. Other Damage Limitations

West Virginia's comparative fault rule places an additional limitation on damages. "Under the comparative negligence doctrine, a plaintiff is not entitled to recover from a negligent tortfeasor if the plaintiff's own contributory negligence equals or exceeds the combined negligence or fault of the other parties involved in the accident or occurrence."⁴⁵

The legislature has further limited recovery of damages under a comparative fault theory in a specific context that may bear on construction law. Under West Virginia's smoke detector statute (W.Va. Code §29-3-16a), violation of the statute does not constitute "by virtue of the violation . . . evidence of negligence or contributory negligence or comparative negligence in any civil action or proceeding for damages."⁴⁶

VIII. RECENT DEVELOPMENTS

Mechanics' Liens

In its 2014 session, the West Virginia Legislature passed, and the Governor approved, H.B. No. 4347, which created an affirmative defense to an action to enforce a mechanics lien. Specifically, H.B. No. 4347 allows an owner to assert as an affirmative defense (or a partial affirmative defense) that he or she is not indebted to the contractor (or is indebted to the contractor for less than the amount of the lien sought to be perfected). This affirmative defense is only available in the case of mechanics liens on specific types of property, such as existing single-family dwellings.

OSHA Construction Safety Program

In its 2014 session, the West Virginia Legislature passed, and the Governor approved, S.B. No. 376, which requires workers at certain public improvement sites to complete a ten hour United States Occupational Safety and Health Administration (OSHA) safety program.

Regulation of Heating, Ventilating, and Cooling Work

In its 2014 session, the West Virginia Legislature passed, and the Governor approved, H.B. No. 4392, which provides for regulation of heating, ventilating, and cooling work (HVAC). Among other things, the Bill provides for the licensing of those performing HVAC work and the promulgation of regulations related to HVAC work by the Commissioner of Labor.

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- ¹ See W. Va. Code § 38-2-15 where the owner is a nonresident or not found.
- ² W. Va. Code § 38-2-34.
- ³ W. Va. Code §§ 38-2-35.
- ⁴ W. Va. Code § 38-2-36.
- ⁵ W. Va. Code § 38-2-39.
- ⁶ *Dunlap v. Hinkle*, 317 S.E.2d 508 (W.Va. 1984).
- ⁷ *Graham v. Beverage*, 566 S.E.2d 603, 613 (W.Va. 2002) (citing Syl. Pt. 1, *Family Savings and Loan, Inc. v. Ciccarello*, 207 S.E.2d (W.Va. 1974)); see also *Roverts v. W. Va. Am. Water Co.*, 655 S.E.2d 119, 124-25 (W. Va. 2007) (rejecting an argument for the existence of a continuing tort and finding that the “general rule” applies).
- ⁸ *Rowe v. Grapevine Corp.*, 456 S.E.2d 1 (W.Va. 1995).
- ⁹ See *Taylor v. Ford Motor Co.*, 408 S.E.2d 270, 273 (W.Va. 1991) (citing *Gibson v. State Dept. of Highways*, 406 S.E.2d 440 (W. Va. 1991)). See also *Basham v. General Shale*, 377 S.E.2d 830 (W.Va. 1988) (where Supreme Court of Appeals of West Virginia declined to apply the discovery rule exception to the U.C.C. statute of limitations).
- ¹⁰ *Taylor v. Ford Motor Co.*, 408 S.E.2d 270, Syl. Pt. 1 (W.Va. 1991).
- ¹¹ *Goodwin v. Bayer Corp.*, 624 S.E.2d 562, 567 (W.Va. 2005) (quoting Syl. pt. 3, *Stemple v. Dobson*, 400 S.E.2d 561 (W.Va. 1990)).
- ¹² See *Gibson v. West Virginia Department of Highways*, 406 S.E.2d 440 (W.Va. 1991).
- ¹³ *Stone v. United Engineering, Inc.*, 475 S.E.2d 439 (W.Va. 1996).
- ¹⁴ *Id.* at 447 (citations omitted). The Court has subsequently emphasized another requirement for when the time period begins to run: “This arbitrary time limit begins to run *when the builder or architect relinquishes access and control over the construction or improvement and the construction or improvement is (1) occupied or (2) accepted by the owner of the real property, whichever occurs first.*” *Neal v. Marion*, 664 S.E.2d 721, 728 (W. Va. 2008) (emphasis added).
- ¹⁵ *Id.* at 450.
- ¹⁶ *Cherrington v. Erie Insurance Property and Casualty Co.*, 745 S.E.2d 508, 521 (W.Va. 2013).
- ¹⁷ See *Webster County Solid Waste Auth. v. Brackenrich & Associates, Inc.*, 617 S.E.2d 851, 858 (W.Va. 2005); partially overruled by *Cherrington v. Erie Insurance Property and Casualty Co.*, 745 S.E.2d 508, 521 (W.Va. 2013).
- ¹⁸ *State v. Janicki*, 422 S.E.2d 822, 825 (W. Va. 1992).
- ¹⁹ *Gauze v. Reed*, 633 S.E.2d 326, 335 (W. Va. 2006).
- ²⁰ See *Van Kirk v. Green Construction Co.*, 466 S.E.2d 782 (W.Va. 1995); see also, *State Ex Rel Vapor Corp. v. Narick*, 320 S.E.2d 345 (W.Va. 1984) (contracts of indemnity against the indemnitee’s own negligence do not contravene the public policy of West Virginia); cf. *Riggle v. Allied Chemical Corp.*, 378 S.E.2d 282, 288-89 (W. Va. 1989).
- ²¹ W.Va. Code § 55-8-14.
- ²² *Id.*
- ²³ *Dalton v. Childress Service Corp.*, 432 S.E.2d 98 (W.Va. 1993).
- ²⁴ *Id.*
- ²⁵ *Wellington Power Corp. v. CAN Surety Corp.*, 614 S.E. 2d 680, 682 (W. Va. 2005).
- ²⁶ *Id.* at 686.
- ²⁷ *Wade v. Chengappa*, 532 S.E.2d 37, 41 (W. Va. 1999).
- ²⁸ *Elkins Manor Assoc. v. Eleanor Concrete*, 396 S.E.2d 463, 468 (W. Va. 1990) (citations omitted) (internal quotation marks omitted).
- ²⁹ *Bowling v. Ansted Chrysler-Plymouth-Dodge, Inc.*, 425 S.E.2d 144, Syl. Pt. 4 (W.Va. 1992); see also *Capper v. Gates*, 454 S.E.2d 54, 64-65 (W. Va. 1994). But cf. *Boyd v. Goffoli*, 608 S.E.2d 169, 186 (W.Va. 2004) (noting that the decision to award attorneys’ fees lies in the sound discretion of the circuit court).
- ³⁰ *Kentucky Fried Chicken of Morgantown, Inc. v. Sellaro*, 214 S.E.2d 823 (W.Va. 1975); see also *Desco Corp. v. Harry W. Trushel Const. Co.*, 413 S.E. 2d 85, 89 (W. Va. 1991).
- ³¹ *Stonebraker v. Zinn*, 286 S.E.2d 911, 64-65 (W.Va. 1982); *Charleston Lumber Company v. Friedman*, 61 S.E. 815 (W.Va. 1908).
- ³² *Aikens v. Debow*, 541 S.E.2d 576 (W. Va. 2000); see, e.g., *White v. AAMG Const. Lending Ctr.*, 700 S.E.2d 791, 798-800 (W. Va. 2010) (discussing what constitutes a special relationship).
- ³³ *Aikens*, 541 S.E..2d at 589.
- ³⁴ *Id.*
- ³⁵ *Id.*

³⁶ *Id.*; *see id.* at 589-90 (indicating that contractual privity is sufficient, but not necessary for establishing an “intimate nexus”).

