Between a Rock and a Hard Place:
Notifying Sureties of a Contractor's Default

Eric L. Singer

Wildman, Harrold, Allen & Dixon
2300 Cabot Drive, Suite 455
Lisle, Illinois 60532
(630) 955-0555 (main) | (630) 955-5826 (direct) | (630) 955-0662 (fax)
singer@wildmanharrold.com

The Contractor is eight weeks behind schedule and the resulting liquidated damages are eclipsing the contract balance. You recommend that the Owner declare a default and make a claim on the Contractor's performance bond. Have you interfered with the Contractor's agreement with the Owner? Have you defamed the Contractor?

Contractors have been extremely aggressive in asserting claims against design professionals in precisely this context, and Courts have allowed some of these claims to proceed to judgment. If you wait too long to notify the surety, however, the surety may disclaim coverage under the bond, leaving the Owner with no choice but to blame you. The contractor default is another tightrope for A/e's, and you must learn to watch your P's and Q's.

Who Made You Boss?

Where do you get the authority to tell on the contractor? The law protects contracting parties from outside interference. A stranger can persuade one party to breach a contract with another and be sued for intentional or "tortious interference" with contract. A stranger can also incur liability for defamatory statements about another.

The A/e and the Contractor each have separate contracts with the Owner. The A/e does not have a contract with the Contractor. The Contractor's agreement with the Owner describes the A/e's duties, and even provides that the A/e will review and judge the Contractor's work. In some circumstances, the A/e will be the initial arbiter of disputes between the Owner and the Contractor. Your contracts therefore provide you with the right and duty to provide advice.

The Privileged Few

Although a stranger to the contract can incur liability for interference, one may have the right or duty to provide advice and can be protected by the doctrine of justification or "privilege." The defense of privilege or justification can be a complete defense to claims of interference or defamation (recall the discussion of a testimonial privilege afforded expert witnesses in the "Playing With Fire" article).

As long as your contract says so, you have the right and contractual obligation to observe the Contractor's work and to advise your client accordingly. AIA documents, for example, contain express obligations to review the work of the Contractors, advise the Owner and provide protection for advice given in good faith (AIA B141 (1997) 2.6.1.3, 2.6.1.7, 2.6.1.8 and 2.6.2.5). Under the law of many states, courts have

created a "privilege" for A/e's in this circumstance, and a potentially complete defense from defamation or interference claims by Contractors.

The defense of justification or privilege is only available when the design professional's opinion is requested or required. The contract should provide a contractual duty to advise the owner. If the contract is silent about the A/e's review of the contractor's work, there may be an argument that the advice was gratuitous and not protected.

Other exceptions to the defense include actions taken in bad faith or actions taken beyond one's contractual authority. Bad faith can be difficult to define and leaves the courts some discretion to do so on a case-by-case basis. Blaming the contractor to cover up a defective design has been held to be "bad faith."

Truth, of course, may also provide a complete defense. Proving the truth, however, is a slow and expensive process. In addition, most construction disputes contain complex and conflicting professional opinion. The real "truth" may be somewhat elusive.

Mind Your P's and Q's

The case law suggests caution when providing an opinion on a contractor default. Your contract, field notes and communications with the owner and surety must rely on objective requirements.

Contractual Foundation. Your contract should describe duties to provide advice to your client. The Contractor's agreement and general conditions should mirror those provisions. (See AIA A201 4.2.2, 4.2.5, 4.2.6, 4.2.11 and 4.2.12, 1997 ed.). You should also have protection for opinions rendered in good faith. (AIA B141 (1997) 2.6.1.8 and 2.6.2.5; AIA A201 (1997) 4.2.6 and 4.2.12)

Any certification of a contractor's default should reference and quote the contract's language and state that you are providing an opinion at the request of the Owner. The stated basis for your opinion should identify express contract provisions.

Concentrate On Objective Criteria. Any written statements should include objectively verifiable criteria. Your suspicions or doubts should not be included.

We doubt that the Contractor will complete the work in accordance . . ." is not recommended.

"The Contractor has failed to complete . . ." or "failed to provide labor necessary for proper execution and completion of the work in accordance with Article 3.4 of the General Conditions of the Contract for Construction" are better.

Nor should you include characterizations, inflammatory descriptions or superlatives in describing the work.

"The worst work we have ever seen," for example, is not recommended.

It is sufficient to say that the contractor has persistently failed to complete the work in accordance with the contract documents, without making derogatory remarks about his crew, superintendent or personal characteristics.

Your construction-phase documentation should also be free from such comments. Inflammatory field notes or comments in meeting minutes may point to "bad faith" or malicious intent, regardless of what is in your notice to the surety. Expletives, references to ethnicity or national origin and other personal characteristics have no place in your field notes. Such comments may provide fuel for a claim of interference.

The Chain of Command. Your contract with the owner requires you to provide advice to your client. The surety bond is a contractual relationship between the owner and the surety. You should advise your client, and have your client advise the surety. Even if you draft the letter to the surety, prepare it for the owner's signature.

The Rock and The Hard Place

Finally, be prepared to defend your opinion, your services and your prior certifications of payment applications (See "Sitting Ducks" for examples of liability to sureties for "overcertification."). The surety and its attorney will carefully review the prior payment certifications, meeting minutes and contractual basis for the default. The surety is not necessarily the A/e's ally.

If you find yourself between a rock and a hard place, call your insurance representative or your attorney before committing anything to writing.

About the Author: Eric L. Singer is with Wildman, Harrold, Allen & Dixon, Lisle, Illinois. His practice concentrates in construction law and in the representation of design professionals in all aspects of construction claims and dispute resolution.
