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CONSTRUCTION LEGAL EDGE

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ARTICLES CONTAINED IN THIS ISSUE OF THE CLE:

Pennsylvania Mechanics' Lien Law Amendments for Dummies

The Amendments to the Pennsylvania Mechanics' Lien Law apply to non-residential construction projects of $1,500,000 or more when an owner files a *voluntary* **Notice of Commencement**. If the owner fails to file a Notice of Commencement, the old rules apply.

Assuming an owner files a Notice of Commencement in the Pennsylvania State Construction Notices Directory, then the subcontractor *must* file a **Notice of Furnishing** within forty-five (45) days of first performing work or supplying materials. [Note that if a subcontractor fails to file a Notice of Furnishing in a timely manner, it forfeits its mechanics' lien rights.]

Within forty-five (45) days after completion of work, the owner *may* file a **Notice of Completion** in the Pennsylvania State Construction Notices Directory. Thereafter, any subcontractor or supplier who has not received a full payment *may* file a **Notice of Nonpayment**. [Note that the filing of a Notice of Completion and Notice of Nonpayment are not mandatory.]

To perfect a mechanics' lien claim, the subcontractor or supplier must comply with the same notice and procedural requirements that have long been in effect.

The Pennsylvania Mechanics' Lien Law Amendments benefit the parties involved in a construction project as follows:

• Owners can protect against paying a general contractor and thereafter facing a mechanics' lien claim by a subcontractor who has not been paid in full by the contractor;

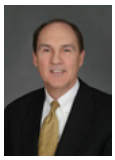
• General Contractors will benefit by having second-tier subcontractors identified and with this knowledge might be able to avoid defending and indemnifying the owner from a

mechanics' lien claim from a sub-subcontractor;

• Subcontractors and suppliers will benefit because owners will provide payment bond information in the Notice of Commencement.

Under the title "Prohibition" found at 49 Pa. C.S. §1501.6 it is unlawful to require a subcontractor not to file a Notice of Furnishing as a condition of entering into, continuing, receiving or maintaining a contract for work or furnishing of materials on a searchable project. A person that violates §1501.6 commits a misdemeanor of the second degree.

The new Amendments to the Pennsylvania Mechanics' Lien Law are found at 49 Pa. C.S. §§1201, 1501.1 to 1501.6.



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Tis the Season for the Holiday Party: How to Socialize Without Stress of Future Litigation

It is that time of year once again when most employers throw a holiday party for their employees. When planning the menu and location, take time to think ahead to avoid some common pitfalls that can turn a holiday party into an expensive grievance, work injury or litigation. Here are your go-to tips for keeping the party safe for all.

Serving Alcohol at the Holiday Party:

If you will be serving alcohol at your office party, should an employee drink to excess and then subsequently be injured or cause an accident, the employer could find themselves in hot water for overserving an intoxicated employee. Dram Shop laws impose liability on the provider of alcohol when a minor has been served. If the employee is over 21, and overindulges and causes harm to himself/herself or another, employers can be held liable under common law theories of negligence. To reduce the possible exposure related to alcohol consumption, consider the following options:

• Hold the event off site at a location where there is a liquor license. This will help shift the responsibility to the offsite location and bartender in attendance.

• If the party is being held at the office, consider hiring a professional bartender or caterer to serve the alcohol and flag any possible intoxicated employees. Ensure that these professionals carry liability insurance.

• Provide employees with coupons or tokens for a set number of drinks (typically 2) in order to limit any issue with overindulging.

• In addition to the above, offer at the beginning of the event to provide alternative transportation home from the event for anyone without question or repercussions.

Workers' Compensation Injuries:

Employers understand that if an employee is insured on the job, they will be able to

apply for workers' compensation benefits. A holiday party, whether on site or off site can also qualify as a "work event" also giving rise to liability. To help ensure that your event is not considered "work related", be clear in letting employees know that the event is not mandatory. Do not conduct work business at the party, such as giving speeches or handing out bonuses.

Overtime Pay and the Holiday Party:

Do you have to pay your employees to attend the holiday party? It depends. If you host the party during work hours, then yes, expect to pay the employees their regular wages during their attendance. If the party is after hours or off site, and is not mandatory, no wages should be required. If, however, you are going to ask certain employees to "work the party" by checking people in or giving out gifts, be sure you compensate them for their time.

