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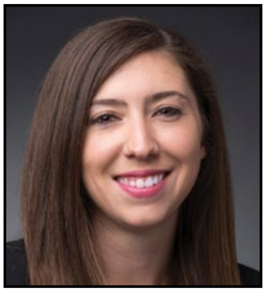
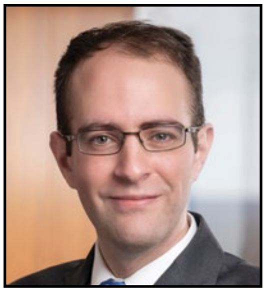
OSHA Retracts Proposed Vaccine Mandate

by Sarah K. Bloom, Associate and Gregory M. Wagner, Associate



Sarah K. Bloom



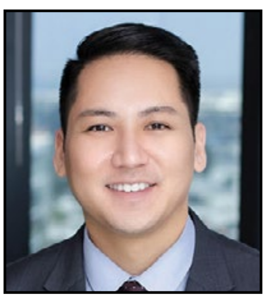
Gregory M. Wagner

Effective January 26, 2022, the U.S. Occupational Safety and Health Administration ("OSHA") withdrew its Emergency Temporary Standard ("ETS") that would have required companies with at least 100 employees to implement certain COVID-19 safety standards in the workplace. The ETS included a requirement that employees either receive COVID-19 vaccinations or undergo weekly testing. OSHA's withdrawal follows the United States Supreme Court's 6-3 decision imposing a temporary stay on the ETS. *See Nat'l Fed'n of Indep. Bus. v. Dep't of Labor*, 142 S. Ct. 661 (2022). In its decision, the Court signaled that the ETS was unlikely to survive a challenge on the merits.

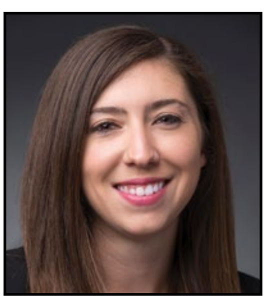
Thus, employers are no longer required to implement the safety standards set forth in the ETS. State and local rules may impose separate requirements which are unaffected by the Supreme Court's decision. In addition, the Supreme Court has not addressed the constitutionality of the vaccination mandate that was imposed by executive order upon federal contractors; that mandate is currently subject to a nationwide injunction. The Court did allow the Department of Health and Human Services' vaccine mandate for healthcare workers to take effect. *See Biden v. Missouri*, 142 S. Ct. 647 (2022).

Is Your Contract "Mission Essential?" Recovering Costs For Performing During A Force Majeure Event Under Federal Regulations

by Joneis M. Phan, Of Counsel and Sarah K. Bloom, Associate



Joneis M. Phan



Sarah K. Bloom

Federal contractors have faced unprecedented challenges performing during the COVID-19 pandemic. Additional costs have included delays and inefficiencies, site closures, quarantines, unavailability of supplies and materials, and full shutdowns of subcontractor operations. For contractors performing under fixed price contracts, the cost impact of COVID-19 was likely severe.

The Federal Acquisition Regulation ("FAR") recognizes "epidemics" as a force majeure event that may excuse non-performance. Many federal contracts include some version of the Default clause, which prevents the government from terminating a contractor for default due to impacts of force majeure events that are beyond a contractor's control, such as an epidemic. *See, e.g.*, FAR 52.249-10. *See also Pernix Serka Joint Venture v. Dep't of State*, CBCA No. 5683 (Apr. 20. 2020). The Default clause, however, operates as a shield from liability, not a sword authorizing recovery. Contractors are now left wondering whether any avenue exists to recover additional costs incurred after performing in the face of the COVID-19 pandemic.

In response to a likely influx of claims and requests for equitable adjustment due to COVID-19 impacts, the federal government largely took the position that contractors were entitled to extensions of time, but not to additional costs. This article explores the avenues that may be available for contractors to recover costs for performing during a force majeure event that would otherwise be non-compensable.

Examine Your Contracts For Explicit Remedies Related To "Mission Essential" Services

While the FAR does not address "mission essential services," clauses required by the various agency FAR supplements may explicitly address performance during emergencies or crisis situations.

Contractors furnishing services to the Department of Defense (DoD) may have an explicit remedy. DFARS 252.237-7023, "Continuation of Essential Contractor Services," was promulgated in response to the 2009 H1N1 influenza pandemic. The clause governs the performance of essential contractor services that support "mission-essential functions" and authorizes contractors to recover costs associated with continuing performance in a pandemic or emergency environment. Mission essential functions are those activities that must be performed under all circumstances to achieve DoD component missions or responsibilities, as determined by the appropriate functional commander or civilian equivalent. Failure to perform or sustain these functions would significantly affect DoD's ability to provide vital services or exercise authority, direction, and control. *See* 48 C.F.R. § 252.237-7023.

