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GETTING PAID: PRACTICAL COLLECTION ALTERNATIVES

Bill Fig
Sussman Shank LLP

There are few things more frustrating to a client than not getting paid for the services and/or goods it provides to a customer on a project. It is especially frustrating when the amount owed may be fairly modest, thereby making it difficult to economically justify collection action. Nonetheless, multiple, small delinquent accounts can add up to a hefty sum and affect the client's cash flow, which necessitates a plan of action. This article discusses collection options to consider to help your client obtain payment from a delinquent customer.

The Construction Lien

When a construction project is involved, the first thought is recording/foreclosing a construction lien on the client's behalf. The obvious initial consideration is whether the client has preserved its lien rights under ORS Chapter 87 *et. seq.* In other words, were the required pre-lien notices sent in a timely manner to the correct parties, and did the client record its lien properly and in a timely matter? However, these questions should not end your initial inquiry. Of vital importance, especially where a modest sum is at issue, is whether the client has the right to seek its attorney fees as part of its lien claim. The risk of paying twice (or more) of the amount of the original debt because of an attorney fee claim often becomes the tail that wags the dog, *i.e.* it is the type of additional economic leverage needed to settle small-dollar claims. Attorney fees may be recoverable in a lien foreclosure action. ORS 87.060(5). However, the right to fees is not "automatic," and there are several traps and pitfalls that can result in the client having a valid lien claim, but no right to seek attorney fees, *see e.g.* ORS 87.027, 87.039(2), and 87.057(3). Thus, whether the client has a right to recover attorney fees may determine whether pursuing the lien claim is worthwhile.

Even if a right to recover fees exists, it is equally important to determine the priority of the client's lien claim *vis a vis* other encumbrances. In Oregon, it is possible for a construction lien to have "super-priority," meaning it has priority over an existing encumbrance, *i.e.* a deed of trust. However, that is not always the case! Under ORS 87.025(6), a lien relating to an alteration or repair does not have super-priority over an existing encumbrance. Moreover, under ORS 87.025(3) and (4), an otherwise super-priority lien may become subordinate to the mortgagee's interest. Foreclosing a lien that results in the client taking the property subject to an existing encumbrance may have little to no value to the client. This is especially true when the lien is for a modest amount or the amount of the preexisting encumbrance is significant.

Attorney Fee Statutes

Next, in the alternative or in addition to a lien claim, the client should consider a breach of contract claim and whether the client's claim falls under ORS Chapter 20 *et. seq.* ORS 20.082

allows the prevailing party to recover attorney fees on a breach of contract claim under $10,000 where the contract is silent as to fees. This includes written and oral contracts. The statute requires that the client make written demand for payment on the delinquent customer at least 20 days prior to filing suit (for us old timers, yes, it used to be 10 days). ORS 20.080 provides a similar remedy for tort claims under $10,000, but requires 30 days' notice. Like a lien, these attorney fee statutes can increase the economic risk to the delinquent customer associated with litigating a claim, which may prompt payment by an otherwise uncooperative customer.

CCB Claims

If the delinquent customer is a contractor registered with the Oregon Construction Contractor's Board ("CCB"), the client may be able to recover from the surety bond the contractor is required to post with the State. ORS 701.131 *et. seq.* sets forth the requirements and time deadlines for asserting a claim against a contractor's CCB bond. A key prerequisite of a CCB claim is sending the contractor a notice of the claim and a demand for payment as required by ORS 701.133. The CCB does not adjudicate complaints/claims. Thus, in order to ultimately reach the bond, you must file suit in state Circuit Court, obtain a judgment against the contractor, and timely tender the judgment to the CCB. The recovery available from the bond depends on the type of project, the contractor's certification, and the "type" of claimant (recovery from a bond can vary significantly - between $3,000 to $75,000; *see* ORS 701.084). The bond also provides an easy source for recovery for all or part of the judgment debt. Importantly, the existence of an unpaid judgment against a contractor suspends the contractor's CCB license, which effectively puts him/her out of business - powerful incentive for a viable contractor to pay up, even on a small claim!

The Personal Guaranty

Hopefully, the client has a clear and concise written agreement with the delinquent customer setting forth the terms and conditions that govern the services and/or goods it provided to the customer. Also, make sure to inquire whether the client has a written guaranty of the principal of the delinquent customer guarantying the obligations of the customer to the client. Like an attorney fee claim, a personal guaranty, which puts the individual's assets at risk, can provide significant leverage to settle a claim and, therefore, significantly enhance the chance of a successful collection of the debt.

Is the Juice Worth the Squeeze?

Before the client undertakes collection action against a delinquent customer, a discussion should be had whether it is "worth it." In other words, is the account a "problem account" that has a heightened risk of a claim being asserted back against the client? If so, it may be better to forego a collection action and "hold" the balance owed on the account as potential leverage, or an offset, in any future action against the client.

For professionals, on most delinquent accounts, it is likely best to wait to pursue a collection action until the statute of limitations on a negligence/malpractice claim has run. In Oregon, the statute of limitations on a negligence claim runs several years before the statute of limitations runs on a breach of contract claim. Filing a collection action after the statute of limitations on the negligence claim has run should reduce the professional client's potential exposure to such a claim.

Show Me the Money!

Once a court enters a judgment against the delinquent customer, absent another source of recovery (*e.g.* a CCB bond) the most popular and usually most cost-effective collection tool is a writ of garnishment under ORS 18.600 *et. seq.* A writ

of garnishment, generally speaking, typically allows money to be taken from the delinquent customer's bank account or paycheck to pay the amount owed to the client. In Oregon, an attorney may issue a writ of garnishment. Writs issued to banks are particularly effective because the writ reaches all of the debtor's accounts in Oregon at the garnished bank. The issuance of a writ of garnishment, whether successful or not in "hitting funds," often persuades a customer with assets to pay the debt to avoid further collection action. Of course, if the delinquent customer has no assets, the judgment may not be collectible. The old adage is true – you can't get blood from a stone

William G. Fig is a partner in Sussman Shank LLP's litigation and construction practice groups. Contact him at 503-227-1111 or wfig@sussmanshank.com.

