

Differing Site Conditions

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Two recent developments have strengthened the statutory requirement for a differing site conditions clause in local agency contracts (Public Contract Code § 7104). One is an amendment to the statute that became effective on January 1, 2007. The other is a recent court case. Together, they assure that the differing site conditions clause is more likely to achieve its goal: Place the risk of unforeseen site conditions on the owner (a) so contractors need not include contingency money in their bids for such problems and (b) so taxpayers will thereby get lower bids on individual contracts, and lower aggregate costs for all public works construction. This article discusses the reason differing site conditions clauses exist, the impact of the two recent developments, and how a differing site conditions claim is proved.

Reasons for Differing Site Conditions Clauses

Every contract allocates risks between the owner and the contractor. The effect of unforeseen conditions is one of those risks. The owner is best able to assess and avoid the risk of unforeseen conditions. It employs engineers and architects to research the project and draw the plans. They get unlimited access to the site. The owner has time for investigations,

and benefits from them by using the information to refine the plans.

On the other hand, a contractor has little time and limited access to the job site while bidding. Further, a contractor bids on many jobs, but is awarded only a few. Money spent on investigations is only recouped on the projects awarded to the contractor. So, money cannot be spent on more than a cursory investigation. The contractor must rely almost exclusively upon its experience and the bidding information provided by the owner.

When a prudent contractor must bear the risk of unforeseen conditions, the bid must include contingency dollars to cover those possibilities. If nothing major is hit on the job, then the contingency money is additional profit for the contractor. On the other hand, if the owner bears the risk of unforeseen conditions, then the prudent contractor does not need those contingency dollars and can bid the lowest possible price. In that case, the owner will only pay for difficult subsurface work when it is actually required. The courts have repeatedly acknowledged these facts, for example: *Condon-Johnson & Associates v. Sacramento Municipal Utility District* (2007) 149 CA4th 1384, 57 CR3d 849, 857: "The nature and accuracy of the information provided by the public entity manifestly bears on the risks to be undertaken by the bidder. To that extent the risk affects the amount of the bid. The more risk the greater the bid." *Foster Const. C. A. & Williams Bros. Co. v. U. S.* (Ct.Cl. 1970) 435 F2d 873: "The purpose of the changed conditions clause is thus to take at least some of the gamble on subsurface conditions out of bidding. Bidders . . . need not consider how large a contingency should be added to the bid to cover the risk. They will have no windfalls and no disasters. The Government benefits from more accurate bidding, without inflation for risks which may not eventuate. It pays for difficult subsurface work only when it is encountered and was not indicated in the logs."

Where a contractor bears the risk of unforeseen conditions, but includes no contingency money in the bid, the contractor risks large losses, even bankruptcy, if it encounters unforeseen conditions. On those jobs the owner also risks tragedy – first, from cost-cutting measures the contractor will take if it hits unforeseen conditions, and then, from fighting contractor claims or picking up the pieces if the contractor abandons the project or goes bankrupt.

That is why most owners bear the risk of unforeseen conditions through a differing site conditions clause (also known as a changed conditions clause). The clause is in the contract used for most private projects: AIA Document A201-1997, § 4.3.4. A federal version (Federal Acquisition Regulations, 48 CFR § 52.236-2) is required in most federal construction and demolition contracts (48 CFR § 36.502); many federally-funded local agency contracts also must have the clause. In California, Public Contract Code § 7104 requires the clause in most local public agency contracts involving excavations deeper than 4 feet (for example, see STANDARD SPECIFICATIONS FOR PUBLIC WORKS CONSTRUCTION [the GREENBOOK] (2006 ed.) § 3-4). The clause also appears as Caltrans Standard Specifications, § 5-1.116 (2006 ed.) and in most Office of the State Architect contracts.

Types of Differing Site Conditions

Traditionally, there are two types of differing site conditions: Type 1 is a condition differing materially from the conditions indicated in the information about the job site that is provided to bidders. Type 2 is an unforeseen and unusual condition that differs materially from the kind of conditions ordinarily encountered in the particular type of work in the particular locality. Public Contract Code § 7104(a)(1) creates a third type of differing site condition on local agency projects: "material that is hazardous waste. . . [and] that is required

to be removed to [certain classes of] disposal site. . ." This addition ensures that the owner takes responsibility for the proper disposal of hazardous wastes.

