

THE DISPUTE RESOLVER

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A View from the Field: Project Execution/Contracting Strategies Large and Complex Industrial Projects

This article presents George T. McLaughlin's "View from the Field" formed throughout the course of his 30+ year career in the industrial marketplace.¹ His article is broken into four parts. Part 1, published in April 2013, describes the evolution of the delivery systems in large and complex industrial projects (oil and gas, process, power, chemical and pharmaceutical). Part 2, published in May 2013, framed the issues facing the engineering and construction industry and lawyers that service those groups. This Part 3 highlights some impacts relative to engineering and construction claims and disputes. The remaining section (Part 4), which we will publish in our next newsletter, will discuss preventive and corrective processes.

Part 3 of 4 – Impact on Claims, Disputes, and Resolutions

Major changes in large and complex project execution strategies are creating new issues as these strategies are implemented; including with claims and disputes. For ease of discussion, the claims and disputes are organized in four groups (and discussed in order of frequency of occurrence). First, scope of work disputes represent the largest (around 75-90%). Following scope, are claims focused on delay (about 5-10%), acceleration (less than 10%), disruption/productivity (about 5%) and terms & conditions (about 5%).

Table 1 provides a relationship mapping (Red Amber Green of RAG format) between the issues (see Part 2) and the dispute/claim types (this Part 3).

¹Since the early 1980's, Mr. McLaughlin has worked worldwide in this industrial marketplace. He serves Owners, Prime Contractors, and Subcontractors. During the past 10 years, Mr. McLaughlin has been Project Manager on three major projects (\$85-330 million USD) and Program Manager on two major programs (\$300+ million USD). Mr. McLaughlin was president and COO of a \$35 million engineering and construction (mechanical, controls and electrical) contractor for five years. For the most part, Mr. McLaughlin's work is performed on location where the relevant work is being performed hence the title "view from the field." Mr. McLaughlin is a principal of McLaughlin & McLaughlin out of Austin, Texas. In this role, he provides program and project management services as well as litigation support services. His contact information can be accessed at his website (www.mclaughlinand_mclaughlin.com) and blog (<http://projectprofessionals.org/>).

Topic / Issue	Dispute / Claim Type				
	A. Scope of Work	B. Delay	C. Acceleration	D. Disruption / Productivity	E. Terms & Conditions
1. Asset Performance	●	●	●	●	●
2. Completion Management	●	●	●	●	●
3. Contracting Strategy Plan	●	●	●	●	●
4. Deliverable Quality, Completeness, and Timing	●	●	●	●	●
5. Free Issue Equipment & Material	●	●	●	●	●
6. Interface Challenges	●	●	●	●	●
7. Multi-Contract Strategy	●	●	●	●	●
8. Owner Project Management Teams	●	●	●	●	●
9. Scope of Work	●	●	●	●	●
10. Time Management / Schedule	●	●	●	●	●

Table 1: Claim to Topic / Issue Relationship

● = direct, ● = indirect, ● = none

A. Scope of Work

In my experience, approximately 75 to 90% of all engineering and construction claims and disputes arise from issues related to scope of work. Often the issue relates to gaps or omissions in the scope of work definition. Under the “mixed contracting strategy,” there is an increased risk of scope of work gaps given the greater number of interfaces and parties. At each interface and contract, scope of work is most commonly defined by the work of predecessor contractors.

- Performance requirements defined by owner business case or concept designer.
- Front End Engineering Design (“FEED”) scope defined by owner or process design deliverable and/or concept design deliverable.
- Engineering and Procurement (EP) contract defined by FEED deliverable.
- Vendor scope of work defined by EP contractor.
- Construction contractor scope of work defined by EP contractor, vendor deliverables, owner input, and other sources.
- Construction support contractor scope of work defined by EP contractor deliverables and/or owner sources.
- Completion contractor scope of work defined by FEED contractor, EP contractor, construction contractors and/or owner (project and/or operations).

At each interface, there may be issues with the scope definition such as being incomplete, excessive, untimely, etc. Hence, the deliverables (from the predecessor contractor) must be carefully defined.