OREGON CONSTRUCTION LEGISLATION UPDATE

Jakob Lutkavage-Dvorscak
Davis Rothwell Earle & Xochihua PC

The 2017 Oregon Legislative Session gaveled to a close on July 7, 2017—technically they refer to the close of the session as *Sine Die* or adjournment without an appointed date for resumption, but I digress. This legislative session was an interesting session for the construction industry because it received a long awaited transportation investment package it sought for several years while also playing significant defense on potential revenue increasing measures that would have greatly affected the industry. Those were just the 800 pound gorillas in the legislative session, there were many other dangerous and helpful woodland creatures (bills) during the session—some nice, some not. Overall the industry came out of the session with some wins, a loss or two, and several draws. It is up to you to determine the wins, losses, and draws, except for the first one which I will give to you.

Transportation Funding Package (HB 2017)

The largest win for the industry was finally getting a transportation funding package passed totaling $5.3 billion for various public transportation projects. While this likely will not have a direct impact on the legal representation of contractors it will certainly mean far more work for public works contractors. The funding package proved elusive in the 2015 legislative session due largely to the Clean Fuels Program passed that year. That bill was passed over the objections of Republican legislators who indicated no transportation package would be passed without the repeal of the Clean Fuels Program. In 2017 that stance softened somewhat in order to get the funding package but the Clean Fuels Program was modified enough to secure passage of the bill.

Predictive Scheduling (SB 828)

At the outset of the 2017 session labor advocates proposed a bill that would require employers to provide predictive work schedules that required payment for four hours of work if the schedule changed within 24 hours of the scheduled work. Weather and scheduling issues in construction often make this sort of certainty infeasible. In the end the bill was reduced to only large employers in the retail, hospitality, and food service industry. The bill also prohibited local governments from mandating predictive schedules. So contractors do not need to worry about these scheduling issues, yet. The issue could resurface in the next legislative session.

Apprenticeship Standards (HB 2162)

The construction industry for several years now has been struggling to find sufficient numbers of qualified workers. This is in part because the hot construction market has made good workers harder to come by. The Great Recession also played its part by forcing a lot of construction workers out of the industry in search of work. Those workers have not all come back to the industry, and the overall force has been depleted

by retirements. In an attempt to increase the supply of qualified workers, the Legislature instituted an apprenticeship program requiring threshold levels of apprenticeship utilization to bid on Oregon public works. The bill passed this session applies to state funded projects over $5 million. It requires a 10% use of apprentices on those projects but exempts ODOT projects. Estimates are that there will only be a few projects in the next year that meet these thresholds which will allow the program to be eased into existence without causing drastic wholesale changes. If your client may be bidding on such projects they need to be aware of the new requirements.

Public Contracting Accountability (HB 3203)

HB 3203 gives contractors another tool to challenge a public entity's decision to self-perform some construction work or put it out for bid. The bill amends ORS 279C.305, increasing the threshold to $200,000 in estimated value for public projects requiring the public entity to prepare plans, specifications, and unit cost estimates and then prepare a full accounting after the completion of the project. Previously the threshold had been $125,000. There is, however, still an exception for resurfacing of roads at a depth of two inches or more with the old $125,000 threshold. But, in statutory language that would feel right at home in an insurance policy, there is an exclusion within that exception if the project is for maintenance patching, chip seals, or other seals as road maintenance. That exclusion could end up being big enough to drive several dump trucks through, but there is a new enforcement provision wherein the contractor can file a complaint with the BOLI Commissioner if it believes there has been a violation of this statute.

Sexual Harassment Policies (HB 3060)

As of 91 days following the *Sine Die* adjournment of the 2017 Legislative Session, all contractors bidding on public projects greater than $150,000 are required to have a sexual harassment policy that meets the new law's guidelines. However, the Department of Administrative Services has been assigned the responsibility to produce a form policy that contractors may use but it does not appear to have been issued yet. Practice Tip: Make sure your public works contractors have a sexual harassment policy in effect when bidding. There are some exceptions within the statute permitting a contractor to bid without having the policy in place yet, but it should be in place following the award of the contract. Consult the bill/statute for further information.

Responsible Managing Individuals (SB 336)

This bill allows a contractor some flexibility when losing a "Responsible Managing Individual" under its CCB license. Contractors can now have a temporary RMI and have up to 14 days to find a permanent RMI.

Housing Review Process (SB 1051)

SB 1051 makes a number of changes to the housing review process that will likely affect developer clients. It requires low-income multi-family developments to have housing applications decided within 100 days for cities with a population greater than 5,000. It also requires all cities greater than 2,500 in population to allow accessory dwelling units. It also prohibits a city from lowering the density of a project if it is in the designated density range for the zone.

In all, the 2017 Legislative Session was a mixed bag for the construction industry. It finally received a transportation funding package after several years of fighting. But, there are also new regulations that will affect bidding on public projects. In other instances the industry was able to secure exemptions on new laws that could have had significant impacts on contractors.

Jakob Lutkavage-Dvorscak is an attorney with Davis Rothwell Earle and Xochihua PC's construction litigation group. Contact him at (503) 222-4422 or jld@davisrothwell.com.

OREGON CONSTRUCTION CASE LAW UPDATE

D. Gary Christensen
Alexander M. Naito
Miller Nash Graham & Dunn LLP

Since our last case-law update a year ago, Oregon courts have issued a few interesting opinions for the construction lawyer. Of course, many relate to insurance defense and coverage. These digest cases of note.

DUTY TO DEFEND & "ONGOING OPERATIONS:" Subcontractor's insurer has a duty to defend general contractor, named as additional insured, for defective work performed by subcontractor, even if the underlying complaint does not identify subcontractor. As long as a court can reasonably interpret the allegations in a complaint in a way that could impose liability on general contractor for subcontractor's work, insurer has a duty to defend. *West Hills Development v. Chartis Claims*, 360 Or 650, 385 P3d 1053 (2016).

Arbor Terrace Homeowner's Association ("Owner") filed a complaint against West Hills Development Company ("General Contractor") for negligence related to original construction of the townhomes and damage resulting from insufficient weatherproofing. General Contractor filed third-party claims against various subcontractors, including L&T Enterprises ("Subcontractor"), who had installed porch columns on the project. General Contractor also tendered defense of the claim to Automobile Insurance Company ("Insurer"), who had issued a general liability policy to Subcontractor. Pursuant to the terms of the subcontract, Subcontractor had agreed to indemnify General Contractor against any liability resulting from Subcontractor's work, and to obtain a general liability insurance policy naming General Contractor as an additional insured. Insurer refused the tender. General Contractor settled with Owner and initiated this action seeking reimbursement from Insurer for its share of the defense costs.

