CONSTRUCTION IN BRIEF

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CONSTRUCTION IN BRIEF

A Quarterly Publication brought to you by the law firm of Cohen, Seglias, Pallas, Greenhall & Furman, P.C.

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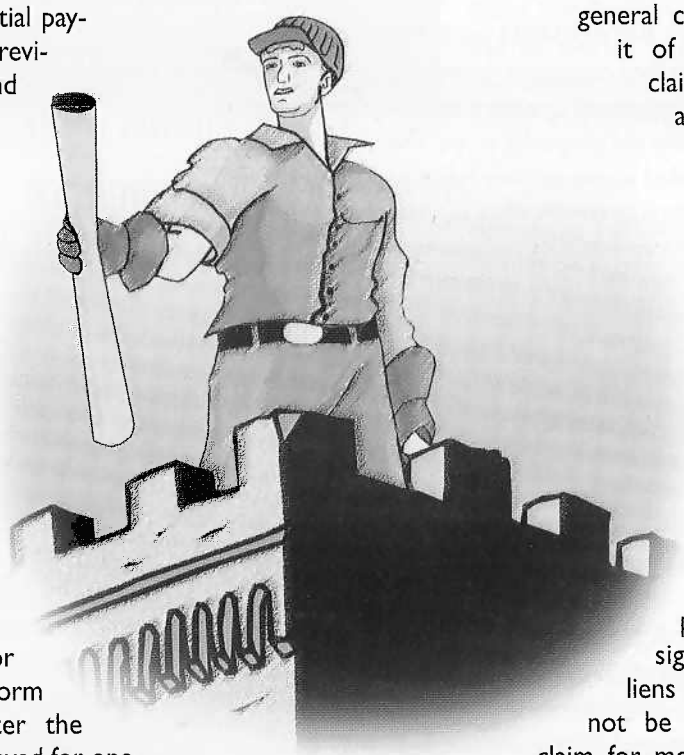
PRESERVE YOUR RIGHTS

A LOOK AT PROGRESS and FINAL PAYMENTS

Imagine you are a contractor (general contractor or subcontractor) that is being delayed on a project. You have submitted the required notice to the owner or general contractor documenting the delay, and requesting reimbursement of the costs incurred and an extension of time. The owner has not yet agreed to pay you any additional money or grant an extension of time. In the meantime, the owner wants to make a partial payment for the work previously performed and demands a "*Waiver of Liens and Claims.*" Should you sign it?



By signing a waiver of liens and claims, a contractor may lose its right to make a claim for additional money. In fact, in a recent federal court case, a drywall subcontractor was asked to perform additional work after the project had been delayed for one year. As required by the contract, the drywall subcontractor signed waivers in order to receive partial payment for the additional work. In addition, the drywall subcontractor sent periodic letters explaining that the change orders did not include all the costs that arose from the delay and that it would be seeking additional costs, which were impossible to quantify until the end of the project. At the end of the project, the drywall subcontractor sued the general contractor, to recover delay damages.

The court found that the drywall subcontractor had waived any claim for additional compensation by signing the waivers. The fact that the subcontractor sent letters to the general contractor notifying it of additional money claimed was immaterial. What the drywall subcontractor had waived could not be recaptured through a letter.

So what is a contractor to do? If you do not sign the waiver of liens and claims, you do not receive the partial payments. If you sign the waiver of liens and claims, you may not be able to pursue a claim for money at the end of the project.

Here are a few helpful suggestions:

- Strike from your contract any obligation to sign a waiver of liens and claims as a condition precedent to the receipt of a partial payment.

(article continued on page 4)

Restrictive Covenants

CAN YOU PROTECT YOUR EMPIRE?

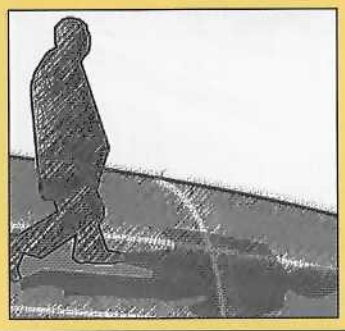
You were more than a bit upset last week when your best sales representative quit to join your biggest competitor. Can you get an injunction to prevent the former employee from taking your customers? It, of course, depends. First of all, unless you can prove that your former employee stole your customer list or other confidential information, an injunction can only be obtained if the employee is bound by an enforceable restrictive covenant. Restrictive covenants generally fall into four categories:

Non-Competition Agreements prohibit an employee from working for a competitor. In order to be enforceable, a non-competition agreement must be reasonably limited in time and geographic scope. This means that a court would almost certainly refuse to enforce a non-competition agreement which says that "Employee shall not during Employee's employment and for a period of five (5) years thereafter, be employed by any Competitor within a radius of 1500 miles from Employer's office." The same agreement may be enforceable if it is limited to six months and 50 miles. Also, a court is far more likely to enforce a non-competition agreement that reasonably defines "competing entities." For example, is "competing entities" defined as "commercial teledata electrical contractors" or "all electrical contractors?"