Contracting Officers must include the Continuation of Essential Contractor Services clause in all solicitations and contracts that are in support of mission-essential functions. *See* 48 C.F.R. § 252.237.7603. In other words, this clause *notifies* prospective contractors that they will be expected to continue performing during disasters and events which might otherwise justify suspending work. DoD promulgated the clause specifically to ensure continuity of contractor services during the H1N1 pandemic and, therefore, a worldwide pandemic is anticipated by the clause. The clause requires contractors to develop and maintain a Mission-Essential Services Plan, which the government can require the contractor to execute in appropriate circumstances.

Thus, some DoD contracts contain an explicit remedy granting clause authorizing monetary relief for additional costs incurred in performing during an emergency event. Even contractors whose contracts do not contain DFARS 252.237-7023 may, however, be able to support claims for monetary relief.

The *Christian* Doctrine May Incorporate Remedies By Operation Of Law

As discussed above, the designation of a contract (or a portion thereof) as "mission essential" is generally effectuated by the Contracting Officer's inclusion of DFARS 252.237-7023 in the solicitation or contract at issue. During the COVID-19 pandemic, however, the DoD's expectation that contractors continue performing appeared to extend beyond contracts that were explicitly designated as "mission essential."

On March 5, 2020, DoD issued a memo to all Services reminding them to incorporate DFARS 252.237-7023 into their contracts for mission essential services. In its memo, DoD recognized that "Today's changing environment has increased the need for continuity of operations . . . . Threats to continuity of operations include natural disasters, severe/inclement weather, pandemic, and a variety of other crisis situations."

Less than a month later, on March 20, 2020, the DoD identified the Defense Industrial Base ("DIB") as part of the "Essential Critical Infrastructure Workforce." The memorandum asserted that the mission essential workforce included "individuals *who support* the essential products and services required to meet national security commitments to the Federal Government and the U.S. Military [including] aerospace; mechanical and software engineers; manufacturing/production workers; IT support; security staff; security personnel; intelligence support, aircraft and weapon systems mechanics and maintainers; suppliers of medical supplies and pharmaceuticals, and critical transportation." (Emphasis added). The "mission essential" designation purportedly applied to "personnel working for companies, and their subcontractors, who perform under contract to the Department of Defense providing materials and services to the Department of Defense and government-owned/contractor-operated and government-owned/government-operated facilities." Upon issuing that designation, the DoD stated that contractors performing such services had a "special responsibility to maintain [their] normal work schedule[s]" in the face of the pandemic.

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DoD's broad definition of "mission essential" services may have swept in contractors and contracts that did not contain the mission essential DFARS clause. Nevertheless, an argument may exist that DFARS 252.237-7023 applies to such contracts by operation of law under the *Christian* doctrine.

Contracting Officers are required to include the Continuation of Essential Services clause (48 C.F.R. § 252.237-7023) in all solicitations and contracts that are in support of mission-essential functions. *See* 48 C.F.R. § 237.7603. Thus, the government's conversion and treatment of previously non-essential contracts as now "essential," may have triggered an obligation to incorporate DFARS 252.237-7023 into the contract as a mandatory clause.

Under the *Christian* Doctrine, mandatory clauses are read into government contracts by operation of law even when they are omitted from the contract. *See G.L. Christian & Assocs. v. United States*, 312 F.2d 418 (Ct. Cl.), cert. denied, 375 U.S. 954 (1963); *see also Appeal of Transcontinental Cleaning Co.*, NASA BCA No. 1075-9, 78-1 BCA ¶ 13081(where agency regulation mandated incorporation of Price Adjustment Clause, *Christian* doctrine applied and contractor was entitled to reimbursement for increased costs); *K-Con v. Secretary of Army*, 908 F.3d 719 (Fed. Cir. 2019) (*Christian* doctrine applied to incorporate mandatory bond requirements into contract; contractor was responsible for costs of obtaining a bond).

No Court has analyzed whether the Continuation of Essential Services Clause is the type of clause that "express[es] a significant or deeply ingrained strand of public procurement policy" to which the *Christian* doctrine is applied. *See Gen. Eng'g & Mach. Works v. O'Keefe*, 991 F.2d 775, 779 (Fed. Cir. 1993) (*Christian* doctrine not applicable to *all* mandatory clauses). Several recent events, however - such as the 2009 H1N1 epidemic, the Ebola epidemic, and several lapses in federal agency appropriations - have brought the issue of mission-essential contractor services to the forefront.

Moreover, the *Christian* doctrine has been applied to clauses that appear far less significant. *See id.* (noting that the *Christian* doctrine has been applied to clauses requiring exhaustion of administrative remedies, implementing Buy American Act, and outlining pre-award negotiating procedures). Neither the Armed Services Board of Contract Appeals nor the Court of Federal Claims has addressed the clause in this context. Nevertheless, an argument could exist that the government's designation of construction contracts as essential, combined with the regulatory and statutory mechanisms for establishing continuity of essential services in the event of a government shutdown, are significant enough to justify application of the *Christian* doctrine.