Insurer argued that it did not have a duty to defend because it was only liable based on Subcontractor's "ongoing operations," which meant its liability was limited to damages that occurred while Subcontractor was actually working on the project. Insurer also argued that the allegations in Owner's complaint did not establish that the damages had been incurred while Subcontractor was working. The trial court disagreed. First, damages "arising out of ongoing operations" could be interpreted to include damages incurred after construction, making the provision ambiguous, and therefore interpreted against the insured. Second, the allegations in Owner's complaint were sufficient to trigger coverage because it alleged improper construction of the porch columns. Relying on extrinsic evidence, specifically the tender letter, the court held that the allegations showed that General Contractor could be held liable for Subcontractor's work.

On appeal, the Court of Appeals affirmed. The Oregon Supreme Court also affirmed, but determined that it was unnecessary to resort to extrinsic evidence. The Court rejected the argument that Owner's complaint must "rule in" coverage. Rather, the duty to defend exists as long as a court can reasonably interpret the allegations to fall within coverage. Because Owner's complaint alleged negligent construction by General Contractor and its subcontractors, the complaint could reasonably be interpreted to result in liability covered under the insurance policy, even if the Subcontractor was not directly named. As to the insured claim that Owner's claim did not allege damage occurring while the Subcontractor performed its work, the Court determined that the exact timing of when the damage occurred was not clear and it was conceivable that damage could have started during the installation. Therefore, because any ambiguity in the complaint is resolved in favor of the insured, there was a duty to defend.

COVERAGE EXCLUSIONS & GARNISHMENT PROCEEDINGS:
Exclusions that have more than one reasonable interpretation in context are ambiguous and resolved in favor of the insured. Underlying judgment in garnishment proceeding is not conclusive evidence that damages are covered. Attorney fees and costs in underlying suit are recoverable against insured. Insurer entitled to jury trial on questions of fact in garnishment proceeding. *Hunters Ridge Condo. Assn. v. Sherwood Crossing*, 285 Or App 416, 395 P3d 892 (2017).

Hunters Ridge Condominium Association ("Owner") brought construction defect claims against developer and general contractor relating to construction of a mixed-use condominium project. The two relevant buildings included 45 residential units on the upper floors and eight commercial units on the ground floor. Developer filed third-party claims against various subcontractors, including Walter George Construction ("Subcontractor"). Subcontractor did not appear and, through various settlements and assignments with developer and general contractor, Owner obtained a default judgment against Subcontractor. Owner then initiated a garnishment proceeding against American Family Mutual Insurance Company ("Insurer"), who had issued a general liability insurance policy to Subcontractor. Both parties moved for summary judgment.

The trial court granted Insurer's motion for summary judgment, finding that a policy exclusion for work involving "multi-unit new residential construction," meaning a "condominium, townhouse, apartment, or similar structure" with greater than eight units built for residential occupancy, unambiguously excluded coverage. The Court of Appeals reversed, noting that an alternative and reasonable interpretation of the exclusion is that it applies only to solely residential construction, and not mixed-use construction. And because both proposed interpretations were plausible, the definition was ambiguous and therefore construed against Insurer, and in favor of coverage.

The Court of Appeals upheld the trial court's denial of Owner's motion for summary judgment. Owner argued that the default judgments, which were obtained after a prima facie hearing establishing Subcontractor's percentage of liability for the settlement amounts, set as a matter of law the amounts the insured became legally obligated to pay. The trial court and the Court of Appeals found that a question of fact existed as to whether some of the damages included as part of the judgments were excluded from coverage. The trial court and Court of Appeals did, however, agree with Owner that attorney fees and defense costs awarded in accordance with the judgments were "costs taxed against the insured" and therefore recoverable from Insurer.

Finally, the Court of Appeals agreed with Insurer that under Article I, Section 17, of the Oregon Constitution, because the garnishment proceeding was a breach-of-contract action, Insurer was entitled to a jury trial on the questions of fact in the coverage dispute.

DAMAGES: Extended overhead costs resulting from project delay are recoverable as consequential damages. To recover additional damages assessed on a percentage basis of costs incurred due to delay, contractor must prove that damages were actually incurred or specifically provided for in the contract. *Big River Construction v. City of Tillamook*, 283 Or App 668, 391 P3d 996 (2017).

Big River Construction (General Contractor") brought suit against the City of Tillamook ("Owner") for breach of contract and related claims associated with expansion of a wastewater treatment plant. Specifically, General Contractor sought compensation for additional costs associated with delay caused by changes in scope directed by Owner. General Contractor also sought payment of several outstanding pay applications. Owner counter-claimed for

liquidated damages. At trial, the jury found in favor of General Contractor.

Owner appealed, arguing that the trial court erred in denying its motion for directed verdict because General Contractor failed to prove its damages with reasonable certainty. The Court of Appeals affirmed in part and reversed in part.

First, Owner challenged General Contractor's claim for extended home office overhead incurred as a result of the delay because the contract provided for overhead in the contract price. The Court rejected Owner's argument, finding that General Contractor could have incurred additional actual overhead costs beyond the contract amount, and such damages are recoverable as consequential damages.

The Court did, however, side with Owner in rejecting General Contractor's claimed damages for additional bonding and insurance costs resulting from delay. General Contractor sought an additional five percent on its total damages for additional bonding and insurance. At trial, General Contractor's project manager testified that five percent was the rate assessed by the insurance company based on the volume of sale, but did not testify as to whether General Contractor actually incurred additional costs. Thus, General Contractor failed to present sufficient evidence that five percent was an appropriate estimate for actual bonding and insurance costs associated with the delay.

Finally, Owner challenged General Contractor's claim for a 15 percent mark-up on its damages for extended general conditions, overhead, and labor. Although the contract provided for a 15 percent mark-up on specified costs, overhead, and profit. There was, however, no contractual basis for General Contractor to recover mark-up on consequential damages or costs not specifically enumerated in the contract.

ATTORNEY FEES: Insured need not obtain a "judgment" memorializing the required payment in order to be eligible for the award of attorney fees under ORS 742.061. *Long v. Farmers Ins. Co. of Oregon*, 360 Or 791, 388 P3d 312 (2017).

