IN CHANGE WE TRUST . . . OR NOT

By Larry W. Caudle, Jr.

One of the most commonly-repeated project management errors we observe in our practice involves performing extra work before receiving written authorization from the owner to do so. Many times, the contractor has the verbal assurance from the owner to pay for the work – or so he or she believes. That assurance can range from something as direct as "I'll process a change order to pay you" to something less certain as "I'll treat you fairly." When these assurances bear no fruit, the contractor must convince a claims board or a judge why it should be paid even though it failed to follow the contract.

This is a tenuous position in which to be, but contractors have sometimes overcome the "written prior authorization" requirement if the owner, on other occasions during a project, verbally authorized extra work and eventually paid for such extra work. In these circumstances, the owner is viewed as having modified the written changes requirement by its conduct. Unfortunately for contractors, a recent court decision put a halt to this argument in California, at least with respect to public contracts.

P&D Consultants, Inc. v. City of Carlsbad, 190 Cal. App. 4th 1332 (2010) involved a contract between a civil engineering firm and the City of Carlsbad, California for the redesign of a city-owned golf course. The contract included a Changes in the Work clause, which required all modifications to be in writing.

During the project, the parties executed five written change orders totaling over $162,000. In each instance, the designer submitted pricing to the City and the City typically took several weeks to prepare and execute the change order. In a few instances, the City's project manager verbally instructed the designer to proceed with extra work pending formal execution of the change order. This process continued without incident until the designer presented to the City a proposed sixth change order for work it deemed extra.

As is often the case with disputed change orders, each side had a different version of the sequence of events. The designer's project manager contended that the City's project manager initially responded that the City was running out of funds for the project, but then told him to keep working and he would "take care of it." During a follow-up inquiry, the City's project manager stated that a change order had been prepared and "was in accounting." The City's project manager, on the other hand, contended that he told the designer no change order was warranted because the work was covered by a previous change order. He nevertheless informed the designer's project manager that "[i]f you feel strongly . . . that you've got additional work outside of the contract and the amendments, put it together with the proper back-up and the City will evaluate it." When the City refused to pay for the work, the designer filed a claim and then filed suit.

At trial, the City raised the "written change" requirement as a defense. The designer, on the other hand, argued that the City modified the "written change" requirement when it verbally authorized the designer to proceed with extra work pending written change orders on several previous occasions. The trial court agreed and ruled for the designer.

On appeal, the California Court of Appeals for the Fourth Appellate District acknowledged the general rule that parties to a contract may agree to modify its terms and that even an oral agreement suffices if carried out by the parties. However, the Court noted, a public body's powers are limited to those expressly granted. In this case, the City's authority to enter into contracts, and to modify them, was limited to written contracts. Furthermore, the Court noted, any attempt by a City employee or officer to bind the City orally is in excess of that person's authority. Accordingly, and although sympathizing with the designer, the Court ruled that no oral contract or contract modification is binding on the City. As to the City's powers, the Court noted that parties contracting with a public entity are presumed to have knowledge of public contracting law, including the restrictions applicable to municipal contracts.

A contractor that fails to obtain advanced written authorization before proceeding with extra work faces an uphill battle recovering for such work. In California, the grade of that hill just increased.

Visit Our Website for More Articles.