Relief May be Available Under A Constructive Change Theory

Even if the Government is reluctant to recognize DFARS 252.237-7023 as part of a Contract under the *Christian* doctrine, relief may be available under a theory of constructive change. As set forth above, Contracting Officers are required to include the Continuation of Essential Services clause in all solicitations and contracts that support mission-essential functions. *See* 48 C.F.R. § 237.7603. Treating a contract as one for mission-essential functions when the contract does not contain that clause may be viewed as a constructive change to the Contract.

By re-designating a Contract as "mission essential," the government required continued performance in the face of a crisis which may otherwise have excused non-performance. This change to the Contract's allocation of risk may justify the recovery of additional costs. Moreover, the costs of developing and implementing an Essential Contractor Services Plan, as required by the clause, may be allowable under the FAR. *See* DCAA Selected Areas of Costs Guidebook: FAR 31.205 Cost Principles, Chapter 13, Continuation of Essential Contractor Services (indicating that plan preparation, maintenance, and execution costs are allowable under FAR Part 31).

Contractors who were treated as "mission essential" despite the government's failure to include DFARS 252.237-7023, or a similar clause, should consider opening a discussion with the government about the impacts of that treatment, and should explore the government's appetite for recognizing a change to the contract.

Moving Forward: Drafting Or Revisiting Your Mission Essential Services Plan

DFARS 252.237-7023 requires contractors to prepare a Mission Essential Services Plan, which explains how the contractor will continue performing during a crisis event. Even if a contract does not contain the mission essential clause, the government has demanded continued performance during a pandemic. Contractors preparing to bid on new solicitations should, therefore, devote some attention to preparing a Mission Essential Services Plan. Where the solicitation does contain the DFARS clause, contractors should devote substantial attention to their plan.

An effective Mission Essential Contractor Services Plan must provide clear and concise details for the agency to reasonably evaluate and accept the plan. In fact, agencies have downgraded proposals that fail to address the issues listed above in sufficient detail, and such decisions have been upheld in bid protests before the Government Accountability Office. *See InnovaSystems Int'l, LLC*, B- 417215, B- 417215.2, B- 417215.3, 2019 CPD ¶ 159 (April 3, 2019). Thus, going forward, agencies may devote more attention to the content of proposed Mission Essential Services Plans in evaluating proposals for future contracts.

Prospective contractors should carefully review solicitations for all requirements related to the Mission Essential Services Plan, and address any specific concerns identified by the agency in detail. At a minimum, such plans must address: (1) challenges associated with maintaining essential contractor services during an extended event, such as a pandemic that occurs in repeated waves; (2) the time lapse associated with the initiation of the acquisition of essential personnel and resources and their actual availability on site; (3) the components, processes, and requirements for the identification, training, and preparedness of personnel who can work from home; (4) any established alert and notification procedures for mobilizing identified "essential contractor service" personnel; and (5) the approach for communicating expectations to contractor employees regarding their roles and responsibilities during a crisis. DFARS 252.237-7024(b).

The plan should also address essential services that cannot be fully provided despite best efforts, costs for preparing the plan, and the costs for keeping the plan in place. Finally, the plan must consider and identify the procedures to maintain the continuity of services "for up to 30 days or until normal operations can be resumed." DFARS 252.237-7023(b)(1).

Conclusion

Contractors seeking to understand how a force majeure event may impact their construction project should seek advice of counsel. If you have questions on any matters related to drafting or enforcing an existing Mission Essential Services Plan, project delay, project suspension, or contractual rights to suspend or terminate, please contact Watt, Tieder, Hoffar & Fitzgerald LLP for assistance.

RECENT DEVELOPMENTS

I'm Subordinated To What? The Conflux Between The Bankruptcy Code And Equitable Subrogation

By Marguerite Lee DeVoll, Partner

Introduction

One of the hallmarks of surety law is the doctrine of equitable subrogation. As the Supreme Court explained, "a surety who pays the debt of another is entitled to all the rights of the person he paid to enforce his rights to be reimbursed." *Pearlman v. Reliance Ins. Co.*, 371 U.S. 132, 137 (1962). As often stated colloquially, the surety "steps into the shoes" of the party benefitting from the surety's performance in order to enforce whatever rights and remedies that party may possess. For example, under a performance bond, a performing surety stands in the shoes of the project owner to utilize the contract balances to fund completion of the project. Subrogation thus serves an important tool in the surety's proverbial "toolbox" to reduce losses sustained when performing under a bond.

When a bond principal files for bankruptcy, however, the availability and use of subrogation as a tool by the surety becomes more complicated. Specifically, sections 509(a) and (c) of the Bankruptcy Code both broaden and limit the surety's rights of subrogation. This article provides a high-level explanation of how

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subrogation interacts with sections 509(a) and (c) of the Bankruptcy Code, and, in particular, highlights how the facts of a case can drive different outcomes.

