

Design and Construction Management Professional Reporter

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New Hampshire Supreme Court Rejects Plaintiff's Argument To Apply Both The "Special Relationship" And Negligent Misrepresentation Exception To The Economic Loss Doctrine

By Colleen M. Palmer, Esq.

THE NEW HAMPSHIRE SUPREME COURT recently discussed the application of the economic loss doctrine and clarified New Hampshire's recognized exceptions to the doctrine. In affirming the district court's decision granting the defendant's motion to dismiss, the Court held that neither the "special relationship" exception nor the negligent misrepresentation exception to the economic loss doctrine applied given the facts of the case. *Plourde Sand & Gravel Co. v. JGI Eastern, Inc.*, 917 A. 2d 1250 (N.H. 2007).

In *Plourde*, a subcontractor for a private construction project located in Pembroke, New Hampshire, Hiltz Construction, Inc. ("Hiltz"), retained Plourde Sand & Gravel Co. ("Plaintiff") to supply gravel to construct the base for a roadway. After the Plaintiff supplied

the gravel for the Project, the Town of Pembroke's engineers, Keach Nordstrom & Associates ("Keach"), hired JGI Easter, Inc. ("Defendant") to test the gravel to ascertain whether the gravel met the Town's specifications.

The Defendant tested the gravel and concluded that the Plaintiff's gravel was unacceptable. As a result of the Defendant's report, Hiltz made the Plaintiff remove

and replace the defective gravel. After the Plaintiff replaced the gravel, the Plaintiff conducted its own test of the originally supplied gravel and determined that the gravel met the Town specifications.

Based on the findings of its independent gravel test, the Plaintiff sued the Defendant in tort. The Plaintiff alleged that the Defendant's negligent testing foreseeably injured the Plaintiff because the Defendant knew or should have known that Keach would rely on the Defendant's report and, further, that Keach would require the Plaintiff to replace the gravel if the Defendant concluded the gravel was defective.

The Defendant moved to dismiss the Complaint based on the economic loss doctrine because the Plaintiff's alleged damages were purely economic losses and, therefore, not recoverable in tort. Because the district court found that the Plaintiff alleged only economic loss damages, the court applied the economic loss doctrine and granted the Defendant's motion to dismiss.

The Plaintiff appealed the decision and argued (1) since the economic loss doctrine is intended to prevent contracting parties from pursuing economic losses against each other, the economic loss doctrine did not apply because the Plaintiff had no contractual privity with the Defendant or alternatively (2) the Plaintiff should be entitled to recover economic loss damages based on the negligent misrepresentation exception to the economic loss doctrine.

New Hampshire recognizes two exceptions to the economic loss doctrine where a plaintiff can pursue a tort action for recovery of economic damages in the absence of contractual privity . . .

The Supreme Court began by reviewing the history of the economic loss doctrine. The economic loss doctrine is a common law rule that prevents contracting parties from pursuing tort claims against each other to recover for purely economic damages. The Court noted that although some states limit the doctrine's application to products liability cases, New Hampshire has expanded its application to other tort cases. See *Lempke v. Dagenais*, 130 N.H. 782, 792 (1988); *Farmers Alliance Mut. Ins. Co. v. Naylor*, 452 F. Supp. 2d 1167, 1172-73 (D.N.M. 2006). The general rule in New Hampshire is that "persons must refrain from causing personal injury and property damage to third parties, but no corresponding duty exists with respect to economic loss." *Plourde Sand & Gravel Co. v. JGI Eastern, Inc.*, 917 A. 2d 1250 at 1254, citing *Ellis v. Robert C. Morris, Inc.*, 128 N.H. 358, 364 (1986); See also *Border Brook Terrace Condo. Assoc. v. Gladstone*, 137 N.H. 11, 18, (1993)("[A] plaintiff may not ordinarily recover in a negligence claim for purely 'economic loss.'").

New Hampshire recognizes two exceptions to the economic loss doctrine where a plaintiff can pursue a tort action for recovery of economic damages in the absence of contractual privity: (1) the "special relationship" exception, and (2) the negligent misrepresentation exception.

