



STATE OF WASHINGTON CONSTRUCTION LAW COMPENDIUM

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This Compendium provides a general overview of Washington construction law. We have attempted to provide as comprehensive a summary as possible, and the outline below summarizes major areas of law involved in construction disputes. This summary, of course, cannot cover every legal issue that may arise in a construction dispute, but we hope this compendium provides a helpful background for those engaged in the rough and tumble world that is the Washington construction industry.

I. ACTIONABLE CLAIMS IN CONSTRUCTION DEFECT LITIGATION

A. BREACH OF CONTRACT

Breach of contract is a common claim in construction defect cases. In Washington, a breach of contract is actionable if the contract imposes a duty, the duty is breached, and the breach proximately causes damage to the claimant. *Nw. Indep. Forest Mfrs. v. Dep't of Labor and Indus.*, 78 Wash. App. 707, 712, 899 P.2d 6 (1995) (citing *Larson v. Union Inv. & Loan Co.*, 168 Wash. 5, 10 P.2d 557 (1932)). Certain questions usually need to be resolved before addressing the specific issue of breach.

For example, did a contract even exist? In terms of offer and acceptance, the mere use of a subcontractor's bid by the general contractor does not constitute an acceptance of the subcontractor's offer to perform work for a stated price. *Milone & Tucci, Inc. v. Bona Fide Builders, Inc.*, 49 Wash. 2d 363, 370, 301 P.2d 759 (1956).

Was a written contract required? Washington's Statute of Frauds requires a written contract where the agreement, by its terms, is not to be performed within one year from the making of the contract. Wash. Rev. Code § 19.36.010.

Is the contractor licensed with the state of Washington? A contractor must be properly registered with the Washington State Department of Labor and Industries before he or she can bring an action for the collection of compensation for the performance of any work or for breach of any contract for which registration is required. Wash. Rev. Code § 18.27.080. There are several exceptions, however, to Washington's registration requirement. Those exceptions are enumerated at Wash. Rev. Code § 18.27.090.

Often, breach of contract disputes arise relating to change orders. What is the effect of an oral change order, where the contract requires a written change order? A "no oral change order clause" may be modified orally or by conduct evidencing mutual assent to the modification. *Davis v. Altose*, 35 Wash. 2d 807, 814, 215 P.2d 705 (1950). Disputes can also arise relating to whether a contractor should be entitled to compensation for performing "extra work" or "additional work." Extra work is work that is not required in the performance of the contract and is done in addition to or in excess of the requirements of the contract. *Dravo Corp. v. Municipality of Metro. Seattle*, 79 Wash. 2d 214, 221-22, 484 P.2d 399 (1971). Additional work is necessarily required in the performance of the contract and without which it could not be carried out. *Id.* With extra work, a contractor may be entitled to additional compensation (including reasonable profit); whereas, with additional work he or she is not. *Id.*

Where a contractor performs work that is not covered by the contract, he or she may be able to obtain compensation based on a theory of quantum meruit. A contractor who has suffered substantial loss as a result of furnishing work and/or materials not covered by the contract may be entitled to compensation when substantial changes occurred that were not covered by the contract and were not within the contemplation of the parties. *V. C. Edwards Contracting Co., Inc. v. Port of Tacoma*, 83 Wash. 2d 7, 14, 514 P.2d 1381 (1973). The critical factor is whether the contractor should have discovered or anticipated the changed condition. *Id.*

Questions can also arise regarding whether an owner can sue a subcontractor for defective work based on a third-party beneficiary theory. Generally, only the parties to a contract can sue to enforce the contract's terms. *Lobak Partitions, Inc. v. Atlas Constr. Co.*, 50 Wash. App. 493, 497, 749 P.2d 716 (1988). When one party contracts with another for benefit a third party, however, then the third party may be able to maintain an action for breach of the contract. *Grand Lodge of Scandinavian Fraternity of Am. v. U.S. Fid. & Guar. Co.*, 2 Wash. 2d 561, 569, 98 P.2d 971 (1940). The key question in determining whether a third party may enforce the contract is whether the parties intended the promisor to assume a direct obligation to the third party at the time they entered into the contract. *Lonsdale v. Chesterfield*, 99 Wash. 2d 353, 360-61, 662 P.2d 385 (1983).

In the construction context, a property owner is generally not an intended third party beneficiary of a contract between a general contractor and a subcontractor. *Warner v. Design & Build Homes, Inc.*, 128 Wash. App. 34, 43, 114 P.3d 664 (2005). Typically, an owner has neither the desire nor the ability to negotiate with and supervise the various subcontractors, which is why the owner hires a general contractor. *Pierce Assoc.'s., Inc. v. Nemours Found.*, 865 F.2d 530, 539 (3d Cir. 1988). The owner looks to the general contractor, not the subcontractors, both for performance of the total construction project and for any damages or other relief if there is a default in performance. *Id.* The general contractor, in turn, looks to the subcontractors for performance and for any damages due to default in performance. *Id.*

B. NEGLIGENCE

Washington does not recognize a claim for negligent construction. *Stuart v. Coldwell Banker Commercial Group, Inc.*, 109 Wash. 2d 406, 417, 745 P.2d 1284 (1987). The bar on claims for negligent construction is generally true for claims seeking economic damages. *Id.* A plaintiff may be able to maintain a cause of action for negligence, however, where there are personal or physical injuries resulting from the manner in which a building was constructed. *See Atherton Condo. Apartment-Owners Ass'n Bd. of Dir.'s v. Blume Dev. Co.*, 115 Wash. 2d 506, 526, 799 P.2d 250 (1990).