³⁷ *But cf. Mid-State Surety Corp. v. Thrasher*, No. 2:04-0813, 2006 WL 1390430 (S.D. W. Va. May 16, 2006.) (finding that a special relationship existed between a surety and an engineering company).

³⁸ *Eastern Steel Constructors, Inc. v. City of Salem*, 549 S.E.2d 266, 275 (W. Va. 2001).

³⁹ *White v. AAMG Const. Lending Ctr.*, 700 S.E.2d 791 (W. Va. 2010); *Glascocock v. City Nat’l Bank of W. Va.*, 576 S.E.2d 540 (W. Va. 2002).

⁴⁰ *See Eastern Steel*, 549 S.E.2s at 275 (“[A] design professional . . . owes a duty of care to a contractor, who has been employed by the same project owner as the design professional and who has relied on the design professional’s work product in carrying out . . . obligations. . . due to the special relationship that exists between the two.”).

⁴¹ *Glascocock*, 576 S.E.2d at 547. *Compare id.* (noting “that the bank was significantly involved in the construction of the Glascocock home—it disbursed funds only on the presentation of bills or receipts and requested an inspection report), *with White*, 700 S.E.2d at 800 (determining that a special relationship did not exist between a lending bank and a borrowing owner of a new house when there was no evidence that the Bank “independently inspected the plaintiff’s new home”).

⁴² *Capper v. Gates*, 454 S.E.2d 54, Syl.Pt. 3 (W.Va. 1994).

⁴³ W. Va. Code § 56-6-31

⁴⁴ *Berry v. Nationwide Mut. Fire Ins. Co.*, 381 S.E.2d 367 (W.Va. 1989).

⁴⁵ *Rowe v. Sisters of Pallottine Missionary Society*, 560 S.E.2d 491, 496 (W. Va. 2001) (citing *Bradley v. Appalachian Power Co.*, 256 S.E.2d 879, 885–86 (W. Va. 1979)).

⁴⁶ W. Va. Code § 29-3-16a(l).

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I. MECHANIC'S LIEN BASICS

In Wisconsin, the term “mechanic’s lien” actually refers to a narrow category of liens applicable to “mechanics” and keepers of a garage or shop.¹ Construction liens are governed by Chapter 779 of the Wisconsin Statutes.

Wisconsin’s lien laws are remedial in nature, and therefore are liberally construed.² However, a lien claimant must strictly adhere to the procedural requirements, or lose lien rights.³

A. Requirements

1. Pre-Lien Notice

In Wisconsin, there are differences in the pre-lien notice requirements which are dependent upon whether the project is a private small project, private large project, private bonded project or public works project. Pursuant to Wis. Stat. § 779.02(1)(c), a project is large “where more than 4 family living units are to be provided or added by such work of improvement, if the improvement is wholly residential in character, or in any case where the improvement is partly or wholly nonresidential in character.” Thus, the construction pertains to a private small project if four family units or less are to be provided or added, the improvement is wholly residential in character, and the project is not a public one as provided in the statutes.

Lien rights will exist only for work related to “improvements” as defined under Wis. Stat. § 779.01(2)(a), and then only if the contractor, subcontractor or supplier complies with the applicable notice and claim procedures.

On private small projects, in order to perfect lien rights, a contractor must (if not already provided in a written contract) provide the owner the notice set forth in Wis. Stat. § 779.02(2) within ten (10) days after first furnishing labor or materials. This notice (whether separately given or included in a written contract) is required to be in at least 8-point bold type, if printed, or in capital letters, if typewritten. The notice notifies the owner of the potential lien rights of “those who either contract directly with the owner or those who give the owner notice within 60

days after they first perform, furnish, or procure labor, services, materials, plans or specifications for the construction.” This ten-day notice is not required to be given on private large projects.⁴

On private small projects, subcontractors, other than those excluded by statute, are required to give a notice to the owner within 60 days after first furnishing labor or materials, again following statutorily prescribed procedures. This 60-day notice is not required to be given on private large projects.

A late notice will still be effective to protect labor and materials furnished after the date of the late notice.⁵

As noted above, the ten-day and 60-day notices are not required on private large projects. However, Wisconsin has a 30-day notice requirement that applies to both private small and large projects. Wis. Stat. § 779.06(2) states that “[n]o lien claim may be filed or action brought thereon unless, at least 30 days before timely filing of the lien claim, the lien claimant serves on the owner a written notice of intent to file a lien claim.” This notice is required to briefly state the “nature of the claim, its amount and the land and improvement to which it relates.” As discussed below, since this 30-day notice is required to be provided prior to the filing of a lien claim (and since lien claims must be filed within six months of the last performance of work), this notice must be given within five months of the last performance of work.

Lien rights arise against the bond provided by the prime contractor on public projects.⁶ However, bond coverage is more restricted than that available on private projects. Second-tier subcontractors and suppliers are not covered by the public project bond.

2. Notice Filing Requirements

Under Wis. Stat. § 779.06(1), a lien claim must be filed within six months of the date that the lien claimant last performed work on the project. A lien claim is to be “filed in the office of the clerk of circuit court of the county in which the lands affected by the lien lie.” The claim must include a copy of the 30-day notice referred to above. The determination of when last labor or materials is furnished can be critical to lien effectiveness. Repair and call back work is not considered for purposes of determining the date of last work.⁷ The owner must be served with a copy of the lien claim within 30 days after filing of the claim.⁸

B. Enforcement and Foreclosure

1. Foreclosure

Pursuant to Wis. Stat. § 779.06(1), in order to foreclose on a lien claim, an action must be commenced against the owner within two years from the date of filing the claim for lien. Wis. Stat. § 779.09 provides that Chapter 846 of the Wisconsin Statutes controls the foreclosure of liens. Chapter 846 deals with mortgage foreclosures. Pursuant to Wis. Stat. § 779.09, all persons having filed claims for liens may join as plaintiffs, and if they do not join, they may be joined as defendants. If a contractor fails to provide a satisfaction of lien when required, it is liable for one-half the amount claimed in the lien.⁹ Filing a false, sham or frivolous lien claim can constitute slander of title under Wis. Stat. § 706.13.