The "special relationship" exception is a narrow exception to the economic loss doctrine. The New Hampshire Supreme Court has allowed plaintiffs to pursue tort actions against banks, attorneys, and insurance investigators when there is a "special relationship" between the parties. The Court adopted the "special relationship" exception to the contractual privity requirement when it allowed a beneficiary to bring a negligence action for financial loss against a bank that failed to establish a survivorship account at the request of the depositor. The Court reasoned that the "special relationship" exception applied because:

[A] relation created by contract may impose a duty to exercise care. In general, the scope of such a duty is limited to those in privity of contract with each other. However[,] considerations of public policy have prompted the recognition of exceptions to this rule, as where the...risk to persons not in privity is apparent.

Robinson v. Colebrook Savings Bank, 109 N.H. 382, 384-85 (1969). See also *Simpson v. Calivas*, 139 N.H. 1, 4-5 (1994)("an attorney who drafts a testator's will owes a duty of reasonable care to intended beneficiaries");

Morway v. Hanover Ins. Cos., 127 N.H. 723, 726 (1986)("investigators owe a duty to the insured as well as to the insurer").

The Court reasoned that in cases where the "special relationship" exception applied, there was a "distinct and articulable relationship" between the parties and it was reasonable to allow the plaintiff to recover economic damages against the defendant because it was reasonably foreseeable that the defendant's negligence would affect the plaintiff. *Plourde Sand & Gravel Co. v. JGI Eastern, Inc.*, 917 A. 2d 1250 at 1256.

In the instant case, the Court refused to apply the "special relationship" exception. The Court found that the litigants were retained by separate entities and they had no relationship with each other. The Court reasoned that the Plaintiff's economic loss arose "solely from disappointed commercial expectations" because the Plaintiff "lost the anticipated profits of its contract" with Hiltz. *Plourde Sand & Gravel Co. v. JGI Eastern, Inc.*, 917 A. 2d 1250 at 1256-57, citing *Anderson Elec. v. Ledbetter Erection Corp.*, 503 N.E. 2d 246, 249 (Ill. 1986). The Court concluded that the exception was inapplicable because there was no "special relationship" between the Plaintiff and Defendant to establish any independent tort duty of the Defendant to the Plaintiff to prevent economic loss. The Court further noted that imposing such a tort duty would disrupt the contractual relationships between and among the various parties. *Plourde Sand & Gravel Co. v. JGI Eastern, Inc.*, 917 A. 2d 1250 at 1256-57.

The New Hampshire Supreme Court also recognizes negligent misrepresentation as an exception to the economic loss doctrine. The narrow negligent misrepresentation exception is based on Restatement (Second) of Torts § 552, which provides:

One who, in the course of his business, profession or employment, or in any other transaction in which he has a pecuniary interest, supplies false information for the guidance of others in their business transactions, is subject to liability for pecuniary loss caused to them by their justifiable reliance upon the information, if he fails to exercise reasonable care or competence in obtaining or communicating the information.

Restatement (Second) of Torts § 552(1).

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Limitation Of Liability Provisions May Not Be Used To Determine Good Faith Settlement Motions

By Carey E. Fillmann, Esq.

THE COURT OF APPEALS OF THE STATE OF CALIFORNIA, Fourth Appellate District, recently affirmed the validity of “limitation of liability” clauses in contracts and held that the clause may not be used against third parties to determine if a good faith settlement was warranted. The court also potentially exposed design professionals to liability for economic damages from parties without contractual privity.

TSI Seismic Tenant Space, Inc. v. Geocon, Inc., 56 Cal. Rptr. 3d 751 (Cal. App. 4th Dist. 2007) involved the design and construction of an apartment complex. Geocon, Inc. (“Geocon”) was retained by Serena Sunbow (“Sunbow”), the developer, to provide geotechnical services. Geocon initially provided a soils report indicating that the soil had “low expansion.” As a result of later soil testing, Geocon changed its professional opinion in subsequent reports to state that the soil had “high expansion.” Based upon this change, Geocon modified its recommendations for the foundation and slabs from its original report.

Sunbow retained TSI Seismic Tenant Space, Inc. (“TSI”) as the general contractor for the project and Swanson & Associates (“Swanson”) to provide structural engineering services. Construction began in 1999. After completion of construction in 2000, the stairs and flatwork began to crack due to expanding soils. Sunbow filed suit against Geocon, TSI, and Swanson. TSI also brought a cross-complaint against Geocon.

