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Cover Page Footnote

The author has been a practicing architect for the past fifteen years.

A CASE FOR FAIRNESS IN PUBLIC WORKS CONTRACTING

*Gene Ming Lee**

INTRODUCTION

Public works¹ provide the infrastructure that enables our country to prosper and grow. Billions of tax dollars are spent each year by our federal, state, and municipal governments on roads, bridges, buildings, and utilities. These expenditures comprise a major sector of the construction industry.² Like private developers, government entities hire private businesses to provide the labor, materials, and services required to produce complex construction projects. Procurement of public works involves a conscious effort by contracting officials to assure that the taxpayer's interests are being looked after. Although taxpayers do not expect those who do business with the government to work for free, there is an expectation that business will be undertaken fairly.

Unlike the private sector, the actions of governmental agencies are subject to public scrutiny.³ Billions of dollars in tax revenue are at stake and the public demands assurances that its money is being spent reasonably. Assuming that funds are properly allocated to necessary projects, the remaining public interest lies in the award process and the construction process. Government agents who award contracts should not personally benefit from the award process; contractors who bid on contracts must do so without collusion; and, those who are awarded contracts must perform as promised. These criteria embody the most obvious aspects of procurement fairness.

Fairness in public works construction implicates other concerns that, although less headline worthy, are nonetheless vital to maintaining the integrity of the bidding process.⁴ Construction is a complex undertaking in which participants must deal with a multitude of unknowns. It is a process that involves the evolution of an idea to a

* The author has been a practicing architect for the past fifteen years.

1. For the purposes of this Note, "public works" are construction projects initiated and financed by government.

2. In 1994, \$129.1 billion was spent on government construction, accounting for more than 25% of the \$500 billion spent on construction overall. U.S. Department of Commerce, *Statistical Abstract of the United States 1995*, 725 (1995). From 1990 to 1992, the construction industry accounted for 4% of the Gross Domestic Product of the United States. *Id.* at 452.

3. Public scrutiny of government procurement has been intensified following a number of scandals involving corruption. New York City and New York State responded to this problem by appointing the New York State Commission on Government Integrity to look into ways of improving laws to prevent corruption, favoritism, and abuse. John D. Feerick, *Reflections on Chairing the Commission on Government Integrity*, in *Government Ethics Reform for the 1990s* 1 (Bruce A. Green ed., 1991) [hereinafter *Ethics Reform*].

4. Among these concerns is the ability to attract bids. *Id.* at 470-71.

graphical and written representation, which then must be ultimately transformed into to a physical reality.⁵ At various points along the way, theory may collide with reality, resulting in conflict.⁶ How these conflicts are handled is crucial to the timing and cost of construction. It immediately affects the allocation of costs between the parties. In the long term, how fairly this is done may affect the number of willing participants in the process. Federal, state, and municipal governmental agencies that contract for construction create their own rules for dealing with these conflicts.⁷ This Note examines these rules, discusses their inequities, and makes the case for reform.

Part I discusses the general process of construction, presenting an overview of its component parts from design to documentation, from bidding to award, and through the act of construction itself. Part II focuses on the special case of public works construction. This part discusses how and why public works differs from private construction. Part III looks at dispute resolution and how different governmental entities have addressed this issue. This part also discusses the shortcomings of these models in achieving fairness. Finally, part IV proposes changes in the way public works are bid in order to minimize potential disputes and the way that actual disputes between the parties are settled in an attempt to be fair. The proposed changes will ultimately create a contracting system that will encourage participation and increase competition.

I. THE PROCESS OF CONSTRUCTION

Building is an inherently complex process that involves directing the efforts of many people to create a given result. Conceptually, it may be divided into two major phases: design and construction.⁸ The design phase includes planning, preparation, and definition of the work to be executed during the construction phase. At the juncture between the design and construction is the process of bidding and award. In order to understand the particular problems of public works contracting, it is useful to first gain a general understanding of these phases of construction.

This part looks at the overall considerations that must be addressed through the phases of a project, using the terminology and definitions embodied in the standard form contract documents of the American Institute of Architects ("AIA").⁹ These documents, taken as a whole,

5. See *infra* part I.B (discussing the design of a project). In the design phase, the architect and engineer prepare construction drawings and written specifications that serve as the basis of a contractor's bid.

6. See *infra* part I.D (discussing problems that arise during construction).

7. See *infra* part III.

8. See Edmond Pachner, *Architectural Contract Administration* 3-4 (1992).

9. Many construction contracts are based on standard form contracts prepared by the AIA. The AIA is an organization that focuses on issues related to the architect-

essentially embody the working relationships within the construction industry. This section then chronologically discusses the phases of a project, from design, to the selection of a contractor, and through the actual construction process. This discussion demonstrates how decisions made in the preliminary phases of design affect the construction.

A. *Balancing Priorities—Money, Time, and Quality*

In any construction project, many variables must be balanced. There is the hard dollar cost for the bricks and mortar; there is the time it takes to achieve a particular result; and there is the value or quality associated with the final product. These are often competing interests. A low construction cost may come at the sacrifice of quality. Accelerating a schedule may result in an earlier completion, but at a higher cost or lower quality. Seeking better quality may mean a longer construction time and a higher cost. All construction projects must contend with these conflicting interests.

1. Money Priorities

Dollar costs are obviously a major factor in construction. A client may have a limited budget, and be unable to proceed if it is exceeded. Accordingly, the project budget and the manner in which it is allocated will affect many aspects of the project. For example, the fee paid to the architect may affect the quality of the documents that will be used to solicit bids from contractors. Presumably, an architect paid a low fee¹⁰ will only invest limited hours on the design and documentation of the project, a fact that may result in an inferior work prod-

tural profession and whose members are registered architects. Standard contracts have been drafted by the AIA since 1888, when it prepared a "Uniform Contract" in conjunction with the National Association of Builders. The first edition of the AIA's standard documents was prepared in 1911. Since then, the AIA has periodically updated the standard documents. For example, AIA Document B141, Standard Form of Agreement Between Owner and Architect (14th ed. 1987) is in its fourteenth edition. For a discussion of the early history of the AIA standard documents, see William S. Parker & Faneuil Adams, *The A.I.A. Standard Contract Forms and the Law* 135-36 (1954).

AIA contracts embody the written agreements between the owner and architect, architect and subconsultants, and owner and contractor. In addition, construction typically incorporate related documents such as the drawings, specifications, general conditions (describing the relationship between the parties and their responsibilities), supplementary general conditions (amending the general conditions to the specifics of the project), and addenda (modifications issued subsequent to issuing the basic contract documents, but prior to the bid itself). Keith Collier, *Construction Contracts* 9 (2d ed. 1987).

10. According to two recent studies by the Professional Services Management Journal, 92% of architects said that price competition is growing. At the same time, the cost of running an office is increasing. *Architects in an Economic Vise*, *Progressive Architecture*, June 1995, at 50.

uct.¹¹ If the project documents are poor, the contractor's bid may not reflect the true cost of the project because there will be unforeseen changes or additions to the project's scope. Unlike the bid of a project, a modification made after the award of a contract cannot be competitively bid.¹² Contractual modifications, commonly referred to as change orders,¹³ are likely to lead to increases in cost, as well as to disagreements between the owner and contractor. Therefore, low fees paid up front to the architect may lead to higher costs through later change orders.

Further, the need to limit costs may influence an owner's approach towards the construction process. If there is a hard budget for a project, an owner must find ways to lock-in costs and minimize the risk of cost overruns. The owner may employ several methods to avoid the risk of increasing costs. A single contract can be made with an entity for the complete design and construction of a project with a design-build team.¹⁴ Alternatively, an owner may agree to freeze the costs of a project by obtaining a guaranteed maximum price from a contractor even before the design documents have been fully completed.¹⁵ Also, a construction contract may be written to require a contractor to assume the risk of uncertain conditions.¹⁶ In each of these scenarios, the owner can maintain a specific project cost, but inevitably sacrifices some control over the quality of the final product.

11. Robert A. Rubin, *Scope-of-Work Disputes*, in *Construction Litigation* 205 (Kenneth M. Cushman et al. eds., 2d ed. 1993) (noting that a failure to invest adequate time and resources results in poor drawings).

12. See *infra* part I.D.

13. A change order is a written agreement that is prepared by the architect and signed by the architect, owner, and contractor modifying the work of the contract, contract sum, and/or the time of performance. AIA Document A201, General Conditions of the Contract for Construction, ¶ 7.2.1 (14th ed. 1987) [hereinafter AIA Doc. A201].

14. A builder may also provide a lump sum price for the design and construction of a project under a design-build model. In such a scenario, the architect works for the contractor rather than the owner. The use of design-build in public works, however, is restricted. Only 27 states have statutes which expressly permit design-build in public works. See William G. Krizan, *Design-Build Faces Legal Hurdle*, *Engineering News-Record*, Aug. 12, 1996, at 17.

15. A guaranteed maximum price agreement is made between an owner and construction manager, who in turn contracts with the individual building trades. The construction manager agrees to the price when the drawings are only sixty percent to eighty percent complete. Andrew M. Civitello, Jr., *Contractor's Guide to Change Orders* 14-15 (1987).

16. From a contractor's point of view, the assumption of risk should be offset by the potential for profit. Keith Collier, *Estimating Construction Costs: A Conceptual Approach* 34 (1984).

2. Time Priorities

Time is an important factor in all phases of a construction project.¹⁷ The longer it takes to produce a project, the longer the construction need remains unfulfilled. Accordingly, competitors working on similar projects will race to be the first on the market to satisfy demand and slower firms will lose out. Additionally, delays mean that income with which the project is to be financed does not flow in. Thus, the viability of a project may depend upon its swift completion.

The time focus exists at every phase of a project. Maintaining schedules to keep the project on track can lead to errors that are costly at later stages. For example, hastily made decisions during the design phase may result in costly changes later during construction. Design documents which are rushed to meet a deadline can be fraught with errors in coordination or ambiguity, making it more difficult for a contractor to obtain a reliable bid.¹⁸ In extreme cases, an owner may seek to reduce development time by choosing to commence construction of a foundation before the building design is completed.¹⁹

When a project falls behind schedule, the owner must contend with the consequences of delays. Delays in one area of construction may impact on the schedule of other areas. This, in turn, may affect the amount of labor required for a task, as well as the cost of labor and materials. A delay may impact costs²⁰ and the ultimate completion date of a project.²¹ Who bears these added costs will depend upon who caused the delay and how the construction contract assigns the risk of such delay.²²

17. See AIA Doc. A201, *supra* note 13, art. 8 (discussing rules regarding timeliness of project progress and completion, as well as obtaining an extension thereof). The key dates specified in a construction contract are the date of commencement of the Work and the date of Substantial Completion of the Work. The latter is certified by the architect based solely on her determination. It is particularly critical because it is a condition precedent for the owner's release of retainage; money contractually held back from the contractor to ensure that the work will be completed. *Id.* ¶ 9.8; see also Frank R. Dagostino, *Estimating in Building Construction* 156 (3d ed. 1989).

18. See *supra* note 11 and accompanying text.

19. Accelerated and overlapping construction phases are used in "fast track" construction. Robert Allan Class et al., *Current Techniques in Architectural Practice* 19 (1970). It is particularly popular in times of high inflation. *Id.* at 21-22.

20. As a result of delays caused by the owner, a contractor is likely to file a claim for damages. See Justin Sweet, *Legal Aspects of Architecture, Engineering, and the Construction Process* § 30.10, at 692-94 (3d ed. 1985).

21. A contractor may also seek an extension in time as a result of an owner-caused delay. *Id.* at 692.

22. An owner may seek to eliminate damages or limit the remedy for an owner-caused delay to an extension of time through the use of a no-damage clause. *Id.* at 692-94.

For a discussion of other risks assigned to the contractor, see *infra* part II.C.2.

3. Quality Priorities

Quality on a construction project can mean many things. Some aspects of quality are outwardly visible. On a building project, for example, quality may reflect the distinctiveness of a design or how successful the building meets the client's needs. Other aspects of quality, such as a building system's long-term durability, are hidden. The type and importance of quality will vary from project to project. For example, the design for a warehouse in an industrial area of town may require inexpensive materials that can be erected quickly and efficiently. In contrast, however, a new courthouse, important to the revitalization of the downtown area, will dictate a look and feel of permanence that comes from a particular design imagery requiring heavy building materials.

Where specific attributes are important, the design documents must spell them out in great detail.²³ A building housing a high-tech supercomputer will require precise electrical and mechanical systems in order to insure an environment in which computers can reliably function. On the other hand, it may not matter in a minor demolition project whether the work is done by explosives or by physical labor, just as long as the result is achieved at minimal cost. There may be many ways to do a job and the specifics must be communicated between the designer and contractor.

Trade-offs between these variables are inevitable and may shift through the course of a project because the construction process is a dynamic one with constantly changing parameters. To the extent possible, however, these trade-offs must be made from the start, because the further a project progresses, the more complex the changes become and the more difficult with which they are to deal.

B. *The Design Phase*

A project begins when an owner defines a construction need and hires an architect.²⁴ The architect acts as the representative of the owner in dealing with governmental regulators such as building departments, zoning commissions, and the like. The relationship is typically contractual, spelling out the terms of engagement, including fees, retainers, and responsibilities.²⁵ As the leader of the design phase, the

23. An owner, for example, may specify that the pipe used in a building be of a particular manufacture. Such was the scenario in the famous case of *Jacobs & Youngs, Inc. v. Kent*, 129 N.E. 889 (N.Y. 1921), authored by Judge Cardozo.

24. The practice of architecture and the practice of engineering are licensed at the state level. See Sweet, *supra* note 20, §§ 13.01-13.08, at 204-31.

25. The typical owner-architect agreement is embodied by AIA Document B141, Standard Form of Agreement Between Owner and Architect (14th ed. 1987) [hereinafter AIA Doc. B141].

architect will assemble a design team.²⁶ This team will include engineers and other professionals that will program, plan, and design a building. In most cases, the architect will have a contract with the owner and the other professionals will be subconsultants paid through the architect. Professional fees are typically set prior to the start of work and most often established as a lump sum.²⁷

Design is a highly collaborative effort that involves a team of specialists representing many disciplines.²⁸ Under the overall direction of the architect, the design team will review client needs, applicable codes, and other restrictions in order to achieve a design that meets the client's objectives. Multiple phases of study take the design through increasing levels of specificity, each stage building upon the basic decisions made during the preceding phase.²⁹ It is a process that looks at problems on a general level and gradually reduces them to the specific. All of this happens against a backdrop of a schedule and a budget.³⁰

The architect's basic services are broken down into different phases. In the Schematic Design, the architect takes a functional space pro-

26. Although this Note focuses on the traditional model of construction, there are many present day variations. For example, an owner may hire a construction manager even before the start of construction in order to make use of particular construction expertise during the design process. See AIA Document B801/CMA, Standard Form of Agreement Between Owner and Construction Manager (1992). The construction manager will review the program, prepare project schedules, prepare cost estimates, and assist in the administration of the construction contract. *Id.* arts. 2-3. Although the use of construction managers is now common for large construction projects, it does not substantially change the owner-architect and owner-contractor relationships, as the owner will typically retain privity of contract with these parties. See Dagostino, *supra* note 17, at 46. Therefore, this Note will not further mention construction managers. See also *supra* note 14 and accompanying text (discussing design-build).