2. Sale

All sales pertaining to judgments obtained in lien foreclosure actions shall be “noticed, conducted and reported in the manner provided for the sale of real estate upon execution and shall be absolute and without redemption.”¹⁰ Pursuant to Wis. Stat. § 779.11, if the sum realized from the sale is insufficient after paying the costs of the action and the costs of making the sale to pay the liens in full, they are to be paid proportionately among the several lien claimants.

C. Ability to Waive and Limitations on Lien Rights

Pursuant to Wis. Stat. § 779.135(1) a provision requiring any person entitled to a construction lien to waive such lien or to claim against a payment bond before being paid for labor, services or materials is void.

II. STATUTES OF LIMITATIONS AND REPOSE

A. Statute of Limitations and Limitations on Application of Statutes

The statute of limitations for contract actions in Wisconsin is six years after the cause of action accrues.¹¹ However, the statute of limitations for claims for salary, wages or other compensation for personal services is two years.¹²

The “discovery rule,” generally applicable to tort claims in Wisconsin, has been expressly rejected for contract claims, regardless of whether the cause of action is extinguished before the claimant is aware of the damage.¹³ In so holding, the Wisconsin Supreme Court noted that contract breaches may sometimes be latent and undetectable. In *CLL Associates*, the Court also rejected the plaintiff’s constitutional due process challenge.

The statute of limitations for negligence actions is six years for damage to property (real or personal),¹⁴ and three years for damages for personal injuries (physical or emotional) or wrongful death.¹⁵

B. Statute of Repose and Limitations on Application of Statutes

Prior to 1961, Wisconsin had a six year accrual statute of limitations, where the accrual did not start until the date of property damage.¹⁶ A statute of repose was then enacted, cutting off claims six years after the construction was completed -- except for claims against owners.¹⁷ This statute was declared unconstitutional on equal protection grounds in 1975.¹⁸ A new statute of repose was enacted in 1976 which, as a result of case law applying it only prospectively, created a gap in applicable limitation periods.¹⁹

Ultimately, a hybrid of an accrual and repose statute was enacted in 1994, effective April 29, 1994.²⁰ Wis. Stat. § 893.89 creates a 10 year “exposure period,” which begins to run on the date of substantial completion. The accrual component of the statute provides that where a claimant sustains damages during the period between eight and ten years after substantial completion, the time for commencing an action is extended for three years after the date on which the damages occurred. Thus, under the statute, there is an absolute 13 year cut off for commencement of suit following substantial completion. This law applies to material suppliers,

as well, although it does not cut off longer warranty periods and does not apply to contribution claims

Notwithstanding the above provisions, a claimant may not be able to take advantage of the statute of repose if a shorter statute of limitations applies. Under Wis. Stat. § 893.89(3), if the claimant sustains damages as the result of a construction defect, and the statute of limitations applicable to the damages bars commencement of the cause of action before the end of the ten year exposure period, the statute of limitations applicable to the damages applies.

Wis. Stat. § 893.89(4) provides certain exceptions to the repose statute. Pursuant to the exceptions, the statute does not apply to:

- (a) A person who commits fraud, concealment or misrepresentation related to a deficiency or defect in the improvement to real property.
- (b) A person who expressly warrants or guarantees the improvement to real property, for the period of that warranty or guarantee.
- (c) An owner or occupier of real property for damages resulting from negligence in the maintenance, operation or inspection of an improvement to real property.
- (d) Damages that were sustained before April 29, 1994.

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

Wis. Stat. § 895.07(2) provides notice requirements and an opportunity to repair “construction defects” primarily with respect to dwellings. Pursuant to the statute, the term “construction defects” refers to a defect in a warranty provided by a contractor or supplier to a consumer, or deficiencies in the construction or remodeling of a dwelling resulting from: 1) defective material; 2) violation of applicable codes; or 3) failure to follow accepted trade standards.

Under the statute, a claimant is required to give written notice to the contractor at least 90 working days before commencing an action. The notice must provide a description of the claimed defect and an opportunity to repair or remedy the alleged construction defect.

Within 15 working days after a claimant serves the notice of claim, or within 25 working days if a contractor makes a claim for contribution from a supplier, the contractor must serve on the claimant a written offer to repair or remedy the construction defect at no cost to the claimant, a written offer to settle the claim by monetary payment, a written offer including a combination of repairs and monetary payment, or a statement that the contractor rejects the claim, stating the reasons for rejecting the claim, and a comprehensive description of the evidence which substantiates the reason for rejecting the claim.²¹ As an alternative, the contractor may provide a proposal for inspection of the dwelling. Detailed procedures for the proposal for inspection are spelled out in the statute.

IV. INSURANCE COVERAGE AND ALLOCATION ISSUES

A. General Coverage Issues

Under Wisconsin law, a breach of contract may be an “occurrence” or “accident” under a CGL policy.²² Thus, the mere fact that a claim against a contractor arises in contract, rather than tort, does not preclude CGL coverage. However, “faulty workmanship” performed under the contract is generally not considered an accident, and therefore claims that allege damages arising solely due to faulty workmanship are typically found not to constitute an “occurrence” for purposes of CGL coverage.²³ Thus, to constitute an “occurrence,” courts have generally held that the faulty workmanship must cause some accidental—i.e., unintended and unanticipated—damage to property other than the property that was the subject of the faulty work.

In *American Family Mut. Ins. Co. v. American Girl, Inc.*, the Wisconsin Supreme Court addressed a number of the insurance issues most common in construction litigation. The defendant was a general contractor, who hired a soil engineering subcontractor to analyze the soil conditions for construction of a warehouse. The soil engineer gave faulty site preparation advice, which resulted in excessive settlement of the soil, causing cracking and buckling of the warehouse foundation, ultimately requiring it to be torn down. The insurer denied coverage on the grounds that the claim did not allege an “occurrence,” and that coverage was excluded under the “business risk” exclusions. The court first found that the claim, though sounding in breach of contract, alleged an occurrence—namely, the unexpected settling of soil caused by the faulty site preparation advice. The Court further concluded that the economic loss doctrine did not preclude coverage, holding that the economic loss doctrine does not determine insurance coverage, which instead turns on policy language.

The Court then addressed a number of exclusions in the CGL policy. The Court rejected the insurance company’s argument that the “contractually-assumed liability” exclusion applied, holding the exclusion does not exclude coverage for all breach of contract liability. Instead it excludes coverage for liability that arises because the insured has contractually assumed the liability of another, as in an indemnification or hold-harmless agreement, neither of which was present in the *American Girl* case. Ultimately, the Court concluded that the property damage would be excluded under the “your work” exclusion. However, because the policy contained a subcontractor exception, and the property damage arose out of the work of the subcontractor soil engineer, the exclusion did not apply, and the policy provided coverage for the claim against the general contractor.