The contract between Geocon and Sunbow contained a limitation of liability clause limiting Geocon’s liability to \$50,000. The limitation of liability clause also contained an indemnity clause in favor of Geocon for any third-party liability above \$50,000. A judicial referee decided that, unless Geocon was grossly negligent, the limitation of liability clause was enforceable.

Both sides used experts for the gross negligence issue. Judge Midlam, the judicial referee, decided that Geocon did not meet the standard of care on at most two occasions, and that this did not constitute

gross negligence. Therefore, the limitation of liability provision was enforceable. Sunbow settled with Geocon for \$50,000. Geocon waived its right to recover attorneys’ fees in excess of \$250,000 conditioned upon a finding of a good faith settlement by the court under California Civil Procedure Code 877.6.

TSI and Swanson opposed the motion on grounds that the settlement was not proportionate to the \$3.4 million in damages attributed to Geocon’s negligence out of the \$6.4 million in total damages; the limitation of liability was not enforceable against third parties; and it went against the interests of the non-settling parties. TSI and Swanson used the testimony of Sunbow’s geotechnical expert to show that Sunbow’s damages were \$6.4 million and that Geocon was responsible for \$3.4 million of those damages. Under Cal. Civ. Proc. Code § 877.6 (c) (2007), if a settlement is found to be in good faith, claims for equitable contribution based on the extent of each parties’ negligence by co-defendants against the settling defendant are barred. Geocon argued that the non-settling parties could still

While the court reaffirmed the enforceability of limitation of liability provisions, such provisions may not be used against parties who are not privy to the agreement or for determining good faith settlements.

argue Geocon's liability to offset their liability at trial and TSI and Swanson were not bound by allocation of fault created by the settlement. The court upheld the motion, finding that even though the liability of Geocon was capped at \$50,000 the settlement was still within "reasonable range" of their proportionate share of the liability.

The appellate court reversed the decision of "good faith" settlement, finding that the lower court abused its discretion. According to the evidence, Geocon's potential liability was \$3.4 million. Although for any claim brought by Sunbow the liability would be capped at \$50,000, the limitation of liability clause did not shield Geocon from third-party indemnity claims. The court found that if a good faith motion were to be granted, Sunbow would be able to pursue claims against the other parties for the entire \$6.4 million without any reduction in amount for Geocon's \$3.4 million liability.

The court reasoned that the rights of all parties must be taken into consideration. The settlement between Geocon and Sunbow itself would not harm the other parties. Geocon did not need a good faith settlement ruling since the limitation of liability provision contained an indemnity in which Sunbow would indemnify Geocon for any liability to third parties above \$50,000. The determination of good faith would, however, allow Sunbow to pursue the entire \$6.4 million in damages against the other non-settling defendants without reduction for Geocon's liability.

In reaching its conclusion, the appellate court looked at Geocon's liability to Sunbow and Geocon's liability to TSI. The court found that since Geocon, TSI, and Swanson each owed a duty to Sunbow and that their combined negligence caused the damages alleged, they are joint tortfeasors. This decision contradicts an earlier California Supreme Court decision, *Aas v. Superior Court of San Diego*, 24 Cal. Rptr. 4th 627 (Cal. 2000). The Court in *Aas* held that a developer could not recover economic losses from a party when the developer and that party have not directly entered into an agreement. *Geocon* extended the duty owed by Geocon to Sunbow, finding that Geocon also owed a duty to TSI and Swanson and opening the door for economic loss recovery when there is not a direct contract between the parties.

In conclusion, while the court reaffirmed the enforceability of limitation of liability provisions, such provisions may not be used

against parties who are not privy to the agreement or for determining good faith settlements. The court suggested that an indemnity provision in which the owner indemnifies the design professional from any third-party claims in excess of the limitation of liability amount is valid. Keeping this decision in mind, design professionals negotiating agreements for projects in California should include an indemnity clause in limitation of liability provisions. An example of this type of clause is as follows:

"To the fullest extent permitted by law, the total liability in the aggregate, of Design Professional and Design Professional's officers, directors, employees, agents, and independent professional associates, and any of them, to Owner and any one claiming by, through or under Owner, for any and all injuries, claims, losses, expenses, or damages whatsoever arising out of in any way related to Design Professional's services, the project, or this Agreement, from any cause or causes whatsoever, including but not limited to, the negligence, errors, omissions, strict liability, breach of contract, misrepresentation, or breach of warranty of Design Professional or Design Professional's officers, directors, employees, agents or independent professional associates, or any of them, shall not exceed the total compensation received by Design Professional under this agreement. Owner further agrees to indemnify and save Design Professional harmless from any liabilities or claims for damages by any person or third party entity in excess of the monetary limit established above arising out of or in connection with any work or services performed by Design Professional for Owner."