The exact language used in the differing site conditions clause varies from contract to contract. Those language differences are important; they may narrow the scope of the clause, generally, or for particular types of problems. On the other hand, if the differing site conditions clause is mandated by a statute, like Public Contract Code § 7104, then the differing site conditions clause cannot be omitted from the contract, nor can the contract language be more restrictive than the statutory language (*G. L. Christian & Associates v. U.S.* (Ct.Cl. 1963) 312 F2d 418).

Owner Efforts to Circumvent Differing Site Conditions Clauses Reign In

Short-sighted owners, who apparently do not appreciate the aggregate benefit obtained from the differing site conditions clause, have attempted to circumvent Public Contract Code § 7104 in two ways: First, they draft contracts that purport to limit type 1 differing site conditions to material differences from the conditions represented in the "contract documents," and, then, they define "contract documents" to exclude the very information most likely to contain information about existing site conditions, namely, the soils report and borings logs. Second, they include "disclaimers" in the contract which purport to shift the risk of differing site conditions to the contractor, despite contrary language in the differing site conditions clause. The two recent developments should end these efforts to circumvent the statute.

The first development: Effective January 1, 2007, Public Contract Code § 7104(a)(2) defines a type 1 differing site condition as: "Subsurface or latent physical conditions at the site differing from those indicated *by information about the site made available to bidders prior to the deadline for submitting bids.*" The last phrase was added. It

precludes and invalidates contract language limiting a type 1 differing site condition to only site conditions materially different from those described in narrowly-defined "contract documents." If information is made available to bidders, the owner obviously intends bidders to consider that information in calculating their bids – and to give the owner the benefit of that information in lower prices. Therefore, all of that information, whether defined as contract documents or not, should be considered in determining whether a type 1 differing site condition has been encountered on the project. As amended, Public Contract Code § 7104(a)(2) so requires.

The second development: In *Condon-Johnson & Associates v. Sacramento Municipal Utility District* (2007) 149 CA4th 1384, 57 CR3d, the court analyzes the word "indicated" in Public Contract Code § 7104(a)(2), and determines that the word prevents general disclaimer language in the contract documents from avoiding a differing site conditions claim. The agency contract contained general disclaimers of liability for site conditions differing from information provided; the language stated that the agency bore no responsibility for the accuracy of the information it made available to the bidders. The trial judge refused to let the jury see the disclaimer language, and the jury returned a \$1.3 million verdict for the contractor. The court of appeal affirmed, holding: "Since the disclaimers wholly denied responsibility for the subsurface conditions indicated, in violation of § 7104, they were properly excluded from jury consideration." This decision is consistent with decisions by courts of other jurisdictions, e.g., *Foster Const. C. A. & Williams Bros. Co. v. U. S.* (Ct.Cl. 1970) 435 F2d 873, 888 ("Even unmistakable contract language in which the Government seeks to disclaim responsibility for drill hole data does not lessen the right of reliance. The decisions reject, as in conflict with the changed conditions clause, a 'standard mandatory clause of broad application,' [including] the variety of such disclaimers of responsibility – that the logs are not guaranteed,

not representations, that the bidder is urged to draw his own conclusions. [citations]"); *Morrison-Knudsen Co. v. U.S.* (Ct.Cl. 1968) 397 F2d 826; *Umpqua River Navigation Co. v. Crescent City Harbor Dist.* (9th Cir. 1980) 618 F2d 588; *Jack B. Parson Constr. Co. v. Utah* (Utah 1986) 725 P2d 614; *Metropolitan Sewerage Com'n v. R. W. Constr., Inc.* (Wis 1976) 241 NW2d 371.

