

Legal & Legislative E-News

Winter 2004

Contractor Gets Stuck w/ Subcontractor Claim

In a rare instance where a subcontractor's claim is **NOT** allowed to be passed through to the owner, a case underscores the importance of contractor compliance with the notice and change order procedures required for subcontracts

Taylor Brothers, Inc./Obayashi (TBO) was awarded a \$90 million contract by the City of San Diego (City) to build a 3.5-mile tunnel under the Pacific Ocean to discharge treated sewage at sea. The underwater tunnel was to be drilled by a tunnel-boring machine and Sehulster Tunnels/Pre-Con (Sehulster) was the subcontractor supplying the precast concrete ring segments that line the tunnel.

During negotiations with Sehulster of the more than \$16 million purchase order to manufacture the tunnel rings, TBO discovered the tunnel-boring machine it had ordered was not compatible with the bid design of the tunnel ring segments. TBO advised the City of the situation and requested the City to redesign the tunnel ring segments rather than having TBO redesign the tunnel-boring machine which would cost between \$300,000 and \$1 million.

Agreeable to TBO's request, the City redesigned the tunnel ring segments and, negotiated Field Order No. 13 which stated that the change of design in the ring segments would not cause an increase in the contract price between the City and TBO. Although TBO had entered into its purchase order with Sehulster before the City completed the revised ring design, TBO instructed Sehulster to manufacture the rings pursuant to the new design. Sehulster advised TBO that additional costs would be incurred and subsequently submitted a \$2.545 million claim for additional work. TBO passed the claim through to the City as a "request for change" but it was rejected by the City on the basis of Field Order No. 13.

The *CMAA S. Chapter's Legal & Legislative E-Newsletter* and the *CMAA S. Chapter's Newsletter* can be viewed on our website at <http://www.cmaanet.org/sca>.

And for more news and events, visit CMAA's website at <http://www.cmaanet.org>.

In *Sehulster Tunnels/Pre-Con v. Taylor Brothers, Inc./Obayashi* (2003) 111 Cal.App.4th 1328, Sehulster brought a suit against TBO and the surety, and TBO, in turn, cross-complained against the City. In California, the Courts of Appeal have concluded

What's Inside . . .

Welcome to the first edition of the *CMAA S. Ca. Chapter Legal & Legislative E-Newsletter*! This publication will cover the latest construction law trends and issues as they relate to the CM industry, and it will be emailed, free of charge, to all CMAA S. Ca. Chapter members. Inside this issue:

Contractor Gets Stuck w/ Subcontractor Claim	Page 1
CMAA Legal Seminar Calendar	Page 2
What was TBO Thinking? A CM's Perspective . . .	Page 3
The Facts about California Licensing of Construction Managers	Page 4
California's Construction Legislation for 2003	Page 5 & 6
SB 1953 & the Alquist Hospital Facility Seismic Safety Act	Page 7
The Latest Construction Industry Court Decisions	Page 8 & 9

If you do not receive your copy of the *CMAA S. Ca. Chapter's Legal & Legislative E-Newsletter*, please email <mailto:SCCMAA@pavenet.net> or view it on our website at <http://www.cmaanet.org/sca>.

that private parties may impliedly abandon a contract when they fail to follow change order procedures and when the final product differs substantially from the original but, citing the *Amelco* case (see the Case Law Background box on page 2), TBO argued that because the City (as a public entity) could not be held liable under an abandonment theory, it follows that TBO could not be held liable for abandonment to the subcontractor. The court disagreed noting that since Sehulster's purchase order was with TBO (not the City), and TBO breached and abandoned that agreement by making the substantial design change, the issue was TBO's abandonment liability to Sehulster not the

CONTINUED ON PAGE 2

Contractor Gets Stuck w/ Subcontractor Claim *(continued from page 1)*

City's liability for abandonment to TBO. TBO could have renegotiated its purchase order with Sehulster, but elected not to and simply imposed the new design on Sehulster without a formal change to the purchase order thus leading to its abandonment. The court also noted that the TBO case dealt with a purchase order between two private entities where one private party supplied goods to another that were paid for from the other party's private profits, not the tax payer's pockets, and therefore, the underlying public policy considerations of the Amelco case were not applicable.

While at the trial court level the jury did allow TBO to recover on a cross-complaint for indemnity against the City, the court later ruled that there was no reason on a contractual basis for TBO to seek indemnity from the City due to Field Order No. 13 which expressly stated there would be no cost impact to the prime contract. The court also noted that to permit TBO to recover under the theory of implied contractual indemnity would be inconsistent with the cited public policy reflected in Public Contract Code §7105(d)(2) which states, "The compensation payable, if any, for amendments and modifications shall be determined as provided in the contract." TBO had requested the City to implement the design change, agreed that it would have no impact on the prime contract price and never requested the prime contract price be modified as a result of the change.

