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Education Law News

Public Works Contracts:

Recent Views of the Courts

California Supreme Court, February 4, 2002: Public Entity May Not Be Held Liable For Abandonment Of Contract

In *Amelco Electric v. City of Thousand Oaks* (2002) 27 Cal.4th 228, the Supreme Court of California held that the “abandonment theory of liability” does not apply against a public entity. Moreover, the Court found, a trial court had erred in allowing a jury instruction on a “total cost theory of damages.”

Facts

In 1992, the City of Thousand Oaks (City) solicited bids for electrical work to be performed in the construction of a Civic Arts Plaza. Of five bids submitted, the lowest was a bid of \$6,158,378 by Amelco Electric (Amelco). During the ensuing two-year period of construction, City submitted to its contractors a total of 1,018 sketches, either clarifying or modifying the original contract drawings; of these, 248 sketches affected electrical cost. In response, Amelco separately requested 221 change orders, ultimately agreeing with City on 32. As a result of these change orders, City paid Amelco an additional \$1,009,728 above the contract price. Amelco conceded that, during the same period, it had performed work inefficiently, but it claimed that these inefficiencies were the result of the large number and the inadequacies of City’s sketches, and a consequence of conflicting directives received from City’s general contractor.

In January 1995, Amelco submitted a claim for \$1.7 million in alleged “noncaptured costs” arising from the change orders. City denied the claim. Thereafter, Amelco sued City, alleging abandonment and breach of contract and increased its claim to \$2,224,842. A jury found in Amelco’s favor and awarded \$2,134,586 on each count (i.e., \$2,134,586 in costs for abandonment, and an equal amount in damages for breach of contract). The Court of Appeal affirmed, holding that: (1) abandonment could be applied to a public contract, and (2) that the jury was not improperly instructed as to the measure of damages.

In the past, California courts have held that a public contract may not be abandoned.

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Prior History of the Case

Private parties may be deemed to have impliedly abandoned a contract when work, not provided for in a contract, and not properly documented with change orders, is performed in sufficient quantity and over a period of time sufficient to render the final project “materially different” from the project contracted for. Under such circumstances, the contract and any addenda are deemed “abandoned,” and the contractor is entitled to recovery of the reasonable value of its work.

Despite this, California courts have denied that a public contract may be abandoned. This conclusion is drawn from the generally accepted principle that a contractor who bids on a public contract knowingly submits to rules of mandatory competitive bidding; accordingly, the contractor “acts at its own peril” if the contractor incurs costs or renders services not specifically provided for under the contract.

The Court’s Decision

Abandonment theory, the Court held, is fundamentally opposed to the public policy underlying California’s competitive bidding statutes. Under section 201062 of the Public Contract Code, “general law cities” are required to submit any contract in excess of \$5,000 to competitive bidding; the contract must be awarded to the lowest responsible bidder. Mandatory competitive bidding on public contracts is, thus, designed to protect the interests of the tax-paying public from the interests of the contracting parties. Allowing a contractor to recover under a theory of abandonment, said the Court, would convert this fundamental purpose of the competitive bidding process. Accordingly, Amelco could not recover its costs for extra work on a theory of abandonment.

The Court next turned to the matter of damages. City did not dispute its liability for breach of contract, but contended that the jury was improperly instructed as to the method of calculating damages. If City had breached or abandoned its contract with Amelco, the jury was instructed, then Amelco was entitled to “the reasonable value of the work performed by it less the payments made by the City.” In essence, this is a “total cost” theory of damages (i.e., damages are calculated as the difference between the contract price and the total cost of performance). Courts, however, disfavor the total cost method, preferring, instead, the more equitable “actual cost method.” (By this method, actual costs are documented and liability is apportioned among the parties.)

In order to assert a total cost claim to damages a party must satisfy the four-part test prescribed in the case, *Servidone Construction Corp. v. United States* (1991) 931 F.2d 860. Under that standard, the party must establish: (1) the impracticality of proving actual losses directly; (2) that the party’s bid was reasonable; (3) that its actual costs were reasonable; and (4) that it was not responsible for the added costs. Even assuming that Amelco had established the first three elements of the four-part test, the Court found that it had *not* established the fourth. Since Amelco had failed to show that it was not itself, at least, partly responsible for its additional costs, the instruction that City’s breach or abandonment of the contract entitled Amelco to total cost-based recovery of damages was improperly given.

Courts prefer the “actual cost method” of calculating damages rather than the “total cost” theory.

Court of Appeals, Second Appellate District, January 22, 2002: Absent an Award of Contract, Breach of Contract and Forfeiture of Bond May Not Apply

In a recent unpublished and, therefore, non-precedential decision, the Court of Appeal held that where the lowest bidder on a public contract seeks to withdraw its bid prior to an award of the contract, no breach of contract exists, nor is the contractor's bid bond forfeited. (*Compton Unified School District v. Universal Construction Maintenance Integration Company, Inc.* (Cal. App. 2d Dist., Jan. 22, 2002, No. B144260) 2002 WL 80261.)

