BALDWIN HASPEL BURKE & MAYER LLC
LAW OFFICES

FEBRUARY 2013

Louisiana Construction Law Update

The ***Construction Law Update*** is published by Baldwin Haspel Burke & Mayer, LLC for the benefit of its clients and others having interest in the construction industry. It includes discussions on Louisiana state and federal court decisions, legislative developments, and tax issues concerning construction-related matters. For further information on the decisions and legislative developments, contact **John Stewart, Jr.** at (504) 585-7846 - jstewart@bhbmlaw.com or **Stuart Richeson** at (504) 585-7839 – sricheson@bhbmlaw.com.

At the end of this newsletter, you'll find a section titled *Tax Law*. It contains a snippet from Baldwin Haspel Burke & Mayer's ***Tax Law Alert***, which provides information on updates and changes in tax law on both the state and federal level. For information on tax-related issues, please contact **Jason Alley** at (504) 585-7819 - jalley@bhbmlaw.com**,** or Matt Miller at (504) 585-7867 - mmiller@bhbmlaw.com.

For information about the firm, please visit our website at www.bhbmlaw.com.

INDEMNITY ALLOWED UTILITY UNDER THE LOUISIANA OVERHEAD POWER LINE SAFETY ACT

The Louisiana Overhead Powerline Safety Act, L.R.S. 45:141, et seq., provides that no person shall perform any functional activity if it is possible the person doing so shall move or be placed within ten feet of any high voltage overhead line, or if it is possible for any part of any tool, equipment, machinery, or material used, handled, or stored by such person to be brought within ten feet of any high voltage overhead line or conductor during the performance of such function or activity, without first promptly notifying the owner or operator of the line prior to the scheduled commencement of the work. The work shall be performed only after satisfactory mutual arrangements have been negotiated between the owner or operator and the persons responsible for the work to be done. If a violation of the Act results in physical or electrical contact with any high voltage overhead line, the person violating the Act shall be liable to the owner or operator for all damages, costs or expenses incurred as a result of the contact.

The Louisiana Supreme Court recently interpreted the Act, and held it establishes a right of indemnity in favor of the owner or operator against a person violating the Act, even if the utility company is at fault, and the individual claiming damages is an employee of the person who violated the Act and from whom indemnity can be claimed. The indemnity extends to damages attributable to the fault of the utility company. In this particular instance, the Court was not able, on the record presented, to make a determination of whether indemnity was actually owed, and remanded the matter to the district court for further proceedings. *Moreno v. Entergy Corporation*, 2012-0097 (La. 12/4/12), 2012 WL 6015581.

CONTRACTOR CONVICTED OF THEFT

Wayman Frost, while doing business as Sunrise Builders of Louisiana, LLC, entered into a contract with Elaine Robertson to rebuild her home which was damaged by Hurricane Katrina. Robertson made several payments to Frost. Frost did not perform the work for which he was paid, and, despite requests by Robertson, failed to return the payments. Frost was convicted of theft under L.R.S. 14:67. He appealed the conviction contending he had no intent to permanently deprive Robertson of her money at the time he took it. The court of appeal found the statute is not limited exclusively to situations in which a defendant has the intent to defraud at the time he takes possession, but includes a defendant's misappropriation by fraudulent conduct of what is already in his possession. Frost's actions of avoiding contact with Robertson, ceasing work on her house, and not repaying the money he took from her could, according to the court of appeal, be construed by a reasonable fact-finder as evidence of his intent to deprive her of the money permanently. The conviction was affirmed. *State of Louisiana v. Frost*, 2011-1658 (La.App. 4th Cir. 9/5/12), 99 So.3d 1075.

CLAIMS BY A CONTRACTOR AGAINST A DESIGN PROFESSIONAL

The Louisiana First Circuit Court of Appeal recently considered whether a construction contractor could assert a claim against a design professional, with whom it did not have a contract, for damage resulting from design errors. The court held that absent privity of contract, the contractor may not assert a cause of action against the design professional based on breach of contract, but the contractor was not precluded from asserting a cause of action in tort based upon alleged negligence. *Greater Lafourche Port Commission v. James Construction Group, LLC*, 2011-1548 (La.App. 1 Cir. 9/21/12), 2012 WL 4320228.

CLAIM FOR DELAY DAMAGES FOR DOTD CONTRACT

The Louisiana Department of Transportation and Development contracted with Barber Brothers Contracting Company, LLC for a highway project in Baton Rouge. The contract provided that DOTD would notify all known utility companies, pipeline owners or other parties affected by the work and endeavor to have the necessary adjustments of public or private utility fixtures, pipelines and other appurtenances within or adjacent to the limits of construction made as soon as possible. The contract also contained a provision stating it was agreed the contractor had considered in its bid all permanent and temporary utility appurtenances in their present or proposed relocated positions and that no additional compensation would be allowed for delays, inconvenience or damage sustained due to interference from the said utility appurtenances or the operation of removing them. Further, when the engineer determines the contractor is experiencing significant delays in the controlling items of work because of delays by others in removing, relocating or adjusting utility appurtenances, contract time credits will be considered for such delays.