This decision places prime contractors in a difficult dilemma. On the one hand, they may not pursue an abandonment claim against a public owner, but on the other hand, they may be liable to their subcontractors on that theory. Under these circumstances, prime contractors must insist on compliance with the notice and change order procedures contained in the prime contract that are incorporated by reference into their subcontracts.

- Gordon Hunt, Attorney,
Hunt, Ortmann, Blasco Palffy & Rossell, Inc.

Case Law Background

On private projects the Appellate Courts have ruled that parties may abandon a contract when they fail to follow change order procedures and when the final product differs substantially from the original. By filing an "abandonment" claim, contractors and subcontractors are able to pursue recovery of the reasonable value of the labor, service, equipment and material furnished for the project, and they are no longer bound by the contract price. For public sector projects, the Federal Courts have applied a similar theory known as the "cardinal change" theory to cases where the government effects an alteration in the work so drastic that it requires the contractor to perform duties materially different from those for which it was originally contracted.

The question as to whether the "abandonment" theory could be applied to a *public project* was undetermined until the 2002 California Supreme Court case of Amelco Electric v. City of Thousand Oaks, 27 Cal.4th 228. In that case, the California Supreme Court held that the theory of "abandonment" does not apply against a public agency because the abandonment theory is fundamentally inconsistent with the underlying purpose of the competitive bidding statutes of public projects.

Don't miss CMAA's Legal Seminars

Learn the fundamental principles of good contract management and understand the ever-changing world of construction law. Each workshop features industry leaders who will highlight recent changes in construction law, review case studies, and share their practical, hands-on experiences, expertise and knowledge. Upcoming seminars include:

DATE	TIME	TOPIC	LOCATION
February 19	8:00 – 10:30 am	Contract Documents Review	The Grand, Long Beach
March 18	8:00 – 11:00 am	Mechanic's Liens, Stop Notices & Bonds	The Grand, Long Beach
		\$55 Members \$85 Non-Members	

For more information about these and other CMAA events, please e-mail <mailto:sccmaa@pavenet.net>. For a complete listing of CMAA S. Ca. Chapter events, event calendar updates, and on-line registration go to <http://www.cmaanet.org/sca>.

CMAA S. Ca. Chapter Legal & Legislative E-News, Winter 2004

CMAA Southern California Chapter Legal & Legislative E-News is published for the members of the Southern California Chapter of the Construction Management Association of America for the purpose of informing the members of local and national construction law trends and issues as they relate to the CM industry. Articles published in CMAA Southern California News contain the opinions of the authors and do not necessarily represent the position of the CMAA Southern California Chapter. Inquiries regarding the newsletter can be directed by email (<mailto:sccmaa@pavenet.net>), fax (562/856-5813) or mail to: CMAA S. Ca. Chapter, P.O. Box 41202, Long Beach, CA 90853.

What was TBO Thinking? A CM's Perspective . . .

After reading the case presented by Gordon on page 1, my initial reaction was to question how such an experienced contractor, Taylor Brothers, Inc./Obayashi Corporation (TBO), could find itself in such a predicament. After reading the case summary from the appeal by Sehulster Tunnels, dated September 12, 2003, it became clear that an attempt to neutralize a bidding error had grown into a much larger issue than expected.

Project Background

TBO was responsible for providing a tunnel-boring machine compatible with the original tunnel ring segment design that met all of the performance requirements of the specifications it had at the time of bidding. In July 1995, after learning it was the lowest bidder, TBO discovered the potential conflict between its design for the tunnel-boring machine and the City's design for the tunnel ring segments. To install the ring segments as designed would require the boring machine to be lengthened, and, although the City was made aware of the problem before issuance of the notice-to-proceed, TBO had prematurely ordered the tunnel-boring machine.

At this point, TBO has two options: redesign the tunnel-boring machine or redesign the tunnel rings. Let's analyze the potential cost and schedule delays associated with each alternative as, presumably, TBO did.

Redesigning the Tunnel-Boring Machine

Since TBO had prematurely taken the initiative to order the tunnel-boring machine (TBM), we can safely assume the manufacturing process had already started. Redesigning the tunnel-boring machine was estimated to cost between \$300,000 and \$1 million but additional cost impacts could also result from manufacturing delays caused by the re-work which could in turn impact the project's critical path.