In addition, cases involving the economic loss doctrine in California should be carefully reviewed. This case suggests that there are circumstances in which third parties may recover purely economic damages without a direct contract between the parties. ■

New Mexico Court Rules That Excess Insurance Carrier Must Defend A Design Professional Even Though The Primary Insurer's Policy Limits Had Not Yet Been Reached

By Julie A. Ciollo, Esq.

I**N DESIGN PROFESSIONALS INS. CO., INC. v. St. Paul Fire & Marine Ins. Co.**, 123 N.M. 398 (1997), the Court of Appeals of New Mexico held that an excess insurance carrier must defend a design professional even though the primary insurer's limits have not yet been reached.

The case arose when the City of Albuquerque contracted with Molzen-Corbin & Associates ("Molzen") to perform engineering, architectural and planning services in connection with construction at an airport. While Molzen conducted a "light-check" at one of the airports runways, the employee of another contractor was electrocuted and died from his injuries. The decedent's estate filed suit against Molzen and other parties.

Molzen carried insurance with both Design Professionals Insurance Co. ("Design Professionals") and St. Paul Fire & Marine Insurance Co. ("St. Paul") with coverage limits of \$1,000,000 and \$1,500,000 respectively. Both insurance companies and Molzen entered into settlement negotiations with the decedent's estate, with St. Paul contributing \$400,000 and Design Professionals contributing \$100,000. Of the \$100,000 that Design Professionals agreed to pay, Molzen paid approximately \$17,373.

After settlement with the decedent's estate, Molzen brought suit against St. Paul for its allegedly bad faith failure to indemnify Molzen for its contribution to the prior settlement. St. Paul and Molzen settled for \$17,373 plus the costs of Molzen's defense and Molzen signed a release, barring any future claims.

After the Molzen-St. Paul settlement, Design Professionals sued St. Paul for the approximately \$74,820 it had paid in settlement of the decedent's lawsuit. Design Professionals argued that since it was only an "excess" insurer, it was not obligated to pay any money towards settlement until St. Paul's policy limits had been reached.

The trial court granted summary judgment to St. Paul, agreeing with St. Paul that the release signed by Molzen precluded Design Professionals from bringing a suit against St. Paul and moreover, that Design Professionals was not an "excess" insurer. It also held that the only rights Design Professionals had against St. Paul were subrogation rights derived from standing in the shoes of Molzen. Thus, the release signed by Molzen would determine what rights Design Professionals possessed against St. Paul.

Design Professionals appealed the ruling to the Court of Appeals of New Mexico. It took issue with the language of the Molzen release, which stated that the release applied "solely with respect to the subject matter of the lawsuit referenced above." Design Professionals argued that the release was not a general one and applied only to the bad faith suit from Molzen. St. Paul countered that the release was for all claims, including claims related to the suit from the decedent's estate.

In upholding summary judgment for St. Paul, the Court determined that Design Professionals had failed to point out any error on the part of the trial court. The main challenge Design Professionals mounted was to dispute the definition of the term "lawsuit" in the release. Design Professionals argued that the term "lawsuit" was limited to the case between Molzen and St. Paul and thus left open a subsequent opportunity for Design Professionals to sue St. Paul. St. Paul contended that the release applied to the decedent's lawsuit, the term "lawsuit" encompassing all claims arising out of that action.

The Appeals Court pointed out that the uppercase "Lawsuit" as written in the release only arose when the release discussed the bad faith suit between Molzen and St. Paul. However, the release used a lowercase "lawsuit" when speaking beyond the Molzen-St. Paul matter. Thus, the generic "lawsuit" was used in reference to the claim filed by the decedent's estate, which gave rise to both St. Paul's and Design Professional's obligations.

Even if the trial court had agreed with Design Professional's interpretation of the term "lawsuit" in the release, Design Professional's claim would have still failed.

The Court also noted that the release stated that the parties would "put to rest all further controversy" and give a "general release of all claims between the parties." This, the Court added, indicated that Molzen never "intended to hold anything back.

