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Chair's Report

Thank you for being members of the Washington State Bar's Construction Law Section. It has been my pleasure to serve as Chair of this Section for 2012-13.

The Construction Law Section Council's primary mission is to get timely information to our members on legal developments impacting construction law in the State of Washington. In support of that mission, this year we have the Spring CLE in Yakima on April 19, 2013, which will focus on residential construction issues; and our Mid-Year CLE in Seattle on June 15, 2013, which will focus primarily on commercial/public works construction issues. Thank you to **Alicia Berry** for organizing the Yakima event and to **Ron English** for his input on the Seattle Mid-Year. Also, a special thanks to Council Members, attorneys, and other professionals who have agreed to speak at those events. We would not have these CLE events if it was not for the generosity of time and talent from these individuals, and their willingness to act as presenters.

Another way to inform our members of construction law development is the Section Newsletter. After many years as Editor, **Larry H. Vance, Jr.** of Winston & Cashatt stepped down. On behalf of the entire Section, we thank Larry for his years of outstanding and exemplary service. We also want to thank **Russell King** of Short Cressman & Burgess for agreeing to take over as the Newsletter Editor. Thank you also to all who are contributing information for the Newsletter. To keep section fees to a minimum, we are making our newsletter available in a digital format only.

The Section Council has also been working on some suggested jury instructions for construction cases. Thank you to **John Evans** of John Evans Law for leading the effort on that issue.

The Council is also offering a new model contract for design build. Thank you to **Scott Sleight** of Ahlers + Cressman for leading that effort. The model contracts drafted by the Section Council are offered, without cost and without warranty, as a starting point for legal practitioners, consumers and contractors to use on small construction projects in Washington.

One of the future goals of the Council is to work on revising Chapters 39.08 RCW (contractor public works bonds) and 60.28 RCW (public works retainage). This is no

continued on next page

Your Input Is Needed!

The Construction Law Section Newsletter works best when Section members actively participate. We welcome your articles, case notes, comments, and suggestions concerning new developments in public procurement and private construction law. Please direct inquiries and submit materials for publication to:

Russell King or **Athan Tramountanas**
Short Cressman & Burgess PLLC
999 Third Avenue, Suite 3000
Seattle, WA 98104
rking@scblaw.com
athant@scblaw.com

In This Issue

Chair's Report from previous page

small task. It is a long-term effort that will involve WSBA Construction Council Members, the Bar Association, government agencies, public officials, construction lobbying groups, and other members of the construction bar.

The Construction Section is also looking for new members. For prospective Council Members, there continues to be an effort for greater diversity of membership. The Council encourages more participation of Construction Councils outside of Metro Seattle. Thank you to our WYLD representative **Amber Hardwick** of Green & Yalowitz who has been promoting our section to the Young Lawyers Committee.

Thank you for allowing me to serve as your Section Chair. On a personal note, I would like to thank **Tom Wolfendale** for his assistance and advice as past Chair. **Tom Larkin** of Fidelity National Law Group will be taking over as Chair in June at the Mid Year CLE. I wish Tom the best in his term as Chair. I will be available to assist him in any way I can. Thanks also to **Ron English** for his acting as secretary / scribe for the Council Meetings and to **Ann Marie Petrich** for her role as Section Treasurer.

Constructively,
Joseph Scuderi – Cushman Law Offices, P.S.

Editor's Report

2013 promises to be a year of change for the better for the construction industry in Washington, and here at the newsletter we are planning to keep pace by implementing a number of improvements. As you've likely already noticed, one of the initial changes is to convert the newsletter to an electronic format (as opposed to a hard copy newsletter). We also plan on issuing the newsletter on a more regular basis, with the goal being at least once a quarter.

As always, we appreciate all contributions to the newsletter. Please email any submissions you may have for future newsletters to me at rking@scblaw.com.

Russell King – Short Cressman & Burgess, PLLC

Key Development Investment, LLC, et al. v. Port of Tacoma

292 P.3d 833 (Div. II, 2013)

by Amber L. Hardwick – Green & Yalowitz, PLLC – Seattle, Washington

***Summary**: Division Two accepted discretionary review to determine whether the Independent Duty Doctrine requires dismissal of plaintiffs' claims. The Court found dismissal improper, reasoning that under Elcon Const., Inc., 174 Wn.2d at 165, and Eastwood, 170 Wn.2d at 417, the Supreme Court has "directed lower courts not to apply the doctrine to tort remedies 'unless and until [the Washington Supreme Court] has, based upon considerations of common sense, justice, policy and precedent, decided otherwise.'"*

In *Key Development*, a property owner (Key) entered a real estate purchase and sale letter of intent with the Port of Tacoma for the purchase of property on which Trinity was a tenant. Trinity wanted Key to sell or lease the property to reduce Trinity's rent payments; Key listed the property for lease.

