



## **NEW JERSEY LAW REVISION COMMISSION**

### **Final Report Relating to Imputing Negligence to a Public Entity**

**June 20, 2019**

The work of the New Jersey Law Revision Commission is only a recommendation until enacted.

Please consult the New Jersey statutes in order to determine the law of the State.

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## Introduction

Imputing negligence of a third party to a public entity, as a means of expanding potential remedies in the context of a contract dispute, came to the attention of the Commission through *City of Perth Amboy v. Interstate Industrial Corp.*, 2017 WL 2152738 (App. Div. 2017). The Appellate Division considered whether an agent or independent contractor's negligence could be imputed to a contracting unit, i.e., a public entity, when an exculpatory clause limited damages against the public entity to an extension of time for performance.

The Court found that “the Legislature did not intend to broaden a public entity’s liability by permitting the negligence of its agents or independent contractors to be imputed to the public entity,” and in the absence of negligence on the part of the public entity, the exculpatory clause was enforceable.

## Background

The City of Perth Amboy (the City) undertook the construction of a municipal complex. Rather than hire a general contractor, it chose to have its business administrator serve as project manager and contemporaneously award contracts.<sup>1</sup> When the process became delayed it instead awarded contracts seriatim, even though some plans and specifications were incomplete.<sup>2</sup>

The City awarded contracts to multiple prime contractors, including the architect (Zemsky), Imperial Construction Group (Imperial), Interstate Industrial Corp. (Interstate), and TAK Construction Co. (TAK), with Safeco Insurance Company of America (Safeco) serving as TAK’s surety, and LX Specialty Insurance Company (LX) as Interstate’s surety.<sup>3</sup> Interstate’s contract specified that additional time for completion was its only relief against the City, Zemsky, Imperial, or other contractors for the results of any delay.<sup>4</sup> Similarly, TAK’s contract contained a provision waiving delay damages for costs arising from Imperial’s direction, and acknowledged that its sole remedy against the City, Zemsky, or Imperial for delays resulting from their negligence, or another contractor’s negligence, would be an extension of time.<sup>5</sup>

The project quickly fell behind schedule, and the City terminated TAK’s contract in May 2007.<sup>6</sup> Safeco assumed TAK’s contractual responsibilities and completed the project.<sup>7</sup> The City then terminated Interstate’s contract in September 2008, and another contractor finished Interstate’s remaining work.<sup>8</sup> After a bench trial in 2014, the court entered final judgment in favor of the City against Interstate, judgment against the City for Safeco, and judgments of no

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<sup>1</sup> *City of Perth Amboy v. Interstate Industrial Corp.*, 2017 WL 2152738, \*1 (App. Div. 2017).

<sup>2</sup> *Id.*

<sup>3</sup> *Id.*

<sup>4</sup> *Id.*

<sup>5</sup> *Id.* at \*2.

<sup>6</sup> *Id.*

<sup>7</sup> *Id.*

<sup>8</sup> *Id.* at \*3.

cause on Safeco's counterclaim for improper termination of TAK and delay damages against the City.<sup>9</sup> The trial court found that the exculpatory clause that limited TAK's remedy to an extension of time also extended the protections of the City "to the negligence of its retained professionals."<sup>10</sup> Although contractor Zemsky was negligent, the City's misplaced belief that Zemsky was acting properly was not based on bad faith or unfair dealing, and therefore the exculpatory clause was enforceable.<sup>11</sup> TAK was not entitled to delay damages.<sup>12</sup>

On appeal, both Safeco and Interstate argued that it was error to enforce the exculpatory clauses.<sup>13</sup> Safeco argued that Zemsky's negligence should have been imputed to the City, thereby precluding enforcement of the clause.<sup>14</sup> Interstate cited the City's bad faith in endeavoring to avoid the consequences of Zemsky's negligence.<sup>15</sup> As well, it argued that the City's decision to award contracts without complete plans was an independent source of negligence.<sup>16</sup>

The Appellate Division affirmed the trial court's upholding of the exculpatory clause on grounds that contractor Zemsky's negligence could not be imputed to the City under N.J.S. 40A:11-19.<sup>17</sup>

#### **Local Public Contracts Law, N.J.S. 40A:11-1 et seq.**

*City of Perth Amboy* considered imputed negligence in the context of the Local Public Contracts Law ("LPCL"), N.J.S. 40A:11-19, as follows:

#### **40A: 11-19 Liquidated damages; void provisions as to contractor's remedies**

Any contract made pursuant to P.L.1971, c.198 (C.40A:11-1 et seq.) may include liquidated damages for the violation of any of the terms and conditions thereof or the failure to perform said contract in accordance with its terms and conditions, or the terms and conditions of P.L.1971, c.198 (C.40A:11-1 et seq.). Notwithstanding any other provision of law to the contrary, it shall be void, unenforceable and against public policy for a provision in a contract entered into under P.L.1971, c.198 (C.40A:11-1 et seq.) to limit a contractor's remedy for the contracting unit's negligence, bad faith, active interference, tortious conduct, or other reasons unanticipated by the parties that delay the contractor's performance, to giving the contractor an extension of time for performance under the contract. For the purposes of this section, "contractor" means a person, his

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<sup>9</sup> *Id.*

<sup>10</sup> *Id.* at \*10.