A second critical issue involves potential impacts resulting from the increased length as a longer TBM will experience greater "skin friction" between it and the tunnel which can cause the TBM to become lodged in the tunnel. Even if the TBM doesn't become permanently stuck -- as it

very well could which would jeopardize the entire project -- efforts to dislodge the TBM would certainly result in schedule delays. These impacts to the project's critical path would force TBO to accelerate work or risk being charged liquidated damages. Acceleration produces inefficiencies that impact production rates, and, while the precise cost implications are difficult to quantify, through experience we know these costs could be significant.

Redesigning the Tunnel Ring Segments

When the potential conflict between the TBM and the tunnel ring segments was identified, TBO was in negotiations with Sehulster for the manufacturing of the tunnel rings. While, as indicated by Sehulster, the new design would increase the cost of the rings, since manufacturing had not yet begun, manufacturing delays would presumably be minimal or nonexistent. With the tunnel rings, unlike the redesign of the TBM, schedule impacts due to re-work would not be an issue.

Most importantly, the City was agreeable to redesigning the tunnel rings -- provided it would not result in an increased contract amount.

The Preferred Alternative

With several opportunities for serious impacts to the project's critical path, redesigning the TBM appeared to be a far riskier option for TBO. Clearly, the preferable alternative was to redesign the tunnel ring segments, despite the additional costs associated with doing so.

TBO directed Sehulster to proceed with the new tunnel ring design and entered into Field Order No. 13 with the City which

documented that TBO agreed there would be no cost impact from the ring segment changes. From this, it can be reasonably inferred that, in exchange for the redesign, TBO was willing to assume the potential liability for the associated cost overruns. So what went wrong?

Absent specific documentation between Sehulster and TBO related to the additional cost of redesigning the tunnel rings, TBO made the assumption the cost of the tunnel ring redesign would be minimal in comparison to the cost impacts associated with redesigning the TBM. In retrospect, this may have been an accurate assessment but the lack of documentation also left TBO, contractually, extremely vulnerable to Sehulster.

The lack of a contract between the City and Sehulster equates to a lack of privity between the parties leaving Sehulster unable to sue the City directly. However, California law protects the interests of the subcontractor by allowing a subcontractor's claim to "pass through" the general contractor and on to the owner. TBO may have erroneously assumed that when Sehulster invoked the contractual pass-through provisions, the City would automatically become responsible for the claim.

What TBO failed to recognize is that the pass-through provision does not assign responsibility, but instead, is simply a conduit designed to shorten the legal process by going directly to the owner. The owner is responsible only if the subcontractor's claim is a result of the owner's breach of contract with the general contractor. In this case, the City had not breached the contract and, since TBO had previously agreed the City would not incur any additional costs, TBO, not the City, is responsible for Sehulster's claim. In addition, because TBO and Sehulster are both private entities, Sehulster may recover against TBO under the abandonment of contract theory.

**- Fahim Boulos, Sr. Construction Manager,
MARRS Services, Inc.**

Under current California Law, lack of proper licensing can result in financial ruin for a construction manager. An unlicensed or improperly licensed construction manager has no right to resort to the courts to recover compensation and may even be required to repay compensation already received.

The Facts about California Licensing of Construction Managers

In discussions with CMAA members we have found considerable confusion and even misinformation as to whether a construction manager is required to have a contractor's license. The general rule is that according to California Law, a construction manager must have a contractor's license and the definition of "contractor" under California Law clearly includes the activities of a construction manager -- even if the individual is working as an independent contractor or as a consultant. Since there are several scenarios under which a construction manager may be contracted, let's quickly examine each.

Agency CM vs. At-Risk CM

Under the "agency" protocol, a construction manager acts as an agent of the owner and does not guarantee a maximum price. According to California Law, a construction manager acting as a consultant, agent or independent contractor to an owner-builder is required to have a contractor's license. Under the "at-risk" protocol, a construction manager extends to the owner a guaranteed maximum price either for the entire project or for some portion of it. Under the at-risk protocol, a construction manager is clearly acting as a contractor and therefore needs a contractor's license.

True Employee

A construction manager working for an owner for wages or on salary is not required to have an individual contractor's license. A contractor, of course, is required to have a contractor's license (except on federal work which is not subject to California Contractor's License Law) and the operations of the construction manager on salary from a licensed contractor is covered by the license of that contractor. There are many situations in which an owner-builder (for example, a subdivider) would be required to have a contractor's license, and a construction manager working for such an owner-builder for wages or on salary would also be covered by the owner-builder's contractor's license.

