

ZACHRY CONSTRUCTION V. PORT OF HOUSTON AUTHORITY

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TWO SIGNIFICANT ISSUES

No Damages for Delay Clauses (NDFD)

Lien Releases

BACKGROUND

Zachry wins bid for project

- Proprietary process for working “in dry”
Efficient and environmental benefits

Contract entered – June 1, 2004

- Zachry controls means and methods

Strict Timeline

- Interim and final
February 1, 2006 and June 1, 2006

BACKGROUND (CONT.)

- Interim to allow delivery of large cranes from China

Construction Begins

Zachry provides PHA with its freeze- will design

- After construction began – had already installed main freeze wall and some freeze pipes
- Zachry claims submitted only for PHA's records and compliance OSHA's safety regulations and to show engineer's stamp

BACKGROUND (CONT.)

- PHA stamped “accepted for records”

Contract provided Zachry responsible for means and methods

The Port Authority shall not have the right to control the manner in which or prescribe the method by which the Contractor performs the Work. As an independent Contractor, the Contractor shall be solely responsible for supervision of and performance of the Work and shall prosecute the Work at such time and seasons, in such order or precedence, and in such manner, using such methods as contractor shall choose...

PHA did not want responsibility/potential liability (control)

PROJECT EXTENSION

PHA decides it wants to expand/extend original project – March 2005

- Adding a sixth wharf section – original design too short for modern ships
- Zachry submitted proposals – beginning in April 2005 (April 13, May 18 and July 11)
- Proposed design for extension – frozen cut-off wall – to be installed near existing/permanent piers
- Design submitted on September 9, 2005
- Change Order for extension (C04) executed on September 27, 2005

DISPUTE OVER EXTENSION DESIGN

One of PHA's engineers expressed concern over extension design

- Because freeze wall too close to existing piers – freezing could compromise integrity of piers
- Some debate over validity of concerns
 - only testing done showed no basis for concern
 - many design professionals did not want to weigh in on

PHA rejects freeze cut-off wall design – October 11, 2005

- Changed September 9 design submission from “correspondence” to “submitted”
- Issued a “revise and resubmit” order
- Doing so after signing CO4

STRAINED RELATIONS

Zachry claims breach

- Project budget and schedule (meeting deadlines) depended on freeze wall design
- They had right to control means and methods – per CO4

PHA sends Zachry letter 3 days later demanding timely completion

- Threatened liquidated damages (LDs) if they did not

Zachry switches to working “in the wet”

OVERTIME

Zachry sufficiently completed first phase (milestone A) before May 15, 2006

- Chinese ship arrived and docked on May 15, 2006

Project substantially completed in October 2008

PHA began assessing LDs in May 2006 - \$20,000/day

- Withheld a total of \$2.36 million in LDs
- PHA later voluntarily stopped withholding LDs

Zachry sued PHA for breach in late 2006

THE TRIAL

Zachry sued PHA for damages

- Additional costs for having to complete Project "in the wet"
- LDs withheld - \$2.36 million
- \$600,000 for amounts withheld for alleged defective dredging

PHA counterclaimed for AFs for bringing claim

THE TRIAL (CONT.)

Jury awarded Zachry \$18,602,697 for breach

Trial court ruled \$2.36 million in LDs improperly withheld

Jury also found:

- \$600,000 for defective dredging properly withheld
- PHA entitled to offset of \$970,000 for defective work on Wharf fenders
- Awarded PHA \$10,500,000 in AFs

Judgment entered for \$19,992,697 – No AFs

COURT OF APPEALS

Reversed

Held NDFD clause was unenforceable

- Refused to apply exceptions
- Focused on language of NDFD
 “Other fault” instead of “negligence”
- Freedom of contract – parties are big boys

Does not necessarily foreclose exceptions under
Texas law

Awarded PHA attorneys fees of \$10,500,000

NO DAMAGES FOR DELAY

The Contractor shall receive no financial compensation for delay or hindrance of the Work. In no event shall the Port Authority be liable to the Contractor or any Subcontractor or Supplier, any other person or any surety for or any employee or agent of any of them, for any damages arising out of or associated with any delay or hindrance to the Work, regardless of the source of the delay or hindrance, including events of Force Majeure, AND EVEN IF SUCH DELAY OR HINDRANCE RESULTS FROM, ARISES OUT OF OR IS DUE, IN WHOLE OR IN PART, TO THE NEGLIGENCE, BREACH OF CONTRACT OR OTHER FRAULT OF THE PORT AUTHORITY. The Contractor's sole remedy in any such case shall be an extension of time.