Non-Solicitation Agreements prohibit an employee from soliciting customers. Non-solicitation agreements must be reasonably limited in time. When drafting non-solicitation agreements, the definition of the "Employer's Customers" must be precise. Does this term include customers for whom the employer has provided services within the past two years (or ten years)? Does it include potential customers?

Anti-Pirating Agreements state that an employee may not, during the employment relationship and for a reasonable period of time thereafter, solicit any other employee to become employed by a competitor.

"...if you start thinking about restrictive covenants after your company loses one or more key salespersons, it may be too late."



Confidentiality Agreements prohibit an employee from disclosing confidential information to any unauthorized person. Unlike non-competition, non-solicitation, and anti-pirating agreements, confidentiality agreements need not be limited in time. Significantly, having a written confidentiality agreement allows an employer to select a definition of the term "confidential information" which fits its business. A typical confidentiality agreement may define this term as "(1) information which the employee learns during the course of performing services for employer; (2) the name, contact persons, credit terms, and/or requirements of any customer or potential customer; and (3) information with respect to the rate schedules, procedures, advertising, finances, organization, plans or strategies."

While some restrictive covenant agreements should include all of the above-described agreements, many should not. When preparing a restrictive covenant, employers should first consult with counsel to determine what provisions would be legally enforceable in their situation. Employers must then temper their restrictive covenant "wish lists" in light of industry standards and their employees' or prospective employees' willingness to tolerate restrictions.

Finally, the timing of when a restrictive covenant is signed is absolutely critical. In some states, including Pennsylvania, a restrictive covenant is legally valid only if (1) it is signed at or before the start of the employment relationship; or (2) the employee receives something of value – such as a raise or bonus that the employee would not have otherwise received – at the time the agreement is signed.

Bottom line: if you start thinking about restrictive covenants after your company loses one or more key salespersons, it may be too late.

-- Jonathan Landesman, *Esquire*

The Business Practice Group Provides Answers

PAYROLL TAXES

Q: ***A business owner has started to receive collection notices from the IRS regarding unpaid payroll taxes. She wants to know what actions the IRS can take against the company and can she be personally liable for these unpaid payroll taxes? What is the Trust Fund Recovery Penalty that the IRS has threatened to assess against her?***

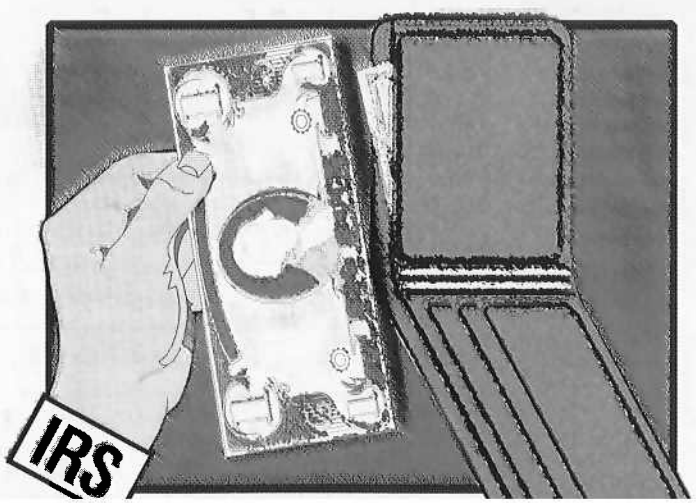
A: If your company owes payroll taxes to the IRS, not only is your business at risk, but you may be personally liable for the unpaid taxes. Once the IRS has determined that the business cannot pay its past due payroll taxes, the IRS can turn to the individuals who the IRS has determined are responsible for the payment of the taxes.

Employers are required to withhold federal income taxes and social security (FICA) taxes from their employees' wages and are liable for payment of these taxes to the IRS. These funds, commonly referred to as "trust fund taxes," are considered to be held in trust and cannot be spent for any purpose. They must be remitted to the government on a timely basis and the employer has a legal obligation and fiduciary duty to do so. It is important to note that trust fund taxes do not include the employer's matching portion of FICA taxes.

In addition to the recourse against a company for these taxes, Congress enacted a provision in the Internal Revenue Code known as the "Trust Fund Recovery Penalty." This provides that any individual who (1) had the duty to collect, account for and pay over trust fund taxes, and (2) willfully failed to pay them, is personally liable.