Licensed Architect Acting as a CM

A licensed architect acting as a construction manager under the at-risk protocol needs a contractor's license in addition to an architect's license. In most cases, the operations of a licensed architect operating under the "agency" protocol are covered by the architect's license. However, if the contract requires an architect to perform activities beyond functions conventionally performed by

architects as described by the licensing laws applicable to architects, a specific legal opinion should be obtained as to the potential requirement of licensure as a contractor.

Registered Professional Engineer Acting as a CM

Here is where the law gets complicated. California Business and Professions Code §7051 exempts a registered civil or professional engineer acting solely in his or her professional capacity from the contractor's license requirement. Under this code a licensed professional engineer operating as an "at-risk" construction manager would not be exempt from the requirement of a contractor's license since the professional capacity of a professional engineer does not include contracting to build a project for a guaranteed maximum price. However, the question of whether a registered professional engineer acting as a construction manager under the "agency" protocol is exempt is a more difficult one to answer.

The professional engineer's licensing act defines "professional engineer" to include a person engaged in the professional practice of rendering engineering services in the evaluation, planning or design of buildings and other structures, and the supervision of construction to secure compliance with specifications and design. Business and Professions Code §6731.1 also provides that "a registered civil engineer may also offer ... construction project manager services, including but not limited to design review and evaluation, mobilization and supervision, bid evaluation, scheduling and general management and administration of a construction project." So the "professional capacity" of a registered *civil* engineer includes construction management services but the "professional

capacity" of a *mechanical* or *electrical* engineer does not.

Section 3 of the statutes of 1990, chapter 786, provides that the act does *not eliminate the need for a general contractor*, or authorize a registered civil engineer *to act as a general contractor*. This reinforces the conclusion stated above that an engineer's license would not authorize an "at-risk" contract because that protocol eliminates the need for a general contractor. Further, if there is no licensed general contractor on the job (if, for example, an owner-builder "subs everything out"), then the licensed civil engineer would need a contractor's license.

- James Acret, Attorney, Thelen Reid & Priest LLP

In California the rules are:

- Any construction manager operating under the at-risk protocol requires a contractor's license regardless of whether the construction manager also carries a license as an architect or engineer.
- A registered civil professional engineer does not need a contractor's license in order to perform services under the agency protocol *provided* there is a general contractor on the job.
- A registered mechanical or electrical engineer may not perform construction management services without a contractor's license.
- In most cases, a licensed architect may perform construction management services through the agency protocol without obtaining a contractor's license, but legal advice should be sought if the duties to be performed on a particular project appear to go beyond services traditionally performed by architects.

California's Construction Legislation for 2003

While 2003 did not produce the type of far-reaching and controversial construction laws that came out of the 2002 Legislative Session, this was a busy year in Sacramento for the construction industry. The Legislature passed and the Governor signed into law, more than 20 significant construction-related bills that deal with a variety of issues including licensing, public bidding, public bonding, school construction, mechanic's liens, notices of completion, temporary labor and construction defects. Below is a brief description of the more significant bills that took effect on January 1, 2004.

AB 14 LAUSD Job Order Contracting (J. Horton): Allows the Los Angeles Unified School District to utilize job-order contracting in procuring public works contracts.

AB 17 Equal Benefits for Domestic Partners (Kehoe): Prohibits a state agency from entering into a contract with a vendor or contractor who does not offer benefits to employees with domestic partners that are equal to benefits offered to employees with spouses.

AB 341 Landscape Contractors – Licenses and Permits – Swimming Pools (Aghazarian): Authorizes a landscape contractor working under that license classification to enter into a prime contract for the construction of a swimming pool or spa provided that it is included within a landscape project and subcontracted to a licensed swimming pool contractor or performed by a landscape contractor who is a licensed swimming pool contractor. Codified as amendments to Business and Professions Code § 7027.5.

AB 276 Penalties for Labor Code Violations (Koretz): Increases the penalty from \$100 to \$200 for a person who does not hold a state contractor's license and employs workers to perform services for which a license is required or for any person with a state contractor's license who knowingly enters into a contract with a person to perform services for which a contract is required and that person does not meet the status of independent contractor or does not hold a state license.

Codified as amendments to Labor Code §§ 210, 225.5, 226, 605, 1021.5 and 1197.1.

AB 453 Defective Bids and Compensation of Contractors: Provides that if a contract awarded by a public authority is later determined to be invalid due to a defect in the competitive bidding process caused solely by the public agency, the contractor shall be entitled to be paid the reasonable cost, excluding profit, of the labor, equipment, materials and services furnished by the contractor prior to the date of the determination, subject to specific conditions.