C. BREACH OF WARRANTY

1. BREACH OF EXPRESS WARRANTY

Breach of express warranty may be available in a construction defect case. Such warranties may be contained in construction contracts, sales materials, or advertising/marketing materials. Although Washington's version of the Uniform Commercial Code ("UCC"), Wash. Rev. Code § 62A.2, contains a number of warranty provisions, construction contracts are not

governed by the UCC. *Arango Constr. Co. v. Success Roofing, Inc.*, 46 Wash. App. 314, 317-20, 730 P.2d 720 (1986) (citing *Christiansen Bros., Inc. v. State*, 90 Wash. 2d 872, 877, 586 P.2d 840 (1978)).

2. BREACH OF IMPLIED WARRANTY

a. IMPLIED WARRANTY OF HABITABILITY

There is a limited implied warranty of habitability in Washington. There are a number of requirements for the warranty to apply. First, the builder-vendor of dwelling must be a commercial builder. *Atherton Condo. Apartment-Owners Ass'n Bd. of Dir.'s v. Blume Dev. Co.*, 115 Wash. 2d 506, 518-19, 799 P.2d 250 (1990). Second, the warranty applies only to the sale of new residential dwelling. *Id.* Third, the warranty protects only the first occupants of residential property. Fourth, the warranty covers only fundamental defects in the structure of a home. *Carlile v. Harbour Homes, Inc.*, 147 Wash. App. 193, 194 P.3d 280 (2008). A fundamental defect is one that renders the home unfit for its intended purpose. *Frickel v. Sunnyside Enters., Inc.*, 106 Wash. 2d 714, 717-20, 725 P.2d 422 (1986). Whether the warranty applies to a particular defect is a case-by-case analysis, *Atherton*, 115 Wash. 2d at 519, which involves is a mixed question of law and fact. *Burbo v. Harley C. Douglass, Inc.*, 125 Wash. App. 684, 694, 106 P.3d 258 (2005). Although a seller is able to disclaim the implied warranty of habitability, such a disclaimer must be conspicuous, known to the buyer, and specifically bargained for. *Burbo*, 125 Wash. App. at 693.

b. IMPLIED WARRANTY OF WORKMANLIKE CONSTRUCTION

In Washington, implied warranties of workmanlike performance are not implicit in construction contracts. *Urban Dev., Inc. v. Evergreen Bldg. Prod.'s, LLC*, 114 Wash. App. 639, 646, 59 P.3d 112 (2002). Contracting parties have their remedies for breach and can negotiate for warranties if they so choose. *Id.* An action for implied warranty of workmanlike performance in construction contracts would be too similar to a cause of action for negligent construction, which is not recognized in Washington. *Id.* (citing *Stuart v. Coldwell Banker Commercial Group, Inc.*, 109 Wash. 2d 406, 417, 745 P.2d 1284 (1987)).

3. WARRANTIES RELATED TO CONDOMINIUMS

The Washington Condominium Act provides a broad array of warranty protection for condominium purchasers. Wash. Rev. Code § 64.34.443 covers express warranties, while Wash. Rev. Code § 64.34.445 covers implied warranties. The paragraphs below discuss only some of the legal obligations related to the Washington Condominium Act. Construction professionals should refer to Wash. Rev. Code § 64.34 or consult with an attorney to determine his or her specific warranty obligations.

Wash. Rev. Code § 64.34.443 states, “express warranties made by any seller to a purchaser of a unit, if relied upon by the purchaser, are created as follows.” The statute then lists four ways to create express warranties. *See* Wash. Rev. Code § 64.34.443. For example, one way to create an express warranty is by any written affirmation of fact or promise that relates to the unit, its use, or rights appurtenant thereto, area improvements to the condominium that would

directly benefit the unit, or the right to use or have the benefit of facilities not located in the condominium creates an express warranty that the unit and related rights and uses will conform to the affirmation or promise. Wash. Rev. Code §§ 64.34.443(1)(a).

Wash. Rev. Code § 64.34.445, provides for certain implied warranties related to the purchase of condominiums. By way of illustration, a person or entity that qualifies as a “declarant” or “dealer” impliedly warrants that the units and the common elements are suitable for the ordinary uses of real estate and that any improvements made or contracted for by the declarant will be free from defective materials; constructed in accordance with sound engineering and construction standards; constructed in a workmanlike manner; and constructed in compliance with all laws applicable to such improvements. Wash. Rev. Code § 64.34.445(2). Wash. Rev. Code § 64.34.445 has been construed to include a guarantee that the builder has examined the materials used and ensured they are of sound quality and suitable for the use to which they are put. *Satomi Owners Ass’n v. Satomi, LLC*, 139 Wash. App. 175, 159 P.3d 460 (2007). Also, unlike the implied warranty of habitability, the implied warranties of § 64.34.445 include less serious defects (i.e., defects that do not meet the threshold for “fundamental”). *Park Avenue Condo. Owners Ass’n v. Buchan Dev.’s, L.L.C.*, 117 Wash. App. 369, 71 P.3d 692 (2003).