Sexual Harassment Claims:

Excess alcohol and a party atmosphere can give rise to inappropriate behavior at a holiday party. To avoid claims of sexual harassment, consider distributing the company policy about sexual harassment before the date of the party and remind the employees to keep things professional. Discourage inappropriate dress and conduct. It is best to avoid the mistletoe and make sure that any Santa at attendance at the party is on his/her best behavior.

Keeping the above tips in mind during the holiday season will help ensure that after the parties are done, no unpleasant surprises will greet the employer in the New Year!

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Be Aware of the Legal Principle of Accord and Satisfaction Before Cashing a "Full and Final Payment" Check

One situation which constantly repeats itself in the construction arena, no matter the diligence by the contractor, is the unhappy customer. Perhaps a customer, whether unjustly or not, feels the work performed was inadequate or that they were misled. When you submit the final invoice, the customer again balks, complaining that the costs are too high and far beyond anything that was quoted. As a well-prepared contractor you show the records where the customer agreed to the materials and costs, but faced with this the customer still refuses to pay.

Instead, after more discussions on the issues, the customer sends a letter outlining his perceived problems and his intention to reach a resolution of the issues, along with a signed check to your company marked "full and final payment." Given the already combative nature of the relationship, you deposit the check as a partial payment for the invoice and ask the customer to remit payment for the other half as soon as possible. Is the customer still obligated to pay the other half of the billed invoice? While the contractor may certainly believe otherwise, it's very likely in this scenario that the customer has no further legal obligation to pay.

The above scenario is a demonstration of the legal principal of accord and satisfaction. Accord and satisfaction is a method wherein the parties to a contract agree to replace an existing agreement and release any debt obligation owed. For a party claiming a debt has

been released through accord and satisfaction, there must be (1) a disputed debt (2) a clear and unequivocal offer of payment in full satisfaction and (3) acceptance and retention of payment by the offeree. *PNC Bank, National Association v. Balsamo*, 634 A.2d 645, 655 (Pa. Super. Ct. 1993). Applying the legal elements to the situation above, and dependent on the exact language of the customer's letter, it appears that the customer successfully showed the elements for accord and satisfaction and that the customer would have no further obligation to pay the invoice.

While this exists as a common law contract principle, in Pennsylvania there is also a specific statute relating to accord and satisfaction for the use of checks. Pursuant to 13 Pa.C.S. § 3311(a) a party alleged to owe money (a debtor) can show that a previous partial payment by check (an instrument) acted as accord and satisfaction for the whole debt if the debtor can show that (1) that party in good faith tendered an instrument to the claimant as full satisfaction of the claim; (2) the amount of the claim was unliquidated or subject to a bona fide dispute; and (3) the claimant cashed or deposited the check. The debtor also has to conspicuously mark the check or accompanying written communication that the payment is being tendered as full satisfaction of the claim. 13 Pa.C.S. § 3311(b). In the initial example, both the letter and "full and final payment" on the check should suffice. If the debtor can prove these elements it can then rely on its partial payment by check as terminating all other obligations to pay.

While the parties should clearly be permitted to mutually modify their obligations to one another, the concern is that an unsuspecting contractor may unintentionally agree to accord and satisfaction of a major debt. A contractor, or his office staff, may have no idea that routinely depositing the signed check which just arrived in the mail could actually cause the contractor to lose the opportunity to recover the full amount of a debt. In some instances this could result in the loss of tens of thousands of potential dollars. As such, recognizing that a customer issued a check for "full and final payment" is critical. This recognition can help to prevent the loss of a major financial claim and allow the creditor to begin taking steps to ensure the full amount owed is recouped.

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Aggressive Bidding or False Claim?

Introduction

As we know, government construction contracts are subject to a number of statutory proscriptions, perhaps none that are more carefully scrutinized than the False Claims Act ("FCA"). The FCA creates liability for any person who: "(A) knowingly presents, or causes to be presented, a false or fraudulent claim for payment of approval; [or] (B) knowingly makes, uses, or causes to be made or used, a false record or statement material to a false or fraudulent claim." 31 U.S.C. § 3729.

With respect to bidding for government construction contracts, every contractor naturally wants to be as aggressive as reasonably possible to secure the award. But is there a point where a contractor's bid is so aggressive that it could be considered "false?"

The law accounts for such a possibility. Indeed, potential liability under the FCA may exist if a contractor's bid is so undervalued that it constitutes "fraud-in-the-inducement." This

means that liability may attach where there is evidence suggesting that the effort to obtain a contract was fraudulent, even in the absence of a specific payment request that was actually "false."