B. Trigger of Coverage

Wisconsin follows the continuous trigger theory. Under this theory, occurrences during multiple policy periods are deemed to have occurred continuously, so that each of the various policies in effect is triggered.²⁴

C. Allocation Among Insurers

Although not specifically decided, Wisconsin courts would likely apply generally accepted insurance law principles in a dispute involving competing insurers. Where an insured has more than one insurer (i.e., a primary insurer and a secondary/excess insurer), the primary

insurer has the sole obligation to provide the defense for the insured (absent a contract to the contrary between the two insurers). *See Loy v. Bunderson*.²⁵ *Loy* stands for the proposition that the duty to defend is personal to each insurer, and a carrier is not entitled to divide the duty or require contribution from another absent a specific contractual right. This same rule appears to apply to the allocation of damages. Absent a written contract that specifically sets forth the allocation between the insurers, damages would be apportioned in accordance with the provisions of the respective insurance policies.²⁶

V. CONTRACTUAL INDEMNIFICATION

Indemnity provisions under Wisconsin law are construed differently, depending upon whether indemnification is being sought for the indemnitor's or indemnitee's negligence. Such agreements will be broadly construed for the indemnitor's negligence and strictly construed for coverage of the indemnitee's negligence.²⁷

In Wisconsin, contracts providing for indemnification of the indemnitee's negligence are valid and are not contrary to public policy.²⁸ However, under the strict construction standard, an indemnitee's negligence will only be covered if the contract unequivocally so states.²⁹ One exception to this rule is when it is clear that the purpose and intent of the parties in entering into the contract was for no reason other than to cover the indemnitee's negligence.³⁰

VI. CONTINGENT PAYMENT AGREEMENTS

Wis. Stat. § 779.135(3) renders void:

Provisions making a payment to a prime contractor from any person who does not have a contractual agreement with the subcontractor, supplier, or service provider a condition precedent to a prime contractor's payment to a subcontractor, supplier, or service provider.

However, Wis. Stat. § 779.135(3) does not prohibit contract provisions that may delay a payment to a subcontractor until the prime contractor receives payment from any person who does not have a contractual agreement with the subcontractor, supplier, or service provider.

In essence, § 779.135(3) prohibits "pay if paid," clauses but permits "pay when paid" clauses. Whereas "pay if paid" clauses operate to shift the risk of non-payment from the prime contractor to the subcontractor, "pay when paid" clauses do not allow a prime contractor to avoid an obligation to pay the subcontractor, but allow a reasonable time for payment.

Because § 779.135(3) prohibits "pay if paid" clauses, courts will not interpret a "pay when paid" clause to yield the illegal result of making the obligation to pay dependent upon the satisfaction of a condition precedent. Instead, a court will interpret a "pay when paid" clause to require payment within a reasonable time. The language of a contract establishing the terms of payment does not create or cancel the language of the contract establishing the obligation of payment." *Patti v. Western Machine Co.*³¹

VII. DAMAGES LIMITATIONS

A. Personal Injury Damages vs. Construction Defect Damages

Wis. Stat. § 895.447 makes void as against public policy any provision limiting tort liability in any contract relating to the construction, alteration, repair or maintenance of a building or other work relating to construction.

Wisconsin's Safe Place Statute, Wis. Stat. § 101.11, obligates employers and owners of places of employment or public buildings to furnish a safe place for "employees therein and frequenters thereof" The statute imposes a heightened standard of care.

B. Attorneys' Fees Shifting and Limitations on Recovery

Attorneys' fees are generally not available in construction contract cases unless provided for by the parties.

C. Consequential Damages

In Wisconsin, the general rule pertaining to the award of damages for defects in the performance of a construction contract is that the party is entitled to what it contracted for.³² In this regard, Wisconsin applies the "cost-of-correction" rule which requires the contractor to correct the defect or supply what was omitted.³³ As an alternative, if the cost of correcting the defect or supplying the omitted item would result in unreasonable economic waste, then Wisconsin courts will apply the diminished value rule.³⁴ Economic waste would generally be considered to occur if the cost of correcting the defect is disproportionate to the defect.

Wisconsin Jury Instruction – Civil 3710 specifically allows for recovery of consequential damages. It reads as follows:

The law provides that a person who has been damaged by a breach of contract shall be fairly and reasonably compensated for his or her loss. In determining the damages, if any, you will allow an amount that will reasonably compensate the injured person for all losses that are the natural and probable results of the breach.

In *Magestro v. North Star Environmental Construction*,³⁵ the Court rejected the argument that consequential damages are not allowed in a breach of contract action unless the parties specifically contract for such damages. Consequential damages are a permitted type of damages and no specific contract clause is required to provide for the recovery of such damages. However, the parties may agree to limit or preclude consequential damages in the construction contract.

D. Delay and Disruption Damages

Delay and disruption occurring in the context of a construction contract provide the basis for the recovery of damages consistent with Wisconsin Jury Instruction – Civil 3710 cited above.

E. Economic Loss Doctrine

The economic loss doctrine has been the subject of substantial attention by Wisconsin courts. In the case of *1325 North Van Buren LLC v. T-3 Group, Ltd.*,³⁶ the Wisconsin Supreme Court held that the economic loss rule barred tort claims arising out of a contract to renovate a building and turn it into condominiums. In so holding, the Wisconsin Supreme Court overturned the ruling of the Court of Appeals. The Court of Appeals had held that the project owner was not limited to pursuing contract claims in its litigation against a construction manager, and could therefore pursue tort claims for negligence and misrepresentation when the construction manager failed to complete the project on schedule. In *T-3 Group, Ltd.*, the Wisconsin Supreme Court determined that the contract was not primarily for services, since the purpose of the contract was to provide a condominium complex rather than to provide construction management services. Therefore, the Court concluded the contract was subject to the economic loss doctrine and the owner could only recover contract damages.

The Wisconsin Supreme Court also addressed the economic loss doctrine in the context of a construction contract case in *Linden v. Cascade Stone Co.*³⁷ In that case, the Court set forth a number of factors to be used in determining whether a mixed contract for products and services is predominantly a sale of a product (and therefore subject to the economic loss doctrine) or whether it is predominantly a contract for services (and thus beyond the reach of the economic loss doctrine). According to the Court, those factors are: the language of the contract, the nature of the business of the supplier, the intrinsic worth of the materials, the circumstances of the parties, and the primary objective of the contract.³⁸

F. Interest

Prejudgment interest is recoverable at the rate of five percent (5%) per year. Wis. Stat. § 138.04. Post-judgment interest is recovered at the rate of 1 per cent plus the prime rate in effect on January 1 of the year in which the judgment is entered if the judgment is entered on or before June 30 of that year. If the judgment is entered after June 30, interest is calculated at 1 per cent plus the prime rate in effect on July 1 of that year.³⁹

Whether prejudgment interest is recoverable is a question of law. Prejudgment interest is available when damages are fixed and determinable or may be measured according to a reasonably certain standard.⁴⁰

G. Punitive Damages

Punitive damages may be recovered in Wisconsin in appropriate cases. In *Wischer v. Mitsubishi Heavy Industries America, Inc.*,⁴⁰ also known as the “Miller Park” case, the Wisconsin Supreme Court held that Wisconsin’s punitive damage statute (Wis. Stat. § 895.85(3)) requires a showing that the defendant acted maliciously to the plaintiff or intentionally disregarded the rights of the plaintiff, not that the defendant intended to injure the plaintiff.