Cary Long ("Owner") filed a claim with Farmers Insurance Company of Oregon ("Insurer") for damage to residential structure incurred from a kitchen sink leak. Insurer made a series of payments within six months of the submission of the proof of loss, the total of which fell short of Owner's estimates of the damage. Thereafter, Insurer made additional voluntary payments, as late as the day before trial. In the end, Owner was awarded an amount more than what had been paid within the first six months after filing the proof of loss, but not greater than the total amount paid as of the date of trial. As a result, the trial court entered a judgment in favor of Insurer. Owner then submitted a petition for attorney fees under ORS 742.061. The trial court denied the petition, and Owner appealed.

The Court of Appeals reversed. According to ORS 742.061(1), if a plaintiff's *recovery* exceeds the amount of any tender made by a defendant within six months of the claim, then plaintiff is entitled to reasonable attorney fees and costs. Insurer argued that the term "recovery" should be construed narrowly to apply only to a money judgment in the action in which attorney fees is sought. Owner, conversely, sought a broader interpretation of "recovery" to include any kind of restoration of a loss, including a voluntary payment.

The Court determined that the text and the context of the term "recovery" was ambiguous, as used in the statute, and thus looked to the intent of the legislature. The purpose of ORS 742.061 is to encourage timely payment of reasonable claims and to discourage expensive and lengthy litigation, but also to compensate the insured for costs to obtain proceeds due to them. As such, awarding attorney fees to an insured satisfies the intent of the statute as long as the insured obtains payments in some form that exceed the timely amount

tendered. Therefore, it followed that just because Owner did not obtain a "judgment" memorializing these payments, it did not make the statute inapplicable. Based on that analysis, the Court held that ORS 742.061 entitled Owner to attorney fees incurred up to the time Insurer voluntarily paid the full amount of the claim, because that amount exceeded the tender made within the first six months of the claim.

BOARD OF ARCHITECT EXAMINERS: A person may offer to render architectural services without being issued a certificate of registration. However, if principals have not submitted an application for registration, they violate ORS 671.020(1) when they make claims of pending licensure in conjunction with advertising architectural projects they have undertaken. *Twist Architecture v. Board of Architect Examiners*, 361 Or 507, 395 P3d 574 (2017).

Architecture firm was formed in 2008 by its two principals and registered as a professional corporation in the state of Washington. During the relevant period, neither principal was licensed to practice in Oregon. The firm entered into an agreement to perform "concept master planning design services" for three projects in Oregon. For each project, the firm produced a feasibility study portraying an aerial view of the development project. During a contested hearing before an administrative law judge, the Oregon Board of Architect Examiners found violations as a result of the firm's preparation of the feasibility studies without an Oregon license. It imposed a $10,000 civil penalty against each party for the unlawful practice of architecture.

ORS 671.010(7) defines "practice of architecture" as "the planning, designing or observing of the erection, enlargement or alteration of any building or of any appurtenance thereto other than exempted buildings." The term is further defined by the board's own regulation as "all analysis, calculations, research, graphic presentation, literary expression, and advice essential to the preparation of necessary documents for the design and construction of buildings, structures and their related environment whether interior or exterior." OAR 806-010-0075(1).

The board interpreted the statute and regulation in tandem to include any activity undertaken in contemplation of the erection of a building. The Court of Appeals, on review, rejected the board's interpretation as being too broad and contrary to legislative intent. Instead, the Court found that the practice of architecture includes the planning or preparing of work for use only in actual construction, rather than planning for a building in the abstract. The evidence in the record showed that the firm had not prepared the feasibility studies in contemplation of obtaining permits and actually constructing the buildings. Thus, the Court reversed the board's decision and penalty.

On appeal, the Oregon Supreme Court affirmed in part, and reversed in part, holding that "in some circumstances, a person 'may offer to render architectural services [in Oregon] without being issued a certificate of registration by the Board, if the architect advises the prospective client and the Board in writing and submits an application for registration in [the] state.'" However, "[w]hen the principals have not submitted an application for registration in Oregon, they are not qualified to practice architecture in Oregon," and thus violate ORS 671.020(1) when they make claims of pending licensure in conjunction with advertising architectural projects they have undertaken in Oregon.

D. Gary Christensen and Alexander M. Naito are attorneys with Miller Nash Graham and Dunn LLP. Contact them at (503) 224-5858, and gary.christensen@millernash.com, and alex.naito@millernash.com

RISKS AND ISSUES WITH THE SUBCONTRACTOR BUYOUT PROCESS

Tyler J. Storti
Stewart Sokol & Larkin, LLC

Prime contractors bidding on construction projects may feel a sense of relief upon learning they are the low bidder who will be awarded the contract. But several potential risks and issues arising during the subsequent "subcontractor buyout" process may catch the unwary by surprise. This article discusses some common issues and legal principles that may arise during that post-award / pre-construction phase.

A. Buyout generally; goals and procedures.

During the buyout phase, the successful prime contractor must formalize and document subcontracts and purchase orders with the lower-tier subcontractors and suppliers, respectively, that will perform the work on the awarded project. This process involves more carefully analyzing details and issues that may have been overlooked or inadequately analyzed during the bidding phase due to time constraints and not wanting to invest too much time before knowing the contract will be awarded. This buyout process affords prime contractors an opportunity to double-check important details involving the lower-tiers to ensure that they will be ready, willing and able to perform their scope in an accurate, complete and timely manner, and a chance to definitively memorialize the terms and conditions of the contract into enforceable and binding subcontract agreements.

Not surprisingly, the buyout phase also gives rise to considerations – and often disputes – relating to pricing. Armed with the leverage that accompanies being awarded the contract, prime contractors are incentivized to maximize profits by seeking to "buyout" the work with the lowest priced subcontractors and suppliers. On some projects, there are legitimate opportunities to negotiate lower pricing. For example, savings may result from value engineering efforts, achieving economies by having a single subcontractor perform multiple scopes, or reducing inefficiencies or overlapping trades not identified prior to bidding. In these (and other) instances, post-award price negotiations may very well be appropriate, assuming any resulting changes to the subcontractor ranks are allowed procedurally (*see* section C below).

However, in addition to procedural limitations on switching subcontractors, there may be ethical and legal risks to inappropriately pursuing lower pricing during buyout. These limitations, risks and considerations are discussed in the following sections.