This circumstance does not arise when the contractor simply presents a low bid. Rather, the bid must be so aggressive and so undervalued that it calls into question whether the contractor had any reasonable basis to believe it to be "real." If the bid falls into that category, further investigation is necessary to determine whether the contractor specifically knew what it was doing, or whether the contractor just made a really unwise decision.

Case Analysis

In 2005, the Court of Appeals for the District of Columbia decided *Bettis v. Odebrecht Contractors of California*, 393 F.3d 1321 (D.C. Cir. 2005). In *Bettis*, the Court held that there could not be liability under the FCA for submitting a bid that may have been intentionally deflated unless there was a fraudulent request for payment (namely, submitting a payment request for work that was never done). However, in 2012, the Court of Appeals for the Ninth Circuit decided *Hooper v. Lockheed Martin Corporation*, 688 F.3d 1037 (9th Cir. 2012). In *Hooper*, the Court held that underbidding *could* be a source of liability under the FCA, regardless of whether there was an actual fraudulent request for payment.

Since 2012, courts and scholars have tried to reconcile *Bettis* and *Hooper*. Although *Bettis* and *Hooper* appear to come to opposite conclusions, a closer look reveals that the conclusions are heavily driven by the facts of each case, and not a difference in opinion about the law under the FCA.

The *Hooper* case involved a "cost plus fee award" contract. The contractor responded to the United States Air Force's solicitation with an initial bid of $439.2 million. The Air Force informed the contractor that that bid was too high, so the contractor decreased it to $432.7 million. When revising the bid price, the contractor's employees were instructed to simply change the cost estimates without using any professional engineering judgment, and without any regard to the actual costs to be incurred. The Air Force accepted the bid, but ended up paying the contractor more than $900 million to construct the project, resulting in litigation. The evidence revealed that the inputs used to compute the final bid price were based on "bad, bad guesses," but were not technically false. Moreover, the evidence revealed that the Air Force's analysis of the bid acknowledged that the inputs were unrealistic and could lead to "cost growth beyond target cost." Nevertheless, the Appellate Court held that there was sufficient evidence from which a trier of fact could conclude that the contractor either knew its costs were highly understated, or deliberately ignored that fact, or acted in reckless disregard of that fact when it submitted its bid. Thus, the Appellate Court found potential liability under the FCA.

In contrast, *Bettis* involved a fixed price bid. The contractor submitted a bid of $167.77 million that was accepted by the United States Corps of Engineers ("Corps"). This bid was $29 million lower than the second lowest bid, and nearly $36 million lower than the Corps' cost estimate. During the course of construction, the contractor sought and received numerous equitable adjustments to the contract. Ultimately, the Corps paid the contractor nearly $268 million for the contract. Litigation ensued. The contractor was alleged to have violated the FCA by submitting a low bid with the intention of seeking equitable adjustments to the price after winning the bid. The evidence revealed that the contractor's failure to calculate costs in accordance with industry standard led to a substantially deflated

bid. Despite this shortcoming, there was a lack of evidence showing that the contractor specifically decided to submit a low bid with the intent of escalating its price later through unmeritorious change orders. As a result, the court rejected the theory that the contractor fraudulently induced the Corps into entering a contract.

Key Considerations

There are key facts that distinguish *Hooper* and *Bettis:* (1) knowledge; (2) contract structure; and (3) intent.

Knowledge: The evidentiary support was different in these cases. In *Hooper,* there was evidence by the contractor's employees that the contractor was well aware of what it was doing when it instructed its employees to lower its costs without regard to the actual cost. Conversely, in *Bettis*, there was a lack of evidence regarding what the contractor actually knew when it submitted its bid to the Corps. There were allegations regarding the contractor's intent, but little evidence showing the contractor's actual knowledge.

Contract Structure: The respective differences in contract structure could have dictated the differing outcomes in *Hooper* and *Bettis*. In *Hooper*, the contract was a "cost plus fee" arrangement which meant that the Air Force was responsible for the costs incurred, and thus sought a bid that accurately estimated the costs that the contractor planned on incurring. Since the contractor knew the value of the costs it would incur, and represented that value to the Air Force, liability could attach if the value proved highly inaccurate. In *Bettis,* the contract was a fixed price bid, which meant that the contractor was responsible for its costs, and simply had to come up with a bid price that it believed would sufficiently compensate it for those costs. Although the contractor was able to seek and obtain equitable adjustments for changes to the contract, the contractor was ultimately responsible for failing to calculate expected costs correctly if the equitable adjustments were denied.