For example, consider a situation where the engineering and procurement contractor (**EP**) is under a lump sum contract with the Owner (**O**). The mechanical erection contractor (**ME**) (under a lump sum contract with **O**) will receive equipment (free issue) from the **EP** vendor (**V**). Several pieces of major equipment are delivered in pieces, requiring major field assembly. The **EP** contract is silent on the precise delivery schedule. The mechanical erection contract is vague regarding the equipment assembly status at delivery. Finally, field assembly reveals serious manufacturing flaws that have to be corrected in the field. Resolution of difficulties and defining remedies and damages regarding each party (**EP**, **ME**, **V**, **O**) presents major scope of work issues.

Authoritative information regarding scope of work issues and case citations can be found in the following references (see Works Cited): (MCAA), (Bramble and Callahan), (Callahan), (Brans and Lerner).

B. Delay

Delay (longer duration or later completion of the work) has been a mainstay of claims, disputes and litigation on construction projects for decades. Analysis of and resolution of delay claims require great skill and (most often) expense. With increased interfaces and changing roles, it is a complex process to identify liability by correlating cause and effect. Since stakeholders may or may not have a shared critical path for their scope of work on a project, cause and effect becomes difficult to assign to individual parties.

The As-Planned Schedule is a basis for most delay claims and analyses. Under the emerging execution and contracting strategies, the overall project As-Planned Schedule can only be produced by the owner. The progress or schedule updates may originate with the contractors; however, the overall updated schedule is likely a responsibility of the owner. If so, establishing entitlement to time extensions and/or damages (compensation for prolongation) becomes a difficult and complex issue.

Consider a civil construction contractor (**C**) under a fixed unit price contract directly with the owner (**O**). Foundation design (e.g. drawings) and bulk materials (e.g. reinforcing steel) are being purchased and supplied (free issue) by the engineering and procurement (**EP**) contractor also under contract to the owner (**O**). Only one or two foundations are on the project critical path. How does the owner deal with schedule and time management regarding the civil, engineering and procurement, mechanical erection (needs the foundation and the equipment) (**C, EP, ME, O**) schedule issues, including delays?

Further, since delay damages and remedies tend to be “indirects” (Leslie O’Neal-Coble), direct labor cost overruns may not be recoverable through a delay claim. Many contracts bar such claims stating that time extensions are the only remedy. Direct labor cost overruns tend to be the major risk to Construction Contractors.

Authoritative information regarding delay issues and case citations can be found in references (see Works Cited) as follows: (McGeehin, Benes and Patrick J. Greene) (Bramble and Callahan) (Wickwire, Driscoll and Hurlbolt), (Pickavance), (Law).

C. Acceleration

Acceleration generally refers to attempts to achieve the same scope of work in a shorter period of time than originally planned. Alternatively, acceleration refers to an effort to achieve a greater quantity of work in the same planned period. Techniques include extending work hours (existing labor), adding labor (same scope), shift work, resequencing of work tasks or scope in parallel rather than sequentially,

and other means. If one considers that base contract plan as the most efficient approach to the work, acceleration generally results in less efficiency. Additional costs are incurred.

Consider a situation (as above in A. Scope of Work) where the engineering and procurement (**EP**) is under a lump sum contract with the owner (**O**). The mechanical erection contractor (**ME**) (under a lump sum contract with the owner) will receive equipment (free issue) from the **EP** vendor (**V**). Several pieces of major equipment are delivered in pieces, requiring major field assembly. The EP contract is silent on the delivery schedule of the equipment. The mechanical erection contract is vague regarding the equipment assembly status at delivery. Since this major equipment is on the project critical path, the owner directs the mechanical contractor to accelerate by using scheduled and prolonged overtime. Remedies regarding each contractor and the owner (**EP, ME, V, O**) present major cost-of-mitigation (acceleration) issues.

Authoritative information regarding acceleration and case citations can be found in the following references (see Works Cited): (Law), (MCAA), (Schwartzkopf, Calculating Lost Labor Productivity in Construction Claims: Second Edition), (Pickavance), (Department of the Army), (Ibbs).

D. Disruption/Productivity

Since Construction Contractors are (likely) at risk for negative labor productivity variances (labor overruns), disruption (as opposed to delay) events represent a major risk. Further, disruption damages tend to be “directs” (in this case, largely direct labor) rather than “indirects” (Leslie O’Neal-Coble).

Recovery of disruption/productivity damages is difficult. Since construction contractors (and engineering contractors) need to manage this risk, contracts with resolution methods will be needed.

