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Bricker & Eckler Construction  
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### ***April Issue Focuses on Public Construction Topics:***

## **Evaluating the Low Bidder’s Finances, Interpreting Public Records Law, And Enforcing Surety Bonds**

*Without any particular scheme of things, our fourth issue in 2003 turned out to have a theme for much of its content: public construction. That is clearly the focus of this month’s lead article, “Does Your Low Bidder Have the Financial Ability To Complete Your Project?” The article discusses what financial records an owner can request from an apparent low bidder and how to evaluate those records to determine if the contractor is really responsible. Is it likely that the low bidder will be able to complete the contract, or will the owner be forced to resort to the surety? (Since private contractors want to hire financially responsible contractors, too, they can undoubtedly pick up a few pointers from this discussion.) This article goes beyond generalities about the importance of good accounting and proposes a new form an owner can require of the low bidder: A Low Bidder’s Financial Responsibility Affidavit. You will even find a sample of the form in the article. Let us know if you find it useful!*

**A**lthough our first column, “What the Legislators Are Considering,” has no particular public construction slant, our second one does. All of the cases summarized in April’s “What the Courts Are Saying” arose from public projects.

We begin with a recent proclamation from the Hamilton County Court of Appeals on the public records law, exemptions from it, and what actions can destroy those exemptions.

Our second case comes from the Court of Appeals for Highland County and deals with the surety bond on a sewer project. When the contractor and supplier modified the contract terms, did the surety still have to pay? It all depended on the terms of the surety bond, according to the court. Mahoning County supplied our final case, which arose from the planned renovation of a Youngstown office building for government offices. The renovation never took place, but the courts had to decide who breached the contract.

For a topic of interest in both public and private construction projects, turn to Holman, Gillis &

Wampler on Construction Documents, which this month takes up the subject of payments to subcontractors. What is said about these payments in the General Conditions? Perhaps more than you think. Sam Wampler’s other column, the ADR Corner, continues its discussion of principled negotiation by illustrating how you can begin to resolve a construction problem by “Bisecting the Problem.” Scarpels ready? Begin!

One corner leads to another, our regular OSHA Corner, which highlights some problems and accidents OSHA has been investigating lately (again, no particular emphasis on public projects). Then our occasional column on Indoor Air Quality puts in an appearance. (We know you will want to read about the theory of toxic furniture.) And we conclude, as usual with a brief listing of upcoming seminars.

April has been a busy month for all of us. So sit down, put your feet up, tilt your monitor to just the right angle, and see what this month’s ohioconstructionlaw.com has to offer.

# Does Your Low Bidder Have the Financial Ability To Complete Your Project?

## Introducing a new document - the *Low Bidder's Financial Responsibility Affidavit*



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### Introduction - The Need for Diligence

Last month, our lead article warned that the construction industry is in the midst of a recession. There is too little work. Too many contractors are chasing too few projects. The result? Some of the weak will not survive. What can an owner do to avoid being caught with a project half built when a contractor fails?

Bricker & Eckler LLP will address these issues in detail during its part of the 2003 BASA/Triad School Facilities Conference and Facilities Fair on May 13 and 14. But the challenge extends beyond the construction of school facilities. Every owner hopes that the low bidder will have the financial ability to complete the project without resorting to the surety. Is there anything an owner can do to be sure of that?

This article provides some of the answers and some practical suggestions, including a new concept created by the Construction Department of Bricker & Eckler LLP: the **Low Bidder's Financial Responsibility Affidavit**. **If there is a single idea you use after reading this article, it should be the Low Bidder's Financial Responsibility Affidavit.**

### Bidder Responsibility

The statutory standard of bidder responsibility and the discretion of boards of education are now firmly established in Ohio case law. A board of education can reject a low bidder as a matter of its discretion if the low bidder is not responsible. In evaluating whether a low bidder is responsible, one criterion boards of education often look at is the bidder's ability to complete the project without resort to its surety. Gathering and evaluating information about a low bidder's finances thus becomes key for any owner if the project is to go smoothly.

### Requesting Financial Information

On most public projects, the bidding documents will require the low bidder to submit financial information. The board of education has express authority to require this under the amendments to § 9.312 of the Revised Code. These amendments require the board of education to keep this financial information confidential and specifically exclude this financial information from the definition of a "public record."

**Key Questions.** So what financial information should a board of education request from an apparent low

bidder? What level of information is needed to determine whether a bidder is responsible? How does an owner know if the information in a bidder's financial statements accurately reflects the bidder's **current** financial status? To answer these questions, it is necessary to understand the types of financial statements that are commonly available and how often they are prepared.

**Types of Financial Statements.** A financial statement is a written report that quantitatively describes the financial health of a company. A financial statement generally consists of six standard documents:

- Balance Sheets,
- Statements of Income,
- Statements of Changes in Stockholders' Equity,
- Statements of Cash Flow,
- Notes to Financial Statements, and
- Supplementary Information.

These documents are the meat of the financial statement and provide information on the company's assets, liabilities, net worth, etc.—all indicators of the financial condition of a company at a specific point in time. Remember this last statement: **indicators of the financial condition of a company at a specific point in time.**

Although financial statements usually contain the same documents, the real difference between different types of financial statements depends on, first, who prepared the statement and, second, the level of investigation used to develop the information contained in the financial statement. Financial statements can be prepared internally or externally, each with different pros and cons.

**Internal financial statements** are often referred to as an In-House Report. In-House Reports are prepared by an internal staff member of the company. The benefit of In-House reports is that they are usually prepared on a quarterly, or even a monthly basis. However, because there is no disinterested third party involved in the preparation of the In-House reports, these reports can be less objective and have a higher likelihood of containing inaccuracies than financial statements prepared externally.

**External financial statements**, which are prepared by a certified public accountant (or CPA, for short), are appropriately referred to as "CPA Reports." The three main types of CPA Reports are Compilations,

Reviews, and Audits. These types of financial statements differ in the level of investigation performed by the CPA to ensure that the underlying information is accurate, with the Audit receiving the most scrutiny.

As Bradford Eldridge, of GBQ Partners LLC, discussed in our November 2002 issue of ohioconstructionlaw.com, a **Compilation** of Financial Statements presents information that is the representation of the company's management, without any undertaking by the CPA to express any assurance on the statements. A **Review** of Financial Statements is a step up from that; the numbers still come from management, but the CPA performs inquiry and analytical procedures before assembling them. Finally, an **Audited** Financial Statement requires even more investigation by the CPA, who must look into and understand all areas of the company's finances.

Time Sensitivity of Financial Statements. Because they are not prepared directly by the company, CPA Reports, especially an Audited CPA Report, provide more security to the owner of a public project.

However, there is a drawback. CPA Reports are generally prepared on an annual basis due to their complexity, which means that their reliability usually will be limited to a specific point in time. For example, in January a contractor may have an audited CPA Report prepared, stating that the company is in good financial condition. That statement is accurate—for January. Then, the contractor may bid a project in December of the same year, and submit the financial statement prepared back in January. The information in the financial statement provided with the bid is eleven months old and may not accurately reflect the current financial status of the company. A lot can happen in eleven months.

Omissions from Financial Statements. The other issue to consider is that no matter what type of financial statement is prepared, the statement may not reflect all financial considerations that may be relevant to a public owner. Financial statements typically do not show issues such as outstanding mechanic's liens, which could affect the stability of a company.

Language for Your Instructions to Bidders. So with this background, what financial information do you want to request from your apparent low bidders? Here is a suggestion for language to include in your Instructions to Bidders:

Financial Information. Within five (5) days of the bid opening, each apparent low bidder will provide the Architect [or Construction Manager or Owner's representative] the following financial information:

- External Financial Statements. Provide financial statements prepared by your Company's certified public accountant for your Company's last three fiscal years, consisting of reviewed or audited financial statements. If less than three years of

such statements are available, provide statements for at least one year. Such financial statements shall include for each year a balance sheet, statement of income, notes to financial statements, and supplementary information, and, if available, statement of changes in stockholders' equity, and statement of cash flow.

