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"Defending the Stimulus Project": Application Of The Spearin Doctrine To Stimulus Package Funded Construction Projects

by Timothy Liam Epstein, Benjamin C. Heinz, and Justin B. Lamb

On February 15, 2009, Congress approved the American Recovery and Reinvestment Act, commonly known as the "stimulus package." Among other things, this package will infuse much needed funds into the construction industry. As a result, the number of government contracts with construction companies will vastly increase in a short amount of time. Therefore, contractors must be aware of the risks associated with government contracts and the means to protect themselves from the same.

The stimulus package calls for $787 billion in spending and tax cuts nationally. The package is a compromise between the White House and Congress that creates "more jobs than the original Senate bill and costs less than the original House bill," says Senate Majority Leader Harry Reid. According to President Barack Obama, this package will create jobs particularly in the construction industry:

> Not just any jobs, but jobs doing the work America needs done: repairing our infrastructure, modernizing our schools and hospitals, and promoting the clean, alternative energy sources that will help us finally declare independence from foreign oil.

Congress earmarked a large portion of the stimulus money to benefit the construction sector. While still President Elect, Obama asked mayors and governors across the United States to suggest "shovel-ready" public projects. These public projects can begin in 90 to 120 days after the signing of the stimulus bill. As a result, the mayors and governors suggested 427 projects, costing a total of $73 billion and potentially creating 850,000 jobs by 2010.

In total, the stimulus package provides $134.8 billion for construction-related projects. $49.3 billion will benefit transportation infrastructure, including $27.5 billion going to highway and bridge construction. $21.3 billion will benefit water and environmental infrastructure, including clean water infrastructure and environmental cleanup programs. $29.5 billion will go towards building infrastructure, including government facilities, school construction, and public housing. $4.7 billion will go towards workforce development, with the majority for creating training and employment services. Lastly, $29.8 billion will benefit energy and technology, including diesel emissions reduction, electricity grids, and state and local government energy grants. Due to the wide variety of sectors set to receive a sharp influx in funds, it is likely that

any area of the construction industry will experience an increase in government contracts.

The construction industry is in particular need of this stimulus package. While the national employment rate is 7.6%, the employment rate in construction overall is 18.2%. In the past two years, the civil engineering sector alone lost 52,000 jobs. Additionally, investment in infrastructure will help state budgetary problems. Michael Bird, federal affairs counsel for the National Conference of State Legislators says, “infrastructure, which is designed to create jobs, can help states balance their budgets by increasing tax revenues and purchasing construction supplies.”

The stimulus package will play a vital role in the revival of the construction industry. Its effects will extend far beyond the immediate future, both in the construction industry and other sectors. The increase in construction projects expected to occur in the next couple of years will consequently lead to an increase in government contracts. As such, it is imperative to anticipate the legal consequences of these specific types of contracts. One legal issue that may arise from this increase involves the application of the *Spearin* doctrine to stimulus-related construction projects. Whether or not the *Spearin* doctrine will be available to a private construction company contracting with the state or federal government afforded stimulus money is an important question needing attention from the very beginning of a project.

In 1918, the United States Supreme Court released its decision in *United States v. Spearin*, 248 U.S. 132, 39 S.Ct. 59, wherein it addressed the issue of implied warranties created by plans and specifications. In *Spearin*, the plaintiff contracted with the United States government to construct a dry dock at the Brooklyn Navy Yard, including the relocation of a section of sewer. *Id.* at 133. The contract required that the plaintiff relocate the sewer section in accordance with the plans and specifications prepared by the government. *Id.* After the sewer had been relocated and during the continued construction of the dry dock, the sewer overflowed and flooded the work site. *Id.* at 134. It was determined that a dam existed within a portion of the sewer not worked on by the plaintiff and that such dam caused the flooding. *Id.* Neither the city nor the government’s plans showed this condition. *Id.* Following this event, the plaintiff informed the government that he would not complete his work on the dry dock until the sewer had been fixed. *Id.* at 135. The government annulled the plaintiff’s contract and proceeded to have the project completed, under significantly different plans and specifications, by different contractors. *Id.* As a result, the plaintiff filed suit for damages, including lost profits and a balance due on the work he had performed. *Id.* The Federal Court of Claims found for the plaintiff and awarded damages. *Id.* at 133.