<sup>11</sup> *Id.*

<sup>12</sup> *Id.*

<sup>13</sup> *Id.* at \*11.

<sup>14</sup> *Id.*

<sup>15</sup> *Id.*

<sup>16</sup> *Id.*

<sup>17</sup> *Id.* at \*12.

assignees or legal representatives with whom a contract with a contracting unit is made.

L.1971, c.198, s.19; amended 1999, c.440, s.28; 2001, c.206, s.1.

Initially, the LPCL allowed publicly bid, local government contracts to include exculpatory clauses that denied delay damages and limited a contractor's remedy to an extension of time.<sup>18</sup> However, a 2001 amendment voided such clauses in most cases, finding them repugnant to public policy.<sup>19</sup> At the time of this case, the amended provision had yet to be construed. Thus, the Appellate Division considered the plain wording of the statute, as well as legislative intent, before finding that the exculpatory clause was valid because there was no evidence that Perth Amboy (the "contracting unit") was itself negligent. Additionally, the court noted that the Legislature did not intend for a contractor's negligence to be imputed to the public entity, thus allowing for a form of relief that otherwise would not exist.

The amendment was modeled on a 1994 amendment to N.J.S. 2A:58B-3, which also forbids exculpatory clauses for a public entity that exhibits "negligence, bad faith, active interference, or other tortious conduct."<sup>20</sup> However, N.J.S. 2A:58B-3 specifically prohibits imputing the negligence of an agent to the public entity:

### **2A:58B-3. Definitions**

a. As used in this act:

"Public entity" means this State or any department, public authority, public agency, public commission or any instrumentality of this State authorized by law to make contracts for the making of any public work, but shall not include any county, municipality or instrumentality thereof.

"Contractor" means a person, his assignees or legal representatives, with whom a contract with a public entity is made.

b. A covenant, promise, agreement or understanding in, or in connection with or collateral to a contract, agreement or purchase order, to which a public entity is a party, relative to the construction, alteration, repair, maintenance, servicing or security of a building, structure, highway, roadway, railroad, appurtenance and appliance, including moving, demolition, excavating, grading, clearing, site preparation or development of real property connected therewith, purporting to

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<sup>18</sup> L.1971, c. 198, § 19, eff. July 1, 1971.

<sup>19</sup> NJ Assem. Comm. State., A.B. 2913, 1/18/2001

<sup>20</sup> *Id.*

limit a contractor's remedy for delayed performance caused by the public entity's negligence, bad faith, active interference, or other tortious conduct to an extension of time for performance under the contract, is against public policy and is void and unenforceable.

*c. Nothing in this section shall be deemed to void any provisions in a contract, agreement or purchase order which limits a contractor's remedy for delayed performance caused by reasons contemplated by the parties nor shall the negligence of others be imputed to the State. [emphasis added]*

d. Nothing in this section shall be deemed to void any provision in a contract, agreement or purchase order which requires notice of delays, provides for arbitration or other procedures for settlement or provides for liquidated damages.

L.1994, c.80.

### **Outreach**

In addition to harmonizing the two statutory provisions, above, outreach to Edward J. Buzak, Esq., a past Chairman of the Legislative Committee of the Association of Environmental Authorities, resulted in his strongly suggesting that the Public Schools Contracts Law be similarly amended.

Mr. Buzak noted that a companion amendment to that statute, specifically N.J.S. 18A:18A-41, was enacted to achieve the same objective as the 2001 amendment to the LPCL. (The Senate Committee Statement also indicates that the bill prohibiting most “no damage for delay” clauses was intended to apply both to the LPCL and to the Public Schools Contracts Law.<sup>21</sup> In addition, several other sections of the amendment applied to both statutes.<sup>22</sup>) Therefore, he suggested that any revision to the LPCL should be extended to the Boards of Education.

### **Conclusion**

Based on the feedback received, the Commission recommends that both N.J.S. 40A:11-19 and N.J.S. 18A:18A-41 be revised to mirror the wording in N.J.S. 2A:58B-3(c) as shown in the Appendix on the following pages, using the definition for “district” in N.J.S. 18A:18A-2 and “contracting unit” in N.J.S. 40A:11-2 when referencing the public entity. As well, N.J.S. 2A:58B-3(c) would be revised to clarify that “the State” refers to the public entity. All three statutory sections would then specifically prohibit imputing the negligence of a third party to a

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<sup>21</sup> NJ S. Comm. State., A.B. 2913, 6/14/2001

<sup>22</sup> NJ Assem. Floor State., A.B. 3519, 12/9/1999

public entity. This will allow for consistency in interpreting all contracts governed by these statutes, thus potentially alleviating the type of sprawling and costly litigation that gave rise to this case.