*Apparent low bidders whose base bid is more than \$3,000,000.00 must provide these external financial statements; those with lower base bids must provide such statements if they are available.*

- Internal Financial Statements. Provide financial statements prepared by your Company and certified as true and correct by your Company's chief financial officer for the last three reporting periods for which they are available, e.g., last three months. You do not need to provide internal financial statements for any periods for which external financial statements are provided. Such financial statements shall include for each reporting period to the extent they are available a balance sheet, statement of income, notes to financial statements, and supplementary information, statement of changes in stockholders' equity, and statement of cash flow.

*Internal financial statements must be provided by each apparent low bidder.*

- Low Bidder's Financial Responsibility Affidavit. Using the form provided in the Bid Documents, provide the Low Bidder's Financial Responsibility Affidavit sworn to before a notary public by your Company's Chief Executive Officer and its Chief Financial Officer. If your Company operates in more than one State, the affidavit may be sworn to by the financial manager and executive responsible for operations where the Project is located.
- Confidentiality. The apparent low bidder shall deliver its financial statements in a sealed envelope marked "Confidential." The board of education and its agents shall maintain the confidentiality of the financial statements. The financial statements are not "public records."

## Low Bidder's Financial Responsibility Affidavit

Financial statements are time-sensitive. Their information may be stale, and they may omit information that could adversely affect your low bidder's ability to complete your project. An owner needs information on which it or its agents can rely that will reduce the time gap and require disclosure of omitted information. That is the purpose of the Low Bidder's Financial Responsibility Affidavit. Here is a suggested form for the Affidavit:

The information in the financial statement provided with the bid is eleven months old and may not accurately reflect the current financial status of the company. A lot can happen in eleven months.

**LOW BIDDER'S FINANCIAL RESPONSIBILITY  
AFFIDAVIT**

State of Ohio  
County of \_\_\_\_\_

The undersigned Chief Executive Officer (or local manager or executive when your Company operates in more than one State) and Chief Financial Officer (or local financial manager or executive when your Company operates in more than one State) of \_\_\_\_\_ (the "Company"), being first sworn, each swear that the following statements are true:

1. The financial statements delivered to the Owner or its agent by the Company present fairly in all material respects the financial condition of the Company as of their respective dates.
2. Since the date of the last financial statement presented to the Owner or its agent, there have been no material adverse changes in the financial condition of the Company, except as disclosed in writing in an attachment to this affidavit.
3. The Company is current in all of its tax payments, including federal withholding taxes, except as disclosed in writing in an attachment to this affidavit.
4. There are no liens filed by the Company's subcontractors or suppliers, regardless of tier, on the Company's projects in the State of Ohio, except as disclosed in writing in an attachment to this affidavit.
5. During the last three (3) years, no Owner or Owner's representative has given the Company notice of default with respect to any Project in the State of Ohio, except as disclosed in writing in an attachment to this affidavit.
6. The Company's surety bonding company has an A. M. Best rating of A- or higher, except as disclosed in writing in an attachment to this affidavit.
7. He or she is not aware of any claim, potential claim, liability, or potential liability that could adversely affect the ability of the Company to complete the Owner's project, except as disclosed in writing in an attachment to this affidavit.

\_\_\_\_\_  
Chief Executive Officer or  
Manager or Executive

\_\_\_\_\_  
Chief Financial Officer or  
Financial Manager or Executive

Sworn to before me, a notary public, by \_\_\_\_\_ and \_\_\_\_\_ on  
\_\_\_\_\_ day of \_\_\_\_\_ 200\_.

\_\_\_\_\_  
Notary Public

**Evaluating the Information**

Once the board of education or its agent gets the low bidder's financial statements and financial responsibility affidavit, how does it evaluate this information?

The person who looks at this information for the owner must understand financial statements in the context of the construction industry. Perhaps the board of education or its Architect or Construction Manager has someone with this expertise on its staff. Most likely that is not the case. There are, how-

ever, CPAs who routinely prepare and review construction company's financial statements. One of these trained professionals should be able to review the financial statements and financial responsibility affidavits submitted by apparent low bidders in a short time.

Spending a little money for this review may avoid huge problems in the future. The reviewer should quickly be able to identify the contractor whose finances are on the brink of disaster. Such a contractor may not be a responsible bidder. A board of education has

the discretion to reject such a bidder as non-responsible, and to request and evaluate the same kind of information from the next apparent low bidder. Preventing your project from being the one on which the contractor goes out of business will be worth the time and effort such a review takes.

NOTE: The authors express their appreciation to Robert A. Biehl, CPA, of GBQ Partners LLC, for his assistance in providing detailed information about the different types of financial statements.

# What the Legislators Are Considering...



**T**his monthly column focuses on legislation pending in Ohio that is of interest to the construction industry. Our goal is to provide a concise summary, including just enough information that anyone who wants to learn more will know where to direct questions about the bills. For the text of any particular bill, go to Bills Online, [www.legislature.state.oh.us/search.cfm](http://www.legislature.state.oh.us/search.cfm).

Occasionally, we will highlight a recently enacted law of particular significance or a pending bill that deserves more than two or three sentences. If you are interested in a bill we have previously highlighted, check out the specific back issue by going to our website, <http://www.ohioconstructionlaw.com/>.

## Summaries of Pending Legislation

### I. Building Codes

#### Including Drainage Protection in County Building Codes, H.B. 25, Rep. Gibbs (R, Lakeville)

This bill would make two changes in the law: It would authorize county commissioners to include regulations in county building codes to protect the existing surface and subsurface drainage when new construction is proposed; and it would repeal the legislation creating the Residential Construction Advisory Committee, which now exists in the Department of Commerce.

*Passed the House on 3/18/03; assigned to the Senate Energy, Natural Resources & Environment Committee.*

### II. Compensation & Wages

#### Compensatory Time in Lieu of Overtime, S.B. 26, Sen. Coughlin (R, Cuyahoga Falls)

This bill, which appeared in the 124<sup>th</sup> General Assembly as H.B. 138, would allow private employers to permit employees to take compensatory time off in lieu of receiving overtime pay. Also, both public and private employers could establish biweekly work periods and allow their employees to elect to work 80 hours within a work period. Opponents noted in the last session that the bill would violate Ohio's Prevailing Wage Law in construction.

*Assigned to the Senate Insurance, Commerce & Labor Committee.*

#### Prevailing Wage on School Construction + Ohio Contractors on Public Improvements, H.B. 45, Rep. Boccieri (D, New Middletown)

This bill, which appeared in the 124<sup>th</sup> General Assembly as H.B. 252, would remove the exemption for school facilities construction from R.C. § 4115.04, Ohio's Prevailing Wage Law. In addition, it would prohibit a board of education or the governing board of a school service center from awarding to any contractor from outside Ohio a contract for work on any public improvement supported at least partially by state money. The sponsor has requested that no hearings be held on the bill.

*Assigned to the House Commerce & Labor Committee.*

### III. Licenses

#### Making Unlicensed Practice of Certain Professions a Deceptive Trade Practice, H.B. 38, Rep. Willamowski (R, Lima)

Unlicensed or unregistered persons who perform, for pay, services for which a license or registration is required would be committing a Deceptive Trade Practice if this bill became law. Introduced for attorneys, the bill would apply to a list of occupations, including engineers, surveyors, real estate appraisers, and asbestos abatement contractors. Persons likely to be damaged or who have been damaged could sue the unlicensed person for in-

junctive relied and damages, and if a court determined that the defendant willfully engaged in the deceptive practice, it could award attorney's fees.

*Assigned to the House Civil & Commercial Law Committee.*

### IV. Public Projects

#### State Contractors: Fair Employment in Northern Ireland, H.B. 15, Rep. Miller (D, Cleveland)

This bill, which appeared in the 124<sup>th</sup> General Assembly as H.B. 186, would require any firm contracting to supply goods or services to the state or to construct a public improvement to implement the MacBride Principles of Fair Employment for any business activities in Northern Ireland.