AB 447 Lien Claims – Release – Attorneys' Fees (Vargas): Increases the amount of attorneys' fees that may be recovered from \$1000 to \$2000 when the owner of real property petitions a court to release the property from a mechanic's lien where no action has been brought to enforce the claim of lien. Codified as amendments to Civil Code § 3154.

AB 544 Temporary Labor (Montanez): Requires a temporary employment agency to have a contractor's license if the agency's employees are performing work activities for which a contractor's license is required and they are not working under the supervision of a licensed contractor.

AB 722 Public Contracts – Bids and Bidding – Reverse Auctions (Matthews): Authorizes the Department of

General Services to utilize the "reverse auction" procurement process for the acquisition of goods, services and information technology. However, the bill also precludes the Department of General Services from utilizing the "reverse auction" process for bidding on specified construction contracts. "Reverse auction" is defined as a competitive on-line solicitation process in which vendors compete against one another on-line in real time. Codified as Public Contract Code §§ 10290.3 and 12101.7.

AB 902 Public Contracts – Awarding Authority – Substitution (Diaz): Authorizes an awarding authority to consent to a prime contractor's substitution of a subcontractor when the subcontractor listed in the bid fails or refuses to execute a written contract for the specified scope of work at the price specified in the subcontractor's bid. Codified as amendments to Public Contract Code § 4107.

AB 903 Construction Defects: Revises and recasts various provisions governing home construction defect actions. Among other things, it will revise the definition of

New legislation only allows state agencies to enter into contracts with companies offering employees domestic partner benefits equal to those offered to employee spouses.

"builder" and will specify the application of certain provisions to general contractors. The law will make technical changes to a builder's election to inspect and the application of certain affirmative defenses, and will recast the provisions relating to the applicable statute of limitations, and the exclusivity of these provisions.

AB 1034 Housing – Building Standards (Mullin): Relates, in part, to local ordinances or regulations governing alterations and repair of existing buildings, and the use of original methods of construction. Allows the use of original methods of construction if that portion of the structure complies with the building code provisions at the time of its construction and

CONTINUED ON PAGE 6

California's Construction Legislation for 2003 *(continued from page 5)*

other requirements governing it at that time are met. Codified as amendments to Health and Safety Code § 17958.8.

AB 1382 Contractors – Arbitration, Civil Penalties and Licensing (Correa):

Under this law, a contractor who fails to comply with an arbitration award issued by the Contractors' State License Board will have its license revoked within 90 days instead of one year. Among other things, the bill also precludes the Board from ordering specific performance of a contract and modifies the requirement that the Board pay the expenses of one expert arbitration witness upon the request of any party. The bill also increases the maximum civil penalty the Board can assess its licensees from \$2,000 to \$5,000 and precludes a contractor's principal, partner or managing officer from disassociating himself or herself from a license to avoid complying with a citation. Codified as amendments to Business and Professions Code §§ 7071.17, 7085.5, 7085.6, 7090.1, 7099.2, 7121, 7122.1 and 7143.

AB 1386 Contractors (Horton): Requires a contractor to demonstrate that he acted promptly and in good faith to reinstate his license upon learning it was invalid in order to demonstrate substantial compliance of the licensure requirements. The law "declares" the intent of the legislature to be that the changes made by the law are declaratory of existing law. Codified as amendments to Business and Professions Code § 7031.

AB 1538 Construction Contractors (Berg): Requires a contractor (except for plumbing, electrical sign and well-drilling contractors) to display its contractor's license number and business name in or on each commercially registered motor vehicle used in its construction business. Codified as Business and Professions Code § 7029.6.

AB 1573 School Construction: Design-Build (Corbett): Existing law requires a school district governing board to be the

employer of the project inspector and the project inspector to be fully independent from any member of a design-build entity or its subcontractors. This law requires the project inspector to act under the direction of either the Director of the Department of General Services or a competent, qualified agent of the school district. Codified as amendments to Education Code § 17250.35.

AB 1745 Public Contracts – Bonds (Committee on Transportation): Gives the DOT discretion to specify that for projects with a contract price greater than \$250,000,000, the required payment bond shall be the lesser of ½ the contract price or \$500,000,000. Codified as amendments to Public Contract Code § 10222, which was effective August 4, 2003, as an urgency statute.

AB 175 State Government (Committee on Budget): Authorizes, in part, the Department of General Services, upon making specified findings, to establish a negotiation process that may be used during various stages of the procurement process when the department procures construction services for itself or on behalf of another state agency. Codified as Public Contract Code § 6611, which was effective August 4, 2003, as an urgency statute.