D. MISREPRESENTATION AND FRAUD

1. INTENTIONAL MISREPRESENTATION/FRAUD

Claims for intentional misrepresentation and fraudulent concealment may be available in the construction context. For intentional misrepresentation, a plaintiff must prove the following elements by clear, cogent, and convincing evidence: (1) a representation of existing fact; (2) its materiality; (3) its falsity; (4) the speaker’s knowledge of its falsity; (5) the speaker’s intent that it be acted upon by the person to whom it is made; (6) ignorance of its falsity on the part of the person to whom the representation is addressed; (7) the latter’s reliance on the truth of the representation; (8) the right to rely upon it; and (9) consequent damage. *Beckendorf v. Beckendorf*, 76 Wash. 2d 457, 462, 457 P.2d 603 (1969).

To prove fraudulent concealment, a homeowner must show: (1) a concealed defect in the premises of a residential dwelling; (2) the builder knew of the defect; (3) the defect is dangerous to the property, health, or life of the purchaser, and (4) the defect was unknown to the purchaser and a reasonable inspection by the purchaser would not have disclosed the defect. *Atherton Condo. Apartment-Owners Ass’n Bd. of Dir. v. Blume Dev. Co.*, 115 Wash. 2d 506, 524, 799 P.2d 250 (1990). In addition, the defect must substantially reduce the property’s value or operate to materially impair or defeat the transaction’s purpose. *Id.* Although a fraudulent concealment claim may exist even though the purchaser makes no inquiries that would lead him or her to ascertain the concealed defect, in those situations where a purchaser discovers evidence of a defect, the purchaser is obligated to inquire further. *Id.* at 525. Fraudulent concealment does not extend to those situations where the defect is apparent. *Id.*

2. NEGLIGENT MISREPRESENTATION

Washington courts recognize the tort of negligent misrepresentation and apply the standard set forth in the Restatement (Second) of Torts § 552. Subject to some important exceptions, that section generally states that Defendant, in the course of his or her business or profession, may be liable for negligent misrepresentation for failing to exercise reasonable care in the supplying of false information for the guidance of Plaintiff in Plaintiff's business transactions. Restatement (Second) of Torts § 552(1). Defendant may be liable for Plaintiff's pecuniary losses if those losses were caused by justifiable reliance upon the information. *Id.* Liability for negligent misrepresentation is limited to cases where Defendant has knowledge of the Plaintiff's reliance; or Plaintiff is a member of a group that Defendant seeks to influence; or Defendant has special reason to know that some member of a limited group will rely upon the information. *Schaaf v. Highfield*, 127 Wash. 2d 17, 24, 896 P.2d 665 (1995).

A plaintiff asserting this claim may encounter some difficulty because he or she must meet the burden of proving each element by clear, cogent, and convincing evidence. *Van Dinter v. Orr*, 157 Wash. 2d 329, 333, 138 P.3d 608 (2006). In addition, the economic loss rule, which is fully discussed below, may severely limit the availability of this cause of action in construction cases.

E. STRICT LIABILITY

Generally, in the construction context, a plaintiff's only avenue to seek strict liability against a defendant is Washington's Products Liability Act ("Act"). The Act does not cover construction services. *Graham v. Concord Constr., Inc.*, 100 Wash. App. 851, 856, 999 P.2d 1264 (2000). The Act may apply, however, to defective products used in construction. Wash. Rev. Code § 7.72. Product sellers and manufacturers are potentially strictly liable for defective products that cause personal injury or property damage. Wash. Rev. Code § 7.72.010(6); *Garza v. McCain Foods, Inc.*, 124 Wash. App. 908, 917, 103 P.3d 848 (2004) ("The act imposes strict liability on any manufacturer of a defective product for resulting injuries."). A homeowner can assert a product liability claim against a product seller or manufacturer without meeting any privity requirements. Wash. Rev. Code § 7.72.030.

The definition of "product" covers nearly all materials used in construction. Product means any object possessing intrinsic value, capable of delivery either as an assembled whole or as a component part or parts, and produced for introduction into trade or commerce. Wash. Rev. Code § 7.72.010(3).

Defective products are unsafe as designed, do not include adequate warnings or instructions for use, or do not conform to the manufacturer's warranties. Wash. Rev. Code § 7.72.030. The Act applies to any claim or action brought for harm caused by the manufacture, production, construction, design, assembly, or installation of a product. RCW 7.72.010(4). Covered claims include but are not limited to those previously based on strict liability, negligence, breach of a duty to warn, or any other substantive legal theory. *Id.*

F. INDEMNITY

1. EXPRESS INDEMNITY

Contractors can freely bargain for indemnity clauses in construction contracts. Indemnity agreements are essentially agreements for contractual contribution, in which one party may look to another for reimbursement. *MacLean Townhomes, L.L.C. v. America 1st Roofing & Builders Inc.*, 133 Wash. App. 828, 138 P.3d 155 (2006). To prove an indemnity claim, a plaintiff must demonstrate that there exists a contract containing an indemnity provision that binds the defendant to reimburse the plaintiff for the amount claimed. *Jacob's Meadow Owners Ass'n v. Plateau 44 II, LLC*, 139 Wash. App. 743, 757 n.3, 162 P.3d 1153 (2007). Absent a contractual indemnity clause in a subcontract agreement, a contractor is not entitled to equitable indemnity from its subcontractors even if the work was defective. *Urban Dev., Inc. v. Evergreen Bldg. Prod.'s, LLC*, 114 Wash. App. 639, 644-47, 59 P.3d 112 (2002).