27. According to a Professional Services Management Journal survey on design fees, the most popular type of fee for architectural services is lump sum. Lump sum fees comprise 40% of contracts. *Fees Improved; Fee Bidding Down*, Architectural Record, May 1996, at 33.

Under the standard AIA contract, fees are broken down into Basic Services, Additional Services and Reimbursable Expenses. Basic Services are usually fixed at a stipulated sum. Additional Services may be provided at a lump sum or timecard basis. Reimbursable Expenses are provided at a multiple of cost. AIA Doc. B141, *supra* note 25, art. 11 (Basis of Compensation).

In a novel approach to professional compensation, one design-build team recently tied part of its compensation to the satisfaction of the building's users. See William G. Krizan, *A Lab Cooks Up New Incentives*, Engineering News-Record, Aug. 19, 1996 at 14.

28. Design of a building of any size takes the efforts of dozens of architects and engineers. Pachner, *supra* note 8, at 3. Adding hundreds of construction workers and millions of construction items makes for the inevitability of errors and omissions by the architect and engineer. *Id.*

29. See AIA Doc. B141, *supra* note 25, art. 2.

30. See *supra* part I.A.

gram³¹ and considers alternative approaches to the project's design.³² Working with the client, the architect will evaluate the alternatives and select a direction for further development. The architect fixes and describes building systems and materials used in the project during Design Development.³³

The design phase culminates in the production of construction documents, which contain the drawings and specifications that detail the particulars of the project's construction.³⁴ Specific construction methods and materials will be spelled out in carefully drafted, scale drawings and detailed specifications. These design documents may not spell out every single condition found within a building, but they are meant to describe to another party the designer's intent.³⁵ The documents spell out specific sizes, conditions, products, and construction methods in order to establish the design as well as the level of quality ultimately achieved. In many areas, the specifics of the design must be completed by the contractor's fabricator and a shop drawing prepared for review by the architect in order to establish compliance with intent of the design.³⁶

C. *Bidding and Award*

The objective of the Bidding or Negotiation phase³⁷ is to hire a responsible contractor to lead the construction phase of the project for a reasonable price. During this phase, the architect assists the owner in obtaining bids and awarding the construction contract. The contractor must review the design documents in order to establish his bid. To facilitate the creation of bids, copies of the design documents and documents describing the working relationship of the parties are furnished for the review of prospective contractors.

31. A space program is a listing of the rooms or functional elements required and their sizes. While the space program may be generated by the owner, a program will often be developed by the architect before the start of design of the project through discussions with the owner. See Bryce Hastings, *Project Programming, in New Directions in Architectural and Engineering Practice* 211 (Howard G. Birnberg ed., 1992).

32. AIA Doc. B141, *supra* note 25, ¶ 2.2.

33. *Id.* ¶ 2.3.

34. *Id.* ¶ 2.4.

35. See *supra* part I.E.4.

36. A shop drawing is a detailed drawing prepared by a manufacturer prior to fabrication showing how the contractor plans to perform the work. Sweet, *supra* note 20, § 15.08(C), at 287-94. The architect will define the critical design parameters for a particular item but leave out many of the specifics, particularly when that item may be available from a number of manufacturers. The contractor must submit a shop drawing, showing how he proposes to do the work, for review by the architect in order to verify consistency with the architect's design intent, as well as to assure that the design conforms with all pertinent field conditions. AIA Doc. A201, *supra* note 13, ¶ 3.12.

37. AIA Doc. B141, *supra* note 25, ¶ 2.5.

Bidding requires a contractor to review the drawings and specifications and estimate his cost to complete the project.³⁸ Superficially, it is an exercise of measuring quantities to establish the amount of materials and labor required. It involves much more, however—particularly in estimating conditions for which there are a number of unknowns. The contractor must understand the logistics of the site in order to estimate project phasing.³⁹ He must also estimate the impact of details not shown on the drawings, establish the inconsistencies between the specifications and the drawings,⁴⁰ and obtain the documents that have been incorporated by reference in the design documents. He must speculate as to the future hourly cost of labor, as well as how inflation may impact material costs. He must also weigh risks that have been assigned to him through different clauses that appear in the construction contract. Thus, assembling a construction bid has very much to do with assessing risk.

In contract terminology, a construction bid is an offer⁴¹ to provide the materials and services described in the design documents for a specific price. An owner may accept the bid (offer) of a contractor or negotiate with a contractor through a process of counter offers to arrive at an eventual acceptance of terms. If, however, an owner has developed a relationship with a particular general contractor, he may forego the entire bidding process and merely negotiate a deal.⁴² Repetitive dealings allow the parties to clearly understand each other's needs and requirements. With the prospect of repeat work, a contractor has an incentive to service the owner's needs rather than "nickel and dime" the owner based on the specifics of the construction documents.⁴³ Also, the specifics of the project's construction documents may not need to be as rigorous if there is an understanding as to the level of quality required based on prior work. In a market with many potential clients and many contractors, neither side holds a superior

38. Sweet, *supra* note 20, § 22.03(C), at 468; see also John D. Calamari & Joseph M. Perillo, *The Law of Contracts* § 2-6, at 42 (3d ed. 1987).

39. A contractor's bid will be based on an estimate of the cost it will take to complete the job. It is based on design information shown on the drawings and other documents provided to the bidder, as well as the contractor's own construction experience and his observations upon visiting the site. Dagostino, *supra* note 17, at 51-52.

40. A contractor has the burden of inquiring about discrepancies that would be recognized by a reasonable bidder before submitting a bid. *Wickham Contracting Co. v. United States*, 546 F.2d 395, 398 (Ct. Cl. 1976).

41. Sweet, *supra* note 20, § 22.04(C), at 473-74.

42. Negotiation has several benefits over competitive bidding. David T. Douthwaite, *Why Procure Construction by Negotiation?*, 25 *Pub. Cont. L.J.* 423, 425-26 (1996). For example, a contractor can be used earlier in the construction process. *Id.* at 426.

43. In a competitively bid construction contract, it is in the contractor's best interest to submit the lowest bid possible in order to win the bid. Once won, the contract price is fixed and the contractor may seek to exclude work by exploiting the ambiguities in the contract in an effort to modify the price and secure additional profit. Sweet, *supra* note 20, § 22.03(C), at 468.

bargaining position. Through good faith negotiation, the parties come to a fair agreement on contractual terms, including price, time of performance, scope of goods and services, the risk allocation, and the methods by which disputes are to be resolved.

Regardless of the award method, the agreement will be memorialized in a contract, which will acknowledge: the drawings and specifications that formed the basis of the bargain;⁴⁴ the terms of the agreement, such as price,⁴⁵ date of substantial completion,⁴⁶ and payments;⁴⁷ responsibilities of the parties;⁴⁸ and the method by which any disputes will be settled.⁴⁹ Although the parties are free to draft an agreement in any way they choose, a standard contract drafted by the AIA is commonly used because the architect will play a major role in enforcing the contract and architects are generally familiar with its terms. Large companies and public agencies may, however, have their own standard contracts.⁵⁰

D. *The Construction Contract and the Problems of Construction*

The typical construction project can lead to almost every conceivable contract issue. While the terms of the agreement may be memorialized by many pages of text, it is likely that many of the terms are far from certain. As noted above, the contractor's bid is based on the construction documents prepared by the architects and engineers.⁵¹ Even design documents produced by the most diligent architects and engineers, however, will leave unanticipated details that require further interpretation and study by the architect during the course of construction.⁵² Further, a mistake by the architect or engineer may require modification of the design long after the award of a construction contract in order to comply with building codes or to assure that the structure will not fail.⁵³ There will also be conditions that were not discovered when the design documents were prepared or that turn out to be substantially different from those which the designers had originally assumed. Finally, as is his prerogative, the owner may wish to make changes to the project during the course of construction that result in contract modification. Thus, the owner and contractor may have at one time agreed to a contract, but that contract is hardly a

44. AIA Document A101, Standard Form of Agreement Between Owner and Contractor Where the Basis of Payment Is a Stipulated Sum, art. 9 (12th ed. 1987) [hereinafter AIA Doc. A101].

45. *Id.* art. 4.

46. *Id.* art. 3.

47. *Id.* art. 5.

48. AIA Doc. A201, *supra* note 13.

49. *Id.* ¶ 4.5.

50. *See infra* note 137 and accompanying text.

51. *See supra* part I.C.

52. AIA Doc., B141, *supra* note 25, ¶¶ 2.6.15-2.6.16.

53. *See supra* part I.E.2.

static document. It must include protocols to resolve disagreements as to the scope of work or the value of changes.

A typical construction contract⁵⁴ anticipates changes⁵⁵ and provides means to deal with these issues.⁵⁶ The contract typically calls upon the architect to determine whether a contractor has "substantially completed" work required for payment,⁵⁷ to determine whether a contractor has met the level of quality established by the design documents,⁵⁸ and to interpret the drawings.⁵⁹ The contract may also allocate risk by specifying the contractor's responsibilities in the event that field conditions vary from those anticipated in the drawings and specifications.⁶⁰

The complex nature of the promises comprising a construction contract compounds the need to resolve disputes between the owner and contractor. A decision regarding even a minor aspect of the work can have far reaching consequences. Delays in one part of the project may mean that other work cannot be started within the project schedule.⁶¹ Starting and stopping work may not result in use of excess materials, but will nonetheless affect the contractor's costs by increasing the use of labor. At the outset, however, the construction contract set a fixed price for the entire project.⁶² Someone will have to decide whether the contract price and/or deadline should be revised. In order to keep the project moving, construction decisions must be made

54. The most frequently used of the standard form documents that relate to the relationship between owner and contractor are AIA Doc. A101 and AIA Doc. A201.

55. AIA Doc. A201, *supra* note 13, art. 7 (addressing changes in the work). The change order is a written document prepared and signed by the architect. It is then submitted for signature by the owner and contractor in order to establish agreement. *Id.* ¶ 7.2.1.

56. *Id.* ¶ 4.2.8 (stating architect's role in preparing Change Orders and Construction Change Directives).

57. *Id.* ¶ 4.2.9 (stating architect's role in determining date or dates of Substantial Completion).

58. *Id.* ¶ 4.2.6 (stating architect's authority to reject work not in conformance with the Contract Documents).

59. *Id.* ¶ 4.2.7 (stating architect's role of reviewing contractor's submittals for conformance with the "design concepts expressed in the Contract Documents").

60. *See infra* note 142 and accompanying text.

61. Delays may be excusable if they are of no fault of the contractor and are sufficiently severe. *See Contracting & Material Co. v. City of Chicago*, 314 N.E.2d 598 (Ill. App. Ct. 1974) (holding that an unforeseeable labor dispute was a valid reason for delay). *But see Shea-S&M Ball v. Massman-Kiewit-Early*, 606 F.2d 1245, 1249 (D.C. Cir. 1979) (stating that "[h]eavy rainfalls, unless they are unusual and extraordinary, are not considered acts of God").

62. Most contractors are engaged on a project for a stipulated sum. However, in projects of limited scope, a contract is sometimes based on the cost of the work plus a fee. *See, e.g., AIA Document A117, Abbreviated Form of Agreement Between Owner and Contractor for Construction Projects of Limited Scope Where the Basis of Payment Is the Cost of the Work Plus a Fee with or Without a Guaranteed Maximum Price* (2d ed. 1987) (standard contract calling for a cost based fee). This discussion focuses on the contracting of larger projects.

quickly. Work may continue while issues are still in dispute,⁶³ with final resolution taking place after work has been done.⁶⁴

E. *The Construction Phase and Disputes*

The actual construction takes place during the Construction Phase.⁶⁵ During construction, the contractor undertakes the bulk of the activity. The contractor must secure the required building permits⁶⁶ and is responsible for keeping the construction schedule.⁶⁷ The contractor's work is monitored by the architect on the owner's behalf.⁶⁸ Where disputes develop between the owner and contractor,⁶⁹ the architect takes on a role akin to an arbitrator.⁷⁰

Given that the drawings and specifications manifest a basis for the contractual agreement and a formal contract binds the parties, one may ask why there should be disputes at all. On the surface, there are many reasons to modify the agreement such as design modifications made after the agreement, errors and omissions made on the design documents, mistake, and unforeseen conditions. At the root of these disputes lies money. Items contrary to either party's assumptions may lead to variations in materials, labor, and time. In order to appreciate the impact of changes, this part discusses some of the changes that may come up during construction.

1. Design Changes

A client's needs may change midway through construction. Also, because a designer works with drawings and rough scale models that can only approximate the actual finished result, it is understandable that aspects of a project cannot be appreciated until they begin to take shape in reality. Rather than complete a project that no longer meets

63. AIA Doc. A201, *supra* note 13, ¶¶ 7.1.2, 7.3.4. A Construction Change Directive is a change in the work agreed to by the owner and architect. The contractor may or may not have agreed to such a change. Regardless, when a contractor receives a Construction Change Directive, the contractor is required to promptly proceed with the change. *Id.*

64. *See id.* ¶ 7.3.6. If the contractor does not agree to the contractual adjustment, the architect is to determine a reasonable amount. The contractor disputing the amount calculated by the architect must account for all costs as they are expended. *Id.* If the issue remains in dispute, the matter is resolved through arbitration. *Id.* ¶ 4.5.

65. AIA Doc. B141, *supra* note 25, ¶ 2.6.

66. AIA Doc. A201, *supra* note 13, ¶ 3.7.1.

67. *Id.* ¶ 3.10.

68. Some of the tasks that an architect will handle during construction are review of drawings and submittals by the contractor, AIA Doc. B141, *supra* note 25, ¶ 2.6.12, visits to the site to become familiar with job progress, *id.* ¶ 2.6.5, preparation of Change Orders, *id.* ¶ 2.6.13, interpreting the contract documents, *id.* ¶ 2.6.16, and certifying the Contractor's Application for Payment, *id.* ¶ 2.6.10.

69. *See supra* part I.D.