Elements Of Equitable Subrogation

The elements of equitable subrogation have been explained differently by different courts. Generally, however, a surety can assert the right of subrogation when: (a) the principal owes an obligation to an obligee; (b) the principal fails to perform that obligation; and (c) the surety, acting not as a volunteer or a primary responsible party, performs that obligation. Sometimes courts consider whether others would suffer an injustice if subrogation is permitted in determining the availability of subrogation.

The right of subrogation generally has two limitations that are often impacted by a bond principal's bankruptcy filing. First, the surety, as subrogor, usually cannot acquire any greater rights than those possessed by the subrogor. Second, the surety must fully perform, *e.g.*, pay in full, before acquiring subrogation rights. [Subrogation, as with many other rights, may be altered pursuant to contract.]

Subrogation Under The Bankruptcy Code – Section 509

Section 509 of the Bankruptcy Code is considered "the statutory enactment of the long-standing doctrine of equitable subrogation." *In re Chateaugay Corp.*, 89 F.3d 942, 947 (2d Cir. 1996). Section 509 provides:

> (a) Except as provided in subsection (b) or (c) of this section, an entity that is liable with the debtor on, or that has secured, a claim of a creditor against the debtor, and that pays such claim, is subrogated to the rights of such creditor to the extent of such payment.
>
> …
>
> (c) The court shall subordinate to the claim of a creditor and for the benefit of such creditor an allowed claim, by way of subrogation under this section, or for reimbursement or contribution, of an entity that is liable with the debtor on, or that has secured, such creditor's claim, until such creditor's claim is paid in full, either through payments under this title or otherwise.

Section 509(a), unlike the general common law principles, allows a surety to be subrogated to the rights of a subrogee "to the extent of such payment." 11 U.S.C. § 509(a); *see also In re LTC Holdings, Inc.*, 10 F.4th 177, 186 (3d Cir. 2021).

Section 509(c), on the other hand, reflects the common law principal of payment in full by subordinating the surety's right of subrogation until the subrogee is paid in full. 11 U.S.C. § 509(c). The purpose behind imposing this limitation (or rather codifying the common law limitation to subrogation) is to protect the subrogee from a competing surety claim until the subrogee is fully paid and to encourage a surety to pay claims in full rather than placing limitations on what it expects to recover from the bankruptcy. *See In re LTC Holdings, Inc.*, 10 F.4th at 186.

How Does Section 509(c) Play Out In The Bankruptcy Context?

Section 509(c)'s payment in full requirement can impact a surety's subrogation rights in several different contexts. Some courts interpret section 509(c) to require the subrogee to be paid in full on its claim *before* the surety receives any payments on its claim. *In re M & S Grading, Inc.*, No. BK02-81632-TJM, 2009 WL 1872636 (Bankr. D. Neb. June 25, 2009). In other instances, the "paid in full" requirement may impact a surety's right to assert the subrogee's rights of setoff. [What constitutes "paid in full" varies based on the facts of the case and in and of itself, could be the topic of a separate article.]

Two Circuit Court cases illustrate how section 509(c) interacts with a surety's subrogation rights to assert a subrogee's rights of setoff: *In re LTC Holdings, Inc.* from the Third Circuit and *In re Chateaugay Corp.* from the Second Circuit.

In *Chateaugay Corp.*, 94 F.3d 772 (2d Cir. 1996), the surety posted a bond to secure a mining operator's black lung self-insurance obligations. When the mining operator filed for bankruptcy, it stopped paying the black lung benefits. The Department of Labor ("DOL") for some months paid the benefits, but then the surety took over and fully performed under the bond.

Thereafter, the mining operator and the DOL entered into a settlement agreement on the DOL's claim for repayment of the black lung benefits it paid. The surety objected on the grounds that risked extinguishing the surety's subrogation rights. The settlement was approved and the surety appealed. On appeal, the Second Circuit affirmed the settlement approval, but expressly noted that the settlement could have no adverse effect on the surety's rights or claims.

After the settlement with the DOL was approved, the Internal Revenue Service ("IRS") filed proofs of claim for post-petition excise tax liabilities. The mining operator and the IRS also entered into a settlement agreement that included the IRS setting-off the post-petition excise by pre-petition tax refunds. The surety objected claiming a superior interest in the tax refund money, and the matter ultimately made its way to the Second Circuit again.

The Second Circuit held that the first settlement order between the mining operator and the DOL resulted in "payment in full" to the DOL. Further, the approval of the settlement order expressly provided that it would not adversely affect the surety's rights. As such, the surety was no longer subordinated to the DOL and could assert whatever rights the DOL possessed, including the claims to the pre-petition tax refund subject to the second settlement with the IRS.

In *LTC Holdings*, the surety issued performance and payment bonds on behalf of a contractor on federal contracts. Pre-petition the contractor/debtor defaulted under one of the contracts and called upon the surety to perform, which it did through a tender agreement. The tender agreement specifically provided that the payment and performance bonds would remain in force and effect until the contract was completed.