Facts

In 1998, Compton Unified School District (CUSD) called for competitive bids on a school modernization project. Due to a clerical error (the inadvertent omission of a zero), general contractor, Universal Construction Maintenance Integration Co. (Universal), submitted a bid some \$300,000 below its intended bid, and \$262,000 lower than the second lowest bid. As a condition of its bid submission, Universal had obtained a bond to cover 10 percent of the total \$1,001,000 bid amount. Universal discovered its error and, within three days, informed CUSD that it would withdraw its bid. Two months later, CUSD sent Universal a letter stating that Universal's notice of withdrawal failed to comply with state law, and demanding it pay \$262,000, as the difference between Universal's bid and the second lowest bid.

Evidence suggested that both parties understood Universal's notice of withdrawal to be a "request," and that Universal understood that it could not unilaterally withdraw its bid. In this respect, CUSD had authority under state law, and the decision to consent to Universal's withdrawal of its bid was a matter within CUSD's power and discretion. Prior to its January 1998 demand, CUSD had neither communicated with Universal regarding its request to withdraw, nor submitted the bid to the state agencies responsible for bid approval. Rather, faced with a November deadline to obtain state approval and secure funding for its school modernization project, CUSD "removed Universal from consideration," and awarded the contract to the second lowest bidder.

The Court's Decision

At issue, both in the trial court and before the Court of Appeal, was whether the trial court's summary judgment as to Universal's ability to withdraw, resulted in an automatic forfeiture of Universal's bond. Under Public Contract Code sections 5106 and 20174, if a contract is tendered to the lowest responsible bidder, and the bidder fails or refuses to enter the contract, the contract may be awarded to the second lowest bidder, and the bidder required to pay the difference between its own and the second lowest bid. Pertinent case law and Public Contract section 20172, however, require forfeiture of a bond only after the successful bidder is, first, awarded and, then, fails or refuses to enter a contract. CUSD had not been in communication with Universal following receipt of its request to withdraw, nor had it submitted Universal's bid for state approval. Moreover, the Court held, Universal's letter providing notice to CUSD could not be considered a "anticipatory breach of contract," as CUSD contended. A bid, observed the Court, is an offer, and "for a contract to exist, an offer must be accepted." Based on these considerations, the Court of Appeal affirmed the trial court's ruling: Where a contract was not awarded, there could be no breach of contract, nor did the bidder forfeit its bond.

Quite simply, when there is no actual award of a contract, there can be no breach of contract.

Court of Appeal, Fifth Appellate District, December 4, 2001: District's Award of Contract Upheld Despite Bid Defects

Minor arithmetical mistakes in a construction contract bid and trivial errors in documents concerning the contractor's compliance with state law constitute inconsequential defects that a government entity may waive in deciding to accept a bid, the California Court of Appeal recently held in an unpublished (non-precedential) decision. (*Nevocal Enterprises, Inc. v. Board of Education of the Fresno Unified School District* (Cal. App. 5th Dist., Dec. 4, 2001, No. F034381) 2001 WL 1558575.)

Prior History of the Case

In mid-1999, the Fresno Unified School District Board of Education (District) advertised for construction bids for a new middle school. The bid specifications called for submission of five separate bids. Bids were to include documentation of the bidder's efforts to utilize Disabled Veterans Business Enterprise (DVBE) subcontractors as required under state law.

Harris Construction Co. (Harris) was the lowest bidder. Although Harris' bid contained several deviations from the bid specifications, District determined the deviations were inconsequential, voted to waive them, and awarded Harris the contract. Nevocal Enterprises, doing business as KH Construction (KH), and the second lowest bidder, challenged the award, claiming Harris' bid contained material errors and deviations that District could not waive. The Court of Appeal ruled in favor of District, upholding its award of the contract to Harris.

The Court's Decision

Though non-precedential, the Court's decision to uphold the contract award illustrates the important distinction between *immaterial* bid defects, which may be waived by a contracting entity and do not obstruct the award of a contract, and *material* defects, which cannot be waived. The defects in Harris' bid were of two types: (1) typographical and arithmetical mistakes in the bid's numerical calculations, and (2) errors in Harris' documentation of its good faith effort to meet the statutory goal of hiring DVBE subcontractors to perform three percent of the bid's dollar amount.

Typographical/Arithmetic Errors. Examining Harris' bid submission as a whole, the Court found that the bidder's intent as to the amount bid on each part of the project was clearly discernable—despite what it described as “abysmal” handwriting, and the omission of the word “thousand” in the written form of some numerical calculations. The Court also found that a \$700 “discount” was an inconsequential deviation in light of the fact that Harris' total bid was more than \$19,000,000, and KH's bid was \$300,000 higher than Harris'.

Errors in DVBE Documents. KH alleged that Harris had failed to properly document its efforts to hire DVBE subcontractors as required under state law. However, the evidence showed: (1) that Harris documented its contact and dates of contact with numerous DVBE entities other than District; (2) that Harris had sent written invitations to bid to at least 64 DVBE subcontractors, and noted the response of all but a few in its bid; and (3) that it had completed the DVBE dollar participation form in a manner that was understandable, if not technically correct.

Because the evidence as a whole showed Harris' bid substantially conformed to District's contract specifications, the Court held District had properly exercised its discretion when it waived the bid defects and accepted Harris' bid.

Immaterial bid defects may be waived by a contracting entity whereas material defects cannot be waived.

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