Clearly, [Molzen] was giving St. Paul what it wanted – a complete release in exchange for remuneration." Design Professionals could offer no evidence to controvert such an intent and show that Molzen planned to limit its release. Thus, the trial court was justified in deciding that the release "was clear and unambiguous in meaning."

Design Professionals also argued that the trial court erred in not allowing it to depose Molzen's counsel to ascertain if it had a limited purpose in mind when signing the Molzen-St. Paul release. The Appeals Court upheld the trial court's ruling, noting that Design Professionals had the opportunity to examine documents and files that might have shown the intention of Molzen in signing the release. Also, the release negotiations had been subject to a confidentiality agreement and the trial court was reluctant to break the agreement

for Design Professionals, given that Design Professionals was not entitled to examine each and every piece of evidence that might possibly relate to its claim.

Even if the trial court had agreed with Design Professional's interpretation of the term "lawsuit" in the release, Design Professional's claim would have still failed. The trial court noted that Design Professionals had done nothing to reserve its rights during the settlement of the decedent's claim and contributed to the settlement without comment. Thus, the Appeals Court was hesitant to permit Design Professionals to subsequently claim that it should not have contributed to the settlement. It noted that other courts had "estopped [insurers] from asserting noncoverage where [they] had not raised the argument before a second insurer's settlement with [a] victim." Certainly, had St. Paul known of Design Professional's position, it would have approached settlement in a vastly different manner. Such a hypothetical strategy would undoubtedly have included a more deliberate and specific wording of the term "lawsuit."

Design Professionals v. St. Paul stands as a caution to secondary insurers to fully participate in settlement negotiations along with the primary insurer and to raise all concerns during such settlement. If no concerns or preservation of rights are raised, the secondary insurer is likely to be estopped from raising any arguments related to the settlement to which it previously gave its consent. This is especially true when a settlement releases the parties from future claims. In such a case, any party seeking reimbursement on a paid claim bears the burden of showing that no other party relied on its actions during the settlement negotiations. Such a burden is especially great when the complaining party contributed to the settlement. ■

Federal Claims Court Rules That Architect's Imperfect Plans Did Not Breach Duty or Contract

By Ben N. Dunlap, Esq.

ON APRIL 29, 2005, THE UNITED STATES COURT OF FEDERAL CLAIMS issued an important opinion defining the standard of care owed by a design professional in fulfilling the terms of a U.S. government contract. In *C.H. Guernsey & Co. v. United States*, 65 Fed. Cl. 582 (2005), the court determined that the architect did not breach its professional duty of care or the implied warranty under its contract simply because its design was costly or difficult to implement.

At issue in *Guernsey* were the design plans and specifications supplied by the architect, C.H. Guernsey, to the United States Army Corps of Engineers for the construction of a pre-engineered metal building at Fort Knox, Kentucky. The contract between the architect and the Corps provided that Guernsey would be liable to the government for damages caused by its negligent performance of any services under the contract.

Guernsey followed closely the requirements provided by the Corps, including stringent specifications for the amount of movement in the structure ("lateral deflection criteria") under certain wind and seismic conditions. A subcontractor selected to construct the building neglected to review the stringent criteria in the plan supplied by Guernsey and instead based its bid on values that were less expensive and easier to implement. The Corps later insisted on the more stringent values, and the subcontractor made its own modifications to the plans, which raised the cost of the project over the amount originally bid by the subcontractor.

The Corps ultimately sought to hold Guernsey responsible for the cost increase, alleging that the architect was negligent in submitting its design specifications and therefore had breached the contract. A Corps Contract Officer assessed Guernsey \$716,000 for its alleged breach. Guernsey filed a petition in the Federal Claims Court seeking declaratory relief, and the Corps counterclaimed, seeking damages for "negligent performance" of services under the contract.

The government argued that Guernsey was negligent in failing to design a building that could be constructed cheaply and easily using standard

methods of the pre-engineered metal building industry, and failing to ascertain that Guernsey's design, with stringent specifications, could be constructed in fact. Guernsey countered that its plans were, in fact, "buildable," and that the government had failed to establish that Guernsey had breached any duty of care owed.