Meanwhile, the Port of Tacoma was in the planning stages for the redevelopment of a container terminal and had begun the process of acquiring adjacent property owned by Superlon. The Port of Tacoma contacted Key about buying its property for the purpose of relocating Superlon. The Port and Key entered a Letter of Intent to Purchase ("LOI"). The Port of Tacoma made representations to Key implying that purchase of the property was a certainty. However, the Port of Tacoma was actively exploring design options that would obviate the need to relocate Superlon and, therefore render the property purchase unnecessary. The Port did not convey this information to Key. Ultimately, the Port failed to purchase the property.

Key and Trinity alleged economic losses and sued the Port of Tacoma for, among other things, tortious interference, fraudulent misrepresentation and negligent misrepresentation. The trial court granted the Port of Tacoma summary judgment dismissal on Key's tort claims under the former Economic Loss Doctrine, stating: "the economic loss rule serves to limit parties to their contract remedies when a loss potentially implicates both tort and contract relief." *Id.* at 839. Trinity's tort claims survived because they were not a party to the contract (the LOI) and were not third-party beneficiaries to the LOI. The parties filed cross-appeals to Division Two of the Court of Appeals ("Division Two").

Evolution of the Independent Duty Doctrine

Division Two presented a well-reasoned chronology of pertinent precedent. The chronology began with *Alejandre v. Bull*, where the Supreme Court enunciated the value of "hold[ing] parties to their contract remedies when a loss potentially implicates both tort and contract relief." *Alejandre v. Bull*, 159 Wn.2d 674, 681 (2007) (barring tort claims where the Alejandres' contract specifically provided for the disclosures that were at issue in the misrepresentation claim.)

Next, Division Two addressed *Eastwood* and *Affiliated*. In contrast with *Alejandre*, in *Eastwood,* the lessor was allowed to maintain a tort claim for waste "[d]espite the existence of contractual lease covenants" addressing the maintenance of the property on the basis that the "duty not to commit waste was independent of the lease." *Id.* at 841. Both *Affiliated* and *Eastwood* allowed tort claims "despite the existence of a contract" when the Supreme Court has specifically established the existing right to a tort claim. *Id.* at 842. Justice Chamber's concurrence emphasized that "*This court* may … decide whether a duty is cognizable in tort" and "it is for *this court* to decide if the tort duty should no longer apply to certain circumstances or events." *Id.* at 842, *citing Eastwood,* 170 Wn.2d at 408. Emphasis added.

Division Two also examined more recent Independent Duty Doctrine cases: *Elcon* and *Jackowski.* In reference to *Elcon*, Division Two focused on the re-admonishment that lower courts should not apply the Independent Duty Doctrine to bar tort claims "unless and until this court has … decided otherwise." *Id.* at 842, *citing Elcon,* 174 Wn.2d at 165, *quoting Eastwood*, 170 Wn.2d at 417. While recognizing an "apparent reluctance" of the Supreme Court to apply the independent duty doctrine to bar tort claims "outside real property sales and construction contexts," Division Two pointed out apparent inconsistencies in its application. Specifically, in *Jackowski,* the Supreme Court expressly allowed tort claims in a real estate sale context. *Id.* at 843, *citing Jackowski*, 174 Wn.2d at 738 (Supreme Court allowed fraud claims and, in non-binding dicta, allowed negligent misrepresentation claims "but only to the extent the duty to not commit negligent misrepresentation is independent of the contract.").

Independent Duty Doctrine and Summary Judgment

Division Two determined that summary judgment on the basis of the Independent Duty Doctrine will rarely be available, stating:

> [A] trial court cannot automatically dismiss … tort claims … based solely on the existence of a contract between them; instead, it must determine whether the … alleged breaches of claimed tort duties arose independently of the contract terms and it must do so on summary judgment taking the facts in the light most favorable to [the nonmoving party], regardless of the likelihood that [the party] would ultimately prevail on those claims at trial.