Some of the public utilities failed to relocate their facilities in time to prevent delays. Contract changes were executed by DOTD and Barber increasing the contract time, but the changes did not increase the contract price. Barber sued for damages alleging it incurred expenses as a result of the utility delays, and was also assessed stipulated damages by DOTD when the utility delays delayed the installation of the storm drainage system. Both DOTD and Barber filed cross-motions for summary judgment on the issue of whether Barber's claim for damages relating to delays was waived. The trial court granted Barber's motion. DOTD appealed.

L.R.S. 38:2216(H) provides that any provision in a public contract which purports to waive, release, or extinguish the rights of a contractor to recover costs of damages, or obtain equitable adjustment, for delays in performing such contract, if such delay is caused in whole or in part by acts or omissions within the control of the contracting public entity or persons acting on behalf thereof, is against public policy and is void or unenforceable and shall be severed from the other provisions of the contract. DOTD contended the statute was not applicable to the issues since L.R.S. 48:250(A) provides that DOTD contracts are to be exclusively governed by Title 48. The statute provides it shall exclusively govern the contracts of the Department of Transportation and Development or let by the Department on behalf of other political subdivisions of the state in addition to the laws of the state relating generally to obligations and the Department not in conflict with it.

The court of appeal held DOTD's argument overlooked the provision for the applicability of other laws not in conflict with Title 48. The court acknowledged it had previously held the provisions of Title 38 remain

applicable to DOTD contracts where they do not conflict with those of Title 48. L.R.S. 38:2216(H) applies to any contract awarded by the State of Louisiana, or any agency, board, commission, department or public corporation of the State. There were no conflicting provisions in Title 48, and L.R.S. 38:2216(H) was applicable to the contract.

DOTD also argued that because equitable adjustment was not waived by the contract, L.R.S. 38:2216(H) was not violated. The court of appeal disagreed, finding the statute does not say that to be prohibited, a contract must waive both cost of damages and equitable adjustment. It states a provision which purports to waive cost of damages or equitable adjustment is prohibited. The judgment of the district court was affirmed. *Barber Brothers Contracting Company, LLC v. State of Louisiana, Through Department of Transportation and Development*, 2011-2305 (La.App. 1 Cir. 11/8/12), 2012 WL 5456099.

ARBITRATION CLAIMS AGAINST A NON-PARTY TO THE ARBITRATION AGREEMENT

ConstructionSouth, Inc. filed an arbitration proceeding against 3901 Ridgelake, LLC for payments due under a contract which included an arbitration clause. CSI later filed a lawsuit against Gayle O. Jenkins, the managing member of Ridgelake, asserting claims related to the contract. Jenkins filed a motion to stay the lawsuit, averring the dispute was subject to the arbitration proceeding. The court ordered the parties to the lawsuit to arbitrate the claims. The arbitrator entered an award in favor of CSI and against Ridgelake and Jenkins as the managing member of Ridgelake. The arbitrator found Jenkins and Ridgelake were alter-egos of one another, and Jenkins was personally liable for Ridgelake's obligations. Ultimately, the court confirmed the arbitration award. Jenkins appealed.

One of the issues discussed by the court of appeal was whether arbitration can be demanded against a non-party. In this instance, Jenkins was found to have consented to arbitration of the claims against her. The court found, additionally, that non-signatories to arbitration agreements can be compelled to arbitrate when the action against a non-signatory party is dependent upon interpretation of the contract that is the subject of the arbitration. In this instance, the claims against Jenkins, personally, depended upon the outcome of the claims against Ridgelake, and she could be compelled to arbitrate. The arbitration award was affirmed. *ConstructionSouth, Inc. v. Jenkins*, 12-63 (La.App. 5 Cir. 6/28/12), 97 So.3d 515, *writ denied,* 2012-1756 (La. 11/2/12), 99 So.3d 676.

CLAIMS UNDER THE NEW HOME WARRANTY ACT LIMITED TO ACTUAL PHYSICAL DAMAGE

Mike Gines purchased a new home built by D.R. Horton, Inc. The air conditioning system was not large enough to maintain an appropriate temperature. Gines sued Horton for reimbursement for a replacement air conditioning system, increased energy bills caused by the system, and attorneys fees and costs. Horton filed a motion to dismiss, contending Gines failed to state a claim under the New Home Warranty Act because the Act requires that an alleged defect result in actual physical damage to the home, there was no physical damage, and the contract between Gines and Horton did not contain a waiver of the physical damage requirement. The district court granted the motion. Gines appealed.