*Assigned to the House Commerce & Labor Committee.*

#### Rural Accelerated School Building Assistance Program, S.B. 54, Sen. Carey (R, Wellston)

Assuring that every two years at least three rural school districts (defined as those whose territory covers more than 350 square miles) have the opportunity to have a project built under the auspices of the Ohio School Facilities Commission is the purpose of this bill.

*Assigned to the Senate Finance & Financial Institutions Committee.*

**Modifications Pertaining to Public Libraries, S.B. 55,  
Sen. Gardner (R, Bowling Green)**

Amid numerous proposals that affect libraries but have nothing to do with construction, one stands out: A proposal to raise the threshold for construction projects requiring competitive bidding from the current \$15,000 to \$25,000. If this bill passes, O.R.C. § 3375.41 would be amended.

*Assigned to the Senate State & Local Government Committee, where hearings are underway 4/30/03.*

**Main Operating Budget for Fiscal Years 2004-2005, Am. H.B. 95,  
Rep. Calvert (R, Medina)**

This mammoth bill would affect almost everything in the State, but one item is of particular interest. It would transfer the Office of the Fire Marshal from the Department of Commerce to the Department of Public Safety, a move thought to affect the interpretations of the Building Code.

*Passed the House as amended on 4/09/03; hearings are underway before the Senate Finance & Financial Institutions Committee 4/29/03 through 5/01/03 and before the Senate Education Committee on 4/30/03 and 5/01/03.*

**Drug-Free Public Works Projects, HB. 136, Ren. G. Smith (R, Columbus)**

If this bill becomes law, the General Assembly would require all contractors and subcontractors who work on public projects to have a written safety program that includes drug and alcohol testing. The Department of Administrative Services would be required to adopt rules for the program, which would have to include drug testing for all job applicants and random testing for both drugs and alcohol thereafter. Termination would be automatic for anyone found possessing drugs on the job.

*Introduced in the House on 3/25/03; assigned to the House State Government Committee.*

**V. Road Construction**

**Vehicles To Display Lights in Road Construction Zones, H.B. 18,  
Rep. Miller (D, Cleveland)**

If this bill passes, vehicles traveling through road construction zones when work is going on and signs are posted would have to display their headlights. Failure to do so would result in a penalty of one point against a person's driver's license and could lead to conviction for a minor misdemeanor, with increasing penalties for additional convictions.

*Assigned to the House Transportation & Public Safety Committee.*

**Transportation Budget, Am. Sub. H.B. 87,  
Rep. Buehrer (R, Delta)**

Two provisions in this large bill have received much of the attention: The proposal to reduce the prohibited concentration of alcohol in a driver's blood from .10 of 1% to .08 of 1%, and the 50¢ a day tax on rental cars. But the bill does much more, including appropriating some \$5.5 billion for the Department of Transportation and the Department of Public Safety. Also of interest to contractors is the fact that, if the bill passes, ODOT's pilot program to permit design-build projects for highways or bridges would become permanent.

*Signed into law by Governor Taft on 3/31/03.*

**VI. Workers' Compensation**

**Workers' Compensation Budget Bill, H.B. 91,  
Rep. Young (R, Leroy)**

Among the many provisions in this budget bill is one that would exempt employers, including construction contractors, from the Workers' Compensation program if they are of certain religious faiths.

*Passed both houses on 4/08/03 but not yet sent to the Governor for signing.*

# What the Courts Are Saying...



This month's focus is on public construction projects, as all three summarized opinions deal with one aspect or another of such projects. But first, we must update you on a case we have covered extensively, *Monarch Construction Co. v. Ohio School Facilities Commission*, 150 Ohio App. 3d 134, 2002-Ohio-6281. (See the July 2002 and November 2002 issues of [ohioconstructionlaw.com](http://ohioconstructionlaw.com), available on our website.) On April 2, 2003, the Ohio Supreme Court announced that it would not accept the case for review, at the same time refusing Monarch's petition for a mandamus (a request that the Supreme Court tell the Court of Appeals what to do). In the courts of Ohio, this case should now be over.

The Ohio courts have been busy, though, with other cases on public bidding and contracts. We begin with a case from the Hamilton County Court of Appeals that clarifies when a confidential document becomes a "public record." This case dealt with business records shared with county officials by a Port Authority to whom they had been given in confidence, but the decision could apply equally to a low bidder's financial information supplied under the recent

amendment to the public bidding law. Then we turn to the Court of Appeals for Highland County and its latest opinion on the circumstances that require a surety to step up and pay a contractor's obligation to one of its suppliers. Our third case this month arose in Mahoning County and deals with the contractual obligations when a planned government project never gets underway. Anyone involved in public construction will want to be familiar with these recent cases.

## Confidential Documents Don't Become Public Records Just Because Agency Shows Them to County

Businesses often need to disclose confidential information to government entities to further business purposes. What assurances do businesses have that confidential information will not be disclosed to the public? What if the business obtains a confidentiality agreement from the government entity? While Ohio law provides protection from disclosure of confidential information, certain actions can result in the waiver of those protections.

A case last month from the Hamilton County Court of Appeals, *State ex rel. Cincinnati Enquirer v. Sharp* (Mar. 14, 2003), 151 Ohio App.3d 756, 2003-Ohio-1186, examined these issues when a newspaper, claiming the legal protections were waived, sought access to confidential information. Although the case does not deal directly with construction, it could certainly be relevant to financial information disclosed by an apparent low bidder to a public owner under last year's amendment to § 9.312 of the Ohio Revised Code, which declares such information confidential and not a public record.

In the *Cincinnati Enquirer* case, an unnamed employer started negotiations with the Cincinnati Port Authority regarding the location, preservation, or expansion of its business within Hamilton County. The business and the Port Authority signed a confidentiality agreement specifically designed to invoke the protections of Ohio Revised Code § 4582.58, which protects financial and proprietary information submitted by an employer to a port authority from disclosure as a public record. Believing the documents were protected by both the confidentiality agreement and the statute, the business provided them to the Port Authority.

At one meeting in March 2002, the Port Authority shared some of the confidential information with Hamilton County senior staff personnel. The Port Authority staff collected the documents at the end of the meeting, and no copies were made during the meeting. About one week later, a reporter with *The Enquirer*, a Cincinnati newspaper, requested the Port Authority produce the documents. The Port Authority declined the request, and the newspaper filed suit (a mandamus action) to compel disclosure of the information.

Two years before, the Ohio legislature had enacted R.C. § 4582.58 specifically to shield information submitted to a port authority from the public records law. Because of this statute, both parties agreed the information was initially protected by the confidentiality agreement and R.C. § 4582.58. However, *The Enquirer* argued the statutory protections were waived when the county reviewed the documents during the March 2002 meeting.

The Ohio Supreme Court has narrowly defined when a waiver of the public records exemption exists. According to the Court, exemptions are usually fully applicable unless a public office with custody of the records discloses the records to the public. However, the protections can be waived through the business' conduct or the conduct of others in several situations. Clearly, information made public by a business will not be protected under the statute. Information disclosed at trial is part of the court record, and the record becomes public information at the conclusion of the trial.

Under Federal public records laws, a federal agency will lose exemptions only if it officially releases the information or when the exact information is otherwise in the public domain. Federal courts have also emphasized that a waiver does not necessarily occur when the public office that possesses the information makes limited disclosures to carry out its business.

Here, the court found the documents were exempt from disclosure under the public records law because the information was never made *public*. The business did not publish the information to the public, nor was it available in the public domain. The information was not disclosed during court proceedings, and the Port Authority did not officially release the information. The Port Authority limited its disclosure to the county to further the economic development plans of the business. Sharing this information with the county for this limited purpose is not a waiver of the exemption.