70. For the view that the architect's inherent conflict of interest makes her an improper arbitrator, see B. Scott Douglass, Comment, *Reassessing the Architect's Role as Arbiter*, 27 U.S.F. L. Rev. 873 (1993).

the client's needs or fails to meet the designer's vision, a design may need to be modified.⁷¹ An owner's budget is typically crafted to allow for a percentage of the project cost to cover such design contingencies.⁷²

2. Mistakes

Design is a long and time consuming process that must take multiple factors into account simultaneously. Often, time is critical and decisions are made on partial or incorrect information. Professionals working on different construction disciplines toil simultaneously to meet a deadline.⁷³ For example, how different building systems interface may not become apparent to the designers until all of the systems are carefully drawn and coordinated or until the systems are actually put into place. Therefore, changes to the project may result from the mistaken assumptions of the architect and engineer.⁷⁴ This places self-interest into the architect's decision in arbitrating disputes. An architect evaluating his own design is mindful that the owner may look to recover from the architect if a change is based on the architect's own error or omission and that the problems caused by the architect may reflect in any future work for the owner.⁷⁵

3. Unforeseen Conditions

It is not possible to be entirely certain of particular construction conditions which cannot be seen. A common example is subsurface conditions. In designing a foundation, one will want to know the depth and composition of each underlying strata. Although test borings will reasonably establish this depth for a particular location, the subsurface topography may drop off significantly a few feet away, making the precise design of a foundation difficult.⁷⁶

Similarly, the existing conditions may not be known because they are often covered over by finished materials. Water may penetrate places that cannot be seen and cause corrosion of steel beams and columns. Cracks in finished materials may be minor or may forecast problems in the underlying substrate. Without invasive exploration,

71. Civitello, *supra* note 15, at 70-71.

72. *Id.* at 70. Owners typically plan on a contingency of 10% of the project cost to cover change orders. *Id.*

73. *See supra* note 28.

74. Architects and engineers may be liable for mistakes in design. Owners, wary of this fact, will often require that their consultants have sufficient professional liability insurance to cover items such as the errors and omissions. Sweet, *supra* note 20, § 18.05, at 391-95.

75. Brian M. Samuels, *Construction Law* 130 (1996).

76. Owners often try to disclaim the accuracy of information obtained regarding subsurface conditions in an effort to place the risk of such conditions onto the contractor. Sweet, *supra* note 20, § 29.04, at 645-58. Such efforts are not always successful. *Id.*

the need for repair may not be known until it is uncovered during construction. A contractor may file a claim based on concealed or unforeseen conditions; however, it will be up to the architect to decide whether the condition is materially different and whether a change in time or cost is to result.⁷⁷

Moreover, excavation may uncover hazardous materials that must be removed or treated by specially trained and licensed personnel. In many cases, all construction must stop in order to insure the health and safety of workers on the site.⁷⁸ Similarly, construction may involve existing structures that contain asbestos or lead paint. Although in both of these cases tests done early in the design process will help prevent some surprises from creeping up during construction, it is not possible to be aware of everything.

4. Interpretation of Documents

Often times, documents must be interpreted during the construction phase.⁷⁹ Drawings and specifications may sometimes be at odds with one another or intentionally leave out specifics that the architect may want to control. In other cases, the contractor must prepare shop drawings of assemblies that are based on the architect's design intent.⁸⁰ While it is preferable that such documents be clear and consistent, at times an interpretation must be made that affects the methods and materials used or whether work must be redone.⁸¹ Much of this decision making is necessarily subjective in nature.⁸² For example, a minor item like a handrail may be required but lack specificity. The contractor, assuming a basic utilitarian function, may have anticipated using an inexpensive steel pipe rail and priced the job accordingly. The architect, on the other hand, may have considered a more aesthetic view and intended that a more elaborately detailed handrail used in another area of the building be replicated here. This dispute will have to be resolved in light of budget and quality considerations.

5. Contractor-Initiated Changes

During the construction phase, a contractor may propose a change in the design or materials used in the project for any number of rea-

77. AIA Doc. A201, *supra* note 13, ¶ 4.3.6.

78. *Id.* ¶ 10.1 (addressing safety precautions and programs). The contractor is to stop work and report conditions to the architect and owner if he encounters asbestos or polychlorinated biphenyl (PCB). *Id.* ¶ 10.1.2.

79. *See supra* note 43 and accompanying text.

80. *See supra* note 32 and accompanying text.

81. The architect is to visit the site and, through such observations, guard against defects and deficiencies in the work. AIA Doc. A201, *supra* note 13, ¶ 4.2.2. The architect also certifies work for payment and may withhold such if it is necessary to protect the owner. *Id.* ¶ 9.5.

82. *See id.* ¶ 9.5. Such withholding may be made based on the architect's opinion.

sons.⁸³ One common reason is to propose a more efficient or less costly method of achieving a particular, agreed-upon result. The outcome may involve a cost credit to the owner, although the contractor will often look to retain the profit that he would have otherwise obtained without the change.

With all of these changes, important decisions must be made. Change orders must typically be approved by the owner, contractor, and architect.⁸⁴ In the first instance, however, someone must determine whether changed circumstances warranting a contractual modification really exist. This requires an understanding as to what was really purchased in the bid price. If the determination is deemed to constitute a change, someone must also determine the value of the change and whether additional time should be allotted for the completion of such work.⁸⁵ In such circumstances, the owner's desire to hold down costs and keep the project on schedule are clearly at odds with the contractor's desire to coordinate the work of different construction trades and to avoid having his profits cut. Given these conflicts, disputes regarding changes are inevitable.

Many ramifications may follow if a change order is required. The architect may be required to issue additional drawings for which she may or may not be compensated.⁸⁶ The overall scope of the project may change, requiring additional work which may mean additional materials and/or labor for which the contractor will claim that he is due additional compensation. Conversely, in some instances a change may result in a reduction of costs, thus providing a credit to the owner. The parties, therefore, must agree to the exact nature of the change and how the agreement is to be modified.

Moreover, a change order may be required to resolve an inconsistency without which other work may not be able to proceed.⁸⁷ This can result in an overall delay in the project's completion. Claims for delays are common when a contractor is unable to complete a task as efficiently as he may otherwise have done, but for the change or the lack of a timely decision. Time is particularly an issue when the contract makes the contractor liable for damages (liquidated or otherwise) incurred because of a missed contractual deadline or when a

83. Civitello, *supra* note 15, at 83.

84. AIA Doc. A201, *supra* note 13, ¶ 7.1.2.

85. *Id.* ¶ 7.2.1.

86. Similar to the work of the contractor, an architect must determine whether such work is part of her basic services contract. If not, she may seek compensation from the owner as an additional service. AIA Doc. B141, *supra* note 25, ¶ 3.1.

87. See Sweet, *supra* note 20, § 24.03(B), at 520-31. Discrepancies may be raised between documents of the same set, such as information on drawings that conflicts with the specifications. See, e.g., *Franchi Constr. Co. v. United States*, 609 F.2d 984 (Ct. Cl. 1979) (citing contract's precedence clause removing conflict between drawings and specifications); *Union Management Corp. v. United States*, 375 F.2d 804 (Ct. Cl. 1967) (adding that contractor was contractually obligated to promptly bring discrepancies to the attention of the Contracting Officer).

contractor misses the opportunity to collect a bonus tied to a timely completion clause.⁸⁸

The interrelationship of the multiple future promises that make up a construction project cause otherwise simple problems to affect the overall job.⁸⁹ It would be impractical to settle all decisions on an adjudicative basis at the time of their occurrence.⁹⁰ Resulting project delays would stand to hurt both the owner and contractor. It is for this reason that the architect is often placed in the role of arbitrator during the construction process.⁹¹ Although the architect has a vested interest in keeping her client (the owner) satisfied, she is at least familiar with the problem at hand. In order to prevent delays, a contractor is typically required to continue to work on the project despite the dispute.⁹² Ultimately, the decision may be protested and settled later under true neutral party arbitration or adjudication after the fact.⁹³ Continuing disputed work may be acceptable, as long as the dispute may be ultimately settled in a fair forum.

II. THE SPECIAL CASE OF PUBLIC WORKS CONTRACTING

In many ways, government contracting of construction work is quite different from contracting in the private sector. At the root of this difference is the manner in which the work is solicited and the manner in which disputes may be resolved. The private contracting model offers many advantages over the government model. That is not to say, however, that government should necessarily look to "go private."⁹⁴ Government contracting must take the form it does because, as noted above, there is a need for accountability to the public.

88. Incentives for meeting a deadline can be either positive or negative. Delays may mean consequential damages or reasonable liquidated damages set by the contract. Calamari & Perillo, *supra* note 38, § 14-31(c), at 642-43. An example of an incentive arrangement is a contractual bonus given to the contractor if he completes the project by a pre-stated date. Dagostino, *supra* note 17, at 153-54.

89. Compounding this problem are factors such as trade usage, course of dealing, and course of performance. Calamari & Perillo, *supra* note 38, § 3-17, at 178-81.

90. Time is an important part of the contract. *See supra* part I.A.2. Since delays will cause additional injuries, the parties have a duty to mitigate damages. Calamari & Perillo, *supra* note 38, § 14-15, at 610-13.

91. *See supra* notes 59 & 68-70, and accompanying text.

92. AIA Doc. A201, *supra* note 13, ¶ 4.3.4. Changes that are agreed to by the architect and owner, but not necessarily the Contractor, are considered Construction Change Directives. While the architect is to determine the change in cost and time resultant from such a directive, the Contractor may dispute such determination and account for all applicable costs. If the dispute is not resolved, it may become subject to the dispute resolution provisions of the contract. *Id.* ¶ 7.3.

93. *Id.* ¶ 4.3.4. In the standard agreement between owner and contractor, controversies dealing with the contract are settled in arbitration under the Construction Industry Arbitration Rules of the American Arbitration Association. *Id.* ¶ 4.5.

94. *But see* Douthwaite, *supra* note 42, at 431 (arguing against the policy of relying primarily upon competitive bidding in public contracting and in favor of negotiated contracts).

This part discusses the unique nature of public works contracting. It begins by examining the various goals that the government seeks to achieve through public works contracting. It then looks at the need for apparent fairness and how this need necessarily results in the competitive bidding process. Next, it explains how competitive bidding has adhesionary consequences, such as unfairly allocated risk. This part discusses the use of in-house architects and engineers and how this affects dispute resolution. Further, this part examines the roots of the government's advantage over contractors in dispute resolution—the doctrine of sovereign immunity. Finally, this part examines the government's perspective and the problems it faces in contracting for construction work.

A. *The Multiple Goals of Public Works*

Government construction serves many purposes. As a primary purpose, construction provides the infrastructure within which government, business, and the public operates. Spending on public works also provides a stimulus to the local economy through the creation of jobs.⁹⁵ It also has allowed government to foster social and economic goals.⁹⁶ Contracting policies have been used to promote small businesses, minority owned businesses, women owned businesses, and local manufacturing.⁹⁷

Government construction, like private construction, aims to achieve an end product which meets the needs of its constituency. This involves bringing a construction project to completion on time and on budget. Since the government rarely uses its own workers to complete its own projects, it must acquire the goods and services it needs through private industry. Most of these goods and services are obtained through publicly held competitive bidding on a sealed bid basis.⁹⁸

The government's secondary goals are achieved through the very act of awarding the work itself. Congress has long used "pork barrel" projects to trade off political favors, including the location of public works projects. During the 1800s, construction of roads, canals, and railroads helped employ new immigrants.⁹⁹ During the Panic of 1893, some cities used public works to deal with twenty percent unemployment levels.¹⁰⁰ In the wake of the Great Depression, the Roosevelt Administration used public works projects to help put the country

95. See *infra* notes 99-101 and accompanying text.

96. See *infra* notes 102-06 and accompanying text.

97. *Id.*

98. See *infra* part II.B.

99. American Public Works Association, *History of Public Works in the United States 1776-1976* 10 (Ellis L. Armstrong ed., 1976) [hereinafter *History of Public Works*].

100. *Id.*

back to work with the formation of the Federal Emergency Administration of Public Works (known commonly as the Public Works Administration).¹⁰¹ Today, public works expenditures are used to stimulate the economy, by creating construction jobs and by providing infrastructure for private sector growth.

Social, as well as economic, goals of government contracting were advanced during the 1970s and 1980s. Growing sentiment against rising foreign debt and the loss of jobs offshore renewed interest in protectionist procurement policies.¹⁰² Today, most states have enacted legislation that gives local manufacturers some preference in procurement.¹⁰³ Construction contracting rules may prescribe workers' minimum wages.¹⁰⁴ Additionally, the civil rights and the women's movements raised issues of present day discrimination based on historical bias. Accordingly, government contracts have promoted participation by small, women-owned, and minority-owned businesses through the use of quotas or targeted percentages.¹⁰⁵ Local governments have encouraged smaller businesses through the division of

101. Jack F. Isakoff, *The Public Works Administration 9-10* (1938). Federal public works proposals were promoted from 1918 through 1932. *Id.* at 11-17. The use of public works to address unemployment was unsuccessfully proposed during the depressions of the 1850s and 1870s. *History of Public Works*, *supra* note 99, at 10.

102. A prime example of protectionism in procurement is the Buy American Act, which requires that products purchased by the federal government be substantially comprised of American made components. *See* Morris D. Davis, Comment, *The Domestic Components Requirement of the Buy American Act: Dismayed in America?*, 36 A.F. L. Rev. 129, 129 (1992). The Buy American Act was passed in 1933 and signed into law on President Hoover's last day in office. In part, it retaliated against similar protectionist legislation passed by the British. Its timing coincided with high unemployment rates brought on by the Great Depression, protectionist sentiment, and the construction of the Hoover Dam. According to the Act, the "end product" procured by the federal government must be manufactured in the United States and "substantially all" of the components making up the product must also be manufactured in the United States. *Id.* at 130. Originally, the definition of "substantially all" meant that no more than 25% of the value of the total product could be comprised of foreign components. This was revised to 50% by President Eisenhower through his Executive Order No. 10,582 (issued on December 17, 1954). *Id.* at 132.

103. Doreen J. Piligian, *Resident Preference Laws and the Award of Public Contracts*, *Construction Law*, May 10, 1990, at 10.

104. Julian E. Lange & Daniel Q. Mills, *The Construction Industry: Balance Wheel of the Economy* 42 (1979). Many state construction contracts set prevailing wage rates that contractors must pay each specific type of worker. In addition, the Davis-Bacon Act (passed in 1931) mandated that workers on federal public works projects must be paid the same wages that workers are customarily paid in the particular locality for the same type of work. *History of Public Works*, *supra* note 99, at 13.

105. *See* *Richmond v. J.A. Croson Co.*, 488 U.S. 469 (1989) (holding that a racial affirmative action program prescribed by state and local governments may be upheld if it is narrowly tailored to promote a compelling interest).