In *Brown v. Maxey*,⁴¹ the Court held that the term “damages” in insurance policies included punitive damages in Wisconsin.

H. Other Damage Limitations

Wisconsin follows the general rule as expressed in the Restatement (Second) of Contract § 351(1) (1979) with respect to liquidated damages. Liquidated damages provisions will only be enforced if the amount is reasonable in light of the expected or actual loss caused by the breach and the difficulties of proving the loss.

In wrongful death actions, Wis. Stat. § 895.04(4) limits non-pecuniary damages for loss of society and companionship to \$500,000 per occurrence in the case of a deceased minor, and \$350,000 in the case of a deceased adult.

VIII. CASE LAW AND LEGISLATION UPDATE

There are no particularly significant developments to report. However, the Wisconsin Court of Appeals recently issued an opinion addressing and clarifying two legal issues common to construction disputes—the statute of limitations/repose and the economic loss rule. *See Kalahari Development, LLC v. Iconica, Inc.*, 2012 WI App. 34, 340 Wis. 2d 454, 811 N.W.2d 825. In that case, Kalahari entered into a design-build contract with Iconica to construct a water park resort, and, in connection with the construction, to provide certain architectural and engineering services. The project was substantially complete on May 4, 2000. In May 2008, Kalahari began to observe water damage, which was later found to be due to “defectively designed and or defectively installed vapor barriers.” *Id.*, ¶ 3. On April 23, 2010, almost ten years after substantial completion, Kalahari filed suit against Iconica alleging two causes of action: one for breach of contract and one for professional negligence related to Iconica’s performance of its design services under the contract. *Id.*

Iconica moved to dismiss the breach of contract claim based on the six year limitations period for contracts, set forth in Wis. Stat. § 893.43. Kalahari argued that since the water damage was not discovered until 2008, the ten year “exposure period” under the statute of repose extended the time for filing. *See* Wis. Stat. § 893.89 (2). The court noted, however, that § 893.89 only applies to “lawsuits that are not otherwise time-barred within ten years after substantial completion.” *Id.*, ¶ 6. Wis. Stat. § 893.89(3) specifically states that “if the statute of limitations applicable to the damages bars commencement of the cause of action before the end of the exposure period, the statute of limitations applicable to the damages applies.” Thus, “when an action is one for contract damages, Wis. Stat. § 893.89(3)(a) directs that its ten-year time limit be compared with the time limit applicable to the contract action to see which is shorter, and that the shorter limit applies.” *Id.*, ¶11. Because Kalahari’s contract claim was subject to the six year statute applicable to contracts, the statute of repose under § 893.89 did not apply, and the claim was properly dismissed.

Iconica also argued that Kalahari’s claims were barred by the economic loss doctrine. *Id.*, ¶ 23. Under Wisconsin law, when a contract covers both products and services, the economic loss doctrine bars negligence claims if the predominant purpose of the contract is to provide a product. *Id.* Kalahari argued that the predominant purpose of the contract was to provide design services. In the alternative, Kalahari argued the predominant purpose test does not apply to claims based on *professional* negligence. *Id.*, ¶24. The Court rejected both arguments. The court held that Kalahari contracted for primarily for a product—a water park

resort and convention center—not for design or construction services. *Id.*, ¶ 32. Similarly, the court held the economic loss rule is applicable to professional negligence claims if the predominant purpose of the contract with the professional was for a product, rather than a service. *Id.*, ¶ 36.

¹ Wis. Stat. § 779.41.

² *Builder's Lumber Co. v. Stuart*, 6 Wis. 2d 356, 361, 94 N.W.2d 630, 632 (1959).

³ *Goebel v. National Exchangers, Inc.*, 88 Wis. 2d 596, 277 N.W.2d 755 (1979).

⁴ Wis. Stat. § 779.02(1)(c).

⁵ Wis. Stat. § 779.02(3).

⁶ Wis. Stat. § 779.15.

⁷ *Tym v. Ludwig*, 196 Wis. 2d 375, 387, 538 N.W.2d 600, 604 (Ct. App. 1995).

⁸ Wis. Stat. § 779.06(1).

⁹ Wis. Stat. § 779.13.

¹⁰ Wis. Stat. § 779.12(1).

¹¹ Wis. Stat. § 893.43.

¹² Wis. Stat. § 893.44.

¹³ *CLL Assocs. Ltd. P'ship v. Arrowhead Pac. Corp.*, 174 Wis. 2d 604, 497 N.W.2d 115 (1993).

¹⁴ Wis. Stat. § 893.52.

¹⁵ Wis. Stat. § 893.54.

¹⁶ *School Dist. v. Kunz*, 249 Wis. 2d 272, 24 N.W.2d 598 (1946).

¹⁷ Wis. Stat. § 893.155 (1975-76).

¹⁸ *Kallas Millwork Corp. v. Square D Co.*, 66 Wis. 2d 382, 225 N.W.2d 454 (1975).

¹⁹ *United States Fire Ins. Co. v. E.D. Wesley Co.*, 105 Wis. 2d 305, 313 N.W.2d 833 (1982).

²⁰ Wis. Stat. § 893.89.

²¹ Wis. Stat. § 895.07(2)(b).

²² *See American Family Mut. Ins. Co. v. American Girl, Inc.*, 2004 WI 2, 268 Wis. 2d 16, 673 N.W.2d 65.

²³ *See, e.g., Kalchthaler v. Keller Constr. Co.*, 224 Wis. 2d 387, 395, 591 N.W.2d 169 (Ct. App. 1999) (“a CGL policy does not cover faulty workmanship, only faulty workmanship that causes damage to other property”); *see also Bulen v. West Bend Mut. Ins. Co.*, 125 Wis. 2d 259, 265, 371 N.W.2d 392 (Ct. App. 1985) (“The policy in question . . . does not cover an accident of faulty workmanship, but rather faulty workmanship which causes an accident.”)

²⁴ *Id.*

²⁵ *See Loy v. Bunderson*, 107 Wis. 2d 400, 427 (1982).

²⁶ *Davis v. Allied Processors, Inc.*, 214 Wis. 2d 294 (Ct. App. 1997) (Where the underlying policy covers punitive damages but the umbrella policy does not, the underlying payout cannot be structured so that the umbrella carrier has to pay more in compensatory damages.)

²⁷ *Barrons v. J.H. Findorff & Sons, Inc.*, 89 Wis. 2d 444, 452, 278 N.W.2d 827, 831 (1979).

²⁸ *Mikula v. Miller Brewing Co.*, 2005 WI App. 92, 281 Wis. 2d 712, 701 N.W.2d 613; *Herchelroth v. Mahar*, 36 Wis. 2d 140, 153 N.W.2d 6 (1967).

²⁹ *Spivey v. Great Atlantic & Pacific Tea Co.*, 79 Wis. 2d 58, 64-65, 255 N.W.2d 469, 472-3 (1977); *Bialas v. Portage County*, 70 Wis. 2d 910, 236 N.W.2d 18 (1975); *Mustas v. Inland Const., Inc.*, 19 Wis. 2d 194, 120 N.W.2d 95 (1963).