SB 66 Local Government Omnibus Act of 2003 (Committee on Local Government): Requires a public agency, prior to rejecting all bids and having the work performed by its employees by force account, to furnish written notice to the apparent low bidder that the agency intends to reject all bids. Codified as amendments to Public Contract Code § 22038.

SB 110 Public Contracts – Contract Specifications (Margett): Allows bid specifications to include a certain "single source" product if the awarding authority makes a finding that a particular material or service designated by a brand or trade name is a necessary item that is only available from one source or in order to

respond to a local or state declared emergency. Codified as amendments to Public Contract Code §§ 3400 and 10129.

SB 113 Mechanic's Liens and Arbitration: Provides that with respect to a lawsuit to foreclose on a mechanic's lien, the mechanic's lien claimant must follow specific procedures in order to secure the right to compel arbitration.

SB 134 Private Works of Improvement – Liens (Figueroa): Requires that certain statements be included in a preliminary 20-day notice in boldface type in regard to notices of completion or cessation. It also requires the owner to notify the original contractor and any claimant who has provided a preliminary 20-day notice prior to the recording of a mechanic's lien or stop notice that a notice of completion or notice of cessation has been recorded within 10 days of recordation. Failure to give notice extends the period of time in which the contractor or claimant may file a mechanic's lien or stop notice to 90 days. Codified as amendments to Civil Code §§ 3097 and 3259.5.

SB 179 Contracts for Labor and Services: Any person or entity who enters into a labor contract for construction or other specified services, when they knew or should have known that the contract does not provide sufficient funding for the labor contractor to comply with all applicable laws and regulations governing labor or services to be provided under the contract, is subject to liability and specified civil penalties.

SB 1079 Department of Consumer Affairs (Committee on Business and Professions): Makes it, in part, a misdemeanor to use the terms "landscape architecture", "landscape architectural" or any other titles, words or abbreviations that would imply licensure as a landscape architect without a valid license from the California Architects Board. Codified as amendments to Business and Professions Code § 5640.

- Chris Roux, Attorney, Weston Benshoof

SB 1953 & the Alquist Hospital Facility Seismic Safety Act

A direct result of the Sylmar Earthquake of 1971 was the California state legislature's initiation of a statutory scheme to establish construction and design standards for the seismic safety of acute care hospitals in California. Commonly known as the Alfred E. Alquist Hospital Seismic Facility Safety Act of 1983, this legislation emphasized that essential facilities such as hospitals should remain operational after an earthquake and established a seismic safety building standards program under OSHPD's jurisdiction for hospitals built on or after March 7, 1973.

The standards were put to the test in January of 1994 when the Northridge Earthquake hit. As intended, hospitals built in accordance with the standards of the Alquist Act resisted the January 1994 Northridge Earthquake with minimal structural damage.

Unfortunately, numerous facilities built prior to the Act experienced major structural damage and had to be evacuated. This prompted the development of Senate Bill 1953 (SB 1953) which increased the structural seismic regulations for healthcare facilities and also included nonstructural components.

Introduced on February 25, 1994, and signed into law on September 21, 1994, SB 1953 established seismic retrofit regulations for all existing general acute care hospital buildings, and created seismic performance categories that applied to all general acute care hospital facilities -- whether new or existing.

Currently there are approximately 470 acute care hospital facilities in California which include 2,673 hospital buildings that are impacted by the provisions of SB 1953. To remain a general acute care hospital facility beyond the statutory deadline, each facility must conduct seismic evaluations, prepare both a comprehensive evaluation report, and submit a compliance plan to meet

A challenging issue for California healthcare providers, seismic requirements for acute healthcare facilities continue to evolve.

specified structural and nonstructural performance criteria -- all of which must be submitted to OSHPD in accordance with the state regulations.

Seismic performance categories include the Structural Performance Category (SPC) and Nonstructural Performance Category (NPC). All general acute care hospital facility buildings must meet SPC-2 criteria ("Life Safety Level") by January 1, 2008, to be in compliance with the provisions of the regulations. Despite this requirement, an acute care facility owner can apply for an extension beyond the 2008 deadline based on one of the following qualifying circumstances:

- Diminished Capacity: OSHPD may grant the hospital an extension for both SPC-2 and NPC-3 requirements if it is evident that compliance will result in an interruption to healthcare services provided by general acute care hospitals within the area. The extensions are granted in one-year increments up to a maximum of five

years beyond the mandated January 1, 2008, date of compliance.