The amount of the penalty is measured by the payroll taxes required to be collected, or collected and not paid. This penalty is civil in nature, not criminal, although the IRS may pursue criminal liability if it concludes there has also been tax evasion. Once assessed against an individual, the penalty is non-dischargeable in bankruptcy and has a ten-year collection statute like most other taxes which have not been reduced to a judgment.

-- Robert J. Birch, *Esquire*



ESTATE PLANNING

Q: ***A client asks to have his estate plan reviewed and advises that a member of his family has Special Needs, which qualify that family member for various governmental benefits. What, if anything, needs to be included in the estate plan in order to protect these benefits?***

A: Special Needs individuals are entitled to receive available governmental benefits and services such as Supplemental Security Income (SSI), Medicaid, Food Stamps, state public assistance and a large number of social service programs. However, income received from a trust or an estate may limit the amount to which a Special Needs individual may be entitled. Fortunately, it is not necessary to disinherit your heir to protect their rights. You can do this with either a Special Needs Trust or an Irrevocable Medicaid Trust, both allow for payment from the Trust for the comfort and welfare of the beneficiary.

A Special Needs Trust gives the trustee total discretion to pay for the needs of the Special Needs beneficiary. This discretion allows the trustee to withhold paying for such needs. The trustee can either refuse a distribution or utilize all or a portion of the trust assets and income for any other beneficiary of the trust. Upon the death of the Special Needs beneficiary, the trust assets may be distributed to the other beneficiaries of the trust. The specific requirements for Special Needs Trusts, however, vary from state to state.

An Irrevocable Medicaid Trust is similar to a Special Needs Trust with one major exception: upon the death of the Special Needs beneficiary, any assets remaining in the trust must first be applied to pay back the government for all payments made by Medicaid for the benefit of the Special Needs beneficiary. Any assets then remaining can be used for or are distributed to the other beneficiaries of the trust.

In addition to making sure that your Will protects your Special Needs beneficiary, it is very important that other family members, such as grandparents, also have their Wills drafted with the same planning and goals in mind. Although the intentions are loving and caring, dedicating any assets to a Special Needs beneficiary (by any means) may result in more harm than good.

-- Lonny S. Cades, *Esquire*

A LOOK AT PROGRESS and FINAL PAYMENTS

COVER FEATURE STORY
-- continued from page 1 --

- If you can not do this (or if its too late to do so), strike from the waiver itself any reference to language such as "claims for any contract balance or credits owed for any labor or material provided pursuant to the subcontract work." Initial these strike outs along with signing the waiver.

- If neither of these steps is possible, send a letter with the waiver that clearly states that you do not release or waive any claim for additional consideration arising out of delay, acceleration or pending change orders.

- Finally, be sure to comply with all notice requirements for pursuing claims in the contract. State in writing that pursuant to the terms of the contract, you are putting the contractor on notice of the claim for additional money. If possible, state the amount of the claim.

The lesson to be learned is that while you may need the partial payment to meet your payroll obligations or pay your suppliers, signing a waiver of liens and claims can truly "waive" your rights. You are altering the terms and conditions of your contract when you sign such a waiver. So make sure that the waiver is as narrow as possible. Failure to take this simple step may prevent you from being paid for the full value of the work you performed.

-- Shawn R. Farrell, *Esquire*

What's New

Over the years, **Cohen Seglias** has grown from a small, Philadelphia-based law firm to a mid-sized regional firm with offices in multiple cities. The offices we have opened in Pittsburgh and Wilmington are a testament to our desire to grow strategically and meet the needs of our clients in areas outside of the Philadelphia region. This growth has translated into our firm being listed in the 2004 Pennsylvania Law Digest as the 54th largest firm in Pennsylvania, our highest ranking to date. As our commitment to our clients brings us to other areas of the Commonwealth, the region and the country, we expect our growth to continue.

NEW PARTNERS, ASSOCIATES & SPEAKING ENGAGEMENTS

Consistent with the growth of the firm, **Cohen Seglias** is pleased to announce that three of its attorneys have been elevated to partner. **Roberta Frankel Bloom**, **Edward T. DeLisle,** and **Thomas C. Zipfel** are the firm's newest partners. Robbie and Ed will continue to work in the Construction Department and Tom in the Labor and Employment Practice Group. In addition, **Lonny S. Cades** has joined the firm as Of Counsel. Lonny was a sole practitioner for many years and brings a wealth of experience in transactional work and trust and estate planning to the Business Practice Group. We would also like to welcome our newest associates: **Lucy Halatyn, Matthew Burns, Jack Graham** and **Gaetano Piccirilli**.