For a look at state minority set-aside programs in public works after the decision in *Croson*, see Deborah S. Ballati, *Legislation Since Croson*, *Construction Law*, Jan. 13, 1993, at 7.

projects among different contracts,¹⁰⁶ even though this practice results in higher project costs than if bid as a single project. Clearly, government construction contracting involves more than just bricks and mortar.

B. *The Appearance of Fairness*

An important aim in the government's procurement of goods and services is the appearance of fairness. Nowhere is this more important than in the start of the relationship with the contractor, at the project's initial bidding stage. The expenditure of large amounts of government money to private industry makes it important that work be awarded free from political influence and corrupt practices. Legislation typically mandates that construction work awards above a stated minimum amount must be made through sealed competitive bidding.¹⁰⁷

Competitive bidding essentially allows anyone meeting the requirements stated in the design documents to submit a bid. If an award is made, it will go to the lowest "responsible" or "qualified" bidder.¹⁰⁸ Because price is the sole criterion used in granting the award,¹⁰⁹ all bidders must offer the same package of products and services based

106. An example of this is New York State, which requires that most public contracting construction work be bid under separate prime contracts rather than under a single general contractor. N.Y. Gen. Mun. Law § 101 (McKinney 1986); N.Y. State Fin. Law § 135 (McKinney 1989 & Supp. 1996).

107. See, e.g., Ala. Code §§ 39-2-2, 39-2-6 (1992 & Supp. 1996); N.Y. Gen. Mun. Law § 103 (McKinney 1986 & Supp. 1996); Pa. Stat. Ann. tit. 71, § 638(8) (1990); 41 U.S.C. § 253(b) (1994). A good example of such a statute is found in the state of Oregon. Competitive bidding is generally required for public contracts, but exceptions to this rule include contracts for supplies valued at less than \$2,500. Or. Rev. Stat. § 279.015 (1993).

The federal government requires sealed bids in most construction work as part of the Competition in Contracting Act of 1984. Pub. L. No. 98-369, §§ 2701, 2711, 98 Stat. 1175, 1175 (1984). One commentator favors negotiation over competitive bidding. See Douthwaite, *supra* note 42.

108. Lange & Mills, *supra* note 104, at 40-41. The operative word here is "qualified." Some states require that public works bidders have a demonstrated ability to do the work. An agency may require information related to prior similar work, as well as financial information about the bidder. Should the agency believe that the bidder is not able to perform the work, the bid may be deemed not responsible and will not be considered. *Id.* The determination that lacks responsibility is normally not appealable, absent fraud or abuse of discretion. Albert E. Phillips & Robert L. Crewdson, *Contracting with the Owner*, in *Construction Contractor's Handbook of Business and Law* 89, 93 (Robert F. Cushman et al. eds., 1992). An unsuccessful bidder, however, challenge the bid. See *infra* note 152.

109. Some states, however, give preference to in-state bids. For example, Alaska will accept an in-state bidder over a nonresident bidder if the former's bid is not more than fifteen percent higher. Alaska Stat. § 36.30.170(c) (1987 & Supp. 1995). Arizona gives a five percent advantage to bidders who use locally manufactured or produced materials, Ariz. Rev. Stat. Ann. § 34-242 (1989), as does New Mexico, N.M. Stat. Ann. § 13-1-21(B) (Michie 1978). Maine gives in-state bidders an advantage when there is a tie between bids. Me. Rev. Stat. Ann. tit. 5, § 1816(8) (West 1989).

on the same design documents and standard agency contract. The bidding process, however, is not always this simple, and in fact can be much more complex.

Sealed bidding procedures are intended to provide "full and open competition,"¹¹⁰ placing all those who are interested in a contract on equal footing. Not every firm will be considered "responsible" or "qualified," however. There are both objective and subjective measures used in denying the opportunity of an award to a potential bidder. On an objective basis, courts have interpreted "responsible" to mean a firm is technically and financially capable of completing a job.¹¹¹ A bidder may need to meet a minimum level of experience with projects of the size and type being bid, and demonstrate sufficient staffing and bonding capability. Furthermore, as seen below, a bidder may be found to be not "responsible" based on more subjective factors.

For instance, an agency may refuse to award a bid to a contractor based on "moral" responsibility.¹¹² In New York City, for example, the belief that a bidder is corrupt or "irresponsible" is grounds for denying the bidder a contract.¹¹³ If the bidder is alleged to be involved in criminal activity, a contract may not be awarded.¹¹⁴ The New York City Comptroller may object to an award "if in the comptroller's judgment there is sufficient reason to believe that there is possible corruption . . . or that the proposed contractor is involved in corrupt activity."¹¹⁵ Denying the application of a would-be contractor is an exercise of subjective discretion; the awarding of a contract is not a right and, therefore, a due process hearing is not required.¹¹⁶

A public agency solicits bids by publicly displaying the Invitation to Bid, advertising in newspapers and trade publications, publishing the Invitation in a government publication, or mailing Invitations to Bid to those on a list maintained by the procuring agency.¹¹⁷ In the Invitation to Bid, the agency will describe the type, location, and approxi-

110. Donald P. Arnavas & William J. Ruberry, *Government Contract Guidebook* 2-17 (1980).

111. Frank Anechiarico & James B. Jacobs, *Purging Corruption from Public Contracting: The "Solutions" Are Now Part of the Problem*, 40 N.Y.L. Sch. L. Rev. 143, 146 (1995).

112. *Id.* at 146-47.

113. N.Y. City Rules & Regs., vol. 4, tit. 9, § 5-02 (1995).

114. Anechiarico & Jacobs, *supra* note 111, at 153-54. In the event of alleged criminal activity, the agency may declare the contractor "non-responsible" without any reason. The contractor may still be awarded the contract, but the award will be delayed. *Id.*

115. N.Y. City Charter, ch. 13, § 328(c) (1990).

116. Anechiarico & Jacobs, *supra* note 111, at 147; *see also* Erving v. Mayor of New York, 29 N.E. 1101, 1102 (N.Y. 1892) (explaining that the lowest bidder is not entitled to a contract).

117. Arnavas & Ruberry, *supra* note 110, at 3-12. *But see id.* at 2-15 (noting that procurement methods vary from agency to agency).

mate size of the project, as well as the formalities of the bidding process.¹¹⁸

The drawings and specifications that comprise the bid package spell out the project's requirements. In addition to the methods and materials depicted in the design documents, specific procedures are established for the bids themselves. For example, the owner may evaluate the contractor's bid for a designated period of time.¹¹⁹ All bidders are given an equal amount of time to prepare their bids. Bidders may attend a walk-through of a project site to familiarize themselves with conditions and may pose clarifying questions to the agency.¹²⁰ Should there be clarifications, changes or modifications to the scope of the project, additional information will be made available to all prospective bidders.¹²¹

Bids are submitted in sealed envelopes at the specific time and place stated in the bid documents.¹²² In pursuit of complete fairness, bids for public contracts are opened publicly at the time and place stated in the Invitation to Bid.¹²³ In this way, public bid openings allow bidders to monitor the process. Upon identification of an apparent low bidder by the government, the bidder may be asked to confirm his bid, ensuring that no mistakes were made.¹²⁴ Simultaneously, unsuccessful bidders have the opportunity to raise challenges. After the completion of this process, assuming all is in order, the bid is accepted and a contract will be signed.¹²⁵

Bidders are general contractors that, if successful, will be responsible for the overall construction of the project. While they may handle certain aspects of a project themselves, general contractors subcontract much of the work to other businesses. The owner, however, may retain some control over the selection of a subcontractor.¹²⁶ Subcontractors are typically smaller and more specialized than general con-

118. Sweet, *supra* note 20, § 22.03(B), at 465-68.

119. *Id.* § 22.03(D), at 468-69.

120. *Id.* at 466-67.

121. *Id.* at 467.

122. *Id.* § 22.03(D), at 468-69.

123. *Id.*

124. See, e.g., *Peerless Casualty Co. v. Housing Auth.*, 228 F.2d 376, 381 (5th Cir. 1955) (allowing a low bidder who had discovered an accounting error to withdraw its bid because, at the time the bid was withdrawn, the award was still subject to approval by the Public Housing Administration, thus, the offer was withdrawn before acceptance); see also *Calamari & Perillo*, *supra* note 38, § 9-27, at 386-88 (discussing unilateral mistake). Relief for mistake in computation had been given if the party receiving the bid knew of the error or if it were obvious. More recently, courts have given relief when such error was not known or so obvious. *Id.* at 387 & n.34.

125. The government, however, expressly reserves the right to reject all bids. *Arnavas & Ruberry*, *supra* note 110, at 3-38 to 3-39. There is no obligation for the owner to make an award. For example, funds may be insufficient for the project or the project may no longer be required. *Id.* at 3-39.

126. AIA Doc. A201, *supra* note 13, ¶ 5.2.3 (stating that the owner may retain the right to object to the use of a subcontractor, and thus affect the price of the contract).

tractors. The successful general contractor signs the contract with the owner,¹²⁷ putting the general contractor in privity with the owner. A subcontractor is responsible only to the general contractor, as the general contractor is the only party with which the subcontractor holds a contract.¹²⁸

General contractors typically work with subcontractors with whom they are familiar because of the general contractor's overall responsibility for the work.¹²⁹ The general contractor may negotiate with the subcontractor or obtain competitive quotes from other subcontractors to ensure that he obtains the most favorable price. To arrive at his bid, the general contractor will tabulate the prices submitted by his subcontractors and add his costs, including those related to the coordination of this effort.

There are situations where sealed bidding is not deemed appropriate. When such an exception is made, a contract will be awarded through the solicitation of competitive proposals. For example, the nature of the procurement may not allow sufficient time to go through the sealed bid process, the nature of the contract may require that factors other than price be considered in awarding the contract, the contract may necessitate discussions with the bidders, or there may only be one proposal submitted.¹³⁰ Situations in which there will only be a single proposal, however, should be avoided. Sole source suppliers have been used to subvert the competitive bid process through the use of political influence.¹³¹

C. *Problems with Competitive Bidding*

Given the need for uniformity, the government bidding process is particularly rigid. Although this rigidity is useful in promoting the appearance of fairness, it is also the basis for other practices that make public works contracting less than fair. The sealed bidding process solicits competition from contractors looking to furnish goods and services on the basis of price.¹³² At the same time, agencies look to shift risks, such as uncertain construction conditions, to contractors

127. For a good example of a typical owner-contractor agreement see AIA Doc. A101, *supra* note 44.

128. See Arnava & Ruberry, *supra* note 110, at 21-2 to 21-3; see also Sweet, *supra* note 20, § 32.01, at 723-27 (discussing the contractual relationship between a contractor and a subcontractor).

129. AIA Doc. A201, *supra* note 13, ¶ 5.3.1 (outlining the responsibilities of the contractor).

130. Arnava & Ruberry, *supra* note 110, at 4-2 to 4-3.

131. An example of such abuse of sole-source procurement was the 1986 scandal involving a contract for hand-held computers purchased by the New York City Parking Violations Bureau ("PVB"). In this case, a PVB deputy director with financial ties to a supplier caused the specifications for the bid to be written in such a way as to give a single supplier an enormous advantage. See Anechiarico & Jacobs, *supra* note 111, at 147-48.

132. See *supra* notes 123-24 and accompanying text.

who are encouraged to undervalue such risk.¹³³ Many agencies employ their own in-house architects and engineers rather than hiring outside consultants, eliminating a potentially neutral and objective force in dispute resolution.¹³⁴ When disputes do arise between the parties, government agencies have an upper hand because of the powers that originate in the doctrine of sovereign immunity.¹³⁵

This section takes an in depth look at some of the problems caused by the sealed competitive bidding process. First, it looks at how bidding on the basis of price creates non-negotiable terms. This section then focuses on risk, one such non-negotiable term, and shows sealed competitive bids unfairly shifts risks to the contractor.

1. Adhesionary Aspects

Sealed bids attempt to reduce the variables of a contract down to a single element—price. Modification of these bid variables are unlikely prior to the contract award. Thus, the terms of government contracts are effectively non-negotiable. Moreover, important factors such as risk allocation and methods of dispute resolution are embedded in an agency's general conditions and standard contract.¹³⁶ Standardized contracts are used in both private and public contracting settings and are necessary as a practical means of determining rights.¹³⁷ While there is room for negotiation in a private construction contract, revision of material terms in a standard agency contract would open up the possibility of challenge by an unsuccessful bidder. Given immutable terms in a form contract, one may argue that the terms of a sealed bid contract are essentially contracts of adhesion.¹³⁸

The rigidity of sealed bidding eliminates the bargained for aspect of the deal. Rather than negotiating on an even-handed basis, the contractor is left with the option to take it or leave it. Since public works often deal with projects such as roads, bridges, tunnels, subways, and other projects not commonly required by the private sector, for con-

133. See *infra* part II.C.2.

134. See *infra* part II.D.

135. See *infra* part II.E.

136. Robert A. Rubin et al., *Construction Claims Analysis, Presentation, Defense 4* (1983) (noting that in publicly bid projects, many public officials prefer a harsh contract that allocates every conceivable risk to the contractor).

137. Contracts for construction are often based on standard documents such as those by the AIA, National Society of Professional Engineers and Associated General Contractors. Sweet *supra* note 20, § 1.09, at 8.

Standardized contracts are useful to both the Owner and Contractor because the parties become familiar with its provisions. Meanings of contractual clauses becomes more certain, having been interpreted over the course of time. In addition, standardized contracts are more convenient to the contracting official who must often enforce several contracts simultaneously.

138. See Sweet, *supra* note 20, § 5.04(C), at 53. Arguing that a contract is adhesive must, however, show that the parties were of uneven bargaining power. *Id.*

tractors whose specialty lies in these areas, this option may mean the difference between working or not working.

2. Risk Allocation and the Forced Bargain

Assuming uneven bargaining power, risk is unfairly allocated within the context of a public works contract.¹³⁹ Selling a completed product or a commodity allows a producer to take stock of his costs and profit before offering the item at a particular price. Construction, however, deals with a future product that is subject to change. With the many unknowns in the construction process, assigning a price implicitly involves assigning a value to the risk inherent in the contract. In order to assure himself a favorable price, the owner typically attempts to assign as much of this risk as possible to the contractor.¹⁴⁰ While this is arguably a valid exercise in the private contracting realm, this may not be so in competitively bid public contracts. Private contracting allows for free negotiation between the parties before establishing the terms and conditions of a contract.¹⁴¹ Conversely, competitive sealed bidding procedures used in public works contracting awards a contract to the lowest bid on a specific package of components with specific, non-negotiable terms. Since the cost associated with risk is a significant component of the price, competitive bidding rewards those who value risk the least. Subsequently, many construction disputes revolve around determining who in fact assumed a particular risk and, thus, who should pay for it.¹⁴²

There are many risks associated with contracting.¹⁴³ Some risks are squarely within the contractor's control. For example, a contractor can manage worker safety through training and instituting proper procedures.¹⁴⁴ Further, a contractor can manage the risk of inflation by ordering materials shortly after the award of the contract rather than waiting and speculating over the price. These risks are best attributable to the contractor because he is in the best position to manage

139. Alternatively, it may be argued that such risk is contractually assumed. *Id.* § 27.03(B), at 594.

140. Rubin, *supra* note 136, at 13 (noting that a fixed price contract assigns project risks almost entirely on the contractor).