The United States Court of Appeals for the Fifth Circuit found the Act provides the exclusive remedy against a builder for a purchaser of a newly constructed home with a construction defect, and the Act excludes from coverage under its warranties any condition which does not result in actual physical damage to the home. Since there was no physical damage alleged, and the Act provided the exclusive remedy against the contractor, Gines' lawsuit was required to be dismissed. The judgment of the district court was affirmed.

The question might well be asked what remedy does the purchaser have under these circumstances? The answer is, apparently, he has no remedy. The court of appeals noted the moral of the story to avoid this harsh result is for the buyer of a newly constructed home in Louisiana to obtain an express waiver of the actual damage requirement of the New Home Warranty Act in the contract of sale. *Gines v. D.R. Horton, Incorporated*, 699 F.3d 812, (5th Cir. 2012).

PAYMENT TO A CONTRACTOR FOR WORK PERFORMED

Alicia Ayo contracted with Thomas Henderson, d/b/a Henderson Home Repair Service, LLC to repair hurricane damages to her home in New Orleans. Ayo made an initial down payment of $20,000.00, although the payment was late according to the contract. Ayo terminated Henderson's contract, and did not pay him for work performed. Henderson sued Ayo. Ayo filed a reconventional demand against Henderson. The trial court awarded Henderson $20,000.00, and dismissed Ayo's reconventional demand. Ayo appealed.

Henderson sought only to be compensated for the work completed. The court of appeal found La. Civil Code art. 2765 provides the owner of a construction project has the right to terminate a contract to build if the contractor has commenced work on the project, but the owner must pay the contractor for his completed work. It held the trial court was not clearly wrong in finding Henderson was entitled to the award rendered by the trial court for the work done. Under art. 2765, his claim was in *quantum meruit* which was properly awarded by the trial court.

Ayo's reconventional demand was found to be merely a claim for damages for delay in completion of the contract. Since, however, Ayo violated the contract by her delinquent initial payment, the court of appeal found she could not claim Henderson's delay in performance caused a loss to her. Her own delay caused whatever loss she might have incurred, if any. *Henderson v. Ayo*, 2011-1605 (La.App. 4th Cir. 6/13/12), 96 So.3d 641.

LIABILITY OF AN INDIVIDUAL MEMBER OF AN LLC

Michael and Carrie Matherne contracted with Matthew Barnum and his construction company, Barnum Construction, LLC, for the design and construction of a bulkhead, boat slip with lift, and deck with walkways at their waterfront property in Springfield, Louisiana. The bulkhead and deck had to be rebuilt. The Mathernes sued Barnum individually and the LLC. The trial court rendered judgment against both.

Barnum contended the contract for the work was with the LLC, and he could not be personally responsible for damages. L.R.S. 12:1320 insulates members of a limited liability company from personal liability for a debt or obligation of the limited liability company, but provides a cause of action against a member of a limited liability company because of any breach of professional duty, as well as for any fraud or other negligent or wrongful act by such person. The court of appeal found Barnum, individually, designed and constructed the work for the Mathernes, and was not acting solely in his capacity as a member of the limited liability company. Thus, he was subject to personal liability. *Matherne v. Barnum*, 2011-0827 (La.App. 1 Cir. 3/19/12), 94 So.3d 782, *writ denied,* 2012-0865 (La. 6/1/12), 90 So.3d 442.

LIENS AND CLAIMS UNDER THE PRIVATE WORKS ACT

The Louisiana First Circuit Court of Appeal considered whether a lessor of equipment, although it did not timely provide the owner of a project with a copy of the equipment lease, had a valid lien against the property or claim against the owner when a lien was timely filed. The court held, since the lessor had not delivered a copy of the lease to the owner within ten (10) days after the equipment was first placed on the site, as required by the statute, the lien was invalid. The lessor, nevertheless, could maintain a claim against the owner for payment. *Hawk Field Services, LLC v. Mid America Underground, LLC*, 47,078 (La.App. 2 Cir. 5/16/12), 94 So.3d 136, *writ denied*, 2012-1660 (La. 10/26/12), 99 So.3d 652.

DAMAGES FOR DEFECTIVE WORK

In considering an appeal of an award by the trial court to plaintiffs of the amount paid to the contractor where the work was found defective, the Louisiana Fifth Circuit Court of Appeal reversed the judgment and remanded the matter to the trial court for a determination as to the cost of repairs that should be awarded. The work was not found to be so defective as to render it useless, and the testimony at trial did not establish the work could not be repaired. In that instance, the appropriate measure of damages is the amount necessary to repair the defects. The record before the court of appeal did not contain sufficient evidence to determine those damages. If the work is so defective that it would be useless, the loss sustained is the price paid for the construction, plus removal

thereof, and the cost of restoring the premises to its former condition. *Melancon v. Tri-Dyne Tele-Pier, LLC*, 2011-1055 (La.App. 5 Cir. 5/31/12), 95 So.3d 576.