Indemnity agreements are subject to the fundamental rules of contract construction, i.e., the intent of the parties controls. *Jones v. Strom Constr. Co.*, 84 Wash. 2d 518, 520, 527 P.2d 1115 (1974). Intent must be inferred from the contract as a whole. *Id.* The meaning afforded the provision and the whole contract must be reasonable and consistent with the purpose of the overall undertaking; and if any ambiguity exists, it must be resolved against the party who prepared the contract. *Id.* In addition, clauses purporting to exculpate an indemnitee from liability flowing solely from its own acts or omissions are not favored and are strictly construed. *Id.* at 520. To be sure, indemnification agreements are void and unenforceable if the agreement indemnifies the indemnitee against his or her negligence. Wash. Rev. Code § 4.24.115.

2. IMPLIED INDEMNITY

A right of implied indemnity arises when one party incurs liability that the other party should discharge by virtue of the nature of the relationship between the parties. *Central Washington Refrigeration, Inc. v. Barbee*, 133 Wash. 2d 509, 513, 946 P.2d 760 (1997). Although the right to indemnity is not implicit in every contractual relationship, a contract governed by the UCC, with its warranties, provides a sufficient basis for an implied indemnity claim. *Id.* at 514 n.4. Likewise, a relationship where one party has expressly warranted its goods to another party provides a sufficient basis for an implied indemnity claim. *Id.* at 516-17. But construction contracts are not governed by the UCC. *Arango Constr. Co. v. Success Roofing, Inc.*, 46 Wash. App. 314, 317-20, 730 P.2d 720 (1986) (citing *Christiansen Bros., Inc. v. State*, 90 Wash. 2d 872, 877, 586 P.2d 840 (1978)). Therefore, UCC implied warranties cannot serve as the basis for an implied indemnification claim. *Urban Dev., Inc. v. Evergreen Bldg. Prod.'s, LLC*, 114 Wash. App. 639, 645, 59 P.3d 112 (2002).

Because warranties of workmanlike performance are not implicit in Washington construction contracts, there is, likewise, no implied duty of indemnification. *Id.* at 645-46. The reasoning is closely tied to the economic loss rule. *Berschauer/Phillips Const. Co. v. Seattle School Dist. No. 1*, 124 Wash. 2d 816, 881 P.2d 986 (1994). Thus, absent an express warranty, there is no implied duty of indemnification in Washington construction contracts.

II. STATUTE OF LIMITATIONS & REPOSE

A. STATUTE OF LIMITATIONS

There are several different limitations periods in construction cases. Written contracts carry a six-year period. Wash. Rev. Code § 4.16.040. Oral contracts have a three-year period. Wash. Rev. Code § 4.16.080(3). Tort-based claims also have a three-year period. Wash. Rev. Code § 4.16.080. Claims under Washington's Condominium Act have a four-year limitations period. Wash. Rev. Code § 64.34.452.

Generally, a statute of limitations begins to run when the plaintiff's cause of action accrues. *Malnar v. Carlson*, 128 Wash. 2d 521, 529, 910 P.2d 455 (1996); RCW 4.16.005. This often occurs when the plaintiff suffers some form of injury or damage. *In re Estates of Hibbard*, 118 Wash. 2d 737, 744, 826 P.2d 690 (1992). In some instances, however, there is a delay between the injury and the plaintiff's discovery of it. *Allen v. State*, 118 Wash. 2d 753, 758, 826 P.2d 200 (1992). If the delay was not caused by the plaintiff sleeping on his or her rights, then the court may apply the discovery rule, which operates to toll the date of accrual until the plaintiff knows or, through the exercise of due diligence, should have known all the facts necessary to establish a legal claim. *Id.* at 758. Courts apply the discovery rule to two categories of cases. *Id.*

In the first type, the defendant fraudulently conceals a material fact from the plaintiff and thereby deprives the plaintiff of the knowledge of accrual of the cause of action. *Id.* Application of the discovery rule tolls the limitation period until such time as the plaintiff knew or, through the exercise of due diligence, should have known of the fraud. *Interlake Porsche & Audi, Inc. v. Bucholz*, 45 Wash. App. 502, 516-17, 728 P.2d 597 (1986); Wash. Rev. Code § 4.16.080(4).

In the second type, the nature of the plaintiff's injury makes it extremely difficult, if not impossible, for the plaintiff to learn the factual elements of the cause of action within the specified limitation period. *Crisman v. Crisman*, 85 Wash App. 15, 21, 931 P.2d 163 (1997). Many construction cases fit within the second category. The discovery rule applies in actions for breach of construction contracts where latent defects are alleged, even though a breach of contract claim ordinarily accrues upon breach. *1000 Virginia Ltd. P'ship v. Vertecs Corp.*, 158 Wash. 2d 566, 578-79, 146 P.3d 423 (2006).

Under the discovery rule, a plaintiff cannot ignore notice of possible defects. *Id.* at 581. When a plaintiff is placed on notice of some harm, committed by another, he or she must make reasonably diligent inquiries to determine the scope of the actual harm. *Id.* The plaintiff is charged with what a reasonable inquiry would have discovered. *Id.* A person with knowledge sufficient to put him or her upon inquiry notice is deemed to have notice of all facts that reasonable inquiry would disclose. *Id.* Whether the plaintiff should have been able to detect defects is a factual question. *Id.*

B. STATUTE OF REPOSE

In addition to the limitations periods above, the Washington Legislature has promulgated a statute of repose that is applicable in the construction context. *See* Wash. Rev. Code §§