B. Bid shopping and its risks.

"Bid shopping" is the term often used to describe a prime contractor's efforts during the buyout phase to artificially coerce subcontractors to accept lower prices from what they originally bid. If successful, such efforts result in the subcontractor accepting the lower price in order to not lose the work, and the prime contractor reaping a larger profit margin. One reported decision described a form of bid shopping as follows:

> [A] contractor obtains quotes from subcontractors that are used in preparation of the contractor's bid on the public works project. Then, after having been awarded the bid, the general contractor would either substitute another subcontractor who would be willing to do the work for less money (thus benefitting directly from the savings), or would use the threat of changing subcontractors to force the original subcontractor to reduce its price. This "bid shopping" practice is regarded as unethical by many in the building industry.

McCandlish Elec. v. Will Constr. Co., 107 Wn. App. 85, 94 (2001).

Commentators have long condemned bid shopping as unethical. *See, e.g*., Zwick, Darin C. and Kevin R. Miller, *Project Buyout*, Journal of Constr. Eng. & Mgt. (March/April 2004) 245, 247 ("Project buyout is not a time to engage in any form of unethical practices such as bid shopping subcontractors or suppliers into lower prices."). In 1995, the Associated General Contractors of America, the American Subcontractors Association, and the Associated Specialty Contractors issued this joint statement on the issue of bid shopping and bid peddling: "Bid shopping or bid peddling are abhorrent business practices that threaten the integrity of the competitive bidding system that serves the construction industry and economy so well." AGC website at www.agc.org/industry-priorities/procurement/bid-shopping (9/22/2016).

C. Subcontractor disclosure and substitution laws

Many jurisdictions, including Oregon, have enacted legislation designed (at least in part) to curb bid shopping, especially in connection with public works construction projects. Such legislation includes Oregon's requirement that prime contractors submit to the public contracting agency shortly after submitting their bid a disclosure of the first-tier subcontractors upon whose quotes the prime contractor's bid is based. ORS 279C.370. The statute requires bidders to disclose first-tier subcontractors who "will be furnishing labor or will be furnishing labor and materials in connection with the public improvement contract" and "will have a contract value that is equal to or greater than five percent of the total project bid or $15,000, whichever is greater, or $350,000 regardless of the percentage of the total project bid." ORS 279C.370(1)(a). That requirement only applies to competitively bid public works contracts with an estimated value of more than $100,000. ORS 279C.370(1)(c) and (d).

Oregon law also limits the circumstances under which and the manner in which listed subcontractors may be substituted after being included on the subcontractor disclosure form. ORS 279C.385 sets forth the permissible reasons for substitution and includes several definitive and common-sense reasons (*e.g*., the subcontractor's bankruptcy, failure or refusal to perform, or lack of a required license or bond) and less well-defined reasons (*e.g*., when the disclosure was the result of an "inadvertent clerical error," or for other "good cause"). An improper substitution not complying with that section may result in a range of potentially severe civil penalties if an aggrieved improperly substituted subcontractor complains. ORS 297C.590.

For public works projects in Oregon, the above-described subcontractor disclosure requirements and substitution limitations (at least insofar as they are applicable and enforced) serve to discourage bid shopping on those projects. There are no such laws or regulations aimed at bid shopping on private construction projects in Oregon. As such, the parties are largely left to their own devices in the private realm, and must look to any available legal theories or remedies available at common law, some of which are summarized below.

D. Whether and when bids may be binding prior to formal written contracts

During the buyout phase, there can be great uncertainty as to the extent to which, if at all, a prime contractor and subcontractor may be legally bound to one another before they have executed a formal written subcontract. Though not very well developed in Oregon jurisprudence, the generally prevailing common law offers some guidance. But the analysis is highly dependent on the exact facts at issue, and the legal result will vary from case-to-case.

One issue is whether the prime contractor who received and relied upon a subcontractor's quote in submitting the bid upstream to the owner can require that subcontractor to execute a subcontract and perform the subcontract work. The majority rule is that, in such a case (and absent any pertinent or limiting language in the quote or contrary understanding between the parties), the subcontractor's quote is generally deemed irrevocable for a reasonable period of time and may be enforced by the prime contractor against the subcontractor. A seminal and widely-cited case standing for this proposition is *Drennan v. Star Paving Co*., 333 P.3d 757 (Cal. 1958).

In *Drennan*, the subcontractor discovered a mistake in its quote and, after the prime contractor had used the quote in its bid on the project and been awarded the contract, the subcontractor refused to enter into a formal subcontract. At trial, the prime contractor was awarded damages to compensate it for the increased costs incurred to secure a replacement subcontractor to perform the subject work. On appeal, the judgment was affirmed with the court holding that the prime's detrimental reliance on the quote rendered it irrevocable for a reasonable period of time, applying section 90 of the Restatement of Contracts. *Drennan*, *supra*.

In Oregon, there is no reported decision in the construction context on that particular subcontracting issue, though Oregon courts have applied the concept of promissory estoppel generally and adopted section 90 of the Restatement. *See, e.g., Schafer v. Fraser*, 20 Or 446 (1956); *Bixler v. First Nat'l Bank*, 49 Or App 195 (1980).

Analyzing the other side of the same issue – whether a subcontractor may bind the successful prime contractor to whom it submitted a quote that was used by the prime contractor in its bid – may yield a different result. The majority rule is that a subcontractor in that situation generally may not use promissory estoppel as a sword to force the prime contractor to contract with the subcontractor. *See, e.g., Elec. Constr. & Maint. Co. v. Maeda Pac. Corp*., 764 F.2d 619, 621 (9th Cir. 1985) ("Generally, the mere use of a subcontractor's bid by a general contractor bidding on a prime contract does not constitute acceptance of the subcontractor's bid and imposes no obligation upon the prime contractor to accept the subcontractor's bid."). Many of the reported decisions on this issue note the lack of certainty and detail that often accompanies a bare subcontractor quote, the indefiniteness of the mere use of the quote as expressing unconditional acceptance, and the general unenforceability of agreements to agree that the parties intend to later reduce to a formal writing. But, as with the other side of the issue, the likely legal result can vary depending on the particular facts and circumstances involved.

Oregon case law is quite sparse on this particular construction contracting situation as well, but several Washington cases illustrate different iterations of the fact pattern and discuss several issues that may arise between subcontractors and prime contractors. *See, e.g., Plumbing Shop, Inc. v. Pitts*, 67 Wn.2d 514 (1965); *Indus. Electric-Seattle, Inc. v. Bosko*, 67 Wn.2d 783 (1966).