141. *See supra* part I.C.

142. An example of such risk allocation is the "no damages for delay clause," in which the owner tries to shield himself from contractor claims based on delays caused by the owner. While present in a contract, the court may find such a clause unenforceable. Samuels, *supra* note 75, at 19.

143. One measure of risk is the continued viability of the entity itself. The rate of business failure in the construction industry is relatively high—13.4% in 1990. Sidney M. Levy, *Project Management in Construction* 4 (2d ed. 1994).

144. A contractor is primarily responsible for complying with the Occupational Safety and Health Act. Sweet, *supra* note 20, at 816.

them.¹⁴⁵ There are, however, risks which the contractor cannot control, but must nonetheless account for when preparing a bid.

The design of a complex structure can take a long period of time from conception to the production of working drawings. During that time, most aspects of the building will be considered and documented in the drawings and specifications.¹⁴⁶ Even then, there will be many aspects of the building that remain unclear or problems that must be decided in the course of construction.¹⁴⁷ The architect cannot know what the answers to these problems or ambiguities will be because the questions have yet to be asked.

In putting together the bid, a general contractor will have several weeks to review the drawings and examine the site before submitting the bid.¹⁴⁸ During this time, he must determine what unknown or undefined aspects are included in the contract and how much they will cost. For example, a foundation may be designed to a given depth. The contractor may encounter bedrock earlier than expected and must blast away rock to achieve the required depth. He may also encounter an underground stream and be required to deal with the added complexities of construction in the middle of water. Subsurface and other hidden conditions will often reveal unforeseen conditions late in the construction process. The contractor is placed in a difficult situation because of this potential for unforeseen complications.

The government will often seek to limit the potential for cost increases. By inserting a contractual clause, the government can seek to limit the contractual effect of delays to an extension of time rather than higher costs.¹⁴⁹ Many owners, including the government, would rather pay a fixed additional cost rather than take on the risk of a much higher cost.¹⁵⁰ One may argue that including such allocated risk

145. The allocation of risk to the contractor in a lump sum agreement is based on the assumption of the contractor's expertise, putting him in the better position to control costs. Phillips, *supra* note 108, at 98-99.

146. See *supra* part I.B.

147. See *supra* part I.E.4.

148. A clause which disclaims liability for conditions which differ from those found at the site requires the contractor to visit the site and familiarize himself with the conditions. Where it would be reasonable for a contractor to see the discrepancy in such a site visit, this clause may shield the owner. *Highland Constr. Co. v. Stevenson*, 636 P.2d 1034, 1036-37 (Utah 1981). *But see Fattore Co. v. Metropolitan Sewerage Comm'n*, 454 F.2d 537, 543 (7th Cir. 1971) (holding contractor not liable when subsurface conditions entitled contractor to an equitable adjustment).

149. See, e.g., *Northeast Clackamas County Elec. Co-op v. Continental Casualty Co.*, 221 F.2d 329, 334-35 (9th Cir. 1955) (holding that owner wrongfully refused to grant contractor's requested extension of time when such a clause existed in its contract); *A. Kaplen & Son, Ltd. v. Housing Auth.*, 126 A.2d 13, 15 (N.J. Super. Ct. App. Div. 1956) (holding that contractor has no claim for damages but only an extension of time to complete the contract). No damage for delay costs clauses may be contractually provided for within the agreement between the owner and contractor and are generally upheld.

150. *But see Differing Site Conditions*, 48 C.F.R. § 52.236-2(a)-(b) (1995). The federal differing site conditions clause provides:

in a construction contract is a valid exercise of the freedom of contract. The better argument, however, is that the dynamics of public competitive bidding make shedding of risk that is out of the contractor's control inherently unfair because it is a non-negotiable term that the contractor is coerced into undervaluing.

If a contractor qualifies his price by refusing to accept certain risks, his bid must be disregarded as not responsive to the bid's requirements.¹⁵¹ Such a deviation would likely prompt a bid protest.¹⁵² An unsuccessful bidder could claim that his bid would have been lower but for the particular provision of the contract. Under federal contracting rules, a bid protest may delay the award, stop the award, or suspend a contract.¹⁵³ Moreover, a successful challenge may result in the contract being re-bid, thus delaying the project. Additionally, a successful protester may be awarded the costs associated with filing the protest, including attorney fees,¹⁵⁴ as well as the costs associated with preparing the bid or proposal.¹⁵⁵ Given this potential impact, terms such as risk allocation are non-negotiable.

A contractor, therefore, must accept risks assigned to him in a government contract, including those that are out of his control. As an element of his bid price, the way in which this risk is evaluated can be crucial. The contractor who undervalues or ignores such risk is rewarded because it reflects in a lower bid price. The contractor who places a higher value on that risk will likely end up with a higher bid price, which in the competitive bid situation, is perceived as asking for

(a) The Contractor shall promptly, and before the conditions are disturbed, give a written notice to the Contracting Officer of (1) subsurface or latent physical conditions at the site which differ materially from those indicated in this contract, or (2) unknown physical conditions at the site, of an unusual nature, which differ materially from those ordinarily encountered and generally recognized as inhering in work of the character provided for in the contract.

(b) The Contracting Officer shall investigate the site conditions promptly after receiving the notice. If the conditions do materially so differ and cause an increase or decrease in the Contractor's cost of, or the time required for, performing any part of the work under this contract, whether or not changed as a result of the conditions, an equitable adjustment shall be made under this clause and the contract modified in writing accordingly.

Id.

151. A nonconforming bid must be rejected if the defect is not waivable. Sweet, *supra* note 20, § 22.03(F), at 469-70; *see also* Arnava & Ruberry, *supra* note 110, at 3-24 to 3-26 (describing the reasons for considering a bid nonresponsive).

152. Policies on bid challenges vary. Some jurisdictions do not allow unsuccessful bidders to challenge an award for lack of standing. The federal government allows contractors to protest under the Competition in Contracting Act. ABA Section on Public Contract Law, *The Protest Experience Under the Competition in Contracting Act 1-4* (1989).

153. 31 U.S.C. § 3553(c)-(d) (1994).

154. 31 U.S.C. § 3554(c)(1)(A) (1994).

155. 31 U.S.C. § 3554(c)(1)(B) (1994).

a higher profit. As a result, the contractor is coerced into undervaluing risk.

D. *In-House Architects and Engineers*

Large government agencies often use their own staff of architects and engineers to prepare the design and documents used for construction.¹⁵⁶ During construction, however, the architect is often placed in situations that require decisions that will affect the terms and scope of the contract.¹⁵⁷ As a direct employee of the owner, however, the in-house professional is placed in an ethical conflict when resolving disputes between the owner and contractor.

An architect may be asked to determine the adequacy of a contractor's work. As a professional, this is an opinion based on acceptable construction practices and what is fair, in light of the construction documents.¹⁵⁸ As an employee of the government agency, however, the architect is also an agent of the owner. That employee may also be responsible for the budget and schedule of the project, factors on which her performance will be evaluated. Given a vested interest, the judgment of an in-house architect is very likely to be biased against the contractor.

One may argue that a consultant architect or engineer hired by an owner faces similar conflicts in dealing with contractors. By favoring the owner, an architect stands to preserve her relationship with hopes of gaining future work.¹⁵⁹ The in-house architect's interest in favoring the owner, though, is stronger because her continued employment depends on that owner, while the consultant architect has many other clients.

E. *Sovereign Immunity—Controlling Dispute Resolution*

A particularly important term in a government construction contract is the one that addresses dispute resolution. Unlike private builders, governments have traditionally been protected from civil lawsuits through the doctrine of sovereign immunity. Many governmental entities have partially waived this right, but this has not placed governments on the same footing as their private contracting counterparts. In response, a variety of dispute resolution systems have been instituted, none of which, however, provides absolute fairness.

156. Even if an outside design firm is hired, the selection process faces some of the same fairness issues raised by competitive sealed bid awards of construction contracts. Unlike construction contracts, however, the hiring of design consultants involves specifics of qualifications as well as design fees. As a result, the selection process has a necessarily subjective component.

157. See *supra* part I.E.

158. Douglass, *supra* note 70, at 888-92.

159. *Id.* at 891-92.

The sovereign immunity doctrine originated in England, where it was not possible to sue the king in the king's court, as "the King could do no wrong."¹⁶⁰ The doctrine was adopted in the American colonies in suits against the crown and was embraced at the time of the Constitutional Convention.¹⁶¹ Sovereign immunity was extended to state governments in federal courts with the enactment of the Eleventh Amendment of the Constitution.¹⁶²

Periodically, Congress saw the need to compensate individuals for particular government wrongs and, in response, passed a number of private relief bills.¹⁶³ Increasing requests for relief led Congress to pass a limited waiver of sovereign immunity that created the Court of Claims to hear contractual claims against the federal government.¹⁶⁴ This waiver was expanded through the passage of the Federal Tort Claims Act to tort claims resulting from non-traditional categories of intentional torts, but explicitly excluded the "discretionary function or duty on the part of a federal agency or and employee of the Government, whether or not the discretion involved be abused."¹⁶⁵ Federal construction contracts were subsequently drafted to include dispute clauses calling for the use of agency Boards of Contract Appeals.¹⁶⁶ Today, construction claims against the federal government may be disputed in either an agency Board of Contract Appeals or the Claims Court.¹⁶⁷

The states have not consistently waived sovereign immunity. Some states have waived sovereign immunity through statute,¹⁶⁸ but the spe-

160. Black's Law Dictionary 1396 (6th ed. 1990).

161. Lewis J. Baker, *Procurement Disputes at the State and Local Level: A Hodgepodge of Remedies*, 25 Pub. Cont. L.J. 265, 267 (1996).

162. *Id.* at 268; see Charles A. Wright, *Law of Federal Courts* 274 (4th ed. 1983).

163. Brian R. Levey, *Tortious Government Conduct and the Government Contract: Tort, Breach of Contract, or Both?*, 22 Pub. Cont. L.J. 706, 713 (1993).

164. *Id.* The Court of Claims was created by the Act of February 24, 1855. *Id.* In 1887, the Tucker Act expressly limited the jurisdiction of the Court of Claims against hearing tort claims against the federal government. *Id.* at 714.

165. 28 U.S.C. §§ 2674, 2680 (1994).

166. Levey, *supra* note 163 at 716-17, 717 n.64.

167. See *infra* part III.C.

168. Alaska Stat. § 09.50.250 (1994); Ariz. Rev. Stat. Ann. § 12-821 (1992 & Supp. 1996); Ark. Code Ann. §§ 19-10-101, 19-11-246 (Michie 1994); Cal. Pub. Cont. Code § 10240.1 (West 1985); Conn. Gen. Stat. Ann. § 4-160 (West 1988 & Supp. 1996); Ga. Code Ann. § 50-21-1 (1994); Haw. Rev. Stat. §§ 103D-703, 103D-711 (1993); Ill. Rev. Stat. ch. 705, para. 505-8 (Smith-Hurd 1992 & Supp. 1996); Ind. Code Ann. § 34-4-16-1.1 (West 1986); Kan. Stat. Ann. § 46-913 (1993 & Supp. 1995); Ky. Rev. Stat. Ann. § 45A.245 (Michie 1993 & Supp. 1996); La. Rev. Stat. Ann. § 38:2181 (West 1989 & Supp. 1996); Me. Rev. Stat. Ann. tit. 5, § 1510-A (West 1989 & Supp. 1995); Md. Code Ann. State Gov't § 12-201 (1995); Mich. Comp. Laws Ann. § 600.6419 (West 1987); Minn. Stat. Ann. § 13.08 (West 1988); Miss. Code Ann. § 11-45-1 (1972); Mont. Code Ann. § 18-1-404 (1995); Neb. Rev. Stat. §§ 81-8, 215 & 81-8, 301 (1994); Nev. Rev. Stat. Ann. § 41.031 (Michie 1996); N.H. Rev. Stat. Ann. § 491:8 (1983); N.J. Stat. Ann. § 59:13-3 (West 1992); N.M. Stat. Ann. § 37-1-23 (Michie 1978); N.Y. Ct. Cl. Act § 8 (Consol. 1994); N.D. Cent. Code § 32-12-02 (1996); Ohio Rev. Code Ann. § 2743.02 (Anderson 1992 & Supp. 1995); Or. Rev. Stat. §§ 30.310 & 30.320 (1988 & Supp.

cifics of court access vary by state.¹⁶⁹ Many states have established administrative boards, similar to the federal Board of Contract Appeals, to hear contractual claims.¹⁷⁰ In some states where legislatures have not waived sovereign immunity, courts have waived it on public policy grounds.¹⁷¹

In most cases, government agencies draft contracts with clauses specifying the method of dispute resolution available to the private party; thus, the rules of the game are set by the government. Although the government has ceded most of these rights voluntarily, it has done so hesitantly.

F. *The Problems of Competitive Bidding—A Government View*

To be fair, competitive bidding presents a number of problems for government agencies as well. Unlike private contracting, public awards must be made without the appearance of bias.¹⁷² While a private developer has complete discretion to exclude a contractor, the same cannot be said for government agencies. Moreover, unlike in private contracting where a builder may develop a particularly good working relationship with a contractor, in government contracting the government cannot assure the selection of a favored contractor because of the sealed bid system.

Any contractor meeting the objective requirements must be considered under the sealed bidding process. The government may exclude a contractor that has submitted an unresponsive bid or is not responsible.¹⁷³ Finding that a bid is unresponsive is an objective determination that the contractor has failed to comply with a material term.¹⁷⁴ Finding a bidder not responsible, however, is a subjective determination that a contractor is apparently unable to successfully complete the project.¹⁷⁵ In either case, the failed bidder may slow down or stop the award process through a bid challenge.¹⁷⁶

1996); 72 Pa. Stat. Ann. § 4651-1 (1995); R.I. Gen. Laws § 37-13.1-1 (1990); S.D. Codified Laws Ann. § 21-32-1 (1987); Tenn. Code Ann. § 9-8-307 (1992 & Supp. 1996); Utah Code Ann. § 63-30-5 (1993); Va. Code Ann. §§ 11-69, 11-70 (Michie 1993 & Supp. 1996); Wash. Rev. Code Ann. § 4.92.010 (West 1988); W. Va. Code § 14-2-12 (1995); Wyo. Stat. Ann. § 1-39-104 (1988).