4.16.300 - .327. Statutes of repose are different than statutes of limitation. *Rice v. Dow Chem. Co.*, 124 Wash. 2d 205, 211, 875 P.2d 1213 (1994). A statute of limitation bars a plaintiff from bringing an already accrued claim after a specific period of time. *Id.* at 211-12. A statute of repose terminates a right of action after a specified time, even if the injury has not yet occurred. *Id.*

Wash. Rev. Code § 4.16.310 is a six-year statute of repose that applies to actions arising out of the construction of a building. *1000 Virginia Ltd. P'ship v. Vertecs Corp.*, 158 Wash. 2d 566, 576, 146 P.3d 423 (2006). Wash. Rev. Code § 4.16.310 requires a two-step analysis for computing the accrual of a cause of action arising from the construction, alteration, or repair of any improvement to real property. *Del Guzzi Constr. Co. v. Global Nw., Ltd.*, 105 Wash. 2d 878, 883, 719 P.2d 120 (1986). First, the cause of action must accrue within six years of substantial completion of the improvement. *Id.* Substantial completion means the state of completion reached when an improvement upon real property may be used or occupied for its intended use. Wash. Rev. Code § 4.16.310. Second, a party must file suit within the applicable statute of limitation, depending on the type of action. *Id.* By requiring that the cause of actions accrue and the statute of limitation begin to run within the six-year window following substantial completion, the repose statute restricts the judicially created discovery rule with a six-year overall bar. *Bellevue Sch. Dist. No. 405 v. Brazier Const. Co.*, 103 Wash. 2d 111, 119, 691 P.2d 178 (1984). Therefore, the discovery rule, if applicable for accrual of actions, is limited to the six year period. *Id.*

III. DAMAGES

A. ECONOMIC LOSS DOCTRINE

The economic loss rule bars recovery for tort claims where a contractual relationship exists and the losses are economic in nature – that is, there is no property damage or personal injury. *Berschauer/Phillips Constr. Co. v. Seattle Sch. Dist. No. 1*, 124 Wn.2d 816, 826, 881 P.2d 986 (1994). As a general principal of law, the economic loss rule “marks the fundamental boundary” between the law of contracts, which is “designed to enforce expectations created by the agreement,” and the law of torts, which is designed to protect citizens and their property by imposing a duty of reasonable care on others.” *Id.* at 821-22 (citations omitted). Whether a loss is “economic” will depend on whether the loss is “properly remediable only in contract.” *Id.* at 822 (noting that economic losses fall on the contract side of “the line between tort and contract”). Generally, economic losses are distinguished from personal injuries or damages to property, which have traditionally been redressed by tort. *Alejandro v. Bull*, 159 Wn.2d 674, 683, 153 P.3d 864 (2007).

In *Berschauer/Phillips*, for instance, the Washington Supreme Court held that recovery of economic losses due to construction delays was limited to remedies provided by the construction contract. *Berschauer/Phillips*, 124 Wn.2d at 826-27. In so holding, the Court affirmed the need to “hold parties to their contracts” and “ensure that the allocation of risk and the determination of potential future liability is based on what the parties bargained for in the contract.” *Id.* As the *Berschauer/Phillips* court noted, the economic loss doctrine applies with special force in the construction industry. On any construction project, there is great importance placed on the “precise allocation of risk as secured by contract. The fees charged by architects, engineers,

contractors, developers, vendors, and so on are founded on their expected liability exposure as bargained and provided for in the contract.” *Id.*

Thus, where parties have contracted with one another, and their damages are economic in nature, courts will not blur the line between tort and contract. Rather, as noted in *Berschauer/Phillips*, courts will “hold parties to their contracts.” However, even if the parties have not expressly allocated the risk of loss, the economic loss rule may still apply. *Alejandre v. Bull*, 159 Wn.2d 674, 687, 153 P.3d 864 (2007). “If the party could have allocated its risk, the rule applies; all that is required is that the party had an opportunity to allocate the risk of loss.” *Id.* Otherwise, courts would risk interfering with the freedom of contract by imposing remedies on parties for which they did not agree.

B. RECOVERABLE DAMAGES

1. DIRECT DAMAGES

Washington courts have ruled that “[a] party injured by a breach of contract may recover all damages that accrue naturally from the breach, including any incidental or consequential losses the breach caused.” *Floor Exp., Inc. v. Daly*, 138 Wn. App. 750, 754, 158 P.3d 619 (2007) (finding that a flooring contractor did have standing to bring suit for consequential damages flowing from the subcontractor’s failure to properly perform work). In case involving breach of a construction contract, the standard measure of recovery is the “reasonable cost of completing performance or remedying defects in the construction if the cost is not clearly disproportionate to the probable loss in value to property. *Panorama Village Homeowners Ass’n v. Golden Rule Roofing, Inc.*, 102 Wn. App. 422, 427, 10 P.3d 417 (2000); citing *Eastlake Constr. Co., Inc. v. Hess*, 102 Wn.2d 30, 46, 686 P.2d 465 (1984) (quoting Restatement (Second) of Contracts § 348 (1981)). In other words, an injured party to a construction contract is entitled to expectation damages, or to “return the injured party to as good a pecuniary position as [he/she] would have had if the breaching party would have performed properly.” *Floor Exp., Inc.*, 138 Wn. App. at 754. If a contractor, for example, performs defective or incomplete work, the owner is entitled to compensation sufficient to repair, replace, or complete the work. The one caveat, as noted in *Panorama*, is that the injured party’s recovery may not be disproportionate to their loss.