E. Conclusion

As the foregoing discussion illustrates, receiving a notice of award is only half of the battle for a successful prime contractor. A number of other steps must be undertaken during the buyout phase to solidify the subcontracts and prepare to commence work. A number of risks and legal considerations, as well as opportunities, await the prime contractor during that phase. Being aware of and skillfully navigating those obstacles can help maximize the likelihood of a successful project going forward.

Tyler Storti is a member of Stewart Sokol & Larkin, LLC, focusing on construction law, business, and commercial matters. Contact him at (503) 221-0699 or tstorti@lawssl.com.

REPAIR WORK MAY EXTEND THE TIME FOR RECORDING A WASHINGTON CONSTRUCTION LIEN

Curtis A. Welch
Sussman Shank LLP

Determining the date on which a lien claimant's performance on a Washington construction project has ceased is often straightforward in the situation where the lien claimant stops performance and does not later resume performance. However, there are many cases where a lien claimant returns to the project after the bulk of his or her performance is complete, either to make repairs or replace defective materials. In that situation, a claimant may be unclear regarding the recording deadline for his or her construction lien. Fortunately, a lien claimant is guided by long-standing and consistent rules established by Washington courts for such cases.

A. Case law

One of the leading cases on this issue is *Friis v. Brown*, 37 Wn. 2d 457 (1950). In *Friis*, a contractor, Friis, worked between April 11th and June 4th to install a furnace in a house that was being constructed by another contractor. Friis did nothing else on the project until September 23rd, at which time he went to the house, made some adjustments, and started the furnace.

The owner failed to pay Friis for his installation work, and he recorded a lien.

The owner argued that Friis's last day of work was June 4th and that his lien was therefore untimely. The Washington Supreme Court rejected the owner's argument and held that the lien was timely. In its holding, the Court stated as follows:

> Under the contract, it was the duty of Friis to see that the furnace was in proper operating condition. His obligation was not fully performed until this was done. Although no new materials were installed September 23rd, Friis did spend considerable time there on that occasion, making adjustments and becoming satisfied that the furnace was in proper working order. This work was not done under a new and independent contract. It was not done for the purpose of prolonging the time for filing the lien, nor of renewing the right to file a lien which had been lost by a lapse of time, but was done in furtherance of the original contract. *See Kirk v. Rohan,* 29 Wn. 2d 432, 187 P.2d 607. We therefore hold that the last work on the contract was performed September 23rd and that the trial court erred in denying the foreclosure of the lien.

Friis, 37 Wn. 2d at 460.

In *Kirk v. Rohan*, *supra*, the contractor, Kirk, was hired to build a garage for Rohan. Kirk and his crew worked on the garage from August 5th until November 19th. Rohan then occupied the garage, and Kirk picked up his tools and equipment from the job site and took away some remaining lumber.

On February 1st of the next year, a heavy rain storm caused water to back up from the street and flood the garage. Rohan called Kirk's foreman, who came to the house on February 4th along with other employees, and remedied the defect.

Rohan did not pay Kirk for the full price of construction of the garage, which led to Kirk recording a lien on May 3rd, using February 4th as the last day. The owner refused to pay, arguing that the lien was untimely because it was not filed within 90 days from November 19th.

The Supreme Court held that the lien was timely, stating the test as follows:

> The law is well settled in this state that work done or materials furnished under a new and independent contract, entered into after the original contract is completed, cannot be tacked onto the original contract to extend the time for filing a lien under the original contract, for labor performed and materials furnished. However, if the work is done or materials furnished at the request of the owner to complete the original contract, or to remedy some defect in the work done, then the time for filing the lien would run from the last furnishing of labor and material, provided the work is not done for the purpose of prolonging the time for filing a lien, or renewing the right to file a lien which had been lost by a lapse of time. In short, if the work done or material furnished at the request of the owner, is in furtherance of the original contract, then the time for filing the lien is extended. We hold, under the evidence, that the work done February 4th was in furtherance of the original contract, and that the filing of the lien on May 3rd was timely.

Kirk, 29 Wn. 2d at 432

In another leading case, *Rieflin v. Grafton*, 63 Wash. 387, 389 (1911), a supplier provided windows and doors and other materials to a general contractor in connection with the new construction of a house. The supplier provided all of its materials between March 2nd and June 2nd, except for two or three panes of glass, which were delivered to the project on August 18th in order to replace defective glass that the supplier had previously supplied. The supplier was not paid, and subsequently recorded its lien on October 14th, within 90 days of the August 18th date. The owner argued that the lien was untimely.

The Supreme Court held that the lien was timely, stating as follows:

> [t]he delivery of August 18 was made upon the demand of one of the owners of the property, for the purpose of correcting defects which he claimed existed. The good faith of the appellant in furnishing these items cannot be questioned. The time for filing the claim of lien had not then expired, and the material was not furnished for the purpose of prolonging the time for filing it, or for the purpose of renewing a right to a lien which had been lost by delay.

Finally, in another well-known case, *Heaton v. Imus*, 21 Wn. App. 914, 916 (1978) *rev'd on other grounds*, 93 Wn. 2d 249 (1980), the property owners hired a contractor, Heaton, to perform rehabilitation work on several of the owners' properties. The owners failed to pay Heaton for work on one of those properties and Heaton recorded a lien.

The owners claimed that Heaton's lien was untimely. At issue in that case was whether labor performed by Heaton and one of his employees on December 29th constituted the last day of performance or whether performance ceased much earlier. The work performed on December 29th consisted only of checking and bracing cables for cement building slabs.

The Court of Appeals held that the lien was timely, and that the 90-day lien period did not start until work was complete on December 29th. The Court stated that "[w]hen additional work is undertaken to remedy a defect in work already completed, the time for filing a lien runs from the

date of performance of the additional labor if the later work was not done (1) under a new and independent contract, (2) for the purpose of prolonging the time for filing the lien, or (3) in an attempt to renew the right to file a lien that had been lost by a lapse of time. *Friis v. Brown,* 37 Wn.2d 457, 460, 224 P.2d 330 (1950))."

B. Discussion

Several points are clear from the above case law and the related case law. The two key factors for determining whether repair work extends the time for recording a lien are whether the work was furnished at the request of the owner, and whether such work was done to complete the original contract. If those factors are met, a court is likely to find that the repair work extends the time for recording a construction lien. Further, meeting those two factors works to cancel out the potentially disqualifying factors referenced in the *Heaton* case, that is, whether the work was done under a new and independent contract, or for the purpose of prolonging the time for filing the lien, or in an attempt to renew the right to file a lien that had been lost by lapse of time.