So, what can we learn from this? Businesses and government entities should be aware that while protections do exist for their confidential information, an inadvertent act—even an act by a government agency—could result in the waiver of those protections. Here, the Port Authority took every precaution and collected the confidential documents after the one-time meeting. If the documents had been treated with less care, had been shared at several meetings, or had been on display at some meeting where the public could have seen them, the outcome of this case might have been different. Then, the information in those documents could have made front-page headlines.

## Court Enforces Terms of Payment Bond Despite Modification of Contract

Surety bonds provide added assurance that a contractor's work will be done or its bills will be paid. On a payment bond, the contractor—known as the "principal" on the bond—contracts to have someone else—the surety—liable for payment to third parties, such as the contractor's materialmen, if the contractor should become unable to make the payments.

The Ohio Supreme Court has narrowly defined when a waiver of the public records exemption exists. According to the Court, exemptions are usually fully applicable unless a public office with custody of the records discloses the records to the public.

The owner, Highland County Water Company, made several payments to the contractor by joint checks made payable to Grooms and its suppliers. Because the contractor used the first check to pay the pre-existing balance on the open account, the payments were always behind.

But is a surety bond a guarantee that payment will always be made, either by the contractor or by the surety itself? No. Sureties have defenses against the contractual obligations created by the payment bond, but, because the relationship is contractual, a

surety can lose or waive these defenses by the language of the contract. Recently, the Highland County Court of Appeals took a fresh look at these issues in *Water Works Supplies, Inc. v. Grooms Construction Co., Inc.* (Mar. 24, 2003), Highland App. No. 01-CA-18, 2003-Ohio-1527.

The appellate court found the surety, Fidelity & Deposit Company of Maryland, liable for payment to the supplier, Water Works Supplies, Inc., despite the surety's defense that the supplier had altered its contract with the general contractor by extending the time for the general contractor to pay. Normally, such a defense would have protected the surety, but here the court found the surety's own contract contained a waiver of that defense.

Grooms Construction Company was the general contractor on a sewer contract for Highland County Water Company. Grooms obtained its supplies for the project from Water Works, pursuant to an "open account" agreement. Because Grooms had an outstanding balance on this account before the sewer project began, Water Works was reluctant to provide more supplies. It agreed to do so based in part on its understanding that there was a payment bond on the project.

The owner, Highland County Water Company, made several payments to the contractor by joint checks made payable to Grooms and its suppliers. Because the contractor used the first check to pay the pre-existing balance on the open account, the payments were always behind. Still, Water Works endorsed the first two checks and the contractor cashed them, paying a portion to Water Works.

Then came the third joint check; Water Works endorsed it but received nothing in return. So Water Works made a claim to the surety for the outstanding balance, which was over \$300,000. The surety refused to pay because Water Works had impaired the surety's rights when it endorsed the joint checks without insisting on the proper payment. The supplier had, in effect, changed the terms of its contract with the general contractor, fundamentally altering the surety's risks on the payment bond by extending the time for payment.

Generally, when the principal (Grooms) and the creditor (Water Works) extend the time of payment by the principal without the consent of the surety, the surety is discharged from its obligation on the payment bond. The court cited three reasons for this rule: 1) The extension of time creates a new contract between the contractor and supplier; 2) The time extension impairs

the surety's subrogation rights, depriving it of the option of performing the original contract; and 3) The time extension increases the surety's risks that the contractor may become insolvent or otherwise unable to perform.

The court found that the Water Works' payment arrangement by Grooms did extend the time for payment. Without more, the surety would not have been liable to Water Works for payment. Indeed, the trial court, following this logic, determined that the surety was not liable.

But the appellate court went further, turning to the express language of the payment bond contract itself to see whether or not the unauthorized extension of time defense should prevail. The court found that the surety waived this defense by agreeing to this specific language in the contract: "No change, extension of time, alteration or addition to the terms of the contract or to the work to be performed thereunder or the specifications accompanying the same shall in any way affect [the surety's] obligation on this bond, and it does hereby waive notice of any such change, extension of time, alteration or addition to the terms of this contract or to the work or to the specifications."

The payment bond specifically waived the surety's right to raise the "extension of time for payment defense." If there were any doubt about this, the court said, it should be resolved against the surety, as the surety controlled the language of the payment bond. So the trial court had erred when it entered judgment for the surety, and the Court of Appeals sent the case back to the trial court for further proceedings.

The supplier's endorsement of joint checks without insisting on immediate payment of its full share could have gotten it into serious trouble. In some states, notably California, the endorsement would be viewed as proof of full payment, under the "joint check rule." Here, the court refused to apply that rule, and Water Works prevailed because of the specific language of the payment bond. Suppliers and subcontractors would be wise to look for such language in the payment bonds on their projects. Still, they would be foolish to rely on such language as a guarantee of payment. If a project owner pays by joint checks, suppliers and subcontractors should refuse to endorse any check without receiving the payment they have earned.

### **"Termination for Convenience" Clause Applies When Project Never Starts**

Sometimes, for a myriad of reasons, a public project is bid and contracted but never gets started. The claims that may arise when this happens depend on the specific circumstances, and the Mahoning County Court of Appeals looked at one set of circumstances last month in *Daniel E. Terreri & Sons, Inc. v. Board of Mahoning County Commissioners* (Mar. 10, 2003), Mahoning App. No. 00 CA 269, 2003-Ohio-1227.

In mid-1996, Mahoning County planned to renovate the old Higbee Building in downtown Youngstown to use as government offices. Terreri bid for two parts of the project, demolition (as a joint venture with Avila Contracting & Supply) and the roof and atrium. Together the contracts came to more than \$2 million and used up much of Terreri's \$3 million bonding capacity. Some 15 months after the bidding, Terreri got both of the contracts, which were signed on September 18, 1997.

Less than a month after signing the contract, Terreri sought a 15% increase in its base bid unless a notice to proceed was issued by October 31, 1997. Its letter of October 10, 1997, offered to **extend its bid** until June 30, 1998, based on the 15% increase. Otherwise, Terreri requested that its bid be withdrawn and its bond returned. As the court pointed out, the letter sounded as if Terreri believed "that the contracts were still in the bidding stage." The court considered this letter Terreri's "first step in repudiating the contracts."

Two more letters followed, on October 23 and December 1, 1997. In the last letter, Terreri declared that it was withdrawing from the contracts. The County waited until early April to announce that it had other plans and was not going to renovate the Higbee Building. In mid-April, Terreri and Avila sued the County Commissioners, the Architect, and two individual defendants (the County Administrator and the Auditor). They alleged several breaches of contract along with a failure to release the construction bond, allegedly causing lost profits. Following a three-day trial, a judge dismissed the individual defendants but awarded the plaintiffs \$471,000 in damages.

The County appealed, and the Court of Appeals saw the facts very differently. It began by looking at the "no damages for delay" clause in the County contracts. This was a very broad clause concluding with these words: "It is understood that such Contractor, Subcontractor, or other Contracting Party assumes all risks of delay in prosecuting or completing the work under this contract." Here, any delay was prior to a notice to commence, as one had never been issued. But the contract set no time limit on when such a notice should be issued. (Deadlines for various parts of the project were stated in calendar days from the issuance of the notice to commence.)

"In Ohio," the court said, "a 'no damages for delay' clause is a valid and enforceable contract provision." The clause here was broad enough to encompass delays in allowing the contractors to begin work, so a delay in issuing the notice to commence did not put the County in breach of its contracts.

On the other hand, the contractors, Terreri and Avila, were "in total breach of the contracts by anticipatory repudiation on December 1, 1997," the date of their third letter, which announced that they were revoking their obligations under the contracts and requesting the return of their bond. At this point, according

to the court, "it would have been a useless gesture for [the County] to issue a notice to proceed as [the contractors] had made their repudiation of the contracts absolute."

The court looked briefly at the exceptions to enforcement of "no damages for delay" clauses, but only one of these would have justified the contractors in abandoning the contracts. That required a delay for "an unreasonable length of time," and the court found that delays before December 1, 1997, were reasonable. So the contractors' abandonment was unjustified.