On appeal, the Supreme Court specifically noted that a contractor is not responsible for the consequences of defects in plans and specifications prepared by the owner when the contractor is bound to perform pursuant to such plans and specifications. *Id.* at 136 (citations omitted). As such, the Court found that by prescribing the exact dimensions and location of the sewer, the government created an implied warranty that if the plaintiff built the sewer in accordance with the plans and specifications, then the sewer would be adequate. *Id.* at 137. The Court further found that this implied warranty was not overcome by standard contract clauses regarding a contractor's duty to inspect the work site, check the plans, and assume responsibility for the work until completion. *Id.* The Court then upheld the trial court's decision and found that the plaintiff was not responsible for restoring the sewer and did have the right to recover damages resulting from the government's subsequent annulment of the plaintiff's contract. *Id.* at 138.

One key aspect of the application of the *Spearin* doctrine is the difference between "design" and "performance" specifications. In *Stuyvesant Dredging Company v. United States*, this difference was explained as follows:

> Design specifications explicitly state how the contract is to be performed and permit no deviations. Performance specifications, on the other hand, specify the results to be obtained, and leave it to the contractor to determine how to achieve those results.

834 F.2d 1576, 1582 (Fed. Cir. 1987). While the *Spearin* doctrine applies to design specifications, there is no warranty for the adequacy of performance specifications. *Id.* But, it should be noted that a single contract can contain both design and performance specifications. *Blake Const. Co., Inc. v. United States*, 987 F.2d 743, 746 (Fed. Cir. 1993).

Given these judicial determinations, success under the *Spearin* doctrine requires more than just a mere error in the design specifications. First, the design specifications do not have to be perfect. *Caddell Const. Co., Inc. v. United States*, 78 Fed. Cl. 406, 413 (2007). As long as the specifications are "reasonably accurate", there is no breach of the implied warranty. *Id.* Furthermore, a contractor's general duty of checking the plans and specifications still applies and prevents the contractor from relying on the implied warranty when the design specification is "patently" ambiguous, inconsistent, or wrong. *Id.* Likewise, the implied warranty is not breached when the plans and specifications, though containing errors, are nevertheless "workable" by way of slight modifications. *Id.* at 416.

Thus, the *Spearin* doctrine remains a useful tool for contractors involved with government construction projects. However, as noted above, in order for the *Spearin* doctrine to apply, the errors or inconsistencies complained of in the plans and specifications must be ones that the contractor had no option but to perform in accordance with them and must be of such significance that the only way to successfully complete the project is through a major revision of the plans and specifications.

The *Spearin* doctrine presents an issue for contractors that should be addressed before the project begins. For stimulus-related projects, contractors should make certain that the government tenders specific design specifications at the very beginning of the project. Without design specifications, a contractor cannot file suit under the *Spearin* doctrine. Furthermore, contractors should carefully check the plans and specifications given by the government because the general duty to do so still exists. The contractor would not be able to recover under the *Spearin* doctrine if the design specification was "patently" ambiguous, inconsistent, or wrong, and the contractor did not check the plans beforehand. Following this protocol, a contractor can ensure that errors by the government for stimulus-related projects will not cause an issue later on when construction begins.

The *Spearin* doctrine provokes an additional concern for contractors seeking stimulus related projects. The federal government's dispersal of funds presents the issue of whether a contractor can file third-party lawsuits against the federal government for stimulus projects. It is important to know the signatories to a government contract to determine whether a contractor can invoke the *Spearin* doctrine against the federal government or against the state government.

At this point, states are still unsure of how the federal government will allocate the stimulus funds. As currently drafted, the stimulus distribution will be based upon the existing statutory formula, allocating the majority of funding to the states. Then, the states will reallocate the funds to project sponsors. The government will give priority to "shovel-ready" projects. To qualify for funds, the state financing authorities must award twenty-five percent of the money to contractors within ninety days. Ultimately, fifty percent needs to be spent by 2009, and the remaining fifty percent needs to be spent within two years. Congress already earmarked most of the states' fund money to certain sectors to ensure that the "money will be spent on projects that can create the most jobs," says Kelvin Atkinson of Nevada, D-North Las Vegas.

Who receives the stimulus funds will determine whether a construction contract is made with the state government or the federal government. For instance, Congress will give some of the funds to federal agencies, such as the $9.2 billion given to the Department of the Interior and the Environmental Protection Agency to use for energy projects. In these cases, the federal government would be a signatory to any contract with a construction company. In instances where states receive funding from the federal government and use it for their own projects, especially "shovel-ready" projects that the state already negotiated, the individual state would be the signatory to the contract.