169. Baker, *supra* note 161, at 269.

170. See *infra* part III.B (discussing procedures in the state of Maryland based on the ABA Model Procurement Code for State and Local Governments).

171. Baker, *supra* note 161, at 270-71.

172. Fairness in competitive bidding is necessary in order to ensure that "honest and capable bidders [will] have enough confidence in the system to submit bids." Sweet, *supra* note 20, § 22.03(A), at 465.

173. Arnavas & Ruberry, *supra* note 110, at 3-23.

174. *Id.* at 3-24 to 3-26.

175. *Id.* at 3-26 to 3-28. A bidder may be found not responsible based on a contractor's lack of resources, ability to meet the prospective schedule, past record of performance, integrity, qualifications, experience, facilities, and skills. *Id.* at 3-26.

176. See *supra* note 152.

It is costly for individual agencies to institute intricate procedures to prevent awarding contracts to corrupt or criminal contractors.¹⁷⁷ Moreover, the paperwork required to submit a bid and the discretionary power yielded by contracting agencies results in disinterest among honest bidders.¹⁷⁸ In many ways, due process allows bad faith actors to continue their ways while the system goes on. This is not to say that the government is powerless. It just means, as this Note suggests, that the government must work harder to encourage good firms to bid and to identify and exclude bad firms through fair means.

Where a contractor has breached the terms of the contract, the government must be sure to follow up using thorough and legal means. To prevent a breach, the government should retain a sufficient percentage of the contract price so that it may leverage payments and secure the proper attention of the contractor.¹⁷⁹ When a contractor breaches his contracts with the government or is found guilty of criminal activities his company should be excluded from bidding for a period of time.¹⁸⁰ Such contractor exclusions, however, should only be made when illegal acts have been proven.¹⁸¹

While the needs are largely the same, the procurement of goods and services in the public sector must be handled somewhat differently than in the private sector. Private industry is largely free to do business in the manner that best suits its interests. One such interest, espoused by modern management techniques, is the establishment of long term business relationships between purchasers and suppliers.¹⁸² Such long standing relationships benefit the parties by focusing on servicing one another's needs rather than staying within the boundaries of the agreement. The key to these mutually beneficial relationships is maximizing efficiencies for the greater whole, thereby reducing costs and increasing profits.

The government may be interested in achieving these efficiencies but must remain primarily concerned with its accountability to the

177. Ethics Reform, *supra* note 3, at 465-69.

178. Anecharico & Jacobs, *supra* note 111, at 165-66; see Ethics Reform, *supra* note 3, at 461. "All too often, the City is faced with a small number of 'niche' bidders, firms whose expertise lies in threading their way through the city contracting maze and who have adapted themselves to its peculiar and confounding logic." *Id.* at 472.

179. Sweet, *supra* note 20, § 26.03, at 569-71. Retainage creates security against certain risks by holding back a percentage of earned progress payments. Federal procurement policies, however, state that retainage must be for good cause. *Id.* at 570.

180. A contractor may be debarred or prohibited from the award of a contract based on a violation of statute. Frank M. Alston et al., *Contracting with the Federal Government* 461-62 (1984).

181. *But see id.* (describing debarment and suspension of contractors). A contractor may be suspended if the agency has reason to believe that he has committed a seriously dishonest act.

182. W. Edwards Deming, *Out of the Crisis* 35 (1982). An example of such are the teachings of W. Edwards Deming, whose work is credited with improvements in quality and productivity in Japan. *Id.* at vii.

people.¹⁸³ Contract awards must be monitored by the public to protect against self-dealing.¹⁸⁴ The appearance of fairness that is achieved by sealed bidding is a key aspect of how goods and services are procured.¹⁸⁵ Although the sealed bidding process has some inherent problems, it is still the best protection we have against corrupt practices and should be continued.

III. EXISTING GOVERNMENT DISPUTE RESOLUTION SYSTEMS

A dispute resolution procedure aims primarily to reach a correct decision through a full and fair hearing of all of the facts. In the contract realm, it is also desirable that such decisions be made swiftly and efficiently. Unfortunately, meeting one aim of dispute resolution typically means compromising the others. A quick decision may not necessarily explore all of the legal issues and provide due process. A full and fair hearing through judicial processes may take years to reach its final disposition. Moreover, given the doctrine of sovereign immunity, the choice of how to settle disputes between government and private contractors is placed in the hands of the government itself.

Given the vast number of states and municipalities contracting for construction services, it is not surprising that a variety of dispute resolution methods have been utilized. This part looks at some methods utilized by various states and municipalities to resolve contract disputes. It focuses on four systems that represent the range of systems currently in place: the heavily government-biased systems used in New York; the Maryland system influenced by the ABA Model Code of Procurement; the federal system of Agency Boards of Standards and Appeals; and the arbitration panels used in California. In particular, this part examines the degree of fairness provided by each of these systems.

A. *New York State—Engineer's Decisions and Non-Neutral Panels*

Public contracting for construction services is particularly cumbersome in New York State. First, there are numerous state, county, and city agencies which independently contract for construction services. Even agencies within the same city often work with different policies and contracts.¹⁸⁶ Thus, contractors holding multiple city contracts

183. See Ethics Reform, *supra* note 3, at 464-65 (summarizing the recommendations of the New York State Commission on Government Integrity on the subject of contracting processes in New York City driven by the need to fairly service the taxpayer).

184. *Id.* at 480-82.

185. *Id.* at 482.

186. Robert J. MacPherson, *In Your Face ADR: New York City's Construction Contract Dispute Procedure*, 25 Pub. Cont. L.J. 301, 306 (1996). Despite at least fifteen years of trying, agencies contracting for public works have been unable to agree upon the same standard contract. As a result, contractors dealing with different city

must become familiar with the particulars of a number of different dispute resolution clauses. One of the most one sided dispute resolution processes—the engineer's decision clause—is used by several New York governmental agencies.

With origins in the construction of railroads and other public works during the early 1800s,¹⁸⁷ engineer's decision clauses were seen as a means of settling construction disputes between owners and contractors. Early engineer's decision clauses allowed an owner to name the party who would decide a dispute.¹⁸⁸ Despite the fact that an owner would often choose a party that would favor himself, such clauses were deemed by the courts to be fair under prevailing notions of freedom of contract. Although lacking a neutral arbitrator, such adjudication was looked upon as a type of arbitration.¹⁸⁹ This was despite the contemporary availability of agreements that called for neutral party arbitration.¹⁹⁰

One hundred and fifty years later, the modern-day engineer's decision clause is hardly different. Included in the standard contract of many agencies, the clause now allows a contractor to bring disputes, which could not be amicably resolved with the agency's contracting officer, to the Chief Engineer, an employee of the agency. Because the contract is the result of a sealed competitive bid, a contractor stands little chance at having such clause deleted from the standard agency contract.¹⁹¹

Contractors have challenged the one sided engineer's decision clause as recently as this year in *Yonkers Contracting Co. v. Port Authority Trans-Hudson Corp.*¹⁹² In that case, Yonkers Contracting ("Yonkers") contended that certain project delays resulted directly from Port Authority Trans-Hudson's ("PATH") misrepresentations of the subsurface conditions.¹⁹³ After negotiations between Yonkers and PATH proved unsuccessful, the issue was submitted for resolution to PATH's Chief Engineer, as provided for by the contract's engineer's decision clause.¹⁹⁴ Anticipating the Chief Engineer's rejection of the claim, Yonkers filed a claim with the court.¹⁹⁵ In a unanimous decision, the New York Court of Appeals held the engineer's decision

departments must understand the specifics of each discrete department's contract in submitting a bid.

187. See *Dubois v. Delaware & Hudson Canal Co.*, 12 Wend. 334 (N.Y. 1834).

188. See Jordan A. Dreifus, *The "Engineer Decision" in California Public Contract Law*, 11 Pub. Cont. L.J. 1, 6 (1979).

189. *Id.*

190. See, e.g., *Carnochan v. Christie*, 24 U.S. 446 (1826); *Underhill v. Van Cortlandt*, 2 Johns. Ch. 339 (N.Y. 1817).

191. See *supra*, part II.C.

192. 663 N.E.2d 907 (N.Y. 1996).

193. *Id.* at 908.

194. *Id.*

195. *Id.*

clause to be valid,¹⁹⁶ citing its prior decision in *Westinghouse Electric Corp. v. New York City Transit Authority*,¹⁹⁷ which dealt with a similar clause.

In *Westinghouse*, Westinghouse contracted with the New York City Transit Authority ("TA") to provide and install power substation equipment.¹⁹⁸ A dispute arose regarding delays and additional work. As a result of this dispute, Westinghouse suspended performance, citing unresolved design issues on the part of the TA.¹⁹⁹ The TA, in turn, found Westinghouse to be in breach of contract.²⁰⁰ Westinghouse submitted its case to the TA's Chief Engineer, who rejected the claim. Westinghouse then sued the TA for breach of contract, claiming that the contract's Chief Engineer's clause²⁰¹ contravened public policy.²⁰²

The Court of Appeals unanimously rejected Westinghouse's contention, stating:

It is firmly established that the public policy of New York State favors and encourages arbitration and alternative dispute resolutions. These mechanisms are 'well recognized as an effective and expeditious means of resolving disputes between willing parties desirous of avoiding the expense and delay frequently attendant to the judicial process.' Thus, '[i]t has long been the policy of the law to interfere as little as possible with the freedom of consenting parties to achieve that objective.' . . . Westinghouse chose, with its business eyes open, to accept the terms, specifications and risk of the bid contract, including the ADR clause. . . . To be sure, when powerful municipalities put their public works jobs out for bid and require

196. *Id.* at 908-09.

197. 623 N.E.2d 531 (N.Y. 1993).

198. *Id.* at 532.

199. *Id.* at 532-33.

200. *Id.* at 533.

201. The dispute resolution clause, Article 8.03 of the contract stated:

(a) In the event the Contractor and Authority are unable to resolve their differences concerning a determination by the Superintendent, the Contractor may initiate a dispute in accordance with the procedure set forth in this Article. Exhaustion of these procedures shall be a precondition to any lawsuit permitted hereunder.

(b) The parties to this contract authorize the Superintendent, acting personally, to decide all questions of any nature whatsoever arising out of, under, or in connection with, or in any way related to or on account of, this Contract . . . and his decision shall be conclusive, final and binding on the parties. . . .

(c) If the Contractor protests the determination of the Superintendent, the Contractor may commence a lawsuit in a Court of competent jurisdiction of the State of New York under Article 78 of the New York Civil Practice Law and Rules or a United States Court in New York, under the procedures and laws applicable in that court, it being understood the review of the Court shall be limited to the question of whether or not the Superintendent's determination is arbitrary, capricious or grossly erroneous to evidence bad faith.

Id. at 532.

202. *Id.* at 533.

competition, low cost and performance in accordance with published specifications, they enjoy a virtual monopolistic-kind of power. But that does not make those contracts adherence agreements.²⁰³

The court further relied on the fact that the chief engineer's decision was reviewable if it was "arbitrary, capricious or grossly erroneous to evidence bad faith."²⁰⁴ Despite the non-neutral status of the adjudicator, the court used the same standard for judicial review as that used under arbitration.

The New York courts are not alone in upholding the enforceability of non-neutral adjudication clauses. Federal and state courts have typically upheld engineer's decision clauses.²⁰⁵ Most courts will overrule an engineer's decision only if it "is manifestly arbitrary or rendered in bad faith."²⁰⁶ If the clause is enforced, the engineer's decision will likely be final. In order to find in favor of a contractor, a Wyoming court, in a split decision, chose to interpret an engineer's dispute clause as a limitation of actions clause rather than a finality clause.²⁰⁷ Cases overruling the decision of an engineer appear to be the exception rather than the rule.

Recently, New York City²⁰⁸ instituted a new method of settling public agency construction disputes.²⁰⁹ As part of its new City Charter, New York City reformed its dispute resolution system by instituting the Procurement Policy Board ("PPB") system.²¹⁰ The PPB aims to "ensure the fair and equitable treatment of all persons who deal with the procurement system of the City of New York."²¹¹ Despite its attempt to form a neutral alternative dispute resolution system, the PPB has fallen short of this ideal.

When a contractor disagrees with the ruling of an agency head, the PPB provides an opportunity to appeal. The PPB first requires that the claim be submitted for review and investigation by the Comptroller's office. There, a contractor may resubmit the materials he gave

203. *Id.* at 534-35 (citations omitted).

204. *Id.* at 532, 534-35.

205. *United States v. Moorman*, 338 U.S. 457, 463 (1950); *Zurn Eng'rs v. State*, 138 Cal. Rptr. 478, 504 (Ct. App. 1977); *see infra* part III.C (describing the current federal system, replacing engineers decision clauses with Boards of Contract Appeals).

206. *J.H. Jenkins Contractor, Inc. v. City of Denham Springs*, 216 So. 2d 549, 553 (La. Ct. App. 1968).

207. *Brasel & Sims Constr. Co. v. State Highway Comm'n*, 688 P.2d 871, 876 (Wyo. 1984).

208. New York City spends more than \$4 billion a year on capital construction. MacPherson, *supra* note 186, at 309.

209. Disputes of the Metropolitan Transit Authority (of which New York City Transit is a part), the NYC Board of Education, and the Health and Hospitals Corporation are not subject to the Procurement Policy Board. Constance Cushman, *The ABA Model Procurement Code: Implementation, Evolution, and Crisis of Survival*, 25 Pub. Cont. L.J. 173, 179, n.26 (1996).

210. New York City Charter ch. 13, § 311.

211. New York City Rules & Regs., vol. 4, tit. 9, § 1-01(b)(5).

the agency head. If the Comptroller fails to settle the claim, the agency head's decision may be reviewed by the Contract Dispute Resolution Board panel ("CDRB"), whose members are specifically chosen to hear the dispute. Comprised of two city officials (the City Chief Procurement Officer and either the Director of the Office of Construction or another City official with relevant experience) and one neutral arbitrator,²¹² the CDRB will review any "memoranda, briefs and oral argument[s]"²¹³ presented by the contractor, but no hearing is held and no witnesses are heard.

Commentators agree that the PPB system is less than fair.²¹⁴ By appointing a panel specific to the dispute and having control over two of the three adjudicators, city agencies retain the upper hand in adjudicating disputes with contractors. In addition to the lack of fairness and due process, PPB procedures are slow.²¹⁵ Thus, the new procedures clearly do not meet their stated purpose: they are neither neutral nor expedient.