³⁰ *Hastreiter v. Karau Bldgs., Inc.*, 57 Wis. 2d 746, 205 N.W.2d 162 (1973).

³¹ *Patti v. Western Machine Co.*, 72 Wis. 2d 348, 353 (Wis. 1976).

³² *See Jacob v. West Bend Mut. Ins. Co.*, 203 Wis. 2d 524, 553 N.W.2d 800 (Ct. App. 1996).

³³ *W.G. Slugg Seed & Fertilizer, Inc. v. Paulsen Lumber, Inc.* 62 Wis. 2d 220, 214 N.W.2d 413 (1974).

³⁴ *Id.*

³⁵ 2002 WI App. 182, 256 Wis. 2d 744, 649 N.W.2d 722.

³⁶ 2006 WI 94, 293 Wis. 2d 410, 716 N.W.2d 822.

³⁷ 2005 WI 113, 283 Wis. 2d 606, 699 N.W.2d 189.

³⁸ *Id.*

³⁹ Wis. Stat. § 815.05(8), Wis. Stat. § 814.04(4) and Wis. Stat. § 815.05(8).

⁴⁰ *Loehrke v. Wanta Builders, Inc.*, 151 Wis. 2d 695, 445 N.W.2d 717 (Ct. App. 1989).

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I. MECHANIC'S LIEN BASICS

Persons Entitled to Liens: “[e]very contractor, subcontractor or materialman performing any work on or furnishing any materials for any building or any improvement upon real property shall have for his work done or plans or materials furnished a lien upon the building or improvements, and upon the real property of the owner on which they are situated to the extent of one (1) acre. If the improvements cover more than one (1) acre the lien shall extend to all the additional real property covered thereby.” Wyo. Stat. Ann. § 29-2-101. To have a lien the work or materials shall be furnished under a contract. *Id.* If the land subject to a lien is within a city, town, or subdivision, the lien will also include the lot. *Id.* Any lien properly perfected shall extend to the entire interest of the owner. Wyo. Stat. Ann. § 29-2-102.

A. REQUIREMENTS

Perfection of a Lien: For a lien to be perfected and enforceable, the following statutorily mandated steps must be taken:

1. In order to perfect the right to file a construction lien, the following preliminary notice requirements apply:
 - (i) The contractor, subcontractor and materialman shall send written notice to the record owner or his agent, of the right to assert a lien against the property for which services or materials are provided if the contractor, subcontractor or materialman is not paid, and the right of the owner or contractor to obtain a lien waiver upon payment for services or materials. Each subcontractor and materialman shall provide a copy of the written notice to the contractor for which the subcontractor or materialman is providing services or materials;
 - (ii) Any notice required under this section shall be sent:
 - (A) By the contractor prior to receiving any payment from owner, including advances;
 - (B) By the subcontractor or materialman within thirty (30) days

after first providing services or materials to the construction project.
(iii) Failure to send the notice required under this section within the time specified shall bar the right of a contractor, subcontractor or materialman to assert a lien;

Wyo. Stat. Ann. § 29-2-1 12.

The notice must be in the same format and contain the same information as the notice contained in Wyo. Stat. Ann. § 29-10-101. The notice forms are required by statute to be available at the county clerk's office of each county. *Id.*

2. Anyone wishing to file a lien must first give twenty (20) days notice to the owner (or his agent) in writing of any claim against real property, a building or improvement, stating the amount of the claim and from whom it is due. Wyo. Stat. Ann. § 29-2-107. The notice must be in the same format and contain the same information as the notice form specified in Wyo. Stat. Ann. 29-10-102. The notice forms are required by statute to be available at the county clerk's office of each county. *Id.*

3. A contractor must file a lien statement, sworn before a notary public, with the county clerk within one hundred fifty (150) days after the last day that work was performed or materials were furnished, or from the date the work was substantially completed or materials substantially furnished, whichever is earlier. Any other person, including subcontractors, must file within one-hundred twenty (120) days after the last day that the contractor directed the individual to perform work or furnish materials. The record owner of the property may record a notice of substantial completion of the project with the county clerk in the county where the project is located. The date of that filing will be presumed to be the date of substantial completion. Wyo. Stat. Ann. § 29-2-106.

4. The lien statement must include the following information, pursuant to Wyo. Stat. Ann. § 29-1-312:

- (i) The name and address of the lien claimant;
- (ii) The amount claimed to be due and owing;
- (iii) The name and address of the record owner against whose property the lien is filed;
- (iv) An itemized list setting forth and describing materials delivered or work performed;
- (v) The name of the person whom the lien claimant alleges is contractually responsible to pay the debt secured by the lien,
- (vi) The date when labor was last performed or services were last rendered or the date of substantial completion of the project;
- (vii) The legal description of the premises where the materials were furnished or upon which the work was performed; and
- (viii) A copy of the contract, if available, or a summary of the lien claimant's contract together with a statement of the location where a copy of the contract, if written, can be obtained.

The lien statement must be in the same format and contain the same information as the form specified in Wyo. Stat. Ann. 29-10-104. The lien statement forms are required by statute to be available at the county clerk's office of each county. *Id.* The recording fee may be assessed as costs in any action to foreclose the lien. Notice must be sent by the lien claimant to the last record owner or his agent in the case of a real property lien within thirty (30) days after the lien statement is filed. The notice shall be in substantially the same format and contain the same information as the form of notice specified in W. S. 29-10-103. The notice forms are required by statute to be available at the county clerk's office of each county. *Id.* All work performed or materials furnished by a lien claimant shall be considered as having been done under the same contract unless more than one hundred eighty (180) days elapse from the date of the performance of any work or the furnishing of any materials and the date when work or materials are next performed or furnished by the lien claimant. Wyo. Stat. Ann. § 29-1-403.

B. ENFORCEMENT OF LIENS

A perfected lien will apply to the "entire interest of the owner." Wyo. Stat. Ann. § 29-2-102. Anyone seeking to enforce a lien is entitled to the right of a judicial sale of the building or improvements; however, if the land upon which an improvement lies would be in substantially the same condition as before the improvement was made, the court may authorize the removal of the improvement, with the party removing the improvement entitled to the reasonable costs associated with removal. Wyo. Stat. Ann. § 29-2-103, 104. A contractor is statutorily required to defend any action initiated by his employee, subcontractor, suppliers, or his subcontractor's employees or suppliers, at the contractor's expense. Furthermore, the owner is entitled to withhold payment to the contractor for the amount of the lien and, if judgment is rendered against the owner, the owner may either deduct the amount of the judgment and costs from any amounts due to the contractor, or recover the amount of the judgment and costs from the contractor, if the owner has already paid the contractor in full. Wyo. Stat. Ann. § 29-2-108. Any action to foreclose on or enforce a lien must be commenced within one hundred eighty (180) days after the filing of the lien statement. After one hundred eighty (180) days have passed since the filing of the lien statement, if no action to foreclose has been initiated, the lien will cease to exist. Wyo. Stat. Ann. § 29-2-109.