Consider a situation where an electrical contractor (**E**) is under a lump sum contract with the owner (**O**). **E** requires the use of scaffolding for installation and erection work. Scaffolding is being supplied (free issue) by a construction support contractor (**CS**) under a time and materials contract with the owner (**O**). The electrical contractor (**E**) is constantly being redirected in its work areas by the owner (**O**) (mitigating delays by another contractor (piping - **P**), who is on the critical path). The scaffolding contractor (**CS**) requires three-day notice to reposition scaffolding. The electrical contractor’s productivity and rate of progress is less than bid. Claims and disputes may be appropriate for some or all parties (**E, CS, P, and O**).

Now consider the above situation (**E** and **CS**) coupled with the complexity that the “other subcontractor – piping (**P**)” is on the critical path due to design changes by the **EP** contactor. Consider whether these design changes (along with other issues) create a “cumulative impact” into the mix of potential claims. Which party(ies) is (are) responsible for this cumulative impact situation (**EP, E, P, CS, O**)?

Authoritative information and case citations regarding disruption can be found in the following references (see Works Cited): (Schwartzkopf and McNamara, Calculating Construction Damages), (MCAA), (Schwartzkopf, Calculating Lost Labor Productivity in Construction Claims: Second Edition), (Pickavance), (Ibbs), (Bramble and Callahan).

E. Terms & Conditions

Performance of the plant or asset that is produced by the capital investment is the ultimate objective of the owner. Historically, a performance guaranty is one method that has been used to deal with this objective. With emerging execution strategies, performance responsibilities become diffused rendering performance guarantees without disputes nearly impossible to obtain.

Consider a situation where the completion contractor (**CC**) (reimbursable cost contract) is attempting to complete commissioning and testing of the plant. **CC** is under contract to the owner (**O**). The required testing is at full capacity for 120 hours (five days) at an online (service) factor of 98%. The online factor is not being achieved due to one piece of mechanical equipment tripping and going off line. This equipment was supplied (free issue) by the **EP** (lump sum contract) (vendor **V**), field assembled and erected by the mechanical erection (**ME**) contractor (lump sum contract) and commissioned by the vendor (**V**) that supplied the equipment. Consider the transaction implications as well as potential claims, disputes and remedies for each party/stakeholder in the situation (**EP, V, CC, ME, O, others**).

Conclusions

Under Turnkey or EPC contracts and execution, the owner’s role was less complex, although arguably more expensive before claims and disputes. This arrangement is depicted in Figure 1, Part 1.

Under the evolving “mixed strategies,” the owner has assumed a greater role and its duties are more complicated. This arrangement is depicted in Figure 2, Part 1.

Since the potential for claims and disputes has increased enormously, there is a greater need for assistance from experienced construction attorneys

(both transaction and dispute/litigation specialists) and/or in-house attorneys. Effective counsel will also guide the stakeholders through the complex proof of remedies and damages. A useful resource is [Construction Damages and Remedies](#), published by the ABA (McGeehin, Benes and Patrick J. Greene).

As execution and contracting strategies are formulated, the overall project scope of work process must be defined in relation to the individual contract packages (individual scope of work). The anticipated form of contract(s) must be consistent with this process and the contractor organizations must be willing to adopt their contracting practices to minimize the scope gap inherent with the mixed strategies.

Disruption / productivity issues will continue to be prominent in the disputes and claims mix. Construction Contractors need methods and ways of working to manage major risk. This management includes: contractual protection, methods of recognition and process for recovery of impacts/damages that are the responsibilities of others. Skills in the claim or dispute resolution process must be upgraded and enhanced. Both Owners and Construction Contractors may need these upgrades and enhancements.

Part 4 of this series will consider some preventive/proactive and corrective/retrospective processes.