Thereafter, the contractor/debtor filed for Chapter 7 bankruptcy. Right before doing so, however, the contractor/debtor filed a federal tax return showing net operating losses and seeking a "carryback" refund for approximately $5.5 million for federal income taxes paid in a prior year.

During the course of the debtor/contractor's bankruptcy, the federal government filed proofs of claim stemming from several breached contracts. As for the debtor/contractor, it had filed litigation against the federal government for, among other things, unpaid contract balances. Ultimately, however, the federal government and the debtor/contractor reached a settlement whereby the federal government's proof of claim would be allowed, the debtor/contractor would dismiss its litigation, and importantly, the federal government would waive its right of setoff against the outstanding pre-petition tax refund.

The surety objected to the proposed settlement on the grounds that it should not be construed to release or impair the rights or claims belonging to the surety, as subrogee to the federal government. The parties ultimately agreed to a settlement order, which approved the settlement, held the tax refund in escrow pending further order of the court, and reserved any and all rights and arguments the parties had regarding the ownership of, or their interest in the tax refund prior to the entry of the order.

An adversary proceeding was subsequently commenced to determine the parties' rights. On summary judgment, the bankruptcy court determined that the federal government had not been paid in full when the settlement order was entered, thus the surety remained subordinated to the rights of the federal government, and the federal government was entitled to waive its setoff rights in order to settle its "superior and remaining claim."

The Third Circuit affirmed the decision on appeal. In doing so, the Third Circuit distinguished the facts in *LTC Holdings* from those in the Second Circuit's earlier decision in *Chateaugay Corp.* Specifically, the Third Circuit explained that in *Chateaugay Corp.*, the first settlement order – which the surety vigorously opposed – resulted in payment in full of the DOL on all its claims (and the surety had previously fully performed). The first settlement order also expressly held that the surety's rights would not be adversely affected. Consequently, when a subsequent settlement agreement with the IRS was proposed, the surety could assert the DOL's rights of setoff to the tax refunds.

In contrast, in *LTC Holdings*, the Third Circuit found that, among other things, the surety had dropped its objection to the settlement order that specifically raised the waiver of setoff rights arguments, and instead, only reserved undefined "rights and arguments" to setoff the tax refund *prior* to entry of the settlement order. Notably, the Third Circuit held that under no scenario could the surety claim that the federal government had been paid in full *prior* to entry of the settlement order. Consequently, the surety was still subordinated to the federal government when the settlement order was entered.

The Third Circuit also found that section 509(c) "places the surety in line behind the obligee, who may exhaust the funds to satisfy his own claim." *In re LTC Holdings, Inc.*, 10 F.4th at 189. Thus, because the surety was still subordinated to the federal government's claim, the federal government was free to pursue its rights, even if it is to the surety's detriment, *i.e.*, waiver of setoff rights.

Conclusion

The disparate holdings in *LTC Holdings* and *Chateaugay Corp.* highlight some of the issues

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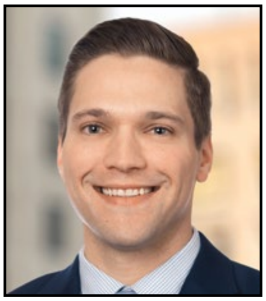
that sureties face when confronted with a bond principal's bankruptcy filing. In particular, the two holdings demonstrate that timing, facts, and even something as simple as language in a stipulated order, can greatly impact a surety's rights of equitable subrogation.

Further, the impact of section 509(c) on a surety's subrogation rights is only one of the many challenges a surety may face when enforcing subrogation rights in a bankruptcy. Sureties need to be mindful that there are several other Bankruptcy Code sections that not only speak directly to issues of subrogation, but also impact the rights of the subrogee through which the surety may ultimately seek to assert a claim. Thus, sureties should seek the advice of bankruptcy counsel when one of their bond parties finds themselves in bankruptcy.



No Signature? Potentially No Problem For Sureties Enforcing A Bond's Forum Selection Clause

by Brian C. Padove, Associate

One of the foundational tenets of contract law is that a party may only be bound by terms they agree to, or in other words, if the party did not sign a contract, that party cannot be bound by the terms thereof. While this principle is generally unwavering, there are certain situations in which a non-signatory to a contract may still be bound by the terms of a contract.

In particular, this non-signatory issue may arise when a payment bond claimant makes a bond claim, subsequently files a lawsuit, but the bond contains a forum selection clause different than the venue of the lawsuit and the surety seeks to enforce the bond's forum selection clause. For example, the claimant may have filed its lawsuit against the surety in federal court, even though the bond provides language specifically mandating that no lawsuit shall be commenced by any claimant other than in a state court where the project is located. Thus, the question then becomes, can the surety enforce the forum selection clause against the claimant when the claimant did not sign the bond and/or never agreed to the terms thereof? The short answer, it depends (yes, that is a very lawyer-like answer). Given recent case law over the past decade, however, the surety has a strong argument in favor of enforcement of the forum selection clause.