Before reversing the trial court's decision, the Court of Appeals investigated another basis for ruling in the County's favor, the contract clause permitting termination for convenience. The contractors claimed this was not applicable because they had not received the required written notice of termination. The court pointed out the flaw in this logic: "It is inconsistent for [the contractors] to argue that [the County] did not strictly comply with the notice requirements of the 'termination for convenience' clauses of the contracts when [the contractors] themselves sent written notice that the contracts were terminated."

Still, under the termination for convenience clause, the County would be liable to pay the contractors for any cost directly resulting from the termination. So the Court of Appeals returned the case to the trial court for a consideration of the "termination for convenience" costs. The court did, however, make one thing clear: The trial court could not consider lost bonding capacity—which had accounted for \$118,500 of the original award—as part of these costs. The County had never been told of the contractors' bonding limits, and there was no proof that the parties had contemplated liability for such costs when they made the contracts.

This case is another interesting example of the truism that "it's not over till it's over." The trial court looked at the same contracts that were before the Court of Appeals, conducted a three-day trial, and concluded that the County owed the contractors \$471,000 for lost profits and lost bonding capacity. Looking at the same contracts, the same "no damages for delay" and "termination for convenience" clauses, and the same facts, the three-judge appellate panel concluded that the contractors had abandoned the contract and were not entitled to lost profits or recovery for lost bonding capacity. The lesson? Don't believe anyone who tells you the law can be predicted.

It should also be noted that the facts of this case predated Ohio's "fairness in contracting" statute, § 4113.62(c), which restricts the use of "no damage for delay" clauses.

Here, any delay was prior to a notice to commence, as one had never been issued. But the contract set no time limit on when such a notice should be issued.

HOLMAN, GILLIS AND WAMPLER ON

# Construction Documents

## Payments to Subcontractors —Serious Business

*Thirty-fifth in a Series—Each issue of ohioconstructionlaw.com discusses important terms found in typical construction documents. This month, Sam Wampler reviews the Provisions of AIA Document A201-1997, the General Conditions, that govern payments to Subcontractors.*

**Overview:** When an Owner, whether public or private, wants to construct a building or other improvement, it ultimately enters into a contract with a Contractor to construct the Project. Often, however, the Contractor is simply the person or entity with whom the Owner conducts its business, and Subcontractors with whom the Owner has no contractual relationship perform the actual construction. This arrangement presents several issues because an Owner cannot enforce the Subcontract (except in certain circumstances) against the Subcontractor, nor can the Subcontractor enforce its Subcontract against the Owner (again, except in certain circumstances.).

What guidance do the General Conditions, AIA Document A201-1997, provide? This article looks first at the relationship between the Contractor and Subcontractor, and how that relationship is governed to some degree by the Contract between the Owner and Contractor under the General Conditions. Secondly, we look at how payments to the Subcontractor are controlled by the General Conditions of the Contract in such a way as to protect the Project and the parties.

**The Contractor/Subcontractor relationship.** The relationship between a Contractor and a Subcontractor is in many ways like the relationship between the Owner and the Contractor. In the Owner/Contractor relationship, the Contractor is responsible to the Owner for performance of the Work and the Owner is responsible to pay the Contractor for its Work. For more detail on payments, see our earlier article, “Show Me the Money”—Payments Under the AIA Documents, An Introduction to the Payment Process and Retainage for Public Projects, in ohioconstructionlaw.com for July 2001 (available at www.ohioconstructionlaw.com). The Owner does have a measure of control over the Subcontractors under the General Conditions of AIA Document A201-1997.

Article 5 of the General Conditions governs the rights of the Owner and Contractor with regard to Subcontractors. For instance, the Owner can reject a



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Subcontractor as provided for in Subparagraphs 5.2.1-.4. See *Selecting (Or Deselecting) The Subcontractors: The Owner's Privilege To Reject a Subcontractor— But Possibly at a Price*, in ohioconstructionlaw.com

for May 2002. The agreement between the Contractor and Subcontractor must also adhere to the Contract between the Owner and Contractor to the extent necessary to protect the rights of the Owner. See Subparagraph 5.3.1. This means that a Contractor cannot require a Subcontractor to agree to any terms that would infringe on the rights of the Owner.

Under the General Conditions, to protect the Owner in the event of the Contractor's default, the Contractor also assigns each of its subcontracts to the Owner, which assignment is only effective upon termination of the Contractor and acceptance of the assignment by the Owner. See Subparagraph 5.4.1. This allows the Owner to continue with the Work using the Contractor's Subcontractors in the event the Contractor is terminated for cause, thereby allowing the Owner effectively to mitigate its damages caused by the default of the Contractor.

**Payments to Subcontractors.** The success of every construction Project is, at its most basic level, a function of two factors: *time* and *money*. A realistic schedule, coupled with effective communication and schedule updates will usually manage the time aspect of a Project, although unforeseen circumstances such as unusually inclement weather (*Snow & Rain & Hail & Sleet Making the Claim for Weather Delays*, in ohioconstructionlaw.com for August 2001), unforeseen site conditions (*OPENING PANDORA'S BOX: The Importance of Planning for Differing Site Con-*

*ditions*, in ohioconstructionlaw.com for September 2001), or other such occurrences can negatively impact the duration of a Project to such an extent that nothing but money can bring it back on track (acceleration, augmenting of workforces, overtime, etc.), and even that may not be possible.

As with time, money is also something the parties can control with a degree of precision and accuracy throughout the Project. Perhaps the least scientific aspect of the money factor is the schedule of values. AIA Document G703 is the Continuation Sheet for the Application for Payment and contains the schedule of values for the Project. Using this sheet allows the parties to break the Project down into components and provides a ready accounting on an item-by-item basis for the Work as it is completed. In addition to showing the scheduled value for each item of the Work, the Continuation Sheet also shows the retainage held by the Owner for each item of the Work.

Once the schedule of values is reviewed and accepted by the Architect and the Owner, it acts as a control document for the flow of money throughout the Project. At any point in the Project, the Owner, Architect or Contractor should be able to look at the current Application for Payment, and by looking at the attached schedule of values determine how much (% and \$\$) has been paid for any particular component of the Project.

The Architect uses the schedule of values to confirm that the amount sought by the Contractor is appropriate to certify for payment. In this way, the Owner, Architect, and Contractor are all working within each other's expectations when it comes to Progress Payments, because the Schedule of Values helps to eliminate financial surprises for everyone. For a more detailed discussion of the role of the schedule of values, see *"Where's the Beef?"—Progress Payments Under the AIA Documents*, in ohioconstructionlaw.com for August 2001.

For a Project that uses Subcontractors, the schedule of values enables the Owner to determine on an ongoing basis the status of the Work related to various subcontracts. In the event the Owner elects to terminate the Contractor and accept the assignment of a subcontract or subcontracts, it has a basis to determine how much is owed to the Subcontractor(s) and may proceed to complete the Work on the basis of this accounting.

**What can go wrong?** When the Contractor submits its Application for Payment on AIA Document G702-1992, it certifies in a sworn statement to the Owner "that all amounts have been paid by the Contractor for Work for which previous Certificates for Payment were issued and payments received from the Owner." What this means is that if a Contractor is paid for a previously certified Application for Payment, it must pay its Subcontractors for amounts received from the Owner before it submits another Application for Payment with the sworn statement referred to above.

Sometimes a Contractor may have a dispute with a Subcontractor over a backcharge, or perhaps the Contractor withholds more retainage from the Subcontractor than is withheld by the Owner. In either event, the Contractor is at risk when it submits its next Application for Payment without disclosing these variances from its usual sworn statement as to previously approved and received payments.

Take, for example, a Contract for public construction. The Owner is limited by law as to the amount it may withhold from a Contractor for retainage, R.C. 153.12-.14. Retainage for labor is withheld at the rate of 8% of the first 50% of labor for the Work billed. This is calculated from the schedule of values on an item-by-item basis. Retainage on materials and equipment is withheld at the rate of 8% for all material and equipment stored or delivered to the job site, but not yet incorporated into the Project. Once such materials and equipment are incorporated into the Project, the balance (retainage) is paid to the Contractor.