Id. at 844. Since a determination of duty has to be decided on a case-by-case basis and even "potential duties" which arise "in connection with" the contract will survive summary judgment, Division Two reflected that the Independent Duty

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Key Development Investment, LLC, et al. v. Port of Tacoma *from previous page*

Doctrine seems to be failing its intended purpose: Unlike the former economic loss rule, the Independent Duty Doctrine does not assist practitioners or the trial courts to determine when a tort duty exists independent of the contract. *Id.* at 845 n.44.

Ultimately, given the confusion on the issue of independent duties in the real estate sales context, Division Two found summary judgment improper, but not without inviting the Supreme Court to provide clarification "[i]f we have misapprehended the Supreme Court's directions in this emerging area of the law." *Id.* at 845 n.48.

Washington State Supreme Court Voids Binding Arbitration in Insurance Contracts

by Steve Beeghly – Kreger Beeghly, PLLC

The Washington Supreme Court has apparently eliminated the use of binding arbitration clauses in insurance policies issued or delivered in the State of Washington. In a unanimous decision filed January 17, the Court held that a "RCW 48.18.200 prohibits binding arbitration agreements in insurance contracts." The provision in the insurance code relied on by the Court reads, in part: "No insurance contract delivered or issued for delivery in this state and covering subjects located, resident, or to be performed in this state, shall contain any condition, stipulation, or agreement … depriving the courts of this state of the jurisdiction of action against the insurer."

State of Washington Department of Transportation v, James River Insurance Company, 176 Wn 2d. 390, 292 P.3d 118 (2013), involved a declaratory judgment action initiated by the DOT against a non-admitted carrier, James River, after the insurer attempted to enforce a binding arbitration provision in the policy to resolve a coverage dispute. While the Court framed the issue specifically as an interpretation of law in the context of binding arbitration clauses in surplus line insurance contracts, the opinion is much broader and may well apply to virtually all insurance contracts issued in the state. There are some nuances in the opinion that arguably may narrow the scope of the case. Nevertheless, we believe it is prudent for insurers, particularly non-admitted insurers that issue surplus line policies in the State of Washington, to review their policies that contain arbitration provisions to determine if this decision may create an impediment to their ability to resolve coverage or claims disputes through arbitration.

Let us know if you would like a copy of the opinion. And, feel free to get in touch with us to discuss this case in more detail and how it may affect your insurance company clients.

Statute of Repose Tolled by Agreement

Wash. State Major League Baseball Stadium Pub. Facilities Dist. v. Huber, Hunt & Nichols-Kiewit Constr. Co., ___ Wn.2d ___, 2013 LEXIS 75 (Jan. 31 2013)

by William A. Linton – Inslee Best Doezie & Ryder, PS – Bellevue, Washington

On January 31, 2013 the Washington Supreme Court issued its decision concerning whether the six-year statute of repose applied to limit a construction defect action by the Washington State Major League Baseball Stadium Public Facilities District ("PFD") against its general contractor and in turn barred the general contractor's claims against its subcontractors.

1. Background

This is the second appeal of claims by the PFD against its general contractor, Huber, Hunt & Nichols-Kiewit Construction Co. ("Hunt Kiewit"). In May 1996, the PFD and Hunt Kiewit executed a construction contract for construction of Safeco Field, home of the Seattle Mariners. The stadium was substantially complete on July 1, 1999. In February of 2005 the Mariners president noticed blisters in fireproofing that had been installed as coating on the structural steel members of the stadium. Subsequent investigation and attempts at repairs revealed that the wrong primer had been applied resulting in widespread failure of the coating and cost several million dollars' worth of repairs.

The PFD filed a breach of contract action in August 2006 against Hunt Kiewit. Hunt Kiewit claimed that the suit was barred by the six-year statute of limitations. In the first appeal, the Supreme Court held that under RCW 4.16.160, the statute of limitations did not apply because the PFD's lawsuit was "for the benefit of the state."

On remand, the trial court ruled on summary judgment that the six-year statute of repose, RCW 4.16.310, applied to bar both the PFD's claims against Hunt Kiewit and the claims by Hunt Kiewit against its subcontractors because the claims did not accrue within six years of substantial completion.

2. The Statute of Repose, RCW 4.16.310, Was Tolled By the Terms of the Construction Contract

The Court in this second appeal first evaluated whether the statute of repose had been tolled by the terms of the construction contract. It appears that it was an established fact that the PFD's action against Hunt Kiewit had not accrued by July 1, 2005 – six years after substantial completion. The reason for this finding is not specifically mentioned in the decision and was not at issue on appeal.