- 1801 Exemption: OSHPD may grant a hospital extension for both SPC-2 and NPC-3 requirements if the hospital agrees that on or before January 1, 2013, designated services shall be provided by moving into an existing conforming building, a new fully conforming building or a retrofitted conforming existing building.
- 2006 Extension: OSHPD may grant hospitals an extension delay for

nonstructural (NPC-3) requirements if the hospital is located in a seismic zone 3 area as indicated in the 1995 addition to the California Building Standards Code, and the facility has met the NPC-2 requirements and

associated deadline.

Of the existing 470 acute care facilities, currently 146 have requested extensions with the overwhelming majority of extensions based upon Diminished Capacity. OSHPD's facilities division has formed a seismic retrofit program unit to handle inquiries and submissions.

While most practitioners in healthcare design and construction are already aware of SB 1953 and the existence of possible extensions, the regulations and laws governing the implementation of the legislation are complicated. With strict statutory deadlines, limited extension options and the vast amount of capital required to upgrade the facilities, this continually evolving issue promises to remain a critical challenge for California's healthcare industry.

**- Michael J. Baker, Attorney,
Burke, Williams & Sorensen, LLP**

For more information on SB 1953 or to download extension request forms, visit <http://www.oshpd.ca.gov>.

The Latest Construction Industry Court Decisions

In an effort to keep CMAA members current regarding recent rulings that effect the construction industry, the CMAA S. Ca. Chapter Legal & Legislative E-Newsletter will, on a regular basis, include brief summaries of recent court decisions.

Howard S. Wright Construction Co. v. Superior Court (106 Cal. App. 4th 314, 130 Cal. Rptr. 2d. 649; November 13, 2003)

In this case, the Court of Appeal reversed the trial court ruling to both expunge (remove) a contractor's notice of lis pendens and remove a mechanic's lien largely because the trial court failed to determine if the owner was a participating owner. Howard S. Wright Construction Co., the unpaid contractor, recorded a mechanic's lien and a notice of lis pendens against the real property and the building in which the contractor had performed work for a tenant — not for the building owner.

The Court of Appeal looked to the long established case of English v. Olympic Auditorium, Inc. (217 Cal. 631; 1933) where the California Supreme Court held that when real property is subject to a lease and the lessee contracts for improvements without the lessor's knowledge, the lien attaches only to the lessee's leasehold interest. However, improvements constructed with the owner's knowledge are deemed to be at the instance and request of the owner unless the owner has posted and recorded a notice of non-responsibility (California Civil Code § 3129). Although in the Howard case the owner had posted and recorded a notice of non-responsibility, the tenant was required by the lease to make certain improvements which nullified the notice of non-responsibility and allowed the tenant to be treated as an agent of the owner. The owner was, therefore, a "participating owner".

Lantzy v. Centex Homes (2003 DJDAR 8638; 2003)

Statutes of limitation that commonly apply to construction litigation (most often California Code of Civil Procedure §§ 337.1, and 337.15) allow claimants three or four years from the date of discovery for any patent deficiency in the design, specification, supervision or construction of an improvement. Although often referred to as a statute of limitation, § 337.15 is actually a statute of repose, which was clearly demonstrated in Lantzy v. Centex Homes.

Civil Code § 337.15 provides that no action may be brought to recover damages for a latent defect in the design specification, supervision or construction of an improvement more than 10 years after the substantial completion of the improvement. Lantzy, the plaintiff, sought the equitable tolling of §337.15. However, the Court

of Appeal stated that § 337.15 requires any action arising out of a latent defect to be brought within ten years of the substantial completion of the work, regardless of the date of the discovery of the defect.

The Court reiterated that §337.15 was passed to protect contractors, construction managers, engineers, architects, and other professionals and participants in the work of the construction industry from unlimited and perpetual exposure to liability arising out of their work.

Kinsman v. Unocal Corporation (2003DJDAR 8039; 1st Dist.; 2003)

In the Kinsman case, the Court upheld the Privette/Toland line of cases in limiting the exposure of the owner of real property in cases where employees of contractors and subcontractors are injured on the job.

Under Privette and Toland, the injured worker is limited to a worker's compensation claim and, if appropriate, a negligence claim against its employer, equipment supplier, or other person or party who may have contributed to the accident and/or injury.