Sometimes, a Contractor will provide for a different amount of retainage in its subcontracts, e.g., 10% of the subcontract amount until completion of the Work thereunder, without distinguishing between labor and material or equipment. This can be detrimental to the Owner and is not permitted by the General Conditions.

Subparagraph 9.6.2 of the General Conditions sets down the rule:

The Contractor shall promptly pay each Subcontractor, upon receipt of payment from the Owner, out of the amount paid to the Contractor on account of such Subcontractor's portion of the Work, the amount to which said Subcontractor is entitled, *reflecting percentages actually retained from payments to the Contractor on account of such Subcontractor's portion of the Work.*

From this language it is clear that the Contractor cannot withhold more retainage from its Subcontractors than is withheld by the Owner under the Owner/Contractor agreement. This is consistent with protecting the Owner from Contractors who default on their obligations and are terminated in accordance with Article 14 of the General Conditions. Otherwise, the Contractor, when terminated, will have money belonging to Subcontractors. If the Owner accepts the assignment of the subcontracts upon termination of the Contractor, the Owner may have to pay twice for a portion of the same Work.

Let's look at how a Contractor's improperly withholding excessive retainage in violation of the General Conditions can impact an Owner.

Sometimes, a Contractor will provide for a different amount of retainage in its subcontracts, e.g., 10% of the subcontract amount until completion of the Work thereunder, without distinguishing between labor and material or equipment.

- Suppose you are a public Owner building a Project and you have a prime Contract with the general trades Contractor for \$6,000,000.
- Assume further that the total labor for all aspects of that Contract is \$2,500,000 and that the Contractor subcontracts all of the Work with various Subcontractors (the total value of the subcontracts is \$4,500,000 after the Contractor's profit and overhead).
- The most retainage that can be withheld from the Contractor is 8% of the first 50% of labor, or the total sum of \$100,000 (8% of \$1,250,000). Assuming a linear progression of the Work, this retainage will reach its maximum halfway through the Project.

If the Contractor's subcontracts provide for a higher and different method of retainage, the Contractor will end up holding much of the Subcontractors' money while all the time telling the Owner the Subcontractors have been paid. In our example, if the Contractor withholds 10% as retainage from progress payments to its Subcontractors, by the halfway point of the Project, it will have withheld \$225,000 (10% of \$2,250,000) from the Subcontractors, or \$125,000 more than was withheld by the Owner.

As the Project progresses from there, the Owner will not withhold any further retainage, while the Contractor may continue to withhold up to another \$225,000 from its Subcontractors, all the while telling the Owner in each Application for Payment that all previous payments have been made to the Subcontractors, "reflecting percentages actually retained from payments to the Contractor on account of such Subcontractor's portion of the Work."

If the Owner decides to terminate because the Contractor fails to perform or becomes insolvent, the Owner will find itself dealing with Subcontractors who will be reluctant to perform their subcontracts without assurances they will be paid their full retainage—retainage that is held by a terminated Contractor and one who may now be insolvent. Although the General Conditions guard against this result, such arrangements find their way into the world of public contracting and present risks that are usually unknown to the Owner until after the damage is done. Fortunately, the public Owner has a Payment and Contract Bond.

**Conclusion.** Owners, Contractors and Subcontractors need to understand the requirements of the General Conditions when it comes to withholding retainage from payments under the Contract and Subcontracts for the Project. The schedule of values provides an excellent guide for making payments. A Contractor who deviates from its retainage agreement with the Owner in its subcontracts is walking on thin ice. With each Application for Payment, the Contractor subjects itself to claims for breach of contract and perhaps even fraud when it certifies that all previous payments have been made to its Subcontractors when in fact it is withholding additional retainage prohibited by the General Conditions.

Some Contractors may follow this procedure innocently as a result of not understanding the Contract Documents, but others deliberately enjoy floating on the Subcontractor's money until the job is complete. For Owners, the risk is that the Contractor will not only enjoy the float but also spend it, placing the Project at risk of final completion. This may be fine for the Contractor, but it is not good for the Owner or the Subcontractors who are left to clean up after a Contractor who floated off into the sunset with their money.

A Contractor who deviates from its retainage agreement with the Owner in its subcontracts is walking on thin ice.

## Construction Claims 101

This seminar will teach both management and field-level personnel important concepts and give practical advice on identifying, avoiding, and winning claims on construction projects, with special emphasis on helpful job documentation techniques.

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- Commonly made claims
- Claims Documentation
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For more information, call Mark at 614.227.4892 or Doug at 614.227.4803.

# ADR Corner

## Negotiating a Resolution—Bisecting The Problem

If you read last month's article, you will recall the scenario with Always Rosy Schools and the construction of its new middle school. The project was behind schedule, the contractors were pointing fingers at each other, and as the Superintendent of Rosy Schools you were about to sit down with the Architect, Construction Manager, and the contractors to resolve the schedule problem.

Now let's add to the facts a little. Shortly before the meeting you receive an executive summary from the construction manager, and you learn that the steel contractor is blaming the mason for holding him up. You also learn that some of the steel was not fabricated properly and by the time it was in place the roofing contractor was delayed. However, the roofing contractor was late in getting submittals approved for a substitute material it preferred for performance and price reasons. Amidst all of this, the plumbing, electrical and HVAC contractors have been grumbling about not having space to work in when they send out their forces. No one has filed a formal claim yet. All you want is for your new middle school to open on time at the end of August.

While all school districts do not get their superintendents this involved in their construction programs, often it takes an executive meeting to shake the tree and get the project moving. Emotions are running high; potential claims are right around the corner; and the project is in jeopardy of not being completed on time. As the Superintendent of Always Rosy, how do you approach this problem?

There are many ways to approach this type of meeting, but in my view there are two very specific ways: The inefficient way and the efficient way. Remember, the time for this meeting is probably limited. All of the key decision makers should be present, and it is likely they will have other meetings to attend. This is not the time to shoot from the hip. Planning is vital.

Before going into such a meeting you should define and prioritize your goals. What *must* you come away from this meeting with? What *should* you come away with? What would you *like* to come away with? You might think of this as the "*must, should and like list*"—in that order. Defining your goals in this way will give structure to the meeting and will ensure an efficient use of the time allotted for the meeting. Let's look at the wrong way to approach this meeting first; reflect on how a little planning will give structure to the problem solving; and look at how a prioritized agenda will aid in resolving the dispute efficiently.

INEFFICIENT (Responsibility first, no time left for Action Plan):

**Superintendent:** I want to thank everyone for taking the time to attend this important meeting. (So far, so good.)

First I would like to know how we find ourselves in such a mess. (Uh-oh.)

**Mason:** The CM is always moving me around to satisfy one of the other contractors, and I can never finish my work in any one area.

**CM:** If you added more masons earlier like we told you, we wouldn't find ourselves in this situation.

**Steel Contractor:** That's right, and if he would just finish one area and move to another, I could get my steel in on time. This is very frustrating!

This is what can happen when you start a meeting at the end instead of the beginning. In my opinion there is no less efficient way to start a meeting of this type than with a historical dialogue of how you got there. Here it escalated the conflict and totally ignored the highest priority of the Superintendent: to get the school open on time.

There probably aren't any reliable studies on the percentage of disputes during construction projects that are resolved through negotiation, as compared with mediation, arbitration, or litigation, but I am willing to bet that the percentage is in the high 90s. I think of a negotiation as any situation that calls for the mutual agreement of two or more parties on what will happen next with regard to any circumstance(s). People on construction projects negotiate almost everything on some level all day long every day. "How many masons are you going to have on the job tomorrow? No more than I have to. You are going to need at least 25. I can't possibly have that many, how about 20? All right, but let's see if we can get up to 25 next week, O.K.? Sure, thanks a lot, and I will see if I can't have 25 here next week." That was a simple negotiation—it goes on all of the time. These parties didn't need a mediator, arbitrator or judge to resolve this problem. They just negotiated what was going to happen next.