1. Priority of Liens:

Liens perfected under Title 29 of the Wyoming Statutes are "on an equal footing without reference to the date of the filing of the lien statement." A perfected lien attaches to the real property, fixtures, materials, machinery or supplies furnished and improvements made in preference to any subsequent lien, security interest or mortgage under any other provision of law which has been perfected upon real or personal property, including a leasehold interest, against which the lien is claimed. Any lien, security interest or mortgage which has been perfected upon real or personal property or upon a leasehold interest prior to the commencement of any construction work or repair of the premises or property shall have priority except as provided by Chapter 7 of this act or W.S. § 29-8-102. If the property is sold due to a foreclosure, and the proceeds are not sufficient to pay all lienholders in full, the proceeds will be prorated according to the amounts of the lienholders' respective claims. Wyo. Stat. Ann. § 29-1-402. The holder of

any prior perfected lien upon the real property is entitled to notice in suits to foreclose the lien; however, a foreclosure proceeding will not be rendered invalid by failure to give the notice required. Wyo. Stat. Ann. § 29-1-404 (West).

2. Satisfaction of Lien:

a. Generally: Wyo. Stat. Ann. § 29-1-313 and § 29-1-314 requires a notice of satisfaction of the lien statement to be filed in the office of the county clerk of any county in which the lien was filed, within thirty (30) days of the payment of any debt that was the subject of the lien. Failure of lien claimant to timely file a notice of satisfaction after receiving a request in writing by certified or registered mail will result in his liability for any actual damages, as well as one-tenth of one percent (.10%) of the original principal amount of the debt, but not to exceed \$100.00 per day, daily until the satisfaction is entered. In addition, the lien claimant must send a copy of the notice of satisfaction to the record owner within five days. Wyo. Stat. Ann. § 29-1-313 and § 29-1-314. The notice of satisfaction must be in the same format and contain the same information as the notice of satisfaction form in Wyo. Stat. Ann. 29-10-106. The notice forms are required by statute to be available at the county clerk's office of each county. *Id.*

b. Substitute Security to Satisfy Lien: A lien may also be satisfied if "the owner of the property, a contractor or subcontractor has deposited with the court having jurisdiction over the lien a corporate surety bond, letter of credit, cash or cash equivalent of established value approved by the court having jurisdiction over the lien claim in the county where the lien was filed in an amount equal to one and one-half times the amount of the lien." Wyo. Stat. Ann. § 29-1-501. The security must guarantee that "if the lien claimant is finally adjudged to be entitled to recover upon the lien, the principal or his sureties, jointly and severally, in the case of a bond, or the issuer of a letter of credit shall pay the claimant the amount of the judgment for at least the amount for which the lien was filed plus costs and attorneys' fees." *Id.* The bond may be filed with the clerk of the district court in the county in which the lien was filed, at any time prior to a final judgment on an action to foreclose the lien, and upon its filing, the lien shall be discharged and released in full; however, the lien claimant may bring an action upon the bond or undertaking within the time allowed for the commencement of foreclosure proceedings on the original lien. *Id.*

C. ABILITY TO WAIVE AND LIMITATION ON LIEN RIGHTS

The timing of filing a lien statement may be altered by an agreement between the parties to the contract, so long as the agreed upon time does not exceed twice the statutorily prescribed time. Any such agreement must be in writing, signed by all parties to the contract, acknowledged by a notary public, and filed and recorded with the county clerk. Any contract between the owner and contractor will not affect or restrict the right of an employee or subcontractor, who is not a party to the contract, to file a lien. Wyo. Stat. Ann. § 29-2-106.

False or Frivolous Liens: If a person whose property is subject to a recorded lien, believes the lien is invalid, forged, knowingly groundless at the time of filing, states a false claim, or contains a material misstatement, that person may petition the court having jurisdiction

over the lien, stating the grounds upon which relief is requested, and supporting the petition by the affidavit of the petitioner or his/her attorney setting forth a “concise statement of the facts upon which the motion is based.” Wyo. Stat. Ann. § 29-1-601(b). The court then may enter an order directing the claimant to appear six (6) to fifteen (15) days after the service of the petition, and show cause for why the relief requested should not be granted. The order must clearly state that if the claimant does not appear, the lien will be stricken and the claimant will be ordered to pay damages of at least \$1,000.00, or actual damages, whichever is greater, as well as the costs and attorney fees of the petitioner. In addition, if the court finds that the claim is invalid, was forged, knowingly groundless at the time of filing, states a false claim, or contains a material misstatement, the court will order the lien stricken, and award the petitioner damages of \$1,000.00, or actual damages, whichever is greater, plus costs and attorney fees. If, however, the court finds the lien to be valid, it will order costs and reasonable attorney fees to be paid to the claimant by the petitioner. *Id.*

II. STATUTES OF LIMITATION AND REPOSE

The following are relevant limitation periods under Wyoming law:

- A. Contracts for Sale under the UCC:** An action for breach of contract for sale must be commenced within four (4) years after the cause of action has accrued. By the original agreement, the parties may reduce the period of limitations to not less than one (1) year, but may not extend it. Wyo. Stat. Ann. § 34.1-2-725.
- B. Actions for Recovery of Real Property:** Ten (10) years after the cause of action accrues. Wyo. Stat. Ann. § 1-3-103.
- C. Actions Upon Written Contracts:** Ten (10) years. Wyo. Stat. Ann. § 1-3-105(a)(i).
- D. Actions on Contracts Not in Writing, Either Express or Implied:** Eight (8) years. Wyo. Stat. Ann. § 1-3-105(a)(ii)(A).
- E. Personal Injury Actions:** Four (4) years. Wyo. Stat. Ann. § 1-3-105(a)(iv)(C).
- F. Actions for Improvements to Real Property:** Wyo. Stat. Ann. § 1-3-111 states:
 - (a) Unless the parties to the contract agree otherwise, no action to recover damages, whether in tort, contract, indemnity or otherwise, shall be brought more than ten (10) years after substantial completion of an improvement to real property, against any person constructing, altering or repairing the improvement, manufacturing or furnishing materials incorporated in the improvement, or performing or furnishing services in the design, planning, surveying, supervision, observation or management of construction, or administration of construction contracts for:
 - (i) Any deficiency in the design, planning, supervision, construction, surveying, manufacturing or supplying of material or observation or management of

- construction;
- (ii) Injury to any property arising out of any deficiency listed in paragraph (i) of this subsection; or
- (iii) Injury to the person or wrongful death arising out of any deficiency listed in paragraph (i) of this subsection.
- (b) Notwithstanding the provisions of subsection (a) of this section, if an injury to property or person or an injury causing wrongful death occurs during the ninth year after substantial completion of the improvement to real property, an action to recover damages for the injury or wrongful death may be brought within one (1) year after the date on which the injury occurs.
- (c) This section shall not be construed to extend the period for bringing an action allowed by the laws of this state.

III. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

Wyoming has no requirements regarding pre-suit notice of claims for contract cases; however, the parties can agree to such terms by including them in the contract. *Scherer Const., LLC v. Hedquist Const., Inc.*, 18 P.3d 645 (Wyo. 2001). There are applicable notice requirements prior to filing a notice of lien and pre-foreclosure notice requirements, as discussed above in the “Mechanic’s Liens” section.

IV. COVERAGE AND ALLOCATION ISSUES

Commercial General Liability (a.k.a. Comprehensive General Liability, “CGL”) policies may cover certain tortious acts, but do not cover claims for breach of contract. In addition, claims regarding intentional or fraudulent acts, including misrepresentations or negligent misrepresentations which result in economic loss, are “deemed purposeful rather than accidental and therefore, are not covered under a CGL policy.” *Shoshone First Bank v. Pacific Employers Insurance Co.*, 2 P.3d 510, 516 (Wyo. 2000). Similarly, the act of conversion has been held to be outside CGL policies, because intentional acts, including conversion, are “impossible to define ... as an ‘accident,’ and, therefore, are not an ‘occurrence’ covered by the policy.” *Reisig v. Union Insurance Company*, 870 P.2d 1066 (Wyo. 1994). This is also grounded in public policy rationale; permitting coverage of intentional torts, such as conversion, may result in individuals approaching a situation with less trepidation, if their intentional actions will be covered by insurance. *Id.*

Wyoming has no law addressing trigger of coverage or allocation of risk among multiple insurers. Allocating of defense costs as to covered and non-covered claims between the insured and the insurer, however, is not permitted in Wyoming.

In summary, unless a policy between an insured and an insurer provides for allocation of defense costs in the instance in which some claims are covered and some are not, Wyoming will not allow allocation of defense

costs from the insurer to the insured. Because the insurer must defend the entire action, permitting allocation with respect to the representation on every claim in the action would lead to judicial inefficiency and a failure to resolve actions timely and consistently. With respect to the costs of prosecuting a counterclaim, unless the policy specifically provides coverage for those expenses, we will not amend the contract.

Shoshone First Bank v. Pacific Employers Insurance Co., 2 P.3d at 516.

V. CONTRACTUAL INDEMNIFICATION

Contractual provisions to indemnify are generally upheld by Wyoming courts, however they are not “looked upon with favor...and are to be strictly construed.” *Amoco Production Company v. EM Nominee Partnership Company*, 2 P.3d 534, 541 (Wyo. 2000) (Citations omitted). The *Amoco* Court held that “[i]f the indemnitee intends to make the indemnitor responsible for a fault in which the indemnitee shares, that goal must be expressed in clear and unequivocal terms beyond any peradventure of doubt.” *Id.* (Citations omitted). There are some statutory limitations to indemnity provisions. Indemnity provisions that indemnify against loss or liability from one’s own negligence in a contract relating to wells for oil, gas, or water, or mines for minerals, are void; however, indemnification for other than the indemnitee’s own negligence is not prohibited by the statute. *Hull v. Chevron U.S.A., Inc.*, 812 F.2d 590 (10th Cir. 1987). The relevant statute, Wyo. Stat. Ann. § 30-1-13 1, states:

- (a) All agreements, covenants promises contained in, collateral to or affecting any agreement pertaining to any well for oil, gas or water, or mine for any mineral, which purport to indemnify the indemnitee against loss or liability for damages for:
 - (i) Death or bodily injury to persons;
 - (ii) Injury to property; or
 - (iii) Any other loss, damage, or expense arising under either (i) or (ii) from:-
 - (A) The sole of concurrent negligence of the indemnitee or the agents or employees of the indemnitee or any independent contractor who is directly responsible to such indemnitee; or
 - (B) From any accident which occurs in operations carried on at the direction or under the supervision of the indemnitee or an employee or representative of the indemnitee or in accordance with methods and means specified by the indemnitee or employees or representatives of the indemnitee, are against public policy and are void and unenforceable to the extent that such contract of indemnity by its terms purports to relieve the indemnitee from the loss of liability for his own negligence. This provision shall not affect the validity of any insurance contract or any benefit

conferred by the Workers Compensation Law (§§ 27-14-101 through 27-14-805) of this state.

The Wyoming Supreme Court has noted, however, that this statute “restricts the freedom to contract, a common law right. Statutes, which preempt common law rights must be strictly construed.” *Union Pacific Resources Company v. Dolenc*, 86 P.3d 1287, 1293 (Wyo. 2004).

VI. CONTINGENT PAYMENT AGREEMENTS

Wyoming has no law addressing contingent payment agreements, other than attorney contingency fee agreements, which are outside the scope of this article.

VII. DAMAGES LIMITATIONS

Damages for breach of contract include compensatory and consequential damages. *JBC of Wyoming Corp. v. City of Cheyenne*, 843 P.2d 1190, 1195 (Wyo. 1992). “The general measure of damages for breach of contract is the amount that is sufficient to compensate the injured party for the loss which full performance of the contract would have prevented or the breach of it has entailed.” *Zitterkoof v. Roussalis*, 546 P.2d 436, 438 (Wyo.1976). The Wyoming Supreme Court has farther expanded this definition, stating:

[t]he damages awarded in an action for breach of contract are designed to put the plaintiff in the same position as if the contract had been performed, less proper deductions. This measure of damages includes recovery for incidental or consequential loss caused by the breach. In *Revosa v. Buhier*, 770 P.2d 235, 237-38 (Wyo.1989), we recognized the measure of damages for breach of contract set out in Restatement, Second, Contracts § 347 (1981): [s]ubject to the limitations stated in §§ 350-53, the injured party has a right to damages based on his expectation interest as measured by (a) the loss in the value to him of the other party’s performance caused by its failure or deficiency, plus (b) any other loss, including incidental or consequential loss, caused by the breach, less (c) any cost or other loss that he has avoided by not having to perform.

G.C.J., Inc. v. Haught, 7 P.3d 906 (Wyo. 2000).

The economic loss rule “bars recovery in tort when a plaintiff claims purely economic damages unaccompanied by physical injury to persons or property.” *Rissler & McMuny Co. v. Sheridan Area Water Supply Joint Powers Board*, 929 P.2d 1228, 1234-35 (Wyo. 1996). The purpose of the rule is “to maintain the distinction between those claims properly brought under contract theory and those which fall within tort principles.” *Id.*

Punitive damages for breach of contract are not recoverable. As stated by the Wyoming Supreme Court in *Waters v. Trenckmann*. Wyo., 503 P.2d 1187, 1190 (Wyo.1972), for punitive damages to be awarded “there would have to be conduct on the part of defendant amounting to aggravation, outrage, malice or willful and wanton misconduct. ...there must be evidence of

spite, ill will or willful and wanton misconduct at the inception of a fraudulent contract and that the remedy for wrongful acts occurring afterwards would be compensatory damages for breach of contract.” *U.S. Through Farmers Home Admin.v. Redland*, 695 P.2d 1031 (Wyo.1985) (Emphasis added).