In the Kinsman case, a carpenter employed by a scaffold subcontractor was injured by exposure to asbestos which had been installed in the 1950s. At trial, the jury found the owner of the project, Unocal, was negligent in the management of the areas where the plaintiff worked and assigned Unocal 15% of the contributing fault. On appeal, the Court of Appeal held that the owner of real property is liable to the employee of an independent contractor only when the owner has control over the work and that control affirmatively contributes to the injury. The Court further held that a property owner cannot be liable to a contractor's employee for a dangerous condition a contractor has created on the land, unless the owner exercised control over the condition and in doing so affirmatively contributed to the employee's injury. The Court of Appeal also found the jury had been improperly instructed, and reversed the verdict and judgment of the trial court.

City of Long Beach v. Department of Industrial Relations (2001 DJDAR 7771; 2nd Dist. 2003)

In this case, the Department of Industrial Relations (DIR) investigated a union complaint regarding an alleged failure to comply with the prevailing wage laws (Labor Code §§ 1720, 1771)

In this summary:

- **A building owner is at risk in a tenant's dispute with a contractor;**
- **A common statute of limitation is actually a statute of repose;**
- **An owner's exposure is limited when an injury occurs on the job;**
- **A city is held responsible for not complying with prevailing wage laws; and**
- **A minimal causal connection may trigger insurance coverage.**

CONTINUED ON PAGE 9

The Latest Construction Industry Court

Decisions (continued from page 8)

on an animal shelter project constructed on City land but built by the SPCA. While the City of Long Beach contributed \$1.5 million (15% of the total estimated cost), it had taken the position that the prevailing wage laws did not apply. The DIR believed they did apply and the Court agreed.

Labor Code § 1720 (a) defines “public works” as construction done under contract and paid for in whole or in part by public funds. The Court of Appeal also said the word “construction” should be interpreted broadly to include architectural design, project management, legal services, surveying and insurance. Approximately \$1 million of the contribution from the City was spent on such services.

The Court reasoned that two of the main purposes of the prevailing wage laws are to ensure a supply of skilled workers and to protect area-wide standards, which are statewide concerns, and not merely local interests. The Court found that the prevailing wage laws therefore apply to charter cities contracting for public works regardless of whether the project itself is strictly a municipal affair.

Vitton Construction Co., Inc. v. Pacific Insurance Co. (2003) DJDAR 8047; 1st Dist. 2003

On this warehouse project a structural steel subcontractor laid the decking, cut holes for skylights and HVAC equipment, and then left the site. The contractor’s employees then attached wood nailers and curbs to the skylight openings but did not cover them. A roofer fell through one of the openings, was injured and sued the owner, the contractor, and the subcontractor, settling for \$6 million. An action followed among the carriers as to equitable indemnity, subrogation and contribution.

Since the structural steel subcontractor’s comprehensive general liability policy included a “blanket additional insured endorsement” which defined an “additional insured” as any organization to whom the subcontractor was contractually obligated, both the prime contractor and the project owner were identified as additional insureds. The policy also stated that such insurance would apply only with respect to liability arising out of the subcontractor’s work.

The trial court ruled the general contractor was not an additional insured but the Court of Appeal disagreed and, in its broad interpretation of the term “arising out of”, found that a minimal causal connection sufficed to trigger coverage under this language. The subcontractor created holes in the roof, left them uncovered, and the roofer accidentally fell through one of them. The fault “arose out of” the subcontractor’s work — regardless of whether it was the subcontractor’s or the general contractor’s responsibility to make the holes safe. The additional insured endorsement does not allocate coverage according to fault.

- Peggy A. Gerber, Esq., Thelen Reid & Priest LLP

CMAA S. Ca. Chapter
Board of Directors
2003-2004

President

Lisa Campbell
Kleinfelder
lcampbell@kleinfelder.com

Vice President

Scott Harral
Jacobs Engineering
Scott.Harral@Jacobs.com

Secretary

Jerome Ruddins
RBF Consulting
jruddins@rbf.com

Treasurer

Greg Hess, CCM
DMJM Management
greg.hess@dmjm.com

Past President

James Davis
Port of Los Angeles
jdavis@portla.org

Legislative Chair

Peggy Gerber
Thelen Reid & Priest
pgerber@thelenreid.com

Membership Chair

Tim Holcomb
Pinnacle One
tholcomb@pinnacleone.com

Newsletter Chair

Art Hadnett
Carter & Burgess
hadnettaj@c-b.com

Program Chair

Allyson Gipson
Bovis Lend Lease
allysonm.gipson@bovislendlease.com

Student Committee Chair

Edward Sparks, CCM
Parsons
Edward.Sparks@parsons.com

CMAA S. Ca. Chapter
Legal & Legislative E-Newsletter
published compliments of

Carter=Burgess

<http://www.c-b.com>