By: George T. McLaughlin, PMP

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DIVISION 1 MEMBER SPOTLIGHT

Joseph D. West

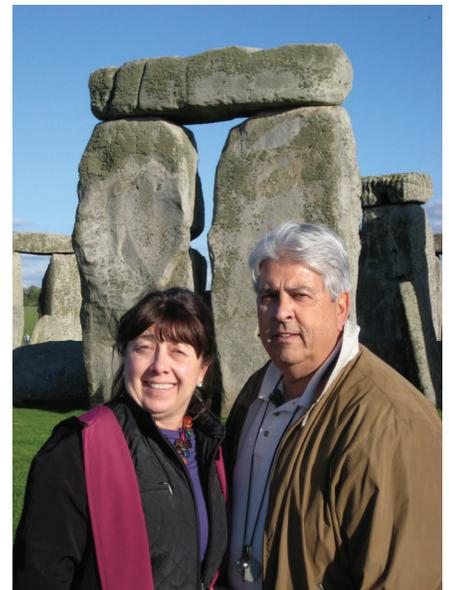
For someone with over 30 years' experience practicing construction law, one would think that Joe West was born to help clients resolve and avoid construction disputes, but Joe's journey to becoming a successful construction and government contracts attorney was less than deliberate, as Joe describes it. Some might even argue that Joe's entire successful career resulted from a need we all share -- a need for convenient parking.

Joe grew up in Shenandoah, Pennsylvania, which Joe describes as a "small coal town". Joe forewent playing football in college, opting instead to pursue a Navy ROTC scholarship, eventually being assigned as a Public Works Officer at a naval facility in D.C. after receiving his engineering degree from Villanova. Having previously been accepted to law school, Joe attended night classes at George Washington University, choosing the school because of its superior parking availability as compared to other schools. But that decision further steered Joe to his ultimate career because, while attending law school, he noticed, then later pursued, a job posting by the Washington Metropolitan Area Transit Authority (WMATA). As luck would have it, WMATA was looking for a young engineer with military and government contract management experience and at least two years of law school. Joe was a perfect (and possibly only) fit. While at WMATA, Joe got to know several successful construction attorneys and eventually joined their ranks.

Since then, Joe has enjoyed success in his career, serving numerous industries and advising contractors, subcontractors, vendors, and suppliers regarding traditional construction issues and disputes, as well as regarding government contracts and work. In terms of his ABA Construction Industry involvement, Joe served as the Chair of Division One, and was also a member of the Governing Committee. Currently, Joe is a partner in the Washington, D.C. office of Gibson, Dunn & Crutcher and Co-Chair of the firm's Government and Commercial Contracts Practice. When not practicing law, Joe enjoys continuing to "practice" his golf game and, like many of us, enjoys embarking on DIY projects at home, then supervising and coordinating the relief and remediation efforts. That notwithstanding, Joe has remained married for over 42 years and has two children.



GIBSON DUNN



Joe and his wife at Stonehenge



Joe walking his daughter down the aisle in France

Recent Developments in Construction Law

The following are some recent cases of interest related to construction law and dispute resolution. If you have a case you would like to submit, please contact a member of the newsletter editorial board.

Case 1

***Bennett v. Spectrum Const., Inc.*, [2012 WL 5877948](#), 2012 Tex. App.**

LEXIS 9629 (Tex. App.—Houston [1st Dist.] Nov. 21, 2012, no pet.) (not designated for publication)

New Exception to Rule that a Written Contract Bars Recovery Under Quantum Meruit Gains Traction in Texas

A contractor hired an individual as a subcontractor to perform electric work on a construction project. The subcontractor began the work, but died before the work was completed. His heir sued the contractor to recover payments owed to the subcontractor for his partial performance. There were disputes as to whether the subcontractor's death amounted to a breach of contract, whether the contract was for personal services, the amount of work completed by the subcontractor, and whether the contractor could offset its costs of completion against the claim asserted by the subcontractor's heir.

To recover under a quantum meruit theory in Texas, a claimant must prove: (1) valuable services were rendered or materials furnished; (2) for the person sought to be charged; (3) which services and materials were accepted by the person sought to be charged, used, and enjoyed by him; and (4) under circumstances that reasonably notified the person sought to be charged that the plaintiff in performing such services was expecting to be paid by the person sought to be charged. During trial, the contractor's representative conceded that these elements were satisfied. Nonetheless, as a general rule in Texas, the presence of an express contract bars recovery under quantum meruit. Because it was undisputed that contractor and subcontractor had an express contract, the court had to determine whether any exception to this general rule applied to allow the subcontractor's heir to recover under quantum meruit.