This article will provide a brief summary of the United States Supreme Court decision in *Atlantic Marine Constr. Co. v. United States Dist. Court for Western Dist. of Texas*, 571 U.S. 49 (2013), in conjunction with the Seventh Circuit's approach for analyzing forum selection clauses. It will then set forth an analysis of the applicability of these rules to payment bond claimants, along with a summary of a concept known as "direct benefits estoppel," and conclude with final takeaways for sureties and payment bond claimants (including subcontractors and suppliers) to consider.

Enforceability Of Forum Selection Clauses

In relevant part, the United States Supreme Court's decision in *Atlantic Marine* impacted forum selection clauses on two fronts. First, *Atlantic Marine* clarified the procedural mechanism parties should follow when seeking dismissal or transfer of a lawsuit involving a valid forum selection clause. Second, the decision affirmed the position that courts favor enforcement of the freedom of contracting between parties, which includes forum selection clauses. As to the proper mechanism, the Supreme Court found that enforcement of a forum selection clause triggers 28 U.S.C. § 1404(a) when a lawsuit is filed in a federal forum different than a federal forum specified in the forum selection clause. If the forum selection clause calls for litigation in a foreign country or state court, however, the "remedy' is to file a motion to dismiss under the common law doctrine of *forum non conveniens*. *Atlantic Marine*, 571 U.S. at 61. As to the latter, the Court noted that a valid forum selection clause should be given great weight in all but exceptional circumstances because it represents and protects the parties' expectations and the interests of the justice system. *Id.* at 63.

Accordingly, there is a strong presumption in favor of enforcing forum selection clauses and, under Seventh Circuit case law, they are *prima facie* valid and enforceable unless enforcement is unreasonable under the circumstances. *See Bonny v. Soc'y of Lloyds*, 3 F.3d 156, 159 (7th Cir. 1993). Seventh Circuit courts narrowly construe this "unreasonable" exception to enforceability and will generally only consider the clause unreasonable and refuse transfer to the chosen forum in the face of fraud, grave inconvenience, or contravention of strong public policy. *See, e.g., Faur v. Sirius Intern. Ins. Corp.*¸ 391 F. Supp. 2d 650, 657 (N.D. Ill. 2005).

In essence, *Atlantic Marine* and Seventh Circuit courts have set forth a three-part test as to enforcement of forum selection clauses: (1) whether there is a valid and enforceable forum selection clause; (2) whether the clause is "mandatory" through the use of obligatory language; and (3) if elements one and two are met, whether there are exceptions present to the general rule of enforceability. Thus, the first step is looking to the agreement to determine whether there is, in fact, a forum selection clause. From there, one looks to whether the clause's language is mandatory. For instance, does the clause state that the claimants "may" file suit in a specific jurisdiction, or is there language stating that any suit on the bond "shall" be filed in the specified jurisdiction? The latter language using "shall" constitutes "mandatory" language in support of enforcement. Finally, courts will look to the exceptions to determine whether there exists any fraud or grave injustice. Note, however, that once a valid and mandatory forum selection clause is established, the burden is on the party opposing transfer to demonstrate that one of the exceptions to enforcement applies.

Payment Bond Forum Selection Clauses

Generally, payment bond claimants do not "accept" the terms and conditions of payment bonds through execution of bonds at issue. In fact, often claimants do not have knowledge of what terms are included in an upstream contractor's payment bond until a copy of the bond is requested when a potential claim arises. The issue arises when the payment bond includes a forum selection clause that the claimant never agreed to and the surety wants to enforce the clause. Unsurprisingly, payment bond claimants may wonder how they can be bound by terms to which they never agreed, that are included in an agreement which they never signed.

The short answer to this question is: although a claimant may not be a signatory to the payment bond, it is foreseeable that a claimant would be bound by the bond's terms, which would include the forum selection clause. According to the Seventh Circuit, a forum selection clause may bind a non-party if that party is "closely related," such that it becomes foreseeable that it will be bound. *Hugel v. Corporations of Lloyd's*, 999 F.2d 206, 209 (7th Cir. 1993). As such, notwithstanding that a claimant does not sign the payment bond and expressly agree to its terms, it is eminently foreseeable that a claimant is the type of party the forum selection clause intends to bind, and thus, the claimant would be bound by the forum selection clause. In other words, a payment bond claimant would clearly be a "closely related" party, whereby it would be foreseeable for that party to be bound. The fact that the claimant did not sign the payment bond should be of no consequence to enforcement of the terms, including the forum selection clause.