As the *Reiflin* court pointed out, a lien claimant's good faith in performing the repair work typically cannot be questioned if the owner requested the work. The owner would have a difficult time arguing that the lien claimant performed the repair work just to prolong the time for filing the lien, if the owner or his or her agent requested that the repair work be performed.

Further, as demonstrated by each of the four cases cited above, even small amounts of repair work or replacement materials are sufficient to extend the time for recording a lien.

It is also clear that it does not matter if the lien claimant charges its customer for the repair work or for the replacement materials.

C. Conclusion

It should be noted that Oregon courts have their own interpretation of whether repair work extends the time for recording Oregon liens. In general, Oregon lien cases regarding this issue are not as liberal towards the lien claimant as are Washington cases. *See, e.g., Pro Excavating v. Ziebart*, 148 Or. App. 436, 441 (1997).

No matter what state's laws are involved however, a lien claimant needs to be vigilant in keeping track of their deadline to record a construction lien. The safest approach of course is for the lien claimant to calculate their deadline by reference to the date on the lien claimant's performance was substantially complete. Should a lien claimant fail to do so however, and the lien filing period from the date of substantial completion has passed, there is nevertheless still hope for the Washington lien claimant provided he or she has performed repair work which meets the factors discussed above

Curtis Welch is Special Counsel with Sussman Shank LLP, focusing on construction law, civil litigation, real property law, and insurance law. Contact him at (503) 227-1111 or cwelch@sussmanshank.com.

NINTH CIRCUIT AFFIRMS $2 MILLION AWARD TO BENSON TOWER CONDOMINIUM OWNERS ASSOCIATION FOR DEFECTIVE VICTAULIC PARTS

Sandra Fraser
Fraser Law

In a recent opinion affirming a $2 million jury award to the Benson Tower Condominium Owners Association (COA), the Ninth Circuit found that Oregon's products liability law does not require "significant" damage to property in order to hold the manufacturer of the defective product strictly liable for the damage. Although the Court's memorandum issued on August 16, 2017 is unpublished, it is likely the holding will affect

the outcome of similar cases pending against the same manufacturer, Victaulic Company.

History

Since 2011, five separate lawsuits filed by luxury condominium and apartment properties in downtown Portland have alleged Victaulic Company sold defective plumbing parts installed during the construction of each property. The Victaulic valves and couplings at issue used a type of rubber that degraded prematurely when exposed to chloramine, a disinfectant used in Portland's domestic water supply. As the rubber disintegrated, alleged property damage ran the gamut from water leaks and failing shut-off valves to the presence of black particles in the domestic water supply believed to be carbon black, a potential carcinogen. One of the plaintiffs, The Indigo at Twelve West Apartments, resorted to supplying bottled water to building residents until the parts were replaced.[1]

Prior to the recent decision in the Benson Tower case, results for plaintiffs in these lawsuits has been mixed. Elizabeth Lofts Condominiums was the first property to file suit, seeking $3.1 million in damages in its complaint filed in state court on October, 2011. The parties settled out of court in 2014 for an undisclosed amount. Edge Lofts COA sought $1.5 million in damages after replacing the allegedly defective Victaulic plumbing parts, and won at trial in June, 2014. However, it was a pyrrhic victory because the jury awarded them only $114,000. The Benson Tower and Avenue Lofts COAs filed their lawsuits in June, 2013 and October, 2016, respectively. The Avenue lawsuit, filed in state court and seeking $1.9 million in damages, is currently set to go to trial December 4, 2017. The most recent case, filed by a group of three plaintiffs, 12RPO LLC, The Vaux COA, and Nine Three Seven COA, sought a total of $23.5 million in damages. According to the most recent docket for this case[2], counsel for the parties informed the court on September 22, 2017 that the action had been settled.

Victaulic Appeal of the Benson Tower's Award

On January 15, 2015, after an 8-day trial, the jury awarded $2M to the Benson Tower COA after determining that Victaulic's defective products caused damage to the Benson Tower's domestic water system[3]. The Benson's other claims for negligence and for an award of punitive damages were denied. Victaulic petitioned the court for a judgment as a matter of law, or in the alternative, a new trial. The Court denied both motions. Victaulic appealed on various points, however their primary argument was that the evidence presented by Benson Tower didn't meet the standards required by Oregon's product liability law to find Victaulic strictly liable.

Oregon's strict products liability law is codified in ORS § 30.920. Under the statute, a seller is strictly liable for "damage to property" which is caused by a product sold in a "defective condition unreasonably dangerous to the user . . . or to the property of the use." Benson Tower alleged, and the jury agreed, that Victaulic sold defective valves and couplings which damaged the building's potable water supply, and was therefore liable for costs associated with repairing the damage.

Victaulic's primary argument on appeal was that the mere presence of black particles in the Benson Tower's potable water supply didn't rise to the level of "significant" damage that Victaulic claimed Oregon's products liability law required,

[1] Njus, Elliot. *Developer Mark Edlen, Two More Condo Properties Join Chorus of Plumbing Defect Lawsuits*. Oregonian/OregonLive. July 9, 2015. http://www.oregonlive.com/front-porch/index.ssf/2015/07/developer_mark_edlen_two_more.html

[2] Filed in US District Court for Oregon as *12RPO, LLC et al v. Victaulic*, case no. 3:15-cv-01411.

[3] The original case, *Benson Tower COA v. Victaulic Company*, was filed in the US District Court for Oregon as case number 3:13-cv-01010.

and that the damages Benson complained of were merely economic loss. Relying on limited economic loss holdings in *Russell v. Deere & Co*., 186 Or App 78 (2003), and *Brown v. Western Farmers Assoc.*, 260 Or. 470 (1974), Victaulic argued that ORS § 30.920 required evidence of "significant" damage to property in order for the product's defective condition to be considered "unreasonably dangerous."

Benson Tower's response pointed the court to *McCathern v. Toyota Motor Corp.*, 332 Or. 59, 79 (2001), in which the Oregon Supreme Court held that the "controlling test [for purposes of establishing the element of "unreasonably dangerous"] . . . is the consumer expectations test." Under the consumer expectation test, a product is "unreasonably dangerous to the user or consumer" if the product is defective "to an extent beyond which the ordinary consumer would have expected." *Id*. The Benson argued the defective products, which experts had shown were contaminating the building's water with black particles thought to be carbon black (a potential carcinogen), and which would inevitably fail and leak water throughout the building, were clearly defective beyond that which the ordinary consumer would expect.