A clause of the contract between PFD and Hunt Kiewit provided that "any alleged cause of action shall be deemed to have accrued in any and all events no later than such date of Substantial Completion." The PFD maintained that this

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Statute of Repose Tolled by Agreement from previous page

contract term tolled the statute of repose as of substantial completion and therefore its 2006 action was not time barred.

Hunt Kiewit argued that the contract provision should not apply at all. It based this argument upon the 1986 amendments to the statute of repose which specifically subjected claims by the state to the statute of repose. "The limitations prescribed in this section apply to all claims or causes of action as set forth in RCW 4.16.300 brought in the name or for the benefit of the state which are made or commended after June 11, 1986." RCW 4.16.310.

The amendments to RCW 4.16.310 were the legislature's response to the holding in *Bellevue School District No. 405 v. Brazier Construction Co.* 103 Wn.2d 111, 691 P.2d 178 (1984), that the construction statute of repose did not apply to actions brought for the benefit of the state.

Holding that contract provisions can set limits on the statute of repose just as they can for the statute of limitations, the Court rejected Hunt Kiewit's argument.

> We do not believe that the public policies furthered by the amendments preclude contractual agreements like the one at issue. Where parties agree to set the time of accrual, as here, they have agreed to alter, to some degree, statutory allocation of risks. Just as contractual modifications of the statute of limitations can vary the effect of policies underscoring particular limitations periods and still be given effect in the individual case, so can modifications that affect application of statutes of repose. This type of agreement has long been allowed. The policies embodied in the amendments are still effective as the law of the State, notwithstanding such individualized contractual agreements.

Having determined that the statute of repose was tolled contractually, the court again applied its prior holding that the statute of limitations did not apply to claims by or on behalf of the state under RCW 4.16.160. *See Wash. State Major League Baseball Stadium Pub. Facilities Dist. v. Huber, Hunt & Nichols-Kiewit Constr. Co.*, 165 Wn.2d 679, 694, 202 P.3d 924 (2009). Thus the Court held the statute of repose had been tolled and the PFD could pursue its claims against Hunt Kiewit.

3. Subcontractors Are Bound by Flow-Down Provisions

The next question addressed by the Court was whether Hunt Kiewit could sue its subcontractors. The subcontracts included typical "flow down" and incorporation by reference language. This included the provision that "the Subcontractor assumes toward the Contractor all obligations and responsibilities that the Contractor assumes toward the Owner and others, as set forth in the Prime Contract, insofar as applicable, generally or specifically, to Subcontractor's Work."

The subcontractors argued that the limitations and accrual provisions of the prime contract should not be enforced against the subcontractors because the flow-down provisions must contain specific "rights and remedies" language to enforce procedural terms. Citing *Sime Construction Co. v. Washington Public Power Supply System*, 28 Wn. App. 10, 621 P.2d 1299 (1980), the Court rejected this argument because the incorporation by reference provisions were not limited to only performance of the subcontractor's work. Instead they encompassed all of the same obligations that the general contractor had to the owner. Thus the subcontractors were bound by the provisions of the prime contract including the limitations and accrual provisions that tolled the statute of repose at the time of substantial completion.

The Court also distinguished cases cited by the subcontractors that invalidated incorporation by reference provisions conflicting with bond claim statutes. The Court reasoned that these cases, like *3A Industries, Inc. v. Turner Construction Co.*, 71 Wn. App. 407, 869 P.2d 65 (1993), are premised upon the conflict between the Little Miller Act (chapter 39.08 RCW) and flow-down clauses that would restrict the right of subcontractors to assert claims against the general contractor's bonds. No such conflict having been found in this instance, the flow-down provisions therefore apply to toll the statute of repose as to Hunt-Kiewit's claims against its subcontractors. For the same reasons, the statute of limitations does not apply to the Hunt-Kiewit's claims against its subcontracts either.

4. Court Questions Applicability of RCW 4.16.326(1)(g).

Hunt Kiewit claimed that because RCW 4.16.326(1)(g) requires the six-year statute of limitations for written contracts to run concurrently with the statute of repose regardless of discovery, the PFD was required to file suit no later than July 1, 2006. The Court disagreed for two reasons. First, it said it was questionable whether this provision would apply where no statute of limitations otherwise applies due to the exemption under RCW 4.16.160 for claims brought in the name of or for the benefit of the state. Second, the Court noted that the effective date of RCW 4.16.326(1)(g) was July 27, 2003 and that the statute had already been determined in prior cases not to be retroactive. Therefore because the Court held that the PFD's action accrued as of substantial completion, i.e., July 1, 1999, the statute did not apply.