In *Panorama*, for instance, a homeowner’s association (the “owner”) sought damages for a defective roof and submitted evidence that it would be cheaper to replace the roof, rather than engage in a labor-intensive repair. *Panorama*, 102 Wn. App. at 428. While the contractor argued that the cost of replacement of the roof would be disproportionate to the owner’s loss, the court noted that the contractor – which bears the burden to challenge the owner’s evidence in order to reduce the award – failed to provide any evidence challenging the reasonableness of the owner’s estimate. *Id.* at 428-29. Thus, the appellate court affirmed the trial court’s award of damages to the owner to replace the defective roofs.

Moreover, once the repair or replacement has been completed, the contractor (or subcontractor) is entitled to restitution for its part performance. See *Ducolon Mechanical v. Shinstine/Forness*, 77 Wn.App. 707, 893 P.2d 1127 (1995). Such restitution is measured by the reasonable value of its services provided. *Id.*

2. STIGMA DAMAGES

With stigma damages, the critical inquiry is whether damage to the property is permanent or temporary. If the damage is permanent, then the court should award stigma damages, or diminution in value damages. *See e.g., Mayer v. Sto Industries, Inc.*, 156 Wn.2d 677, 132 P.3d 115 (2006). In *Mayer*, for example, the property damage involved a contractor's application of Exterior Insulation Finish System (EIFS), a known defective product. The Mayers proved – by “unrebutted expert testimony” – that they had “suffered a permanent loss because they will have to disclose that the home is sided with EIFS.” As the court held, “where the damage to real property is permanent, a plaintiff is entitled to recover, not only for the costs of restoration and repair, but also for the property's diminished value.”

In contrast, if the damage is temporary – and the property is capable of being restored – then the damages should be limited to restoration damages. *Pepper v. J.J. Welcome Const. Co.*, 73 Wn. App. 523, 871 P.2d 601 (1994), *rev'd on other grounds, Phillips v. King County*, 87 Wn. App. 468, 490, 943 P.2d 306 (1997). In *Pepper*, for instance, the court held that water run-off and deposits of sediment on plaintiff's property did constitute temporary damage that could be remedied. For this reason, the court held that restoration costs were the proper measure of recovery.

3. DELAY DAMAGES

Delays can be quite common in construction projects, and they are typically caused by the owner, contractor, or a combination of both. With respect to owner delays, there is an implied term in every construction contract that holds that the owner will not hinder the contractor's performance, and for such delays the contractor may recover additional compensation. *Bignold v. King County*, 65 Wn.2d 817, 399 P.2d 611 (1965). In *Bignold*, for instance, the Washington Supreme Court affirmed a monetary award for a contractor due to the county's engineers' arbitrary refusal to shut down a project despite adverse weather conditions, which significantly increased the contractor's operating costs and required the contractor to perform extra work. *Id.* at 825-26.

A contractor may similarly be held liable for damages resulting from delays in performance. *See e.g., Brower Co. v. Garrison*, 2 Wn. App. 424, 428-29, 468 P.2d 469 (1970). If there is no time period for performance prescribed in the contract, performance is presumed to be due within a “reasonable time.” *Id.* (discussed in Kelly Kunsch, 1C Wash. Prac., Methods of Practice § 90.27 (4th ed.)). In addition, as delay damages can often be difficult to measure, many owners insert a liquidated damages clause in the construction contract. *Id.* As liquidated damages clause provides a fixed measure of damages, and is generally favored by Washington courts unless the clause constitutes a penalty. *See Brower*, 2 Wn. App. 433-34 (holding, in 1970, that a \$50 per day liquidated assessment was not excessive to compensate an owner for a contractor's delays).

4. PUNITIVE

In general, punitive damages are not awarded in Washington. However, punitive damages may be available when federal law, or the law of some other jurisdiction, governs the

merits of a case. *See generally Dailey v. North Coast Life Ins. Co.*, 129 Wn.2d 572, 919 P.2d 589 (1996) (“Since its earliest decisions, [Washington courts] ha[ve] consistently disapproved punitive damages as contrary to public policy.”); *see also* Karl B. Tegland, 5 Wash. Prac., Evidence Law and Practice § 402.20 (5th ed.)

5. ATTORNEY FEES AND COSTS

In Washington, attorneys’ fees and costs may be recovered by the prevailing party as costs of litigation where permitted by contract, statute, or a recognized ground in equity. *White Coral Corp. v. Geysler Giant Clam Farms, LLC*, 145 Wn. App. 862, 866 n.4, 189 P.3d 205 (2008); *citing McGreevy v. Oregon Mut. Ins. Co.*, 128 Wn.2d 26, 35 n.8, 904 P.2d 731 (1995).

When there is a construction contract, Washington courts will award reasonable attorney fees “where such contract [] specifically provides that attorney's fees and costs, which are incurred to enforce the provisions of such contract [], shall be awarded to . . . the prevailing party.” RCW 4.84.330; *see Mike's Painting, Inc. v. Carter Welsh, Inc.*, 95 Wash.App. 64, 975 P.2d 532 (1999) (Arbitration panel had authority to award attorney fees to subcontractor and general contractor who prevailed on claims for breach of contract).

As for a statutory basis, construction disputes will at times entail violations of the Consumer Protection Act (“CPA”), which provides for recovery of attorney fees to the injured party. *See* RCW 19.86.090; *Mayer v. Sto Industries, Inc.*, 123 Wn. App. 443, 98 P.3d 116 (2004) (awarding attorneys fees to homeowners for siding manufacturer’s violations of the CPA), *affirmed in part, reversed in part* 156 Wash.2d 677, 132 P.3d 115 (2006).