Last month I introduced the readers to principled negotiation. This approach to negotiation has been and continues to be studied at the Harvard Negotia-



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tion Project. Over the years the Project has observed human behavior that has shaped their theories in the field of negotiation. While their theories have changed over the years, the basic principles have remained the same:

- Separate the people from the problem;
- Identify and focus on interests, not positions;
- Explore options for mutual gain; and
- Use objective criteria to legitimize an agreement.

This month I will focus on the first principle—*Separate the people from the problem*—and demonstrate its value in resolving construction disputes, particularly those that relate to time-sensitive issues. I believe this may well be the single most important step the parties can take when attempting to resolve a serious dispute during a major construction project, particularly if the dispute involves multiple parties and the need to keep the project moving.

Let’s help the Superintendent for Always Rosy Schools plan for the meeting. Remember, *must—should—like*:

Developing an action plan first separates the people from the problem. The whole issue of responsibility for the problem and the consequences of the schedule slippage is secondary to the more important issue of getting the project back on track, and the meeting should necessarily proceed in that order.

**Must—**

- Have occupancy in time to open school in August
- Recover from the schedule slippage
- Define critical areas for recovery
- Develop an action plan for recovery
- Determine who must do what
- Establish firm milestones for recovery

**Should—**

- Set up a process to monitor adherence to recovery plan
- Weekly report to the Superintendent of Always Rosy
- Monthly follow-up meetings until complete
- Set up a process to address failure to adhere to recovery plan
- Establish additional costs to implement the recovery plan

**Like to —**

- Determine what happened to cause the schedule to slip
- Determine who contributed to the schedule slippage
- Determine whether contractors have claims for schedule slippage

This is a simple but effective plan. Notice that the Superintendent has focused the first part of the meeting on action to resolve the immediate concern—completion of the middle school on time. This accomplishes two things: 1) It immediately makes

the meeting a collaborative process—the team must focus on the highest priority of the Project, completion on time; and 2) It avoids the less productive discussion of who is to blame for the problem facing the team at the moment. I call this “bisecting the problem.”

Developing an action plan first separates the people from the problem. The whole issue of responsibility for the problem and the consequences of the schedule slippage is secondary to the more important issue of getting the project back on track, and the meeting should necessarily proceed in that order. Otherwise the parties could very well consume the entire meeting with argument on who is at fault without ever addressing the process of recovery.

It takes a firm commitment from the Superintendent to insist that the meeting proceed in this manner and that the parties stick to the agenda. In this way, before any discussion takes place about blame, fault, responsibility, etc., the parties must agree on an action plan to recover from the schedule slippage. Often the meeting will run out of time to resolve all of the issues, but if nothing else happens, it is important the parties agree on a process to complete the project on time.

Now, let’s look at how the Superintendent might start the meeting in light of the agenda:

EFFICIENT (Bisect the problem—Solution first, responsibility second):

**Superintendent:** I want to thank everyone for taking the time to attend this important meeting. When we started this project a year ago, I was confident that this team would complete this project on time, and I still have that confidence. But we need to leave this meeting with a plan today, and that is first and foremost on our agenda.

While I realize there are reasons we are behind schedule, I am less interested in those reasons than I am in how we are going to recover from where we are today. I know there is a way to do this, and by the time we leave today we will have found out how that is going to happen. I am depending on all of you here today to help us figure this out because without the benefit of your experience and knowledge of this project, it won’t happen.

Because completion is so important to this project, I must insist that we not discuss who might be responsible for our problem unless and until we agree on an action plan to finish this job on time. Will everyone at least promise to stay focused on arriving at an action plan first before we start talking about whose fault it is that we had to come to this meeting? [At this point, the Superintendent should go around the table and get a firm promise to follow the agenda and the rule

that there will be no accusations, complaints or finger pointing until after an action plan is reached and agreed on.] Once that is accomplished, we can then move on to the questions regarding responsibilities for our problem and how to address them. Any questions? OK, would the CM please present a proposed revised schedule to recover from this problem and let's go around the table one at a time and give your input. Once we have gone around once, we will then begin a discussion as a team to fine-tune this plan and make those adjustments that everyone can live with. Remember, action plan first, discussion about why we're here later.

What has happened here? First, the Superintendent took charge of the meeting. The participants were thanked for taking time for the meeting, and the confidence of the Superintendent in the team was affirmed. This starts the meeting on a positive and collaborative note. The problem was then bisected, in part by separating the people from the problem. There will be no discussion about whose fault it was that the schedule slipped. Instead, the entire focus will be on solving the problem caused by the schedule slippage, the completion date. This is a problem for everyone sitting at the table. This will help to keep much (not all) of the emotion out of the first part of the meeting. The parties can do what they do best, figure out how to build the middle school by the end of August.

This is not to say that some finger pointing will not set in throughout the meeting, but it is up to the Superintendent who is running this meeting to remind the parties of their promise. Unless the finger pointing is contributing to the action plan, it has no place in the meeting at this point. Having a definite goal and a corresponding agenda gives the parties a reference point in their meeting to control the discussions toward an orderly and productive result.

When running such a meeting, you may be required to cut off a participant who is straying into issues of fault/responsibility before the action plan is complete. Always assure them that you will get back to the issue of fault/responsibility if time permits, or it can be rescheduled to a later time. In this way that party will not feel cut out of the discussion, only postponed.

The Superintendent of Always Rosy is off to a good start by taking the time to plan the meeting, building an agenda that is prioritized and addresses the *must, should, and like* issues. By separating the people from the problem, the team can now focus on building an effective action plan that will achieve the goals announced by the Superintendent. In the context of a construction problem that is time sensitive, this approach helps the parties focus first on developing an action plan to resolve the primary problem of time, and reserves the more emotional issues for later. The next time you have a meeting that addresses

time-sensitive matters, try bisecting the meeting—solution first, fault second.

Next month we will pick up with the second principle in principled negotiation, having the parties *focus on interests, not positions*. As we shall see, the Superintendent for Always Rosy Schools has already headed the parties in this direction in the agenda, but we will see how exploring interests can reveal issues formerly unknown to the parties and may uncover opportunities for mutual gain. Check back next month and see how the Superintendent implements the plan and facilitates the meeting by focusing on *interests*. Bear in mind, principled negotiation is often referred to as "*interest-based negotiation*." More on that in May.

When running such a meeting, you may be required to cut off a participant who is straying into issues of fault/responsibility before the action plan is complete.

## Did you know?

**W**e have indexed the first 35 issues of [ohioconstructionlaw.com](http://ohioconstructionlaw.com), and the three indexes—for 2000, 2001, and 2002—are available on our website,

[www.ohioconstructionlaw.com](http://www.ohioconstructionlaw.com).

Whether you want to find references to a specific case, articles written by a particular person, or commentary on a topic of interest, just go to the annual index at the top of the website and scroll down (or better yet, do a "find," using "Control-F" if you really know your way around the Internet), and you will come to a listing of everything we published about that case, by that author, or on that topic during the specific year.

For instance, a search for "Bidding" in 2002 turned up eleven entries: 4 lead articles, 5 case summaries, and 2 highlights of related bills. Once you find these, what do you do? Just scroll further down the page until you come to the particular month that includes the article you want to read. All 39 of our issues (counting this one) are available at our website, at no cost, and you can access them at any time—even after midnight!

# What's New in the World Of Job Safety?

*The Occupational Safety and Health Administration (OSHA) can seriously affect any contractor or construction project. Compliance with OSHA regulations can be time-consuming and tedious, but it is essential to maintain a viable position in the construction industry. This month, as always, we report on recent developments in the world of OSHA.*

## North Carolina Issues Alert Regarding Tilt-Up Panels

Tilt-Up building panels are favored over other construction methods in certain building applications. Casting complete concrete panels either on or off-site and then tilting them up into place can provide cost savings and allow for better quality control compared to other methods of wall construction. However, the technique is not as well understood as more traditional methods of construction. This lack of understanding can lead to tragic consequences, as an accident in North Carolina revealed last year.