5. Conclusion

It should be noted that the standard construction contract terms that tolled the statute of repose in this case were part of the standard AIA contract documents. However, many standard contracts do not contain similar provisions. Therefore the inclusion or exclusion of similar tolling provisions should be evaluated when drafting construction documents involving public contracts.

Contract Formation During the Bid Processs, and a Contractor's Protest Rights

by Athan Tramountanas – Short Cressman & Burgess, PLLC

Even after a public entity awards a public works contract, a contractor that is subsequently divested of this award cannot sue for monetary damages — only injunctive relief. This important decision was issued in December 2012 by the Washington Court of Appeals Division III. The case was *Skyline Contractors, Inc. v. Spokane Housing Authority*, 172 Wn.App. 193, 239 P.3d 690 (2012). The Court rejected Skyline's claims.

Background

In February 2010, the Spokane Housing Authority issued an invitation for bids to furnish and install windows in 75 homes as part of a federally funded project.

The IFB required that bidders have "a minimum of five years of documented experience." Skyline, which submitted the low bid, had only been in business for three years. However, it represented in its bid that it had the "full intention of subcontracting all installation of the windows" to a subcontractor with 21 years' experience.

Spokane HA notified Skyline that it "shall be awarded the contract." However, in subsequent preconstruction meetings, Skyline was unable to provide Spokane HA with evidence of an agreement with the experienced subcontractor mentioned in the bid. Spokane HA, which had not yet executed a written contract with Skyline, rejected its bid and selected another contractor.

Skyline Sues

Skyline filed suit, seeking monetary damages and an injunction preventing Spokane HA from executing a contract with the next-lowest bidder. At an initial hearing, the court granted Skyline a temporary restraining order.

If Skyline had posted an adequate security bond, the TRO would have prevented Spokane HA from executing a contract with any other contractor until the case was resolved. However, Skyline failed to post the bond. At this point, Spokane HA signed a contract with the next lowest bidder. Skyline proceeded to seek monetary damages under its breach of contract claim. The trial court dismissed this claim, and Skyline appealed.

When Does a Contract Exist?

The Court held that a contract in fact existed between Skyline and Spokane HA, even though a written contract had not yet been signed. Washington case law holds that an IFB by a public entity is a solicitation for offers. The bids submitted by contractors constitute offers to contract. Acceptance of a low bid constitutes acceptance of an offer.

Thus, a contract comes into existence when the public entity awards the contract, even when a written contract document will be signed later. In this case, an enforceable contract existed when Spokane HA stated that the contract "shall be awarded" to Skyline.

The Court held that Spokane HA's reason for terminating Skyline did not excuse it from executing its owner/contractor agreement.

Can Monetary Damages Be Recovered?

Even though the Court held that there was a contract, and that the contract had been breached, it did not allow Skyline to recover monetary damages for breach of contract. If this had not been a public contract, Skyline would have been entitled to damages.

The Court based its decision on the need to protect public funds in the competitive bidding process. A successful lawsuit by a disappointed bidder would cause the public purse to suffer twice — the public entity would pay more for the project by selecting a higher bidder and would pay damages to the disappointed bidder.

Because of this, Washington case law holds that a disappointed bidder's only remedy is to sue for an injunction to prevent the public entity from executing a contract with anyone other than the low responsible bidder. Once a contract is in place, the issue becomes moot and the bidder has no remedy.

Surprising Elements of the Decision

The decision in this case is surprising because the Court applied rules regarding bid protests and disappointed bidders to Skyline, even after the Court held that a contract existed. This is the first time a court has expressly held in a reported case that a contractor cannot recover monetary damages for breach of contract when a public owner changes course and awards the contract to another bidder. In essence, even though it found a contract existed, the Court treated this case like a bid protest rather than breach of contract.

This decision raises many questions. Can a public owner terminate a contractor for non-performance after a project is half-completed and go with the second-lowest bidder? Is the contractor's only remedy an injunction? Does even that remedy disappear after the public entity enters into contract with the second-lowest bidder?