In terms of equity, Washington courts will award fees and costs under a theory of equitable indemnity, or the “ABC” rule. *Jacob’s Meadow Owners Ass’n v. Plateau 44 II, LLC*, 139 Wn. App. 743, 759, 162 P.3d 1153 (2007). Equitable indemnity, or the ABC rule, holds that “when the natural and proximate consequences of a wrongful act by defendant involve plaintiff in litigation with others, there may, as a general rule, be a recovery of damages for the reasonable costs incurred in the litigation, including compensation for attorney’s fees.” *Id.* In *Jacob’s Meadow*, for example, the court held that attorney fees incurred by a general contractor in defending against a developer’s claims were recoverable as damages due to a subcontractor's breach of the duty to indemnify the contractor. *Id.*

IV. INSURANCE COVERAGE FOR CONSTRUCTION CLAIMS

This section will provide a brief summary of insurance law as it relates to construction claims and disputes.

In Washington, “an insurance policy is to be construed in accordance with the general rules applicable to other contracts.” *Graingrowers Warehouse Co. v. Central Nat’l Ins. Co. of Omaha*, 711 F. Supp. 1040, 1044 (E.D. Wash. 1989) (citing *State Farm General Ins. Co. v. Emerson*, 102 Wash. 2d 477, 480, 687 P.2d 1139 (1984)). An insurer may have a duty to indemnify and/or defend its insured, although the duty to defend (including the obligation to pay for the insured’s costs of defense) is separate from and far broader than the insurer's duty to indemnify. *See Time Oil Co. v. Cigna Property & Cas. Ins. Co.*, 743 F. Supp. 1400, 1419 (W.D.

Wash. 1990). Insurers must defend their insured against any claim that might possibly be covered by the policy of insurance. The Washington Supreme Court recently summarized the general principles that define liability insurers' broad duty to defend their insured in *Woo v. Fireman's Fund Ins. Co.*, 161 Wn.2d 43, 52-53, 164 P.3d 454 (2007):

The rule regarding the duty to defend is well settled in Washington and is broader than the duty to indemnify. The duty to defend arises at the time an action is first brought, and is based on the potential for liability. An insurer has a duty to defend when a complaint against the insured, construed liberally, alleges facts which could, if proven, impose liability upon the insured within the policy's coverage.

Id. (citations omitted) (emphasis added); *see also Griffin v. Allstate Ins. Co.*, 108 Wn. App. 133, 138, 29 P.3d 777 (2001) (“The general rule is that insurers who have reserved the right and duty to defend are obliged to defend any suit which alleges facts wherein, if proven, would render the insurer liable.”).

An insurer must look outside the complaint, and reasonably investigate, when allegations in a complaint are not sufficiently clear or when allegations are in conflict with known or readily-ascertainable facts. *See Truck Ins. Exchange v. Vanport Homes, Inc.*, 147 Wn.2d 751, 761, 58 P.3d 276 (2002).

With respect to insurance exclusions, property damage caused by “faulty workmanship” is often excluded from coverage. *See City of Oak Harbor v. St. Paul Mercury Ins. Co.*, 139 Wn. App. 68, 159 P.3d 422 (2007) (holding that coverage for damage to liner of city's wastewater treatment lagoon as result of dredging contractor's negligence was barred by faulty workmanship exclusion of city's property insurance policy). However, there are often exceptions to the faulty workmanship exclusion which provide coverage for an “ensuing loss” – that is, property damage caused as a result of the faulty workmanship. *See Allstate Ins. Co. v. Smith*, 929 F.2d 447, 449-50 (9th Cir. 1991).

In *Allstate*, for example, the court held that the faulty workmanship exclusion at issue should be limited to the particular *product* that was faulty; not to the entire construction *process*. In this case, a contractor had failed to place a tarp on a roof and, as a consequence, equipment inside was damaged by rain. The insured argued that the exclusion for faulty workmanship should not apply to the entire construction process (i.e., not placing a tarp over a roof at night), and thus the equipment damaged as a result should be covered under the policy's “ensuing loss” clause. The insurer argued that the faulty workmanship clause should exclude coverage for all damage to the site because the construction process itself was faulty. The court endorsed the insured's interpretation, noting that the faulty workmanship exclusion applies to a product, not process, and that the insurer's broad reading of faulty workmanship would effectively render the ensuing loss clause meaningless. *Id.* at 450. However, this area of law is not clearly defined, as other courts have read the faulty workmanship exclusion more broadly to exclude coverage for the entire construction process. *See e.g. See City of Oak Harbor v. St. Paul Mercury Ins. Co.*, 139 Wn. App. 68, 159 P.3d 422 (2007) (noting cases nationwide that have interpreted the faulty workmanship exclusion broadly to mean a process; not a resulting product).

V. CONSTRUCTION LIENS

A. WORK/MATERIALS SUBJECT TO LIEN

Mechanics' and materialmen's liens (collectively "construction liens") are governed by statute. RCW 60.04.900. The applicable lien statute provides that "any person furnishing labor, professional services, materials, or equipment for the improvement of real property shall have a lien upon the improvement for the contract price of labor, professional services, materials, or equipment furnished." RCW 60.04.021. That is, a construction lien is a security interest in property to secure payment for services, labor and material provided to improve the property.