B. ABA Model Procurement Code and Maryland

Dispute resolution is one of the issues that the American Bar Association ("ABA") addressed in adopting the Model Procurement Code for State and Local Governments ("MPC").²¹⁶ The ABA began consideration of the MPC in 1970. Its original objectives were to eliminate waste and corruption in government procurement.²¹⁷ It soon expanded its purpose, however, to include "ensur[ing] the fair and equitable treatment of all persons who deal with the procurement system."²¹⁸ Specifically, Article 9 of the MPC deals with legal and contractual remedies. Among the issues it addresses is how a contractor may appeal a chief procurement officer's decision.²¹⁹

The ABA's coordinating committee set out to draft a model code rather than a uniform code.²²⁰ Because it is a model, states and municipalities are free to adopt whatever parts make sense thereby enabling them to draft a code that meets their particular needs. Since its adoption, MPC-based purchasing laws have been adopted by twenty-

212. MacPherson, *supra* note 186, at 305. The neutral arbitrator typically is selected with contractor participation from a list kept by the city.

213. New York City Rules & Regs., vol. 4, tit. 9, § 7-05(g)(2).

214. See MacPherson, *supra* note 186, at 301-02; see also *Are the City's Contract Resolution Procedures Fair?*, 1 City L. 46 (1995) (noting that an arbitration panel working under the PPB system favored New York City).

215. MacPherson, *supra* note 186, at 302 (citing a minimum of 300 days between submission of a dispute to final disposition).

216. Model Procurement Code for State and Local Governments (1980) [hereinafter MPC].

217. F. Trowbridge Vom Baur, *A Personal History of the Model Procurement Code*, 25 Pub. Cont. L.J. 149, 152-53 (1996).

218. MPC, *supra* note 216, § 1-101(2)(e).

219. *Id.* § 9-501.

220. Vom Baur, *supra* note 217, at 161-62.

seven local jurisdictions and fifteen states.²²¹ One of the more successful examples of the MPC can be found in Maryland.²²²

In 1980, the Maryland legislature enacted the "Procurement Article," a set of procurement rules that essentially codified a version of the ABA's MPC.²²³ The Procurement Article established a unified set of rules for those who contract with the state, and replaced the rules set by individual state agencies. Among the provisions of the Procurement Article was a method of dispute resolution.²²⁴

At the heart of the Procurement Article was the establishment of the Maryland State Board of Contract Appeals ("MSBCA"). The MSBCA was given jurisdiction over all contractual disputes involving the state of Maryland, including bid protests raised by unsuccessful bidders. Members of the three person MSBCA are appointed by the Governor for a term of five years.²²⁵ Knowledgeable in public construction,²²⁶ MSBCA members are unrelated to the agencies contracting the work—making it a "neutral" forum.

According to Procurement Article procedures, the procurement officer makes an initial interpretation of the terms of the contract when a contractor makes a claim.²²⁷ Should the contractor disagree with this determination, he may appeal to the upper levels of the agency for review.²²⁸ Meanwhile, the contractor is obliged to continue with the directed work. If the dispute remains unresolved after agency review, the contractor may appeal the agency's decision to the MSBCA.²²⁹ The MSBCA has jurisdiction to hear disputes over any contractual issue, with powers to require parties to file briefs and allow discovery.²³⁰ Decisions by the MSBCA are reasoned, published decisions afforded precedential value. MSBCA decisions may be appealed by either party to the Maryland appellate court.²³¹

C. Federal System—Board of Standards and Appeals

The genesis of the federal system of contracting originated in wartime military procurement.²³² World War I saw an increase in pro-

221. Louis F. Del Duca et al., *Annotations to the Model Procurement Code for State and Local Governments with Analytical Summary of State Enactments* at vii-x (2d ed. 1992).

222. For an informative discussion of the procurement system in the State of Maryland, see Scott A. Livingston, *Fair Treatment for Contractors Doing Business with the State of Maryland*, 15 U. Balt. L. Rev. 215 (1986).

223. Act of May 27, 1980, ch. 775, 1980 Md. Laws 2661.

224. Md. Code Ann., State Fin. & Proc. §§ 15-215 to 223 (1995 & Supp. 1996).

225. *Id.* § 15-207.

226. *Id.*

227. *See id.* § 15-218(b)(1).

228. *Id.* § 15-218(d).

229. *Id.* § 15-220(a).

230. *Id.* § 15-221(b)-(c).

231. *See id.* § 15-223.

232. *See Dreifus, supra* note 188, at 25.

curement by the War and Navy Departments. In response to the resulting increased contract claims and disputes, the Secretary of War created the War Department Board of Contract Adjustment.²³³ While this department disbanded years after World War I, a similar board, the War Department Board of Contract Appeals ("WDBCA"), was created during World War II.²³⁴ The WDBCA was a part of the War Department, reporting to the Secretary of War, but was independent from the division responsible for procurement.²³⁵ Decisions of the WDBCA were treated as quasi-judicial and held firm and conclusive on issues of law as well as fact,²³⁶ absent fraud or gross mistake by the WDBCA.

Reform of the federal system of construction contracting came as the result of *United States v. Wunderlich*,²³⁷ which established a particularly high standard of review for decisions by a non-impartial adjudicator. In *Wunderlich*, Martin Wunderlich contracted with the Department of the Interior to build a dam.²³⁸ Wunderlich had a dispute with the contracting official, which he appealed to the Secretary of the Interior as required by the dispute clause of his contract.²³⁹ After an unfavorable ruling from the Secretary of the Interior, Wunderlich sued in the Court of Claims.²⁴⁰ After the Court of Claims set aside the Secretary of the Interior's decision, the Supreme Court granted certiorari.²⁴¹

In a 6-3 decision, the Supreme Court held that a clause in federal contracts providing for final decisions of disputes by a department head should be enforced and that "[t]he decision of the department head, absent fraudulent conduct, must stand under the plain meaning of the contract."²⁴² The Court rejected the Court of Claim's standard of "'arbitrary,' 'capricious,' and 'grossly erroneous,'" and distinguished it from actions which implied bad faith.²⁴³ In his dissent, Jus-

233. *Id.*

234. *Id.* at 26-27.

235. *Id.*

236. *United States v. Moorman*, 338 U.S. 457, 463 (1950).

237. 342 U.S. 98 (1951).

238. *Id.* at 98.

239. The clause provided that:

Except as otherwise specifically provided in this contract, all disputes concerning questions of fact arising under this contract shall be decided by the contracting officer subject to written appeal by the contractor within 30 days to the head of the department concerned or his duly authorized representative, whose decision shall be final and conclusive upon the parties thereto. In the meantime, the contractor shall diligently proceed with the work as directed.

Id. at 99, n.1.

240. *See id.* at 98.

241. *Id.*

242. *Id.* at 100.

243. *Id.*

tice Douglas questioned the high standard set by the majority, noting that:

The instant case reveals only a minor facet of the age-long struggle. The result reached by the Court can be rationalized or made plausible by casting it in terms of contract law: the parties need not have made this contract; those who contract with the Government must turn square corners; the parties will be left where their engagement brought them. And it may be that in this case the equities are with the Government, not with the contractor. But the rule we announce has wide application and a devastating effect. It makes a tyrant out of every contracting officer. He is granted the power of a tyrant even though he is stubborn, perverse or captious. He is allowed the power of a tyrant though he is incompetent or negligent. He has the power of life and death over a private business even though his decision is grossly erroneous. Power granted is seldom neglected.²⁴⁴

Limits are needed on the discretion given to government officials.

In response to the *Wunderlich* case, Congress enacted legislation revising the method of dispute resolution in government contracting. The "Wunderlich Act" provided that:

No provision of any contract entered into by the United States, relating to the finality or conclusiveness of any decision of the head of any department or agency . . . shall contain a provision making final a question of law the decision of any administrative official, representative, or board.²⁴⁵

As a result of this act, Boards of Contract Appeals were established for most federal agencies.

Currently, disputes regarding federal construction contracts are governed by the Contracts Dispute Act of 1978.²⁴⁶ The stated purpose of the Act was to help "induce resolution of more contract disputes by negotiation prior to litigation; equalize the bargaining power of the parties when a dispute exists; provide alternate forums suitable to handle the different types of disputes; and ensure fair and equitable treatment to contractors and Government agencies."²⁴⁷ In order to achieve this, the Act establishes a bifurcated system under which a contractor may choose to bring a dispute of greater than \$50,000 before an agency Board of Contract Appeals ("BCA") or to the United States Court of Claims.²⁴⁸

244. *Id.* at 101.

245. 68 Stat. 81 (1954) (codified as amended at 41 U.S.C. §§ 321-22 (1994)).

246. Pub. Law No. 95-563, 92 Stat. 2383 (1978) (codified as amended at 41 U.S.C. §§ 601-13 (1994)).

247. Alston et al., *supra* note 180, at 446 (citing S. Rep. No. 1118, 95th Cong., 2d Sess., at 1 (1978)).

248. 41 U.S.C. §§ 606, 609 (1994). If an agency does not have a large enough load of appeals from contracting officer decisions to justify its own full-time BCA, a BCA of another agency may be used to decide appeals. *Id.* § 607(c).

An agency may establish a full-time BCA to decide appeals from the decision of a contracting officer.²⁴⁹ Although part of the agency, the BCA is not related to a division that contracts out the work. There are at least three BCA members on a board.²⁵⁰ Members must have at least five years of experience in public contract law and serve in the same manner as administrative judges.²⁵¹ Procedures followed by a BCA are prescribed by the Office of Federal Procurement Policy.²⁵² The appeals process is a fully adversarial process of discovery, hearings, and written decisions.²⁵³ The ruling of the BCA may be appealed to the U.S. Court of Claims for the Federal Circuit by either the contractor or the agency.²⁵⁴ While such an appeal of a ruling by a BCA may be made, "apart from questions of fraud, determination of the finality to be attached to a departmental decision on a question arising under a 'disputes' clause must rest solely on consideration of the record before the department."²⁵⁵

One may argue that, although it is not a participant in the construction project itself, the agency BCA is part of the agency and would, therefore, be predisposed to rule for the agency. The contractor has the option, however, of utilizing the Court of Claims instead of the BCA. Given that such an option exists, the agency BCA has a vested interest in maintaining at least the appearance of being a fair forum. A contractor may be amenable to using the BCA rather than the Court of Claims if he believes the BCA to be not only fair, but also a quicker solution to the dispute. The average BCA decision is reached within two to four years of its filing.²⁵⁶ BCA decisions can be appealed to the Court of Claims for the Federal Circuit,²⁵⁷ where the standard of review is whether "the decision is fraudulent, or arbitrary, or capricious, or so grossly erroneous as to necessarily imply bad faith, or if such decision is not supported by substantial evidence."²⁵⁸

249. *Id.* § 607(a)(1) (1994).

250. *Id.*

251. *Id.* § 607(b)(1).

252. Alston et al., *supra* note 180, at 452-53 (citing the OFPP *Final Rules of Procedure for Boards of Contract Appeals Under the Contract Disputes Act of 1978*, June 14, 1979, Gov't Cont. Rep. (CCH) ¶ 79,604).

253. *Id.* at 454-56.

254. 41 U.S.C. § 607(g)(1)(A) (1994).

255. *United States v. Carlo Bianchi & Co.*, 373 U.S. 709, 714 (1963) (interpreting the standard of judicial review under the *Wunderlich Act*). Given the quasi-judicial nature of agency BCA's established by the Contract Dispute Act of 1978, it is clear that present day appeals are not to be *de novo* reviews.

256. Maria R. Lamari, Note, *The Role of Alternative Dispute Resolution in Government Construction Contract Disputes*, 23 Hofstra L. Rev. 205, 213 (1994) (citing findings by Barbara Z. Korthals-Altes, *The Applicability of Alternative Dispute Resolution Techniques to Government Defense Contract Disputes*, May 1986, at 3, reprinted in *Administrative Conference of the United States, Sourcebook: Federal Agency Use of Alternative Means of Dispute Resolution* 163 (1987)).

257. Pub. Law No. 95-563, 92 Stat. 2387, § 8(g)(1)(A).

258. *Id.* § 10(b).

D. *California—Arbitration Panels*

In 1968, the case of *Zurn Engineers v. State of California*²⁵⁹ raised the issue of engineer's decision clauses in the state of California.²⁶⁰ *Zurn* concerned a contract with the state for construction of a dam.²⁶¹ The contract authorized the State Engineer to decide claims for additional compensation. Thus, *Zurn* filed a claim with the State Engineer for \$1.2 million of additional work. *Zurn* was awarded only \$127,000.²⁶² According to the contract, the engineer's decision was "[f]inal and conclusive unless it is fraudulent or capricious or arbitrary or so grossly erroneous as necessarily to imply bad faith."²⁶³ *Zurn* sued the State in Superior Court for breach of contract.²⁶⁴ The Superior Court ruled in favor of the contractor in the amount of \$896,000.²⁶⁵ The State of California appealed this decision to the Court of Appeals, where the court found that the State Engineer did not provide the contractor sufficient due process,²⁶⁶ and returned the case for reconsideration by the State Engineer.²⁶⁷ The court, however, upheld the engineer's decision clause, making such decision final absent allegations of fraud or an arbitrary or capricious decision.²⁶⁸

As a result of the *Zurn* decision, the California Legislature passed a law providing for neutral arbitration of all existing state construction contracts.²⁶⁹ Further, an executive order was issued by Governor Edmund G. Brown in 1978 that provided for an arbitration clause in all state construction contracts.²⁷⁰ Although the *Zurn* case settled the law in favor of the engineer's decision clauses in California, the legislature and Governor rendered the decision moot.²⁷¹

259. 138 Cal. Rptr. 478 (Cal. Ct. App. 1977).

260. For a thorough discussion of *Zurn* and the cases which led up to it, see Dreifus, *supra* note 188, at 1-18.

261. *Zurn*, 138 Cal. Rptr. at 481.

262. *Id.* at 485.

263. *Id.* at 480.

264. California's state and local governments have never been covered under the doctrine of sovereign immunity. Dreifus, *supra* note 188 at 84-5.

265. *Zurn*, 138 Cal. Rptr. at 480.

266. *Id.* at 501.

267. *Id.* at 504.

268. *Id.* at 494.

269. "Any dispute arising from a construction contract with a public agency, which contract contains a provision that one party . . . shall decide any disputes arising under that contract, shall be resolved by submitting the dispute to independent arbitration, if mutually agreeable, otherwise by litigation in a court of competent jurisdiction." Cal. Civ. Code § 1670 (West 1995).