Direct Benefits Estoppel

A surety looking to enforce a bond's forum selection clause against a non-signatory payment bond claimant can also look to the doctrine of "direct benefits estoppel." This doctrine generally applies to non-signatories who, on the one hand, embrace a contract's benefits, but on the other hand, during litigation, attempt to repudiate a clause in the contract, such as a clause mandating arbitration. The United States District Court for the Northern District of Texas addressed this issue in *Quality Custom Rail & Metal, LLC v. Travelers Cas. and Sur. Co. of America*, No. 3:13-cv-3587-D, 2014 WL 840046 (N.D. Tex. March 4, 2014). Specifically, the *Quality Custom* court noted that the direct benefits estoppel doctrine would apply when a "non-signatory" payment bond claimant knowingly seeks and obtains benefits from the contract/bond or seeks to enforce the terms of the contract/bond which contains the forum selection clause. The court then determined that by seeking to enforce the terms of the bond by bringing a lawsuit against the surety for unpaid labor, the payment bond claimant was seeking direct benefits under the bond. Thus, the claimant could not then claim that the forum selection clause did not apply to it simply because the claimant was not a signatory to the bond.

In short, the direct benefits estoppel doctrine generally provides that a party cannot pick and choose which provisions apply to it. That is, a payment bond claimant cannot bring a lawsuit seeking payment from a surety under a payment bond, and then assert that, because it did not sign the bond, it is not bound by the bond's forum selection clause.

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Takeaways

One of the fundamental maxims of contract law is that parties may generally only be bound by terms to which they agree. In the payment bond context, however, this answer is not always clear. For claimants who, prior to a claim arising, may have no knowledge of a payment bond's terms, they still may be bound by the terms of the bond – even though they never agreed to such terms. On its face, this goes against what many would believe is common sense. Given that the claimants are attempting to recover under the bond, however, it is not surprising that the claimant must also be bound by the other terms of the bond.

Thus, contractors, subcontractors, and suppliers making payment bond claims should be aware that they are not only entitled to rights under the payment bonds, but they also may be obligated to comply with other terms of the bond even though they never agreed to such terms. For sureties, *Atlantic Marine*, in conjunction with the direct benefits estoppel doctrine, may provide guidance to disregard foundational contract law principles (that contract terms are only enforceable against signatories to a contract) and for the enforcement of a forum selection clause against payment bond claimants, regardless of whether the claimants agree to resolve their dispute in the chosen forum.

An Association's Right To Sue In Its Representative Capacity Requires It To Comply With The Arbitration Agreements Signed By Each Of Its Members

by Mariela M. Malfeld, Partner

In Florida, when a homeowner or condominium association files a lawsuit acting in a representative capacity for its members, the association has no greater rights than that of its members had they raised their claims on an individual basis. Premised on this logic, the Third District Court of Appeal of Florida held that a homeowners' association was bound by the arbitration agreements to which each of the homeowners agreed would apply to any disputes pertaining to their homes.

In this case, Martinique is a community in Miami-Dade County consisting of 26 townhouse buildings. Prior to closing, the developer and the original purchasers at Martinique executed a purchase and sale agreement containing an arbitration provision that applied to the disputes pertaining to their homes. In addition to the Purchase and Sale Agreement, upon each home sale, the developer recorded a special warranty deed for each home. Each Special Warranty Deed also contained an arbitration provision nearly identical to that of the Purchase and Sale Agreement.

In the lawsuit, the association alleged there were stucco issues at the exterior walls of the individual homeowners' homes causing damages and that it was responsible for maintaining the stucco at the homes' exteriors. The developer moved to dismiss and compel the dispute to arbitration on the basis that the association was bound by the arbitration provision in its members' (the real property owners) Purchase and Sale Agreement and Special Warranty Deeds. According to the arbitration agreements, any disputes "arising under or relating to" a member's home were "subject to binding arbitration as provided by the Federal Arbitration Act (9 U.S.C. §§1 et seq.) and not by or in a court of law or equity." The trial court denied the developer's motion, however, holding that there was no arbitration agreement between the association and the developer and that the lawsuit concerned matters that the association was obligated to maintain.

The developer appealed. The Third District Court of Appeal, relying on precedent from its sister court, the Second District Court of Appeal, agreed with the developer, holding that the association's right to proceed in its representative capacity required it to abide by the members' agreement with the developer to arbitrate the disputes. *See Pulte Home Corp. v. Vermillion Homeowners Ass'n, Inc.*, 109 So.3d 233, 235 (Fla. 2d DCA 2013). Even if the association had an obligation to maintain some aspect or portion of that property, and could therefore bring suit in its representative capacity, it was nevertheless the homeowners who were the real parties in interest.

As an aside, the association also argued that the arbitration provision in the Purchase and Sale Agreement and Special Warranty Deed should be deemed void against public policy under Florida Statute § 720.3075(1)(b), which prohibits the inclusion or enforcement of clauses in homeowners' association documents, including declaration of covenants, articles of incorporation, bylaws, or any other document of the association, that prohibit or otherwise restrict an association from bringing a lawsuit against a developer. The Third District Court of Appeal found this argument unavailing as neither the Purchase and Sale Agreement nor the Special Warranty Deed, both of which included the arbitration provision, were not association documents.