The Court concluded that Guernsey was not negligent in using stringent criteria in its plans, since the "lateral deflection" values were a particular concern of the Corps and Guernsey was appropriately responding to that concern. The court also noted that the cost of using Guernsey's original design would not have exceeded the Corps' overall estimated contract price and that the architect's design had not caused unreasonable delay because Guernsey had proposed a suitable solution only twelve days after the potential design problem was discovered.

Further, Guernsey did not breach an implied warranty to provide design services free from defect. The issue here was whether the "lateral deflection" criteria were "design" or "performance" specifications. Architects are liable for any defect in design specifications because contractors must adhere to them without deviation or modification. In contrast, performance specifications set out objectives, leaving methods for obtaining them up to the contractor and, thus, do not incorporate an implied warranty.

The court determined that the "lateral deflection" values were a performance, not design, specification, because the subcontractor had discretion to decide how to accomplish them. Therefore, those criteria in Guernsey's plan did not impose an implied warranty to be free from defects.

Concluding that Guernsey had not breached the standard of care for a design professional, the court ruled that “there is a wide difference of opinion in the industry about the appropriate deflection criteria to use in constructing a metal building.” Thus, even though Guernsey’s plans incorporating stringent deflection values made the building more difficult to construct, they did not constitute a breach of the architect’s standard of care because that standard does not require that a design be “easy to implement.”

The court’s ruling demonstrates that a contractual obligation requiring non-negligent design services does not demand perfection. Where a contractor has discretion in implementing the plans supplied to it, the architect cannot be liable for a defect under a theory of implied warranty. Finally, significant differences in opinion about the efficacy of a design suggest that the architect has not breached the professional standard of care. ■

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The New Hampshire Supreme Court recognized the negligent misrepresentation exception in *Spherex, Inc. v. Alexander Grant & Co.*, 122 N.H. 898 (1982). In that case, the Court relied on Restatement (Second) of Torts § 552 and affirmed tort liability of an accounting firm for damages sustained by a third party creditor who relied on unaudited financial statements prepared by the accounting firm.

The Court later limited the application of Restatement (Second) of Torts § 552 in another accountant negligence case. In *Demetracopoulos v. Wilson*, 138 N.H. 371 (1994), the Court held that the defendant accountant was not liable to the plaintiff, who had been fired after the accountant submitted a report to his employer that the plaintiff had entered into an unauthorized employment contract. The Court reasoned that because the defendant accountant’s report “was not intended for the plaintiff’s ‘benefit and guidance’” and the plaintiff “did not rely or act upon the report,” the plaintiff could not support a negligent misrepresentation claim under Restatement (Second) of Torts § 552. *Demetracopoulos v. Wilson*, 138 N.H. 371 at 375.

The Court likened the instant case to *Demetracopoulos* and refused to apply the negligent misrepresentation exception. The Court pointed out that the Defendant had no communications with the Plaintiff regarding the Defendant’s gravel testing and that the Defendant provided its gravel test report to Keach, not the Plaintiff. The information contained in the Defendant’s report was not directly communicated to the Plaintiff and the Plaintiff only learned about the Defendant’s conclusions because the information was passed along by the other parties. Although Keach may have relied upon the Defendant’s report, the Plaintiff did not claim, nor could it claim, that it relied upon the Defendant’s report. Since the Plaintiff did not rely upon the Defendant’s information, the Plaintiff cannot maintain a claim for negligent misrepresentation.

The economic loss doctrine continues to be a complicated doctrine with varied exceptions. With this decision, the New Hampshire Supreme Court has taken another step to clarify the application of the doctrine to New Hampshire cases. ■

Federal Claims Court Ruling Suggests That A Plaintiff's Claims For Breach Of Contract Specifications And Differing Site Conditions May Be Combined

By Melissa S. Lee, Esq.

IN *ORLOSKY INC. V. UNITED STATES*, 64 Fed. Cl. 63 (2005), the United States Court of Federal Claims considered whether a plaintiff could maintain separate claims for damages based on differing site conditions and for breach of warranty of contract specifications, where the alleged defect in the specifications was the failure to disclose the differing site condition. Because the plaintiff asserted additional claims for defective specifications based on facts other than the differing site condition, the court denied the defendant's motion for summary judgment on this issue.