Physical Condition Existing When the Contract Was Executed

Regardless of whether it is type 1 (differing from the conditions indicated in the information about the job site that is provided to bidders) or type 2 (differing from the kind of conditions ordinarily encountered in the particular type of work in the particular locality), the differing site condition must be an actual physical condition of the job site (*Olympus Corp. v. U.S.* (Fed. Cir. 1996) 98 F3d 1314, 1318; *Bateson-Stolte, Inc. v. U. S.* (Ct.Cl. 1962) 305 F2d 386; *Hallman v. U. S.* (Ct.Cl. 1948) 80 F.Supp 370). It also must be a condition that existed at the time the contract was executed (*Olympus Corp. v. U.S.* (Fed. Cir. 1996) 98 F3d 1314, 1317; *John McShain, Inc. v. U.S.* (Ct.Cl. 1967) 375 F2d 829, 833; but see *Hoffman v. U.S.* (Ct.Cl. 1964) 340 F2d 645, 648-51, using the date of the notice to proceed date instead of the date of the contract). Acts of God are not differing site conditions (*Turnkey Enterprises, Inc. v. U. S.* (Ct.Cl. 1979) 597 F2d 750), unless they combined with other unforeseeable conditions (*John A. Johnson Contr. Corp. v. U.S.* (Ct.Cl. 1955) 132 F.Supp 698). Thus, groundwater at a higher level than is shown on the geotechnical report, which was caused by unusually heavy rain before bid day, is not a differing site condition; however, higher groundwater which was caused by an upstream dam overflowing before bid day could be a differing site condition, even if the overflow was caused by unusually heavy rain.

Material Difference from Conditions Indicated or Ordinarily Encountered

Again, regardless of whether it is type 1 or type 2, the differing site condition must be "materially different" from the conditions indicated in the information about the job site that is provided to bidders (type 1) or from the kind of conditions ordinarily encountered in the particular type of work in the particular locality (type 2). Materiality usually turns upon the unique facts existing on the particular job. Facts that often bear on the question of materiality are: (a) differences in the quality of the substances encountered, (b) differences in the quantity of work required as a result of the condition, or (c) changes in the construction techniques required in order to deal with the condition.

Site Inspection Requirement

Regardless of whether a type 1 or type 2 differing site condition is claimed to exist, it does not qualify if it could have been discovered in a reasonable site inspection. The failure to actually make such an inspection will not defeat the claim unless the condition would have been discovered in such a reasonable site inspection (*Vann v. U.S.* (Ct.Cl. 1970) 420 F2d 968). A "reasonable inspection" is different for a type 1 differing site condition than for a type 2. For a type 1, it is a reasonable walk through the site (*Stock & Grove, Inc. v. U.S.*, (Ct.Cl. 1974) 493 F2d 629). For a type 2 differing site condition, it is a reasonable site investigation based upon the lack of any indications concerning the site conditions in the information provided to bidders (*McMullan & Sons, Inc. v. U.S.* (1980) 226 Ct.Cl. 565). In both cases, the test is what a reasonably competent contractor in the appropriate trade would have discovered -- not what an expert in the particular condition would have discovered (*Ets-Hokin Corp. v. U.S.* (Ct.Cl. 1970) 420 F2d 716). The scope of the reasonable inspection is probably not affected by the typical site inspection clause (*e.g.*, AIA Document A201-1997, § 1.5.2; Federal Acquisition

Regulations, 48 CFR § 52.236-3; STANDARD SPECIFICATIONS (Caltrans 2006) § 2-1.03).

Proving a Type 1 Differing Site Condition

As a general rule, to establish a type 1 differing site condition the following six things must exist (see *Weeks Dredging & Contr., Inc. v. U.S.* (1987) 13 Cl.Ct. 193).

(1) The information about the job site that was provided to bidders must indicate the existence of conditions which are different from those actually found on the job site. (*Condon-Johnson & Associates v. Sacramento Municipal Utility District* (2007) 149 CA4th 1384, 57 CR3d 849, 857, defines "indicated" in Public Contract Code § 7104 as establishing, "as the public policy of California, that a contractor may draw reasonable deductions from the 'indications' in a contract of the subsurface conditions that might be found at the site." This is consistent with interpretations of the federal differing site conditions clause, e.g., *Foster Const. C. A. & Williams Bros. Co. v. U. S.* (Ct.Cl. 1970) 435 F2d 873, holding that a differing site conditions claim could arise from design features that required different subsurface conditions than were actually encountered.)