Lessons for Contractors

For contractors, the lesson from Skyline is to seek injunctive relief when protesting a public owner's intent to award a contract to someone other than the low responsible bidder. The contractor should seek injunctive relief even if it has executed a contract with the public entity. Incurring the cost of posting the bond (which Skyline did not do) is preferable to losing out on all other remedies.

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Contract Formation During the Bid Processs, and a Contractor's Protest Rights *from previous page*

Lessons for Public Owners

For public owners, the lesson is to make sure that IFBs clearly define the manner in which contractor bids will be accepted. If the owner does not intend to have a contractual relationship with the selected contractor until certain conditions are met (like a signed contract with a subcontractor), the IFB should clearly state the conditions.

If the public owner does not intend to have a contractual relationship with the contractor before a written contract is executed, the IFB should clearly state that acceptance does not occur until the contract document is signed. When the public owner selects the lowest responsible bidder, it should announce its intention to award the contract, confirm that the contractor meets all of the conditions (and resolve any bid disputes), and then execute the contract documents.

Supreme Court Rules that an Arbitration Clause is Unconscionable – Application to Construction Contracts Explored

Gandee v. LDL Freedom Enterprises, Inc.,
__ Wn.2d __, 293 P.3d 1197 (2013).

by John Ahlers – Ahlers & Cressman PLLC

This case involves a debt adjustment contract between a consumer and a financial institution. In May 2008, the consumer (Gandee) entered into a contract with a company (LDL Freedom Enterprises, Inc.), in which LDL agreed to assist Gandee with financial matters pertaining to consumer loans. Three years later, Gandee sued LDL in Superior Court, asserting violations of the Consumer Protection Act (RCW 19.86, *et seq*.), and the Washington Debt Adjustment Act (RCW 18.28, *et seq*.). The contract between LDL and Gandee contained the following arbitration and severability clause:

> **Arbitration.** All disputes or claims between the Parties related to this Agreement shall be submitted to binding arbitration in accordance with the rules of [the] American Arbitration Association within thirty days of the dispute date or claim. Any arbitration proceeding brought by client [Gandee] shall take place in Orange County, California. Judgment upon the decision of the arbitrator may be entered in any court having jurisdiction thereof. Prevailing party in any action or proceeding related to this Agreement shall be entitled to recover reasonable legal fees and costs, including attorneys' fees which may be incurred.
>
> **Severability.** If any of the above provisions are held to be invalid or unenforceable, the remaining provisions will not be affected.

LDL moved to compel arbitration and Gandee opposed the motion, contending that the arbitration clause was unconscionable and that LDL had failed to move for arbitration within thirty days as required by the arbitration provision. The trial court agreed and denied LDL's motion to compel arbitration because it was not "timely brought" and that the arbitration clause was unconscionable. The case was appealed to the Washington Supreme Court.

The Supreme Court first looked at the issue of unconscionability. In Washington, in order to find that an arbitration clause is unconscionable and thus invalid, it must be "substantively" unconscionable. A term is substantively unconscionable where it is "one-sided or overly harsh," "[s]hocking to the conscience," "monstrously harsh," or "exceedingly callous."[1] Generally, where the contract contains a severability clause similar to the one set forth above, the non-valid or unconscionable terms are severed from those terms that are appropriate and the contract is enforced without the inappropriate terms. However, where the unconscionable terms "pervade" an arbitration agreement, the Court will "refuse to sever those provisions and declare the entire agreement void." [2]

The consumer challenged three aspects of the arbitration agreement. The venue provision requiring that the case arbitration be heard in Orange County, California, the thirty-day private statute of limitation provision, and the prevailing party attorneys' fees clause.

- **Venue/Location of the Arbitration:** With regard to the venue provision, Gandee argued that holding the arbitration in Orange County, California effectively denied her the ability to vindicate her rights. Courts recognize this type of prohibitive cost challenge to mandatory arbitration clauses. Generally, Washington courts will accept an affidavit describing a party's personal financial information, as well as the fee schedule from the American Arbitration Association, as sufficient evidence to meet the burden of demonstrating "prohibitive costs." In this instance, in addition, Gandee indicated what the travel costs, hotel costs and American Arbitration Association fees demonstrated that the cost to litigation in California exceeded the amount of her claim.

  LDL argued that the American Arbitration Association fee did not apply because the clause only required that the arbitration be submitted in accordance with the rules of the American Arbitration Association, not that the American Arbitration Association actually had to administer the arbitration itself. The Court criticized LDL, however, because it did not provide any information with regard to any other

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Supreme Court Rules that an Arbitration Clause is Unconscionable – Application to Construction Contracts Explored *from previous page*

arbitration association and what it would have cost. Thus, the Court found LDL failed to factually rebut Gandee's showing of financial hardship and held that Gandee prevailed on this issue.