Who signs the contract is especially important when applying the *Spearin* Doctrine. In *United States v. Spearin*, 248 U.S. 132 (1918), the Supreme Court held that "if the contractor is bound to build according to plans and specifications prepared by the owner, the contractor will not be responsible for the consequences of defects in the plans and specifications." Thus, there is an implied warranty in a contract that the plans the owner gives to a contractor are both accurate and suitable for their intended use. The *owner* is liable to the contractor if the contractor cannot finish a project due to inaccurate or unsuit

For contracts as a result of the stimulus, whether the *Spearin* Doctrine applies depends on whether the state or the federal government commissions the project. Mutual intent to contract is necessary for an implied in fact contract. *Rick's Mushroom Service, Inc. v. United States*, 521 F.3d 1338. If a state signed a contract that the federal government funded with stimulus money, only the state could have an implied warranty under *Spearin.* It would be difficult to attach the United States government to a contract for which it only appropriated funds because it does not have the mutual intent necessary for a contract. However, if the contract is signed with a federal agency, such as when the EPA commissions the project, the United States government would sign the contract. Therefore, an implied warranty could exist under the *Spearin* Doctrine, allowing the contractor to sue the United States for inaccurate or unsuitable plans. In sum, the *Spearin* Doctrine assigns liability to the *owner* of the property who signed the contract, and not just the government entity who indirectly appropriated the funding.

In 1988, the Supreme Court expanded *Spearin* in *Boyle v. United Technologies Corp.*, 487 U.S. 500 (1988). In *Boyle*, the Court firmly established that government contractors could seek derivative immunity from suits by third parties arising out of the performance of their contracts (i.e. "the Government Contractor Defense"). The Government Contractor Defense is grounded in the federal government's immunity from suit for the performance of discretionary functions as codified in the Federal Tort Claims Act, 28 U.S.C. § 2680(a) (2006) (hereinafter "FTCA").

Boyle involved a suit against the manufacturer of a military helicopter by the father of a pilot killed when unable to escape a crashed helicopter due to a design flaw in the escape hatch. The Court reasoned that the selection of appropriate designs for military equipment was clearly a discretionary function. Furthermore, allowing second-guessing of such designs would ultimately result in exactly the type of financial burden on the government which the discretionary function exception in the FTCA was intended to prevent. Essentially, the Court feared the liability of contractors would be passed on to the government in the form of increased contract prices or even the inability to obtain contracts with quality contractors. *Id.* at 507.

Boyle established three prerequisites for application of the government contractor defense: (1) the government must have approved reasonably precise specifications; (2) the equipment must conform to those specifications; and (3) the supplier must have warned the government of any dangers associated with the equipment known to the supplier, but not the government. *Id.* at 512.

Since the Court's decision in *Boyle*, lower federal courts have been divided concerning whether the Defense should be expanded outside the realm of military procurement contracts and products liability suits, to apply to nonmilitary contractors or to service contracts. Although some Circuits have been reluctant to expand the *Boyle* holding, many have applied the Government Contractor Defense in non-military and service contexts. For instance, the Defense has been applied to contractors participating in environmental cleanup efforts after hurricanes (*Richard Lexington Airport District v. Atlas Properties*, 854 F. Supp. 400 (D.S.C. 1994); *Weggeman v. AshBritt, Inc.*, 2007 U.S. Dist. Lexis 49197). Therefore, although the scope and applicability of the Government Contractor Defense varies by jurisdiction, it should certainly be a consideration for any attorney defending construction cases arising out of government work.

Some Practical Considerations for Contractors and Attorneys:

One weak point plaintiffs consistently, and often successfully, attack is the degree of government participation in the design process and the intensity of the government's oversight of the contractor's work. The Defense will not apply if the government has merely rubber-stamped the contractor's design or actions, although the *Boyle* opinion and subsequent decisions have clearly stated contractor involvement in the design process does not negate the application of the Defense. The rationale is that, without government participation, oversight, and substantial review, there is insufficient exercise of government discretion to bring the work under the exception to the FTCA. Thus, careful documentation of government collaboration in the design process and

oversight during the project is essential and should be considered when preparing contract documents and while the work is proceeding.

Additionally, the government contractor is well advised to carefully follow the scope of work and specifications contained in the contract documents. Independent deviations from the contract specifications, whether purposeful or negligent, can also leave the contractor out in the cold. Again, such deviations from government approved plans and activities negate the necessary government collaboration and oversight to trigger the governmental discretionary function.

CONCLUSION

In light of the recent passing of the American Recovery and Reinvestment Act ("the Stimulus Act"), contractors should be mindful of the various applications of the *Spearin* doctrine and the Government Contractor Defense. A careful review of the viability of the defenses in your jurisdiction, combined with careful drafting of contract documents and documentation of the government's participation and oversight on your "stimulus-funded" project, could lay the groundwork for a powerful defense for your clients participating in stimulus-related government work should liability arise.

This issue of The Critical Path has been edited by the Construction Defect Specialized Litigation Group of the Construction Law Committee. If you would like to join this SLG, please contact Kathy Davis at krdavis@carallison.com

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