Intent: The intent of each of the parties appeared quite different. In *Hooper,* the evidence showed that the contractor had previously submitted a bid in another project that was lowered by almost 50% in order to secure the contract award. In *Bettis*, the evidence showed that the contractor had every intention of fulfilling its obligations when it submitted its bid, and simply (badly) misjudged the actual value.

The differing views presented in *Hooper* and *Bettis* were illustrated in *In re Bank of New York Mellon Corporation Forex Transactions Litigation*, 991 F. Supp. 2d 479, 483 (S.D.N.Y. 2014). The plaintiffs in that case relied on *Hooper* to try and prove that a fraudulent inducement had occurred. The defendants relied on *Bettis* to prove just the opposite. The facts of that particular case were more analogous to *Bettis,* not *Hooper.* Specifically, the court noted that the contract in *Hooper* was "supposed to reflect the contractor's good-faith estimate" but the "contractor was liable because it knowingly understated" the amount of its costs. Those facts were not present in the *Bank of New York* matter, so liability did not attach.

Conclusion

"Fraud-in-the-inducement" liability under the FCA is not specifically dictated by any case holding, but, rather, is dictated by the facts of each case. The contractor's knowledge, the contractor's intent, and the contract structure are all particularly important. Only careful examination of those facts can help one determine if aggressive underbidding is actionable under the FCA.

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Delay in Payment to Subcontractor May Prove Costly

The Court of Common Pleas of Crawford County, Pennsylvania recently entered a verdict against a general contractor on a school construction project that reminds us all of the substantial damages that will be awarded to contractors and subcontractors under the Pennsylvania Contractor and Subcontractor Payment Act or the Pennsylvania Prompt Pay Act when a payment is wrongfully delayed by a general contractor or owner. While the verdict out of Crawford County represented eight years of delayed payment by the contractor, it clearly demonstrates the potential impact on your business with respect to the penalties built into the statutes. By applying the terms of the Prompt Pay Act, the subcontractor's original claim for unpaid work of $78,000.00 in 2008 resulted in a judgment by the Court in 2016 in excess of $230,000.00 plus ongoing interest of eighteen percent per annum until the judgment is paid.

The two contractor's statutes mentioned above, by their mandatory terms, enhance the legal interest rate of six percent to an effective penalty interest rate of 18% per year and then allow for the award of attorneys' fees to the prevailing party. When the potential claim of the subcontractor under the penalty statute(s) exceeds the amount originally claimed, you are well advised to seek a business settlement sooner, rather than later, even at the risk of the loss of a little pride. The business decision, rather than an emotional response, always needs to take precedence when determining whether to delay payment to a subcontractor for any reason.

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Storage Tank and Spill Prevention Act Penalty Math or How I Learned to Stop Worrying by Contacting Counsel

Some construction costs are area-specific. Costs associated with site protection and municipal permitting fees, for example, can vary with the project location. Costs associated with regulatory violations, however, need not be incurred if local counsel is retained at the beginning of the project.

The Pennsylvania Storage Tank and Spill Prevention Act (the "Act") is an example of the potential regulatory pitfalls waiting for unwary contractors. The Act was passed in 1989 to address the problem of tank leaks that could contaminate groundwater. To understand the scope of the potential problems associated with such spills, you need only look to Charleston, West Virginia in 2014. The Elk River spill on January 9, 2014 contaminated the drinking water for the city of Charleston with crude MCHM, a chemical used to remove impurities from coal in order to reduce the pollutants produced during combustion. The spill originated from leaks in above-ground storage tanks. The residents of Charleston were unable to use their water in any way for ten days, and expensive, time-consuming litigation resulted.

The Act is designed to prevent events like the Elk River spill, so the penalties are potentially crippling. Although the Act has been around for more than twenty years, the Pennsylvania Department of Environmental Protection (the "DEP") is still struggling to force contractors

to comply with the Act's requirements. The overall complexity of the ever-changing regulations adopted by the DEP has been blamed for much of the non-compliance. But we all know the old adage: ignorance of the law is no excuse. Overly complex or not, the regulations are the law, and the penalties can be severe.