- **Prevailing Party Attorneys' Fees:** Next, the Court addressed the "loser pays" attorneys' fees provision, which the consumer argued was one-sided and harsh because Gandee brought her suit under the Consumer Protection Act (CPA) and only the consumer is entitled to attorneys' fees. Under the arbitration clause, however, attorneys' fees were awarded to the prevailing party (which could be either party). Thus, the Court reasoned "loser pays" provision in the arbitration clause serves only to benefit LDL, which effectively chills Gandee's ability to bring suit under the Consumer Protection Act. Therefore, the Court found this term in the arbitration clause one-sided, overly harsh, and thus, substantively unconscionable.
- **Contract Suit Limitation:** With regard to the thirty-day private statute of limitations, the Court acknowledged that such contractual statute of limitations are valid, enforceable and will control over general statutes of limitations, unless prohibited by statute. Here, the arbitration clause shortens the statute of limitations from four years, provided by the Consumer Protection Act, to thirty days. The Court held that the statute of limitations provision of only thirty days was unconscionable.

Having found that three of the challenged provisions of the arbitration clause were unconscionable, the Court then went on to determine whether severance of the provisions should apply, or whether to invalidate the arbitration clause as a whole. Finding that the four-sentence arbitration clause contained three unconscionable provisions, the Court determined that the entire clause could not be severed from the overall contract. LDL argued, in its brief to the Supreme Court, that the Court should nevertheless enforce the arbitration provision because it "waived" any objectionable provisions. The Court found that this offer coming at the appeal was too little too late. The Court ruled that if it allowed such an after-the-fact-waiver to occur, parties would load up their arbitration agreements "full of unconscionable terms, then when challenged in court, offer blanket waiver." The Court held that the arbitration clause was unenforceable.

The Court then went on to distinguish the Federal Arbitration Act, which preempts state law. Based on federal court cases, the state justices reasoned that the U.S. Supreme Court would agree that this arbitration provision was unconscionable and thus unenforceable.

Comment: What application does this ruling have for construction contractors? Envision the situation in which a small local subcontractor does business with a large out-of-state general contractor, performing a project in Washington. The arbitration clause in this subcontract provides resolution of disputes in accordance with the American Arbitration Association, has an arbitration locale of Denver, Colorado, containing a prevailing party attorneys' fees clause, and requires that the contractor bring an action under the arbitration clause within 90 days of the date of the occurrence giving rise to the claim. Under the Gandee case, it very well could be that a court would invalidate such an arbitration clause, considering the cost of arbitrating the case in Denver, Colorado versus in Washington. The American Arbitration Association's fee, if the dispute exceeds $1 million, is $11,450 without compensation of the arbitrator(s), which could be tens of thousands of dollars if the dispute takes a week or longer to resolve. The court has already ruled that a 180-day private statute of limitations is unconscionable in another case.[3] If the project involved public works and a bond claim is involved, the Washington Bond Claim statute (RCW 39.08.030) provides only attorneys' fees to the prevailing claimant and no reciprocal fees to the bonding company or the general contractor. Under the logic of Gandee, since the arbitration clause contains a prevailing party arbitration fee provisions, by including a prevailing party attorneys' fees provision in the arbitration clause, the court could well find that such a provision has a chilling effect on the subcontractor. The prevailing party attorneys' fees clause in the bond is one-sided and benefits only the claimant (subcontractor). A "loser pays" two-sided attorneys' fees provision might be seen as unconscionable under the same logic employed in the Gandee case. Finally, a 90-day statute of limitation, compared with the Bond Claim, statute which provides a six year statute of limitations, might be the final straw and the Court could find the entire provision unconscionable as it did in the Gandee case. This is a practice pointer to keep in mind when confronted with an overly harsh and one-sided arbitration provision.

1 Relying on *Adler v. Fred Lind Manor*, 158 Wn.2d 331, 344-45, 103 P.3d 773 (2004).

2 *Adler v. Fred Lind Manor,* 153 Wn.2d 358.

3 *Adler v. Fred Lind Manor*, 153 Wn.2d 355-58 (finding that a 180-day private statute of limitations was unconscionable).

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Construction Law Section
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