NO DAMAGES FOR DELAY CLAUSE (CONT.)

Court's Instruction (to Question No. 3):

FN1. In Question No. 3, the trial court instructed the jury as follows with respect to section 5.07:

You are instructed that §5.07 of the Contract precludes Zachry from recovering delay or hindrance damages, if any, unless you find that the delay or hindrance damages, if any, resulted from a delay or hindrance that was the result of the Port's actions, if any, that constituted arbitrary and capricious conduct, active interference, bad faith and/or fraud.

NO DAMAGES FOR DELAY CLAUSE (CONT.)

These clauses fairly common in construction industry

Powerful – gives owner a lot of freedom and leverage

- Remedy is extension of time

Can be read to give owner complete impunity

Subject to negotiation?

NO DAMAGES FOR DELAY CLAUSE (CONT.)

Should there be exceptions?

- If so, what standard should be?

LIEN RELEASE

Trial Court held (on directed verdict) that
LDs withheld were invalid

- Constituted a penalty – did not make clear in lieu of other damages

PHA did not appeal ruling

But PHA claimed claims for LDs were
released

- Based on lien release signed during course of Project

LIEN RELEASE (CONT.)

Required to get paid

- Pay applications – periodic payments (monthly)
- Contract required lien release – Section 6.07 – requires “waivers and releases of liens”
- “Affidavit and Partial Release of Lien for Zachry Construction Company” – Releases all liens for work performed that is the subject of that payment

LIEN RELEASE (CONT.)

PHA claims lien release releases not only liens but any claims for work covered by periodic payment

Release does not say "release" but has release type language

Release language:

"ZCC (Zachry) hereby acknowledges...partial payment on Payment Estimate Number ___ and that it has no further claims against PHA for the portion of the work completed and listed on the Schedule..."

LIEN RELEASE (CONT.)

Release in title but not in body

Releases typically narrowly/strictly construed

- Must “mention” the claim to be released

Releases not a form – Changed over life of Project

- Started with broad/general release language – “all causes of action”
- Deleted broad language
- Added back in broad language and then carved out claims in suit (after litigation began)

LIEN RELEASE (CONT.)

Jury held not a release

- Wrongful withholding of LDs not excused by release

Court of appeals reversed – held lien release was a release of claims too

- Focused on language of release
- Strong Dissent – notes inability to determine what is being released

SUPREME COURT

Any limit to NDFD clauses?

PHA raising immunity claim too

- Chapter 271 of Local Gov't Code
 - Limited abrogation of immunity
 - Exceptions to NDFD clause engrafted by trial court sound in tort

IMMUNITY

Immunity waived by Local Gov't. Code

(a) The total amount of money awarded in an adjudication brought against a local governmental entity for breach of a contract...is limited to the following:

(1) the balance due and owed by the local governmental entity under the contract...***including any amount owed as compensation for the increased cost to perform the work as a direct result of owner-caused delays...***;

(2) the amount owed for change orders or additional work the contractor is directed to perform by a local governmental entity in connection with the contract...

(b) Damages awarded in an adjudication brought against a local governmental entity arising under a contract subject to this subchapter may not include:

(1) consequential damages, ***except as expressly allowed in Subsection (a)(1);....***

Tex. Loc. Gov't Code §271.153 (Vernon 2005) (A17).

IMMUNITY (CONT.)

What is waived?

- Just damages expressly set forth in contract?
- All damages that flow from breach of contract – common law damages?

Statute seems to carve out some common law damages – For owner caused delays

SUPREME COURT (CONT.)

Numerous Amica Curie:

PHA

City of Arlington
City of Fort Worth
Travis County
Harris County
Conference of Urban Counties
Texas Municipal League
City of Houston
Conference of Urban Counties

ZACHRY

Associated General Contractors of Texas,
Inc.
The American Subcontractors Association,
Inc.
National Systems Contractors Association
Electrical Contractors Association
Associated General Contractors-Texas
Building Branch
Associated Builders and Contractors of
Texas
Zurich Surety
Texans for Lawsuit Reform
Associated General Contractors of Texas,
Inc.
Texas Civil Justice League
Texas Aggregates and Concrete
Association

SUPREME COURT (CONT.)

All Amicus filed in favor of PHA argue for immunity

Zachry's Amicus supporters focus primarily on NDFD clauses

- Some comment on lien release

SUPREME COURT (CONT.)

Project had numerous problems

A lot of exclusionary rulings by trial court

PHA trying to hide behind their construction manager CH2MHill

7 Briefs on Merits – 5 on Petition for Review