Secondly, Victaulic argued that the building's potable water was not separate property from the plumbing system itself, instead, it was part of an integrated system such that any damage was not to other property and was just economic loss. Here, Victaulic sought to rely on Comment *h* to § 402A of the Restatement (Second) of Torts (1965)[4] in which the drafters discussed the fact that a carbonated beverage could not be distinguished between the product and the container, that the two become an "integrated whole."

The court was not persuaded by Victaulic's arguments. Citing testimony from Benson Tower witnesses confirming the presence of black particles in the building's potable water system throughout the building, and multiple expert opinions related to the probability that the black particles were a result of the EPDM rubber from Victaulic's valves and couplings which prematurely degraded after contact with chloramine, the Court first declined to follow the standard suggested by Victaulic and held that Oregon product law does not require "significant damage" to find a product "unreasonably dangerous." The Court also shut down Victaulic's second argument that the potable water is simply part of the plumbing system, citing *City of Pomona v. SQM N. Am. Corp.*, 750 F.3d 1036 (9th Cir. 2014) (contamination of groundwater supply is damage to property), "unlike a carbonated beverage and the bottle it comes in, plumbing valves and potable water are not an 'integrated whole' packaged and sold together that may appropriately be considered a single product."[5] The Court affirmed the District Court's ruling on the basis that the Benson provided substantial evidence that the defective Victaulic parts "degraded prematurely and leached possible carcinogens into Benson's potable water supply."[6]

Although the case will not act as precedent for future defect cases, it provides insight into prevailing Oregon law on economic loss and products liability, and the extent of damage required to prevail on strict products liability claim.

Sandra Fraser is an attorney with Fraser Law LLC, focusing in construction and business law. Contact her at (503) 201-1376, or sandra@fraserlawllc.com

[4] ORS 30.920(3) incorporates The Restatement (Second) of Torts (1965) into the statute.

[5] *Benson Tower COA v. Victaulic Company*, Case No. 15-35119, fn. 2 (Aug. 16, 2017)(not for publication).

[6] *Benson Tower COA v. Victaulic Company*, Case No. 15-35119, p.4 (Aug. 16, 2017)(not for publication).

CONTRACTING TIPS FOR CONTRACTORS

Ryan Hunt
Garrett Hemann Robertson PC

As a litigation attorney that routinely represents clients in construction defect claims, it is easy to lose sight of issues that can be resolved on the transactional side of our work for contractors. Often, litigators are focused on the specific task before them and the contract documents at issue. We are busy shoe-horning those issues to best fit the case law that supports our position. That is what makes many of us a great resource for anyone that drafts the contract documents that we could very well need to defend in the future. As a former senior partner of mine once told me, "Litigators really make the best transactional lawyers because they know the difficulties with defending the very documents I am drafting."

Having said that, what are some tips that litigators can pass along to anyone that drafts construction contracts? The answer is there are many, almost too many to fit into a single article. However, there are a few pointers I routinely at least discuss with any client that asks me to draft or review a contract for them. Here are a few of the highlights.

Contracting in a Post-*Goodwin* World

As I am sure we all know, the construction defect bar had a bit of a surprise with the decision reached in *Goodwin v. Kingsmen Plastering*. In that case, the court let us all know that the statute of limitations to bring a negligent construction claim was 2 years, with a discovery rule. I can tell you that I was surprised by this result, as there was a sort of "understanding" that there was a 6 year statute to bring a negligence claim.

So why does *Goodwin* matter? One of my first thoughts as I drafted my next contract post-*Goodwin* was that this was the perfect opportunity for the AIA accrual clause to rise from its ashes and be useful again. The standard AIA accrual clause provides that any claims or causes of action accrue at the time of substantial completion. With *Goodwin* now guiding us, this is significant. If we combine *Goodwin* with good accrual clause language, we can now limit our client's exposure to a negligence claim to 2 years with no discovery rule. That is a very big deal for our contractor clients. For that reason, I routinely put that language into any contractor/owner agreement, and I suspect many others are doing the same.

Do Fees Really Matter?

Another big issue that I see with my contractor clients is whether an attorney fee clause is a good idea. The knee jerk reaction is typically, but of course a fee agreement in any contract is a great idea because it gives your client leverage to resolve payment disputes. However, I don't agree.

The only time our contractor clients are ever going to sue their customer is to get paid. However, there are multiple reasons why an owner may sue our contractor clients (allegedly negligent work, fraud, breach of contract, aesthetic claims, etc.). Why would we give leverage to the client by giving them a fee claim to heap upon their alleged claims? I argue that we never should. If our clients really are not getting paid, the lien statutes give them a fee claim without putting that into their contract only to be used against them for the inevitable negligent construction counterclaim to any payment dispute. For that reason, my vote is to leave these fee clauses out of any contract with an owner.

To Arbitrate or Not to Arbitrate

The final issue that routinely comes up is whether an arbitration clause is good, or even advisable. Ultimately, this is up to the client. Many clients like the fact that an arbitrator (or sometimes even three) knowledgeable in construction will be who makes the ultimate decision. This is logical because no one knows how 12 strangers may come

out on a construction dispute. However, arbitration does not come without risks.

The biggest risk I warn any client about is what if the arbitrator(s) get it wrong? There is no higher arbitrator to appeal a legal mistake to. That can only be done in the court system, which means staying in the local circuit court is probably best.

The second risk is cost. If I try a case in circuit court, I do not have to pay the judge to preside over the proceedings, or the jury to give us a decision. That is not true in arbitration. The arbitrator(s) expect to get paid, and those costs add up quickly. This is yet another reason to strongly consider whether arbitration is prudent.

Conclusion

These are just a few of the issues that a litigator can bring to the fore when drafting contract documents for a client. The best way to understand how the documents matter, and what words you use matter, is to defend them in court. That only comes with experience in the courtroom. It would be a mistake not to take advantage of that experience when working on the transactional side of things for your client. As the same seasoned former partner of mine once told me, "The goal of good contract documents is to put as many hurdles as you can in front of someone who wants to bring a claim. The more opportunities for failure you build in for your client, the more likely you will succeed in the long run."

Ryan Hunt is a shareholder with Garrett Hemann Robertson P.C. focusing on Construction Law. Contact him at (503) 581-1501, ext. 732, or rhunt@ghrlawyers.com