

ROGERS JOSEPH O'DONNELL

To: AGC CA-LAC Members
From: Tyson Arbuthnot
Date: November 8, 2010
Re: New Case Summaries through November 5, 2010

1. *Mepco Services, Inc. v. Saddleback Valley Unified School District*
10 C.D.O.S. 13918, docket No. D055018 [Cal. App. 2nd Dist.] (November 2, 2010)

Contractor who successfully defended suit on performance bond was entitled to attorney's fees pursuant to fee provision in bond.

Saddleback Valley Unified School District entered into a contract with Mepco Services, Inc. to perform to construct a public project. The contract required Mepco to obtain a performance bond. The bond included an attorney fee provision. That provision stated: "Contractor/Principal and Surety agree that if the DISTRICT is required to engage the services of an attorney in connection with the enforcement of this bond, each shall pay DISTRICT's reasonable attorneys' fees and costs incurred, with or without suit, in addition to the above amount."

A dispute arose, and Mepco sued Saddleback for breach of contract. Saddleback countersued for breach of contract and sought liquidated damages for Mepco's delay in completing the project. Saddleback also sued the surety, asserting a cause of action for breach of the performance bond as to both defendants. A jury trial resulted in a judgment in favor of Mepco. The jury found that Mepco had fulfilled its obligations under the contract and that Saddleback had materially breached the contract. The trial court awarded Mepco its attorneys' fees pursuant to the provision in the bond.

Saddleback appealed, arguing that it was not a party to the bond contract and fees were not available under its contract with Mepco for the project. The court of appeal affirmed, holding there was no error in the award of fees. It explained that under the terms of the performance bond provision, Mepco and the surety were jointly and severally liable for any attorney fees that Saddleback might incur in prosecuting an action to enforce the bond. Civil Code §1717 makes that provision reciprocal. Thus, if Saddleback would have been entitled to attorney fees for prevailing on a performance bond claim against the surety and/or Mepco, then the surety and/or Mepco would be entitled to attorney fees for their defense of such a claim.

2. *Coral Construction, Inc. v. City and County of San Francisco*
50 Cal. 4th 315 [Cal. Sup. Ct.] (August 2, 2010)

State constitutional prohibition against public contracting laws discriminating or granting preferential treatment based on race or gender does not violate political structure doctrine.

Plaintiff, Coral Construction, Inc., sued to challenge San Francisco's Minority/Women/Local Business Utilization Ordinance. The ordinance required San Francisco to give specified discounts to contract bids submitted by certified minority-owned business enterprises and women-owned business enterprises. The emphasis of the ordinance was to provide race- and gender-conscious remedies to ameliorate the effects of past discrimination in the awarding of city contracts.

Coral sought an order compelling the city to adopt neutral contracting policies and to cease implementing the ordinance. Coral asserted that the ordinance violated article I, §31 of the California Constitution, which bars all state and local governments and entities from discriminating on the basis of a protected class in the operation of public employment, public education, or public contracting. On cross-motions for summary judgment, the trial court struck the ordinance as violative of this constitutional provision.

The city appealed, arguing that (1) §31 was preempted by the International Convention on the Elimination of All Forms of Racial Discrimination (Race Convention), a human rights treaty ratified by Congress in 1994; (2) §31 offended the *Hunter/Seattle* political restructuring arm of equal protection jurisprudence; and (3) pervasive past discrimination in public contracting converted the ordinance into a remedial measure required by the federal equal protection clause, thereby preempting §31.

The court of appeal rejected the city's arguments, and the California Supreme Court affirmed the court of appeal decision. The court found that, as explained in the official ballot pamphlet presenting the proposed measure to the voters, §31 was intended to "eliminate state and local government affirmative action programs in the areas of public employment, public education, and public contracting to the extent these programs involve 'preferential treatment' based on race, sex, color, ethnicity, or national origin. The specific programs affected by the measure, however, . . . depend on such factors as (1) court rulings on what types of activities are considered 'preferential treatment' and (2) whether federal law requires the continuation of certain programs." Section 31's ban on preferences includes exceptions for "bona fide qualifications based on sex," existing court orders or consent decrees, and actions which must be taken to avoid a loss of federal funds to the state.

The Supreme Court concluded that §31 of the California Constitution, which forbids public entities from awarding public contracts to discriminate or grant preferential treatment based on

race or gender, does not violate the political structure doctrine as enunciated by the United States Supreme Court.

3. **Los Angeles Unified School Dist. v. Great American Ins.**
49 Cal. 4th 739 [Cal. Sup. Ct.] (July 12, 2010)

A contractors need not prove intentional misrepresentation to recover compensation for a public entity's failure to disclose material information.

The Los Angeles Unified School District contracted for construction of a school. The district became dissatisfied with the contractor's performance and terminated the contract, and then sought new entities to contract with for the completion of the project using a no-bid exception to public contracting requirements. The district ultimately selected Hayward Construction Company, Inc., to complete the project. The completion agreement provided for cost-plus compensation not to exceed \$4.5 million. The completion agreement also provided that Hayward's work included the items on the pre-punch list. Great American Insurance Company issued a \$4.5 million performance bond in guarantee of Hayward.

Shortly after starting work, Hayward asserted that because of the need to correct certain defects not on the pre-punch list, the project would cost more than anticipated. The district paid an additional \$2 million to complete the project, but expressly reserved the right to recover this payment as an advance. After completion of the district demanded return of more than \$1 million of this "advance." Hayward and Great American refused. The district sued for breach of contract and of performance bond. Hayward cross-complained for breach of contract and rescission. The trial court held in favor of the district on its motion for summary judgment, and the defendants appealed.

The court of appeal reversed both the grant of summary adjudication and the judgment on the pleadings, holding that Hayward could maintain a cross-action for breach of contract based on nondisclosure of material information if it could establish that the district knew material facts concerning the project that would have affected Hayward's bid or performance and failed to disclose those facts to Hayward.

The California Supreme Court affirmed, holding that a contractor need not prove an affirmative fraudulent intent to conceal. Under *Souza & McCue Constr. Co. v. Superior Court* (1962) 57 Cal. 2d 508, "[a] contractor of public works who, acting reasonably, is misled by incorrect plans and specifications issued by the public authorities as the basis for bids and who, as a result, submits a bid which is lower than he would have otherwise made may recover in a contract action for extra work or expenses necessitated by the conditions being other than as represented." In this case, the court explained, it was necessary to decide whether a contractor may also recover when the plans and specifications are correct, but the public authority failed to disclose information in its possession that materially affected the cost of performance.

Slightly modifying the court of appeal decision, the Supreme Court concluded that a contractor on a public works contract may be entitled to relief for a public entity's nondisclosure in the following limited circumstances only: (1) the contractor submitted its bid or undertook to perform without material information that affected performance costs; (2) the public entity was in possession of the information and was aware the contractor had no knowledge of, nor any reason to obtain, such information; (3) any contract specifications or other information furnished by the public entity to the contractor misled the contractor or did not put it on notice to inquire; and (4) the public entity failed to provide the relevant information.