FIRM NEWS

Recent And Upcoming Events

Ankura Construction Forum, January 18, 2022; Webinar. **Brian C. Padove** spoke on Supply Chain Crisis: Mitigating Risk in Uncertain Times.

ABA Tort, Trial and Insurance Section's Fidelity and Surety Law Committee's Mid-Winter Conference, January 19, 2021; Nashville, Tennessee. **Hanna Lee Blake** presented on Takeover Agreements.

AACE 6th Annual Northeast Symposium, April 1, 2022, Tysons Corner, Virginia. **Christopher J. Brasco** and **Matthew D. Baker** will present on "Damages Without A Cause: Liquidated Damages Are A Penalty When Owners Recover Damages for Their Own Delay."

Southern Surety & Fidelity Claims Conference, April 27-29, 2022; Clearwater, Florida. **Christopher J. Brasco** and **Mariela Malfeld** will speak on "10 Risk Management Maxims That Will Reduce Your Bond Exposure Every Time."

ABA Tort, Trial and Insurance Section's Fidelity and Surety Law Committee's Spring Meeting, May 5-6, 2022; Hilton Head, South Carolina. **CharCretia Di Bartolo** will speak on "Taking Care of Business – Bonds for Employers (Workers Compensation Bonds)."

Construction Financial Management Association's (CFMA) 2022 Annual Conference & Exhibition, May 16, 2022; Atlanta, Georgia. **John E. Sebastian** and **Brian C. Padove** will co-present "From Supply Chains to Inflation – Managing Fluctuating Challenges and Risks."

AACE National Conference, June 26-29, 2022; San Antonio, Texas. Christopher J. Brasco and **Matthew D. Baker** will present on "No Half Measures with Half Steps: Re-examining Time Loss Through the Prism of the Half Step Methodology."

Honors

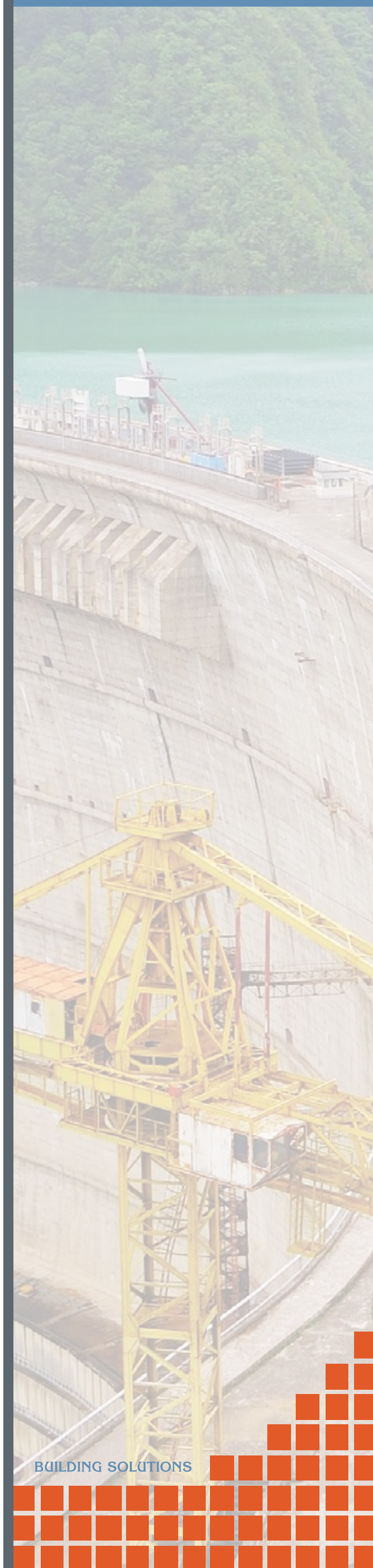
John E. Sebastian has been selected as a Fellow to the **Construction Lawyers Society of America** (CLSA). The CLSA is an invitation-only international honorary association composed of preeminent lawyers specializing in construction law and related fields. Fellowship is limited and selective, with lawyers being invited into Fellowship upon a proven record of excellence and accomplishment in construction law at both the trial and appellate levels.

Publications

The Law of Commercial Surety Bonds, "Workers Compensation Bonds," **CharCretia Di Bartolo**, May 2022.

CFMA Building Profits, December 2021, "How Can Subcontractor Prequalification Benefit the Contractor?", **John E. Sebastian** and **Brian C. Padove** (co-authors).

ABA Tort Trial and Insurance Practice Section, *Fidelity and Surety Law Newsletter*, Fall 2021, **John E. Sebastian**, Editor.



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The Watt, Tieder, Hoffar & Fitzgerald newsletter is published quarterly and is designed to provide information on general legal issues that are of interest to our friends and clients. For specific questions and concerns, the advice of legal counsel should be obtained. Any opinions expressed herein are solely those of the individual author.

Special Thanks to Editors, **Timothy E. Heffernan, William Groscup, Christopher M. Harris** and **Marguerite Lee DeVoll**.

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