The case arose out of a contract awarded by the United States Department of the Navy (the "Navy") to the plaintiff ("Orlosky") for electrical work to be done at San Nicolas Island, Point Mugu Naval Air Weapons Station, in Point Mugu, California ("San Nicolas"). The contract concerned a coordination study of the electrical high voltage system of San Nicolas Island, as well as the replacement of fuses and the resetting of reclosers. Reclosers, similar to circuit breakers, are switches that may be shut off in the event of a short circuit. They may be either pole-mounted or installed at ground level on pads encased in tamper-proof structures.

The Navy's solicitation for contract bids informed prospective bidders that they were expected to conduct a site inspection prior to submitting a bid. Accordingly, the Navy conducted a site visit, which was attended by six bidders. Orlosky was not represented at the visit, but nevertheless bid for and was awarded the contract.

After receiving the award, Orlosky inspected the site and discovered that, contrary to the contract's specification for pole-mounted reclosers, the reclosers at San Nicolas were pole-mounted reclosers that had been installed in a pad-mounted position. This condition required welding and engineering work that Orlosky had not contemplated when submitting its bid.

Because the actual conditions with respect to the reclosers contemplated a scope of work that differed from that specified in the contract, Orlosky alleged that it was forced to incur delays and perform work in violation of OSHA safety requirements. Orlosky initiated suit, claiming breach of contract, equitable adjustment due to differing site conditions, equitable adjustment due to breach of implied warranty, equitable adjustment due to delays, and breach of covenant of good faith and fair dealing.

The Navy moved for summary judgment arguing, *inter alia*, that Orlosky should be prevented from asserting a separate claim for breach of warranty of contract specifications because the alleged defect in the specification was the failure to disclose the alleged differing site condition. The Navy relied upon the decision of the Federal Circuit Court of Appeals in *Comtrol, Inc. v. United States*, 294 F.3d 1357 (Fed. Cir. 2002) to support its argument.

In *Comtrol*, a contractor unexpectedly discovered quicksand at a construction site. The contractor claimed that the quicksand constituted both a differing site condition as well as a defect in the design specifications. The Federal Circuit held that because the alleged defect in the specification was the failure to disclose the alleged differing site condition, and because the two claims were inextricably intertwined, the claim would be treated as one, governed by the specific differing site conditions clause.

The Court in *Orlosky* distinguished *Comtrol* on the grounds that Orlosky asserted an additional claim that it was required to perform work in violation of safety regulations and manufacturer's warranties. The Court held that such a claim created a factual dispute that could not be resolved through summary judgment. Furthermore, the Navy's conduct in requiring such work could constitute a form of defective specification that Orlosky would not have been able to foresee even had it conducted a pre-bid site inspection. Accordingly, although the Court granted summary judgment in favor of the Navy on Orlosky's claims for differing site conditions and breach of warranty of specifications with respect to the conditions discoverable during the site inspection, it denied summary judgment insofar as the Navy may have created a defective specification by requiring Orlosky to perform work in violation of applicable safety ordinances.

The Federal Claims Court's decision in *Orlosky* suggests that if an alleged defect in contract specifications arises from an alleged differing site condition, a court may treat all allegations as a single claim, particularly if the claims are perceived as intertwined, and a separate basis for a claim of defective specifications does not exist. ■

Upcoming Design Professional Roundtables

September 12, 2007

Boston

"Mock Development Project Initiation Meeting for a Brownfield Development, Including Environmental and Political Implications"

September 19, 2007

New York

"10 Most Common Areas of Design Professional Exposure"

October 18, 2007

Boston

"BIM Professional Liability Issues"

October 25, 2007

New York

"Mergers & Acquisitions—An Overview of the Acquisition Process for a Private Company Transaction"

November 8, 2007

Boston

"The Design Professional's Risks During the Construction Phase"

November 28, 2007

New York

"BIM Professional Liability Issues"

More information will be posted on
www.donovanhatem.com. To register, please
e-mail roundtable@donovanhatem.com.

Immigration Impact On Employment Practices

By Gwen P. Weisberg, Esq.

IN LIGHT OF THE CURRENT IMMIGRATION CLIMATE, and the resulting increase in workplace audits, all employers should take the time to determine whether they are in compliance with all employee documentation requirements. Although often overlooked, immigration considerations may significantly affect a company's employment practices and, for those companies failing to take immigration seriously, the results can be devastating. These requirements are equally applicable to private individuals who may employ non-immigrant aliens to perform household maintenance and care services.