Roberta Frankel Bloom


Edward T. DeLisle


Thomas C. Zipfel

Finally, **Cohen Seglias** continues to speak to the construction community about issues of interest. **Roy S. Cohen** recently spoke to the Federated Electrical Contractors, a trade organization with offices in 60 different cities around the country and the world, about preventing, preserving and prosecuting construction claims. In addition, Roy will be speaking about project insurance at the Construction Super Conference in San Francisco in December. **Jason A. Copley** recently discussed avoiding claims through proper project documentation at a meeting of the DelChester Chapter of the National Association of the Remodeling Industry, and about bond claims at a surety seminar presented by the Construction Financial Management Association. In addition, **Thomas C. Zipfel** and **Jonathan Landesman** recently spoke to Human Resources professionals from over 40 companies on the basics of management of employee relations and HR responsibilities.


Roy S. Cohen


Jason A. Copley

-- Edward T. DeLisle, *Esquire*

PROJECT DELAYS

COMPLYING WITH YOUR CONTRACT WHILE KEEPING THE PEACE

There is an old saying that "the squeaky wheel gets the grease." In construction, however, contractors know the squeaky wheel may not get repeat business. Many contractors, therefore, tend to ignore events that impact a schedule, avoid adversarial interaction and wait until the project is completed before looking at delay damages. This tactic can be very risky considering the potential financial loss that can result from this business decision.

Almost all construction contracts, including the standard AIA form contract, contain notice provisions. Generally, these provisions require a contractor to provide written notice of delays. The notice must state the impact to the schedule, the length of the delay and the costs incurred, within a few days of the event.

A contractor's failure to provide this notice in the proper time frame may bar a claim for additional time and money. While these provisions often seem unfair, contractors must play the hand they are dealt in order to protect their companies in delay situations.

As a result, every effort should be made to notify the owner or general contractor of potential cost and schedule changes. Even if the contract does not include a notice provision, contractors should implement internal policies and procedures that guide field personnel in documenting a project.

While no contractor wants to be adversarial, contractors should develop a form notice letter that describes the delaying event, and at the very least, reserves the right to claim cost and schedule consequences at the completion of the project Using a carefully drafted form in an informative, yet cooperative tone, will usually provide the necessary notice without unduly disturbing existing and future business relationships.

"...contractors must play the hand they are dealt in order to protect potential claims."

A form system will also simplify the notification process and allow contractors to quickly notify all relevant parties of the delaying event without much effort. From the contractor's standpoint, this type of notice may seem like a mere technicality. To many judges who strictly construe these provisions, notification of a delay is critical to alert a general contractor and owner of the delay at a time when corrective action can be taken.

For these reasons, field personnel should be instructed to send these notice letters after each and every delaying event. Field personnel should also discuss the events documented in these letters at project meetings and make sure that they are included in the written meeting minutes.

These contemporaneous notice letters and meeting minute discussions eliminate the contractual defense of ignorance. They also will help protect a contractor from liquidated damage claims asserted by the owner or general contractor. Most importantly, they protect the contractor from the possibility of losing their claim.

-- Patrick J. Kearney, *Esquire*

A Note From The Editors

Welcome to the Fall 2004 Edition of ***Construction in Brief***. This publication brings you practical advice on preserving the rights of your business. In this market, it is extremely important to maintain good relations with your clients and other contractors, while at the same time ensuring that you are not giving up the right to full payment. The **topics** covered in this edition include: issues with progress and final payments, how to protect claims for additional money due to project delays, protecting your customer base when one of your sales representative leaves to join a competitor, estate planning for Special Needs individuals, and payroll tax liability.

Please feel free to submit suggestions for future articles that may be of interest to you, either by regular mail or e-mail to: **jcopley@cohenseglias.com**.

As always, if you have a specific legal concern, we recommend that you consult with counsel so that you may receive the best possible advice. See you next issue.

-- Jason A. Copley, *Esquire*
-- Janet L.Treiman, *Esquire*
Editors, *Construction In Brief*

BEWARE:

NEW COBRA NOTICE REQUIREMENTS

We encourage all employers to begin using the Department of Labor's new model notices to ensure compliance with COBRA's new and very strict notice requirements.

The new model notices are available on line at:

www.dol.gov/ebsa/regs/fedreg/final/2004011796.pdf

Questions regarding a specific legal matter? We recommend that you speak with a CohenSeglias attorney:
PHONE: 215-564-1700 **E-MAIL:** jgreenhall@cohenseglias.com

CSPG&F

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- Restrictive Covenants Advice
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- Notice of Delay
- News and New Partners

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