The Act covers storage tanks that are both above and below ground. Relevant to contractors, it covers a broad range of activities including all "activities to install, modify or remove all or part of a storage tank system or storage tank facility," other than maintenance. As soon as a contractor engages in "tank handling activities," the Act makes the contractor subject to a host of federal and state regulations: "a person may not install, construct, erect, modify, operate or remove from service all or part of a storage tank system or storage tank facility in a manner that violates the act, this part or applicable Federal regulations adopted under the Resource Conservation and Recovery Act of 1976." Furthermore, with very few exceptions, only a specially certified installer may perform the work.

If any of the applicable regulations are violated, or a certified installer is not used even if the work is otherwise in compliance, the DEP may be empowered to impose penalties. The regulations set forth a detailed formula for the computation of penalties, though many of the areas are discretionary. The factors considered are seriousness of the violation, duration, and willfulness. When there is a release event, the DEP can add environmental damage, savings/profit realized by the violator, and the cost of restoration. Taking the example of a technical violation without a release of any potentially hazardous substance, formula looks like this:

Penalty = Violation Seriousness x Duration x Willfulness
(P = VS x D x W)

The "Violation Seriousness" ("VS") is the "potential or actual impact (risk) to the environment and/or human health." It is calculated based on the following ranges:

> Low Risk Violation = $100-$1,500
> Medium Risk Violation = $1,000-$3,000
> High Risk Violation = $2,000-$5,000

Generally, "Low Risk Violations" are things such as the failure to use a certified installer, failure to register tanks, failure to submit closure reports, and failure to maintain records/documents.

The "Duration" ("D") factor is difficult because the DEP can use metrics ranging from "occurrences" to days:

> Duration addresses the longevity of a specific violation in terms of time or the number of occurrences. A duration factor may be in number of days, months, weeks, years or occurrences.

A higher number will necessarily result in a much higher penalty.

"Willfulness" ("W") ranges from "Basic Liability" to "Deliberate." The closer the act is to "Deliberate," the higher the multiplier in the formula. This is complicated by the difficult to parse definitions of "Basic Liability" (factor 1) and "Negligent/Reckless" (factor 2).

Below is an example of the range of penalties possible where there is only a simple low risk violation like one a contractor is likely to encounter unwittingly:

Minimum VS Range

	VS	D	W	Total
Basic Liability	$100.00	1	1	$100.00
Negligent/Reckless	$100.00	1	2	$200.00

Maximum VS Range

	VS	D	W	Total
Basic Liability	$1,500.00	1	1	$1,500.00
Negligent/Reckless	$1,500.00	1	2	$3,000.00

Now, imagine that there are ***two*** tanks per violation instead of just one and the potential penalties facing the contractor go up to $200 - $6,000. Then, imagine that the DEP uses a "Willfulness" factor of "Negligent/Reckless," a "Duration" factor of days, and that the project lasts one year. The range in that scenario becomes $146,000 - $2,190,000; a serious problem for any project. Finally, consider the definition of "Negligent/Reckless": "the person should have known the legal requirements and acted in such manner that the person's actions or omissions violated these requirements." It is not hard to imagine events that can fit that description.

The Pennsylvania Storage Tank and Spill Prevention Act is just one example of a law that contractors doing work in Pennsylvania may encounter "the hard way." Pennsylvania is not in any way unique in this regard. Consulting with local counsel early in the project can cut down on the risk that you will end up learning all about the costs associated with a violation of the law.


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Where In The World?

Construction Mystery: It is said that you could visit this wondrous city every day for the rest of your life and never see it all. Only the highest realm of society could access this ceremonial city for its first 500 years. Formerly, uninvited visitors faced execution, but now you can tour this World Heritage Site for the price of admission. The scale of this complex is immense, approximately 980 buildings---the world's largest collection of preserved ancient wooden structures----spread over 180 acres. Courtyards were constructed to accommodate up to 100,000 onlookers. The complex dates back to 1420, and the damage of time has been corrected with buildings re-gilding and repainting in their original vibrant hues. Within many of the buildings, you will find priceless art, including ancient timepieces, jadeware, paintings, and religious art.

Question: What is the name of this complex and the city and country where it is located?

Last Issue Answer: Hofdi House, Reykjavik, Iceland

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If you would like to be added to or deleted from the Distribution List of the CLE, please contact Joe Bosick (the Chair of the CPC) at JJB@Pietragallo.com.

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