No employer may employ or continue to employ an alien who does not have proper documentation. Any employer who either hires, or fails to terminate, an alien who has not been "admitted" to the U.S. with proper immigration documents, violates the Immigration and Naturalization Act. 8 U.S.C. §§1324a. Nor may an employer discriminate against an alien. 8 U.S.C. §1324b. The employer is subject to civil and criminal penalties which may include monetary fines, debarment from federal contracts, limitations on its ability to hire aliens in the future and, in cases where a pattern or practice of conduct is demonstrated, imprisonment.

Employment Verification Guidelines

Form I-9

Within 3 days of the hire of any employee—U.S. citizen, Lawful Permanent Resident ("LPR") or non-immigrant alien—the employer and employee must complete an I-9 form issued by the United States Citizenship & Immigration Services ("USCIS"). This form verifies an employee's citizenship and authorization to work lawfully in the United States. Although there are a few exceptions to the I-9 requirement, they pertain only to persons who have been continuously employed beginning prior to November 6, 1986, and must be analyzed on a case-by-case basis. In all other instances, the employer must undertake the following steps to document the hire of a new employee:

- Obtain photocopies of documents listed on the back of the I-9 form.

The back of the I-9 form contains 3 columns of documents; Column A lists those documents that verify both citizenship and the ability to work; Column B documents verify citizenship; and Column C documents verify authorization to work. An employee may produce one item from column A, or one each from columns B and C. Retain all photocopies in the employee's I-9 file. Please note that column A still contains certain documents not acceptable to the USCIS. Employers should consult their attorneys.

- Fully complete the I-9 form and maintain it in a file separate from the employee's personnel file.

Following completion of the I-9 form, calendar the expiration date of the employee's verification documents and, when approaching that date, communicate with the employee to ensure that the documents, with the exception of the permanent resident card, are timely renewed. The employee may provide the employer with a receipt demonstrating that he has timely filed an application to renew the document, but the document must be produced within the time allowed by USCIS or the employee may lose his right to work and to remain in the U.S. If the employee continues to work without renewing the documents, the employer is subject to monetary, administrative, and/or criminal penalties.

It is prudent to periodically conduct an "I-9 audit" to verify valid and up to date documentation for each employee. It is also advisable to perform this audit whenever there is a change in ownership of

a business because, under certain circumstances, the new owner may have to file a new petition with the USCIS for authorization to continue to employ the foreign national workers.

Guidelines for H-1B Non-Immigrant Visa Holders

Termination of Employment

If an employer has sponsored an alien's application for an H-1B non-immigrant visa, that employer must immediately notify the USCIS, in writing, if the employee's employment terminates prior to the expiration of the terms of the alien's visa. In fact, the USCIS must be notified in writing if there are any changes in the terms and condition of the alien's employment that might affect his eligibility for the non-immigrant visa. 8 C.F.R. §214.2(h)(11). If the changes in employment are significant, the employer will likely have to file a new Labor Certification Application with the Department of Labor, and an amended H-1B petition with the USCIS. Unless the alien has lawfully transferred his H-1B visa to a new employer, the former employer must immediately notify the USCIS of the termination of an alien's employment to avoid liability for payment of the alien's wages for the duration of the visa term while the alien remains in the United States.

Pursuant to 8 C.F.R. §214.2(h)(4)(iii)(E), an employer who dismisses an employee prior to the end of the duration of the visa must pay the reasonable costs of return transportation of the alien to his last place of foreign residence. If alien has not been dismissed but voluntarily terminates his employment prior to the expiration of the validity of the visa, payment of transportation costs is not required.

Transfer to Another Employer

As of October 2001, an alien whose H-1B non-immigrant visa has been sponsored by one employer may change employers with relative ease. Prior to that date, the alien could not begin his new employment until the USCIS had approved his new employer's H-1B visa petition. Although the new employer must still submit a new Labor Condition Application to the Department of Labor (ETA 9035) and an H-1B visa petition to the USCIS (I-129), and comply with all posting and public access file requirements, the employee may begin to work after the employer files the petition and receives a receipt from the USCIS, but before the petition has been approved by the USCIS.

Although it may be inconvenient to alter employment practices to accommodate immigration requirements, failing to do so may have a significant adverse impact upon one's business. If in doubt as to whether your business is in compliance with current immigration requirements, please consult your attorney. ■

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