## Appendix

### Model language:

#### 2A:58B-3 Definitions

a. As used in this act:

"Public entity" means this State or any department, public authority, public agency, public commission or any instrumentality of this State authorized by law to make contracts for the making of any public work, but shall not include any county, municipality or instrumentality thereof.

"Contractor" means a person, his assignees or legal representatives, with whom a contract with a public entity is made.

b. A covenant, promise, agreement or understanding in, or in connection with or collateral to a contract, agreement or purchase order, to which a public entity is a party, relative to the construction, alteration, repair, maintenance, servicing or security of a building, structure, highway, roadway, railroad, appurtenance and appliance, including moving, demolition, excavating, grading, clearing, site preparation or development of real property connected therewith, purporting to limit a contractor's remedy for delayed performance caused by the public entity's negligence, bad faith, active interference, or other tortious conduct to an extension of time for performance under the contract, is against public policy and is void and unenforceable.

c. Nothing in this section shall be deemed to void any provisions in a contract, agreement or purchase order which limits a contractor's remedy for delayed performance caused by reasons contemplated by the parties nor shall the negligence of others be imputed to the State.

d. Nothing in this section shall be deemed to void any provision in a contract, agreement or purchase order which requires notice of delays, provides for arbitration or other procedures for settlement or provides for liquidated damages.

L.1994, c.80.

**Proposed changes** (proposed additions shown with underline and deletions with ~~strikeout~~):

## **2A:58B-3 Definitions**

a. As used in this act:

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"Contractor" means a person, his assignees or legal representatives, with whom a contract with a public entity is made.

b. A covenant, promise, agreement or understanding in, or in connection with or collateral to a contract, agreement or purchase order, to which a public entity is a party, relative to the construction, alteration, repair, maintenance, servicing or security of a building, structure, highway, roadway, railroad, appurtenance and appliance, including moving, demolition, excavating, grading, clearing, site preparation or development of real property connected therewith, purporting to limit a contractor's remedy for delayed performance caused by the public entity's negligence, bad faith, active interference, or other tortious conduct to an extension of time for performance under the contract, is against public policy and is void and unenforceable.

c. Nothing in this section shall be deemed to void any provisions in a contract, agreement or purchase order which limits a contractor's remedy for delayed performance caused by reasons contemplated by the parties nor shall the negligence of others be imputed to the ~~State~~ public entity.

d. Nothing in this section shall be deemed to void any provision in a contract, agreement or purchase order which requires notice of delays, provides for arbitration or other procedures for settlement or provides for liquidated damages.

L.1994, c.80.

## **40A: 11-19 Liquidated damages; void provisions as to contractor's remedies**

a. Any contract made pursuant to P.L.1971, c.198 (C.40A:11-1 et seq.) may include liquidated damages for the violation of any of the terms and conditions thereof or the failure to perform said contract in accordance with its terms and conditions, or the terms and conditions of P.L.1971, c.198 (C.40A:11-1 et seq.). Notwithstanding any other provision of law to the contrary, it shall be void, unenforceable and against public policy for a provision in a contract entered into

under P.L.1971, c.198 (C.40A:11-1 et seq.) to limit a contractor's remedy for the contracting unit's negligence, bad faith, active interference, tortious conduct, or other reasons unanticipated by the parties that delay the contractor's performance, to giving the contractor an extension of time for performance under the contract.

b. Nothing in this section shall be deemed to void any provisions in a contract, agreement or purchase order which limits a contractor's remedy for delayed performance caused by reasons contemplated by the parties nor shall the negligence of others be imputed to the contracting unit.

c. For the purposes of this section, "contractor" means a person, his assignees or legal representatives with whom a contract with a contracting unit is made.

L.1971, c.198, s.19; amended 1999, c.440, s.28; 2001, c.206, s.1.

#### **18A:18A-41. Liquidated damages**

a. Any contract made pursuant to chapter 18A of Title 18A of the New Jersey Statutes may include liquidated damages for the violation of any of the terms and conditions thereof or the failure to perform said contract in accordance with its terms and conditions, or the terms and conditions of chapter 18A of Title 18A of the New Jersey Statutes. Notwithstanding any other provision of law to the contrary, it shall be void, unenforceable and against public policy for a provision in a contract entered into under Chapter 18A of Title 18A of the New Jersey Statutes to limit a contractor's remedy for the contracting unit's negligence, bad faith, active interference, tortious conduct, or other reasons unanticipated by the parties that delay the contractor's performance, to giving the contractor an extension of time for performance under the contract.

b. Nothing in this section shall be deemed to void any provisions in a contract, agreement or purchase order which limits a contractor's remedy for delayed performance caused by reasons contemplated by the parties nor shall the negligence of others be imputed to the contracting unit.

c. For the purposes of this section, "contractor" means a person, his assignees or legal representatives with whom a contract with a contracting unit is made.

L.1977, c. 114, § 1, eff. June 2, 1977. Amended by L.1999, c. 440, § 77; L.2001, c. 206, § 2, eff. Aug. 8, 2001, eff. Apr. 17, 2000.