(2) The contractor's interpretation of the information provided to bidders must be that of a reasonably prudent contractor.

(3) The contractor's reliance on the information provided to bidders must be reasonable.

(4) The conditions actually encountered must differ materially from the conditions indicated in the information provided to bidders for the particular location on the project.

(5) The failure of the contractor to foresee the conditions actually encountered must have been reasonable.

(6) The difference between the conditions indicated and the conditions actually encountered must be the cause of additional costs incurred by the contractor and/or additional time required to complete the work.

The specific language of the differing site conditions clause may vary these requirements, if it is enforceable (see *Condon-Johnson & Associates v. Sacramento Municipal Utility District* (2007) 149 CA4th 1384, 57 CR3d 849, holding that disclaimers cannot negate the differing site conditions clause; compare *E. H. Morrill Company v. State of California* (1967) 65 C2d 787, 423 P2d 551, 56 CR. 479, holding a general disclaimer will not avoid the warranty of the correctness of the plans flowing from positive assertions about job site conditions).

Proving a Type 2 Differing Site Condition

A Type 2 differing site condition is harder to establish than a type 1 (*Charles T. Parker Constr. Co. v. U. S.* (Ct.Cl. 1970) 433 F2d 771). The contractor cannot have known of the condition, nor have reasonably anticipated finding it (*Southwest Engineering Co. v. U.S.* (1975) 206 Ct.Cl. 892). It must be an unusual condition for that locality, but need not be a geological freak (*Western Well Drilling Co. v. U. S.* (N.D.Cal. 1951) 96 F.Supp 377).

Notice to the Owner

Regardless of whether it is type 1 or type 2 differing site condition, every differing site conditions clause requires the contractor to give the owner notice of the claim before the condition is disturbed (AIA Document A201-1997, § 4.3.4; Federal Acquisition Regulations, 48 CFR § 52.236-2; STANDARD SPECIFICATIONS FOR PUBLIC WORKS

CONSTRUCTION [the **GREENBOOK**] (2006 ed.) § 3-4; Public. Contract Code § 7104). That notice is designed to allow the owner to determine whether a differing site condition exists and, if so, how to handle it (*Schnip Bldg. Co. v. U.S.* (Ct.Cl. 1981) 645 F2d 950).

Even though most of the differing site conditions clauses call for written notice to the owner, the federal courts have accepted oral notice if the contractor can prove it was given (*Shepherd v. U.S.* (Ct.Cl. 1953) 113 F.Supp 648). They have also refused to foreclose a differing site conditions claim despite the lack of proper notice, if the owner otherwise obtained knowledge of the condition (*S. Kane & Sons, Inc.* 78-1 BCA ¶ 13,100) or if the owner suffered no prejudice from the lack of notice (*Parcoa Inc.* 77-2 BCA ¶ 12,658). California courts should do the same thing, by construing the notice requirement as a covenant, not a condition (Civil Code §§ 1436 & 1636; Code of Civil Procedure § 1859; *Yamanishi v. Bleily & Collishaw, Inc.* (1972) 29 CA3d 457, 105 CR 580), by construing it liberally to avoid the forfeiture of a legitimate claim (Civil Code §§ 1442 & 1670.5; *Hawley v. Orange County Flood etc. Dist.* (1963) 211 CA2d 708, 27 CR 478), by exercising the court's equitable power to excuse a condition that would cause a forfeiture (Civil Code §§ 3275 & 3369; *O'Morrow v. Borad* (1946) 27 C2d 794, 167 P2d 483), or by finding that notice was waived (Civil Code §§ 3513 & 3515; *Weeshoff Constr. Co. v. Los Angeles County Flood etc. Dist.* (1979) 88 CA3d 579, 152 CR 19).

Once a differing site condition is found, then most differing site conditions clauses create a contractual right to a change order. In that change order, the contractor should be compensated for all of the effects of the differing site condition, including overhead, profit and time extensions. Under state law, the failure to issue that change order is a breach of the contract.

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