

BreakingGround

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Legal Perspective

Public or Private Construction Projects? The Line is Becoming Increasingly Blurry

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Historically, it was fairly easy to determine whether a construction project was public or private. Government entities built public projects, and private owners and/or developers built private projects. As our country tries to pull itself out of the worst recession it has faced in many years, however, taxpayer funds are being used for everything from bailing out banks, saving U.S. auto companies, to funding a massive stimulus package. Many of these funds will ultimately be used by private companies which is causing a significant blurring of the line between public and private construction projects. From a legal perspective, the private use of public funds creates issues on three main fronts: (1) project procurement (bidding), (2) applicable labor wage rates, and (3) project payment protections (payment bonds and/or mechanics' liens).

First, with respect to project procurement, while many public contracting laws have historically required that public construction projects be awarded to the "lowest responsible bidder," several federal agencies (including the U.S. General Services Administration, and the Army Corp of Engineers) now permit the use of "best value" procurement, which allows the agency to separately evaluate both technical qualifications and price proposals and award the project to the entity that the agency determines represents the best combination of technical capabilities and price (even though the entity may not be offering the lowest price).

At the state level, the Pennsylvania Department of General Services ("DGS") has also recently begun using the "best value" method of procurement for certain projects. One of the interesting legal questions regarding "best value" procurement in Pennsylvania has been how the process would work given the Separations Act, which requires that owners on public projects award separate prime contracts for the following trades: general, electrical, plumbing, and HVAC. This question was answered in late 2007 by the Pennsylvania Supreme Court, which ruled in *Pennsylvania Associated Builders*

and Contractors, Inc. v. Commonwealth Department of General Services, 932 A.2d 1271 (Pa. 2007), that pursuant to the Commonwealth Procurement Code, DGS was not obligated to follow the Separations Act when implementing "best value" procurement.

Historically, in the private sector, owners have been free to award contracts using whatever method they so desire without any obligation to award the contract to the lowest bidder (or even to the bidder presenting the "best value"). In essence, the only restriction on private owners is that they are obligated to do what they say they are going to do. In other words, if a private owner indicates in a written request for bids that they will award the project to the lowest bid submitted by any of the contractors invited to bid, then the owner must do so.

For the stimulus money that is sent directly to public agencies, we expect those agencies to simply follow their standard procurement process. The more interesting question is whether the stimulus money that is distributed to private entities comes with any public procurement strings attached to it. This issue will not be resolved until there is a court challenge to a stimulus-funded contract that is awarded without following public procurement standards. For example, as part of the Capital Assistance Program of the Troubled Assets Relief Program, banks will be receiving millions of dollars to issue in loans, which, in many cases, will go to construction projects. There is certainly an argument to be made that these public funds should only be loaned on projects that comply with the applicable public procurement laws – this argument, however, will have to be ruled on by a court before we will know what procurement limitations, if any, are tied to these funds.

Second, with respect to applicable labor wage rates, public projects generally require that the labor constructing those projects be paid a certain level of wages, i.e. the "prevailing wage." Most states maintain prevailing wage act statutes applicable to projects in each particular state utilizing state funds, and public projects utilizing federal funds are bound by the wage rate requirements of the Davis-Bacon Act. These rates may be higher than would otherwise be required by the locality or by any applicable collective bargaining agreement, and thus must be considered as part of this public/private issue. Further, these state and federal

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prevailing wage act statutes require strict record keeping that a contractor on a private project may not employ.

Third, with respect to project payment protections, the law has again historically differentiated between public projects (where contractors do not have the right to file a mechanics' lien, but where payment bonds are required) and private projects (where contractors have mechanics' lien rights). The question in today's economy, however, is how do we determine whether a project is public or private?

A recent case decided by the Pennsylvania Superior Court, *Cornerstone Land Dev. Co. v. Wadwell Group*, 959 A.2d 1264 (Pa. Sup. Ct. 2008), addressed this unique intersection of public and private construction work. In this case the Court ruled that the sewage pump work at issue was for a "purely public purposes" and therefore could not be liened by the plaintiff lien claimant. On this project, the plaintiff had a contract with (and paid for by) a private entity, who conveyed title to a public municipal sanitary authority before the work was complete (and before the lien was filed). The Court ultimately ruled, "The manner in which the pump station was being used when [the plaintiff] filed its lien exempted the station." The difficulty for contractors with this case is that the owner at the start of the project was not required to have a payment bond posted (because the owner was a private entity), yet, at the end of the project the contractors and material suppliers did not have lien rights because

the Court ruled that the project was for a public purpose. This decision therefore leaves contractors in this scenario without a statutory payment protection, and leaves them with only a standard breach of contract action to enforce payment obligations.

In *Cornerstone*, the Superior Court set forth the following four factors for courts to consider when determining whether the "public use" exemption applies where a project is owned by a private entity but where the work is used for "purely public ends": (1) whether the government or a private entity managed and controlled the attached property when the lien was filed; (2) whether the property was constructed and paid for by a private entity; (3) whether the property was being used to further proprietary motives when the lien was filed; and (4) whether execution on the lien would disrupt an essential public service. The answers to these four questions will guide contractors in determining whether the project at issue will be judicially deemed to be "purely public" and therefore exempt from mechanics' lien claims.

Interestingly, with respect to prompt payment laws, the United States District Court for the Middle District of Pennsylvania has held that (on a federally-funded project) the availability of a federal bond claim under the Miller Act, 40 U.S.C. §§ 3131 *et seq.*, does not prevent a contractor from simultaneously pursuing a private claim under Pennsylvania's Contractor and Subcontractor Payment Act, 73 P.S. §§ 501 *et seq.* ("CASPA"). *Scandale Assoc. Builders & Eng., Ltd. v. Bell Justice Facilities Corp.*, 455 F. Supp. 2d 271 (M.D. Pa. 2006). Under this line of reasoning, the issue of whether a project is public or private should not impact a contractor's ability to recover under CASPA; however, this case did not address the related issue of whether the prompt payment provisions in the public project Commonwealth Procurement Code preempt the application of CASPA on state-funded (as opposed to federally-funded) public projects.

While the multi-billion dollar influx of taxpayer funds into the construction market will certainly serve to boost the nation's struggling economy, significant issues remaining regarding the largely ignored issue of whether the projects that will be constructed with these funds should be viewed as public or private projects. As discussed above, the areas of greatest concern relate to project procurement, labor costs, and project payment protections. Contractors should think through their rights in these three areas as they consider going after these projects that exist on the increasingly blurred line between public and private construction. **BC**

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