270. Dreifus, *supra* note 188, at 96 (Exec. Order B 50-78, dated Dec. 8, 1978).

271. Curiously, the changes made in the wake of *Zurn* did not ultimately benefit the contractor in the case. In the follow-up case of *Pascal & Ludwig, Inc. v. State*, 179 Cal. Rptr. 403 (Cal. Ct. App. 1981), the contractor sought to make use of the new arbitration legislation rather than gain a rehearing with the State Engineer. *Id.* at 404. Alternatively, the contractor argued that the engineer's decision clause should not be enforced because it was a contract of adhesion and contrary to public policy. *Id.* at 408. On the issue of arbitration, the court upheld a trial court ruling that the contrac-

The current California system is codified at section 10240 of the California Public Contract Code. Under this Code, agency contracts provide for arbitration of disputes in front of a seven member arbitration committee. Three of the committee members are appointed by the Governor,²⁷² one member is appointed by each of the three major government agencies that contract for construction work (Department of General Services, Transportation, and Water Resources),²⁷³ and one non-voting member is appointed (Director of the Office of Administrative Hearing).²⁷⁴ The members appointed by the Governor must have experience working for a general contracting firm.²⁷⁵ Therefore, the composition of the arbitration board is evenly balanced between potentially pro-agency and pro-contractor voting members. Because the arbitration board may only rule on issues involving monetary damages, the court system is potentially available where other remedies are sought by the parties.

IV. A PROPOSAL FOR REFORM

Public works projects account for a major portion of government budgets at the federal, state, and municipal level. With great amounts of tax revenue at stake, governments seek to prevent corruption, minimize construction costs, and generally provide a fair deal for the taxpayer. These policies, however, place contractors at a major disadvantage and are often unfair. Many contractors choose to avoid government projects.²⁷⁶ As a result, competition is reduced and prices are higher.²⁷⁷ Those contractors that remain are often those who have mastered the bureaucracy.²⁷⁸ The less fortunate become the system's victims.

This part looks at the inequities of public works contracting, showing how the system is unfair to contractors. It continues by discussing sealed competitive bidding, arguing for its continued use despite its flaws. Finally, this part proposes reforms to the public works procure-

tor had been given an adequate legal remedy by being given a rehearing with the State Engineer and that, therefore, arbitration was not available to the contractor. *Id.* at 409. The court also rejected the contractor's contention that its subsequent ruling in *Graham v. Scissor-Tail, Inc.*, 623 P.2d 165 (Cal. 1981) (standardized contract where one party has superior bargaining power may be considered a contract of adhesion and be held unenforceable) should be applied in this case. 179 Cal. Rptr. at 409.

272. Cal. Pub. Cont. Code § 10245(a) (West 1985). Originally, the three Governor appointees were construction industry persons appointed by the Associated General Contractors of California. Dreifus, *supra* note 188, at 101 (Executive Order B 50-78, item 4, Dec. 8, 1978).

273. Cal. Pub. Cont. Code § 10245(a) (West 1985).

274. *Id.* § 10245(c) (West 1985).

275. *Id.* § 10245(a) (West 1985).

276. Ethics Reform, *supra* note 3, at 470-72 (New York State Commission on Government Integrity report citing a lack of bidders for city contracts).

277. *Id.* at 474-77 (noting higher prices as a result of the lack of competition).

278. *Id.* at 472.

ment system, focusing on ways to prevent disputes and, if needed, settle disputes fairly.

A. *Inequities of Public Works Contracting*

Design and construction of building projects can be quite long and complicated.²⁷⁹ The multiple promises that make up a construction contract are intricately intertwined, making modification to the contract difficult. In addition, construction provides many opportunities for change orders subsequent to the award of a contract.²⁸⁰ The divergent interests of an owner in getting the most product for his money, and the contractor in minimizing expenditures on a fixed fee, make construction disputes inevitable. Public works projects cause particular problems because of the inequitable position taken by the government in bidding projects and in settling disputes.

Competitive sealed bidding procedures that predominate in government procurement have inherently adhesionary characteristics.²⁸¹ By reducing competition to the single variable of price, terms and conditions of a bid are essentially non-negotiable. This process also allows the government to unfairly allocate risks to the contractor, particularly risks that are not under the contractor's control.²⁸² This risk allocation is particularly unfair because the competitive bidding system coerces contractors to undervalue risk. Under this scenario, the government may take more risks than is desirable because it is not forced to internalize those costs.

Adding to the government's advantage is its superior position in dispute resolution that originated in the doctrine of sovereign immunity.²⁸³ The sovereign nature of government makes suing the government only possible with its permission. Although this immunity has been waived to various degrees, government has typically reserved the upper hand in dispute resolution by drafting contracts that specify methods of dispute resolution that are not always fully neutral. In addition, many of the day-to-day decisions on a project that affect the scope and interpretation of a contract are made by an architect. Government agencies often use in-house architects, creating a direct conflict when these architects are forced to make discretionary decisions regarding the rights of a contractor as against the government owner.²⁸⁴

279. *See supra* parts I.B, I.C.

280. *See supra* part I.E.

281. *See supra* part II.C.1.

282. *See supra* part II.C.2.

283. *See supra* part II.E.

284. *See supra* part II.D.

B. *Sealed Competitive Bidding*

Sealed competitive bidding creates many problems, which grow out of the adhesions aspects it creates in public works contracts.²⁸⁵ It is a complex process that requires strict procedures and bureaucracy. Assuming that both are considered qualified, a company with a bad or mediocre history is given the opportunity to compete on the same basis as a company with a track record of satisfactory performance with an agency. The value of sealed competitive bidding, however, does not lie in the good it does but in the bad it prevents.

Sealed competitive bidding affords the opportunity for public scrutiny and makes it more difficult for corruption in the award process. Because of the large sums of money involved, bid determinations left to subjective discretionary factors would present too great an opportunity for influence peddling. The process is also benefited by enlistment of unsuccessful bidders acting as watchdogs.

C. *A Proposal*

Our system of public works contracting leaves much room for improvement. Rather than looking to secure the upper hand for the government, procurement policies need to focus on increasing competition by attracting competent and reputable companies to do business with the government. The best way to achieve this goal is to make the system completely fair. Nowhere is fairness put more to the test than in the realm of dispute resolution.

The following proposal attacks the lack of fairness in dispute resolution on two levels. On one level, we can enhance fairness by preventing conflict. By being more precise about what is being purchased, both the government and the contractor can better define the contractual relationship, as well as properly allocate risk between the parties. On another level, fairness will be enhanced if neutral fora for dispute resolution are offered. Full and fair methods of dispute resolution will place the government and contractor on even bargaining positions, making it more likely that disputes will be settled on a mutually-agreeable, negotiated basis.

1. Preventing Disputes

The primary source of dispute in construction is change orders. While it is impractical to think that change orders can be totally eliminated, there are many ways in which they may be reduced. As the owner, the government controls many sources of potential dispute. Therefore, government agencies that contract for public works should take a proactive role in preventing disputes.

285. See *supra* part II.C.

The scope of work included in a project should be defined with an eye towards specificity. If the type or design of a system is important, it must be designed and detailed to enable the contractor to be sure of what exactly he is bidding. Even if there are subsequent changes, it is best to establish at the outset a firm basis from which adjustments may be made.

Clauses that seek to allocate risks to the contractor should not be used in a competitive bid situation. Unlike costs for materials and labor that can be calculated on the basis of numerical quantities and methods of construction, risk is a component of the bid that must be assessed on a subjective basis; in fact, owners seek to minimize the appearance of risk in order to obtain favorable prices. Because the cost associated with risk is embedded in the price offered in the bid, sealed bid competition rewards those who undervalue the true cost of such risk to the detriment of those who attempt to accurately assess the risk. Once signed, the owner uses the contract to enforce the risk allocation as it is established in the agreement.

Elements of risk not under the contractor's control should be removed from competitively bid public contracts. The government should pay for all contingent conditions when and if they are encountered. The first means of removing the risk is eliminating the possibility that a contingent condition will arise in the first place. During the design phase, government projects should involve more exploration of field conditions so that the contractor's bid can better reflect actual conditions.

Where information on a given condition is available, it should become the objective basis of the bid. For example, when boring logs show bedrock at a given depth, the contractor should be able to rely on this information in his bid. Where adjustments can be reasonably expected, provisions for modifying the contract should be made a part of the bid price. For example, unit prices should be used for adjusting the price based on the condition actually encountered. Where alternate scenarios may be envisioned, prices for those conditions should also be solicited within the bid.

Despite all of this, an owner may still want to eliminate the problems of risk. This can be achieved through capital planning which can provide some measure of guarantee in order to assure that sufficient funds have been allocated. This can be achieved by paying a fixed up-front cost. Though it is here argued that contractors are not capable of taking on this risk, it should be possible to find a third party who is both willing and capable of doing so—this, in fact, is the whole concept behind insurance.

Insurance could be purchased on a project-by-project basis. Since the amount of risk will vary with the precautions taken, diligence in investigating conditions may be rewarded in the form of reduced premiums. Because the premium is not masked by the price of goods and

services, and because the carrier is taking on the risk voluntarily, the owner ends up paying the true cost of such risk.

2. Settling Disputes Fairly

Even with good faith and reasonable planning by both parties in the bidding phase, disputes will inevitably arise. Since a dispute over one aspect of a project may affect other aspects, such as time and money,²⁸⁶ dispute resolution in construction really has two components—initial rulings and final dispositions. In both cases, public works contracting is problematic. If the ultimate means of resolving the dispute is fair and impartial, however, the initial ruling is less critical. Therefore, government agencies should adopt a policy of negotiated dispute settlement backed by a full and fair adjudication before a neutral party.

An architect paid by the government or, in the case of many public agencies, a direct government employee, cannot be neutral toward the owner. In fact, the dispute that the architect is charged with settling may have in fact been caused by an error or omission by the architect herself. Nonetheless, it is important that someone intimately familiar with the project be empowered to make preliminary rulings in order to allow construction to proceed without delay. Short of hiring a neutral party to be on hand in anticipation of disputes, the architect is in the best position to make an initial ruling. A wrong ruling may be corrected afterwards so that one party is not unfairly enriched. If no ruling were made until a neutral party could sit and hear all of the facts, delays to the project would hurt all parties.

The only way to assure fair disposition of a dispute is to offer final adjudication of the issue by a neutral party. Engineer's decisions clauses clearly do not meet this benchmark, because an employee of the government agency involved in the dispute is ruling on the dispute, and could not be considered neutral. Such a decision could easily favor the agency without violating the arbitrary, capricious, or bad faith standard used by the court in granting judicial review. Panels which are primarily chosen by the agency, such as New York City's PPD, are also non-neutral.

Adjudication by a court, an option under the federal system, would offer the best chance of achieving fairness. It would provide full due process in an adversarial proceeding and produce a reasoned, written decision. While the judge would be knowledgeable in the law, she may lack knowledge in construction practices. In addition, relying on the courts for the adjudication of public works construction cases would add to the huge backlog of cases already handled by our courts. Additionally, time becomes a factor that militates against a fair result.

286. See *supra* part I.A.

Cash-strapped contractor plaintiffs may be forced to settle or may not survive long enough to see their cases heard.

Of the forums currently used by the government in public works dispute resolutions, the ABA, federal agency BCA, and California arbitration panel models each offer some promising aspects that would make them appropriate for particular situations. In each of these cases, board members are full-time members chosen based on an expertise in construction practices. That full-time members are chosen for a term of years, rather than for the particular conflict as in the New York City PPD, provides continuity; also, these members need not fear that their jobs depend upon the result of their decision. Each of these boards offers the possibility for precedential value through the use of reasoned written opinions.

Of these boards, the ABA model provides the most neutral forum because its board has no ties to the agency involved in the disputes. In contrast, the BCA under the federal system is actually a part of the agency. As a check, however, the contractor could elect to have his dispute heard in the Court of Claims. Under the California system, three of the six voting members are appointed by the agencies most likely to be parties to a public works construction dispute. Although the other three members appointed by the Governor would seem to present a balance for the contractor, the Governor is not bound to nominate contractor-friendly board members. As a result, the California arbitration board may be neutral, but is not necessarily so.

Because some municipalities may not have the volume of decisions to merit setting up their own board, states should make their boards accessible to local governments. Small towns or counties should also consider using neutral party arbitration, favored by private construction parties. The Arbitration Association of America has a construction division, which has formal rules particular to the construction industry. The use of arbitration in construction disputes has a long and successful history. Panels of neutral arbitrators may include former judges and construction industry personnel. Although the arbitration process does not lead to the development of case law, it can be significantly cheaper and result in swifter justice.

Agencies should adopt a policy that promotes amicable dispute resolution through good faith negotiation. Having a fair and neutral forum available to resolve disputes not only helps assure that the correct result is obtained, but also eliminates unfair bargaining positions. A negotiated settlement saves both parties resources in reaching an adjudicated settlement.

CONCLUSION

Fairness in governmental construction contracting is both a worthy goal and beneficial to taxpayers. Unfortunately, complete fairness in

government contracting is the exception rather than the rule. Although sovereign immunity granted government superior position in dealing with contractors, public agencies ceded some of this power to make this relationship more equitable. At the same time, courts have consistently allowed governments to dictate the terms of construction agreements. The combination of such standardized agreements and sealed bid, competitive bidding have made for less than completely fair results.

Despite judicial rulings that enforce unfair bargains such as those that included engineer's decision clauses, there are indications that change is afoot. Legislatures have come to embrace some of the suggestions that the ABA proposed in its Model Code for Procurement. This Note endorses reform of procurement procedures in the construction services industry and suggests that changes should be addressed at multiple levels.

One of the hidden factors of unfairness is the allocation of risk. By placing risk in the hands of competitive bid contractors, agencies reward those who disregard or undervalue risk. This Note suggests that agencies should minimize risk by exploring hidden conditions before bidding drafting contingencies into bid documents. Where an agency is unwilling to take on the cost of unforeseen conditions, it should contract with third parties that are better equipped to insure against such risk.

Finally, a fair means of final adjudication must be in place for instances when disputes inevitably arise. The use of neutral parties in such adjudication is necessary not only to achieve a fair result, but to equalize bargaining power so that both sides have incentives to negotiate a settlement in good faith.

One could argue that contracting officers in public agencies should be given discretion in dealing with bad contractors who win contracts through public bidding. There will always be those who abuse the system. Engineering decision clauses and other non-neutral adjudication systems provide such discretion. But the dangers in these procedures outweigh their advantages. Though the vast majority of those working in the public sector look out for the public good, unfair dispute resolution provisions create the potential for abuse. Proper legal channels must be used to curb contractor abuses. "Cutting corners" on due process is not the answer.

When dealing with the government, those of us who have faith in our legal system ultimately believe that we should be treated fairly. Those who have not be treated fairly will avoid dealing with the government. Such has been the case with governmental construction contracting. Though forces of change continue to act, there is much work to be done. By earning the trust of those who contract with the government, we all stand to gain.