The accident, in which three workers were killed and two injured, occurred when a 23-foot high x 20-foot wide concrete wall panel weighing 20 tons fell as seven workers were having lunch in the panel's shade. The workers were unaware that the recently placed panel's temporary braces were being removed.

An investigation revealed that, contrary to an inspector's report, several of the welds connecting the wall panel to the roof trusses were not completed. Neither was the bottom of the panel secured to the floor slab.

The North Carolina Department of Labor, which investigated the accident, issued a statewide alert because of the prevalence of Tilt-Up construction in the state and the apparent lack of knowledge about the Tilt-Up process. Fines totaling nearly \$33,000 against five different contractors are proposed in this particular accident.

## Excavating Near Overhead Power Lines Results in Fine

Since the project started in May 2002, a 142-mile natural gas pipeline running from Illinois to Wisconsin has had five known over-

head power line contacts. The most recent incident occurred when a truck boom hit a power line while unloading material. One worker was injured. In one of the earlier accidents a worker was paralyzed. OSHA has proposed a \$150,000 fine.

## Riding in Pickup Bed Results In Fatality, Willful Violation

Nowhere in the OSHA regulations will you find a specific prohibition against riding in the back of a pickup truck. However, there exists the omnipresent "general duty clause," which requires an employer to provide a safe working environment for all workers. Many citations are issued under the general duty clause when an accident occurs and no specific regulation fits the facts very well. Some of these are even for willful violations.

Such was the case recently when an employee was fatally injured on a road construction project when he fell while placing traffic warning signs from the back of a pickup truck. The employer argued unsuccessfully that since the truck was being operated off the road, it was not reasonable to assume such an injury could occur.

## OSHA Updating Cranes and Derricks Standard

In response to calls from industry, the OSHA negotiated rulemaking committee has begun the process to update OSHA's cranes and derricks standard. First, OSHA will pick members of the Crane and Derrick Negotiated Rulemaking Committee. OSHA's picks will then be subject to public comment. The first Committee meeting is expected in late Spring.

## Steel Erection Data Eagerly Awaited

The impact of OSHA's new steel erection rules, which went into effect in January 2002, has not yet been quantified. Preliminary statistics show that from January 18, 2002 to October 17, 2002, 38 steel erection worker deaths were reported across the U.S., compared to an average of 35 deaths during the same nine-month period over the previous seven years. But OSHA says it's too soon to make a statistical conclusion.

One area of controversy is that the rule allows a worker the option of tying off when working between 15 and 30 feet. Proponents of this exception point to incidents where workers were killed when they could not disengage their safety harnesses from a piece of steel that had fallen, and they were consequently crushed. Opponents point to examples of untied workers slipping and falling.

There will be a formal evaluation of the new rules after three years.

## Virginia Denies Workers' Comp Benefits to Worker Who Violated Safety Rules

Because he was injured while violating a safety rule, a construction worker in Virginia was recently denied workers' compensation benefits. Ironically, the worker was installing fall protection equipment when he fell 25 feet from a bridge deck. The injured man, an experienced ironworker, could not recall how the accident occurred because of head injuries he received.

The North Carolina Workers' Compensation Commission determined that the worker violated his employer's safety rule by not tying off himself while installing stanchions for a safety cable from which other workers would later tie off. He was wearing his harness and lanyard when he fell, and they were found to be in working order.

An appeals court found that the worker had willfully violated the safety rule, and so his employer was not required to pay workers' compensation benefits pursuant to North Carolina law. (Caution: This rule varies from state to state and would probably not apply in Ohio.) The court rejected an argument that the worker could not physically tie off while installing the stanchions when the employer produced a video contradicting that claim.

## Quick Reference

### WHERE IS YOUR REGIONAL OSHA OFFICE?

Region V (Includes Ohio)  
**Michael G. Connors,**  
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### OSHA WEBSITE

<http://www.osha.gov>

### SAFETY AND HEALTH STANDARDS FOR THE CONSTRUCTION INDUSTRY

[http://www.osha-slc.gov/  
Publications/CRM/TOC.html](http://www.osha-slc.gov/Publications/CRM/TOC.html)

## Indoor Air Quality

# Recent News from the Mold Front

*This month's Indoor Air Quality Column looks at recent mold-related developments from around the country, first discussing a mold lawsuit here in Ohio, then taking a quick look at Maryland insurers' efforts to reduce mold financial exposure, and ending with a California court ruling that limits a workplace mold plaintiff's remedies to workers' compensation.*

### Ohio

The Ohio case, reported last month in [ohioconstructionlaw.com](http://ohioconstructionlaw.com), involved an unusual mold claim. Workers employed by the Ottawa County Board of Mental Retardation and Developmental Disabilities (the MRDD) charged that the building they worked in made them sick. Their lawsuit claimed that visible mold in the building caused symptoms such as sinus infections, headaches, lung illness, vomiting, diarrhea, fatigue, and anxiety.

For reasons not given in the court's opinion, the employees were moved to another building. Still not satisfied, they complained that by failing to clean the filing cabinets, furniture, equipment, and personal belongings that were also moved, their employer continued to expose them to harmful mold. This novel theory never got tested. Instead, the court dismissed the case on a procedural issue—it ruled that the Board of MRDD was statutorily immune from such a lawsuit. The theory of "toxic furniture" remains untested. But it does suggest an additional step an employer can take to make sure its employees have no basis for a mold claim: Clean the furniture, and be sure everybody knows you have done so.

### Maryland

The latest insurance battleground over mold coverage is in Maryland. Here the Maryland Insurance Administration recently ruled that insurers may limit mold coverage on personal and commercial policies to \$50,000. On the other hand, insurers are prohibited from restricting the reporting of mold-related losses to the policy period in which the loss occurred.

The Administration characterized its decision as a "middle ground" because it prevents insurers from

completely excluding mold coverage while giving them the ability to cap their exposure. The Administration did not see a mold problem in Maryland anywhere near the reported magnitude in some southern states such as Texas. In fact, State Farm Group, with a 23% Maryland market share, reported only 12 mold claims in Maryland in the first nine months of 2002. The average claim value was \$15,500. By comparison, when all the counting is done, Texas expects up to 60,000 mold claims in 2002.

### California

A California court recently ruled that an employee exposed to mold has only the workers' compensation system to look to for relief, unless there is clear evidence of concealment of the problem on the part of the employer. The employee's symptoms included headaches, rashes, and fatigue. She was immediately transferred to another work area when she reported her symptoms to the company nurse. Air quality testing revealed higher mold levels outside the building compared to the interior. The building had been cleaned three years earlier in response to a mold infestation.

Based on these facts, the court ruled that the plaintiff did not establish that the employer concealed the presence of mold or that the employer concealed the connection between mold and the employee's symptoms. With no proof of concealment, the employee had no claims beyond workers' compensation.

With mysterious phenomena like microbial exposure, it is easy to see why proving employer concealment might be difficult—especially in comparison to more visible and obvious hazards, such as unsafe machinery or faulty safety equipment.



**Doug Shevelow, P.E.**  
Construction Claims Analyst  
Bricker & Eckler LLP

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Date & Time	Seminar	Location	Attorneys	Sponsors
May 13-14, 2003 8:30 to 4:30	15 <sup>th</sup> Annual School Financing & Construction Seminar: How Best To Ensure That Your Project Will Be Successful	Hilton—Easton Columbus, OH	M. Holman, M. Evans S.L. Gillis, G.Parks J. Rosati, M. Taylor S. Wampler	BASA/Triad
Oct. 16, 2003 8:30 to 4:30	5 <sup>th</sup> Annual County Construction & Financing Law	Columbus, OH	M. Armstrong L. Liggett	County Commissioners Association & County Engineers

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