Construction liens exist primarily to protect contractors and subcontractors. Due to the inherent risk of nonpayment on a construction job, the Washington Legislature determined that contractors and subcontractors required a greater remedy for non-payment for their work beyond the often limited remedy to sue on their contracts. *Jackson v. Flohr*, 227 F.2d 607 (9th Cir. 1955). This risk is particularly underscored with a failed construction project, in which there are typically a long list of claimants.

As a general matter, the Mechanics' and Materialmen's Liens statute are "strictly construed, and equitable considerations cannot ameliorate its effects." *Van Wolvelaere v. Weathervane Window Co.*, 143 Wn.App. 400, 404, 177 P.3d 750 (2008); *see also Lumberman's of Washington, Inc. v. Barnhardt*, 89 Wn.App. 283, 286, 949 P.2d 382 (1997) ("[C]ase law has established that mechanics' and materialmen's liens are creatures of statute, in derogation of common law, and therefore must be strictly construed to determine whether a lien attaches"). Therefore, a potential lien claimant must closely abide by statutory requirements, or else risk forfeiting his or her rights.

B. TIME LIMIT FOR FILING LIEN

One primary statutory requirement a potential lien claimant must follow is to provide a written "pre-claim notice" to the owner of their right to claim a lien. RCW 60.04.031; *Van Wolvelaere v. Weathervane Window Co.*, 143 Wn.App. 400, 404, 177 P.3d 750 (2008). Notice must be given to both the property owner and to the "prime contractor" who contracts directly with the owner "to assume primary responsibility for the creation of an improvement to real property." RCW 60.04.011(13). RCW 60.04.031 provides a sample pre-claim notice, which even includes guidance on the appropriate font size (ten-point type). In general, the pre-claim notice states that the potential lien claimant is a participant in the project and has or is about to "provid[e] professional services, materials, or equipment for the improvement of [the owner's] property" which would entitle him or her to make a lien claim. RCW 60.04.031. However, there are broad exceptions to the pre-claim notice requirement. A pre-claim notice is not required of (1) persons who contract directly with the owner; (2) laborers whose lien is based solely on performing labor; or (3) subcontractors who contract directly with the prime contractor. RCW 60.04.031.

For those parties who are required to provide a pre-claim notice, the notice "may be given at any time, but only protects the right to claim a lien for materials, services, or equipment supplied" after 60 days before the date notice is given by mail or personal delivery. RCW

60.04.031. That is, the pre-claim notice only permits a lien on those improvements that are furnished 60 days prior to notice. The 60 day time limit is shortened to 10 days for the new construction of a single-family residence. RCW 60.04.031

C. LIEN PRIORITIES

Liens take precedence in order of time – the first in time being the first in right. *See* RCW 60.04.061; *see also Seattle Mortg. Co., Inc. v. Unknown Heirs of Gray*, 133 Wn. App. 479, 136 P.3d 776 (2006). Mechanics’ and materialmen’s liens attach at the time the lien claimant commences work or first delivers material or equipment to the site. RCW 60.04.061. Exactly when work “commences” or material is “delivered” is a subject of dispute. *See Mannington Carpets, Inc. v. Hazelrigg*, 94 Wn. App. 899, 973 P.2d 1103 (1999).

In *Manningham Carpets*, the court addressed the priority of a materialmen’s lien against real property. In this case, a contractor, Manningham, shipped carpet “F.O.B.” to a property site in March. In April, two deeds of trust were recorded against the property. In May, a carrier delivered Manningham’s carpet to the site. Manningham maintained that his lien took priority over the deeds of trust. By shipping the carpet, Manningham argued, it was placed into the legal possession of another—thus constituting a “delivery” sufficient for a lien to attach. The court disagreed, stating: “The purpose of allowing a lien to attach to secure the price of building materials is that those materials have some *special connection to the property* being encumbered. Because there can be no lien where the material is neither used in the building nor taken to the premises, it follows that at least one of those conditions must occur before the lien will attach.” *Id.* at 909 (emphasis added) (citations omitted).

Therefore, courts in Washington analyzing lien priority will make a specific inquiry as to when materials, or services, attach to the site and form some “special connection” to the property. Simply arranging for the delivery of materials to a site is not sufficient to establish lien priority.

D. TIME LIMIT FOR FILING LAWSUIT TO FORECLOSE LIEN

A lien does not “bind the property” for longer than eight months. RCW 60.04.14. Thus, once a lien is recorded on property, it remains in effect for eight months and a lien claimant must file suit to foreclose on the lien within that time period. *Id.* In addition to the eight-month restriction, a lien claimant is also required to file suit to foreclose on a lien “not later than 90 days after the person has ceased to furnish labor, professional services, materials, or equipment.” *Id.* As one court has noted, these statutory time period restrictions are effectively a statute of limitations upon the duration of a lien. *See Kinskie v. Capstin*, 44 Wn. App. 462, 464, 722 P.2d 876 (1986).

However, the statutory eight-month period for foreclosing on a recorded lien claim does not conclusively limit a claimant's underlying lien rights. *See Geo Exchange Systems, LLC v. Cam*, 115 Wn.App. 625, 65 P.3d 11 (2003). In *Geo Exchange*, the court noted that a lien claimant may “file successive liens so long as the claimant is still working or providing materials under the contract.” That is, even though a first lien may expire after eight months, the lien claimant may still revive amounts owed by filing a second lien. In keeping with the statute,

however, the lien claimant must file a successive lien “no later than 90 days after the claimant completed the work on the project.” *Id.* at 633.

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