Texas allows recovery in quantum meruit despite an express contract in three situations: (1) when a plaintiff has partially performed an express contract but, because of the defendant's breach, the plaintiff is prevented from completing the contract; (2) when a plaintiff partially performs an express contract that is unilateral in nature; and (3) when a plaintiff breaches a construction contract, if the defendant accepts and retains the benefits arising as a direct result of the plaintiff's partial performance. The court determined that none of these three exceptions applied. The first two exceptions did not apply because the contractor did not breach the subcontract and the subcontract was not unilateral. The third exception did not apply because the subcontract was for personal services and because personal service contracts are considered terminated on death, terminated on the subcontractor's death. Once the subcontract terminated, the contractor could not prevail on an argument that failure to perform the remaining work constituted a breach.

The court felt that, under the circumstances, refusing to permit the quantum meruit claim asserted by the subcontractor's heir would have an "absurd" result. As a result, the court created a fourth exception to the rule, allowing recovery where there is mutual abandonment by the parties, or where further performance is prevented by a cause for which neither party is responsible. The court would also allow recovery for a plaintiff who had not substantially performed through no fault of his own. Reasoning that the subcontractor's death prevented further performance and that neither party was responsible for the subcontractor's death, the court held that the subcontractor's death excused further performance of the subcontract. The court rejected the argument that the express subcontract barred recovery under quantum meruit.

Case 2

United States ex rel. O.L.S., Inc. v. Southwind Constr. Servs., **2013 U.S. App. LEXIS 2635, 2013 WL 452858 (10th Cir. Feb. 7, 2013)**

Whether a Party Can Make a Claim Against a Miller Bond Depends On Whether Privity Requirements Are Met in the U.S. Court of Appeals for the Tenth Circuit

The Miller Act requires a prime contractor who is awarded a government construction contract to furnish a bond for the protection of first-tier and second-tier subcontractors who carry out the work provided for in the government contract. In *Southwind*, the U.S. Court of Appeals for the Tenth Circuit discussed the uncertainty among the circuit courts in deciding whether it was still proper for courts to focus on substance, rather than form, in determining who is a “subcontractor” for purposes of the Miller Act, particularly in light of the Supreme Court’s decision in *J.W. Bateson v. U.S. ex rel. Bd. of Trs. of Nat’l Automatic Sprinkler Indus. Pension Fund*, 434 U.S. 586, 590, 98 S. Ct. 873, 55 L. Ed. 2d 50 (1978).

In *Southwind*, the prime contractor on a government construction project delegated a large part of its duties under the contract to a related entity as a first-tier turnkey subcontractor. The first-tier turnkey subcontractor contracted with a second-tier subcontractor for part of the work and that second-tier subcontractor leased equipment from a third-tier subcontractor. When the second-tier subcontractor failed to pay the third-tier subcontractor, the third-tier subcontractor brought a claim against the prime contractor’s Miller bond.

The third-tier subcontractor argued that the court should look at the substance, rather than the form, of the parties’ contractual relationships and recognize that the first-tier Subcontractor was the de facto prime contractor. Accordingly, the third-tier subcontractor wanted the court to treat the second-tier subcontractor as a first-tier subcontractor, which would have made the third-tier subcontractor a second-tier subcontractor entitled to make a claim against the bond under the Miller Act.

The court acknowledged that the theory of piercing the corporate veil might permit a nominal second-tier subcontractor to be treated as a first-tier subcontractor or a nominal first-tier subcontractor to be treated as a prime contractor under the Miller Act. Nonetheless, the court declined to decide that issue because it was undisputed that the third-tier subcontractor had failed to establish a basis for disregarding the prime contractor’s separate corporate existence from its first-tier turnkey subcontractor. Because the Miller Act defines the term “prime contractor,” the court determined that it could not use a functional approach to determine the prime contractor’s identity.

The court then discussed the uncertainty among the circuit courts following *Bateson* on whether a party could make a claim against the bond if it does not have a contract with the prime contractor or a first-tier subcontractor. Ultimately, the court declined to address the issue because, even assuming a first-tier subcontractor was found to be an alter-ego of the prime contractor, the third-tier subcontractor would not benefit because the first-tier subcontractor was not a party to the prime contractor’s bond. The court refused to alter the terms of the bond agreement unilaterally and extend the surety’s obligations to the first-tier turnkey subcontractor. Thus, the third-tier subcontractor was not permitted to make a claim against the Miller bond.