EXTENSION OF TIME FOR ABNORMAL WEATHER CONDITIONS, AND CERTIFICATION OF APPLICATIONS FOR PAYMENT

The First Circuit Court of Appeal found that a contract provision allowing extensions of time for abnormal weather conditions did not mean extensions would be granted for any adverse weather conditions. The court held the amount of rain at issue did not amount to abnormal weather conditions.

The contractor's surety objected to an award against it for payments made by the owner to the contractor which the owner later claimed were for defective work. The applications for payment were certified by the engineer. Each certification stated the application met the requirements of the contract documents. The court of appeal found the certifications did not state the work had been performed in a proper manner or that the final product would be acceptable to the owner. Further, the contract documents specifically provided the engineer's certification for payment is a representation to the owner, not the contractor, that the work is in accordance with the contract documents to the best of the engineer's knowledge, information and belief. The court of appeal found the surety was liable for the payments. *Hartec Corporation v. GSE Associates, Inc.*, 2010-1332 (La.App. 1 Cir. 2/24/12), 91 So.3d 375, *writ denied*, 2012-0972 (La. 6/22/12), 91 So.3d 972.

PUBLIC WORK BID NOT CONSIDERED NON-RESPONSIVE

The plans and specifications for a dredging project for the Greater Lafourche Parish Commission provided that all irregular bids would be rejected, and included a condition that a bid would be considered irregular if it did not contain a unit price for each pay item listed, except in the case of authorized alternate pay items. The presumptive low bidder included monetary values for three multiple quantity items in the unit price and unit price extension columns, but for two single quantity items completed only the unit price extension column and left the unit price column blank. The Louisiana Attorney General concluded the failure to provide a monetary value for the unit price of a single quantity item did not render the bid non-responsive. The pay items at issue did not involve items with multiple quantities. Therefore, the requirement to provide a unit price for such items was inapplicable. Attorney General Opinion, 12-0125 (7/18/12).

ABILITY OF AN UNLICENSED CONTRACTOR TO OBTAIN PAYMENT FOR WORK

The Louisiana First Circuit Court of Appeal considered the question of whether an unlicensed contractor who represents he is licensed is precluded from recovering damages for unjust enrichment or quantum meruit for work performed. The court found the only instance where fraud would prevent an unlicensed contractor from recovering under the doctrine of quantum meruit is when it entered into a contract with a public body. In this instance, there was no contract, and the work was not performed for a public entity. The contractor was allowed to recover. *Sam Staub Enterprises, Inc. v. Chapital,* 2011-1050 (La.App. 4 Cir. 3/14/12), 88 So.3d 690.

TAX LAW ALERT

RECHARACTERIZATION OF RENTAL INCOME AS ACTIVE UNDER SELF-RENTAL RULE

In Veriha v. Commisioner, 139 T.C. No. 3 (August 8, 2012), the Tax Court held that income that the taxpayers received must be characterized as active income under the "self-rental rule or the recharacterization rule" of Treas. Reg. §1.469-2(f)(6). The taxpayer was the sole owner of a trucking company that was structured as a C corporation. Two other entities leased equipment to the C corporation. One was an S corporation, 99% owned

by the taxpayers, which generated net income from the leases, and the other was a single member LLC, reported on Schedule C, which reported a net loss. The taxpayers initially reported the net income from the S corporation as passive income, and the loss on Schedule C as a passive loss.

The IRS determined that, under Treas. Reg. §1.469-2(f)(6), each tractor and each trailer must be considered to be a separate "item of property" and that the income that the taxpayer received from the S corporation must be recharacterized as active income because it was received for the use of property in a business in which the taxpayer materially participates. The taxpayer argued that they were not individually leasing property, but rather that the entire fleet of tractors and trailers was leased to the corporation and should be treated as one item of property, thus resulting in a single net income or loss from the combined income of the two operations.

The court ruled in favor of the IRS on the issue of whether each item was a separate item, noting that the corporation had signed a separate lease for each tractor or trailer, thus treating each one as a single item. The court further held that the S corporation income must be characterized as active because of the self-rental rule.

BALDWIN HASPEL BURKE & MAYER LLC
LAW OFFICES

Contact Us:

Baldwin Haspel Burke & Mayer, LLC

1100 Poydras Street, Suite 3600

New Orleans, LA 70163

www.bhbmlaw.com | bhbm@bhbmlaw.com

Phone: (504) 569-2900 | Fax: (504) 569-2099

If you would like to receive an electronic or print copy of this newsletter, please visit www.bhbmlaw.com/signup