



Texas Supreme Court Limits the Enforceability of No-Delay-Damages Provisions

The Texas Supreme Court held that a no-delay-damages provision cannot shield an owner from liability for deliberately and wrongfully interfering with a contractor's work. *Zachry Constr. Corp. v. Port of Houston Auth.*, No. 12-0772, 2014 Tex. LEXIS 768, at *43 (Tex. Aug. 29, 2014). The court not only reaffirmed five exceptions to the enforceability of no-delay-damages provisions but also held that, as a matter of public policy, such provisions cannot be enforced—regardless of what the contract states—if the delay resulted from the owner's deliberate, intentional, and wrongful conduct, which may include instances where an owner's decision results in the increased delays.

The *Zachry* opinion may aid contractors seeking to avoid the effect of no-delay-damages provisions in the face of actions by an owner, and serves as a warning to owners that reliance on contractual provisions is not a foolproof defense where the owner plays an active role in project management decisions that result in longer time periods and higher costs.

Background

Zachry Construction Corporation ("Zachry") and the Port of Houston Authority of Harris County ("the Port") entered into a contract for Zachry to construct a wharf

on the Bayport Ship Channel. The Port set a two-year completion schedule. To accommodate the Port's aggressive timetable, Zachry developed a plan using soil dredged from the channel to construct an eight-foot-wide earthen berm and form a wall around the future construction area. Zachry installed a refrigerated pipe system in the wall delivering super-cooled brine, freezing the wall and keeping the work area clear and dry.

Nine months into the project, the Port sought to increase the size of the wharf by 332 feet. Zachry proposed building another freeze wall to complete the additional construction under dry conditions, but the Port apparently had concerns that this plan might destabilize piers near the construction site. The Port, however, did not raise its concerns with Zachry at the time, and a change order was then issued based on Zachry's plan.

Two weeks later, the Port ordered Zachry to resubmit a plan without the freeze wall. Zachry attempted to dispute this directive, but the Port refused to negotiate. Zachry finished the original section of the wharf, removed the freeze wall, and continued work on the additional 332-foot extension. The completion of the additional section without the aid of the freeze wall

took substantially longer, which resulted in the Port withholding a total of \$2.36 million in liquidated damages from Zachry's payments. Zachry eventually completed the project more than two and a half years after the contract deadline.

Zachry filed suit claiming approximately \$30 million in damages from the delays caused by the Port. The Port pointed to the contract, which precluded delay damages. The no-delay-damages provision stated in part:

- Zachry or any of its subcontractors or suppliers shall receive no financial compensation for delay or hindrance to the Work, regardless of the source of the delay;
- Zachry was not entitled to financial compensation even if the source of the delay resulted from events of *force majeure* or the negligence, breach of contract, or other fault of the Port; and
- Zachry's sole remedy shall be an extension of time.

See *Zachry*, No. 12-0772, 2014 Tex. LEXIS 768, at *8. Zachry successfully argued that the Port's intentional actions rendered this clause unenforceable. After a three-month trial, the jury found that (i) the Port breached the contract by rejecting Zachry's freeze wall design, resulting in \$18,602,697 in delay damages, and (ii) the delay was the result of the Port's arbitrary and capricious conduct, active interference, bad faith, and fraud.

Enforceability of the No-Delay-Damages Provision

In general, a contractor may agree to assume the risk of construction delays and not seek damages under Texas law. Nevertheless, there are five recognized exceptions to this rule — where the delay: (i) was not intended or contemplated by the parties to be within the purview of the provision; (ii) resulted from fraud, misrepresentation, or other bad faith on the part of one seeking the benefit of the provision; (iii) has extended for such an unreasonable length of time that the party delayed would have been justified in abandoning the contract; (iv) is not within the specifically enumerated delays to which the clause applies; and (v) was based upon active

interference with the contractor or other wrongful conduct, including arbitrary and capricious acts, willful and unreasonable actions, without due consideration and in disregard of the rights of other parties.¹

Here, while Zachry argued that the second and fifth exceptions applied and the jury agreed, the court of appeals held that, even if the Port's conduct fell within an exception, the "other fault" language in the no-delay-damages provision was intended to cover the kind of misconduct by the Port found by the jury. The Texas Supreme Court rejected this conclusion for two reasons.

First, as a matter of textual interpretation, the court doubted whether "other fault" was intended to include the kind of deliberate, wrongful conduct in which the Port engaged. The court of appeals' interpretation was particularly flawed, according to the supreme court, in light of the purpose of no-delay-damages provisions. Specifically, experienced contractors can assess potential delaying events when estimating and bidding public works, but they cannot assess potential delays that may arise due to an owner's direct interference, willful acts, negligence, bad faith fraudulent acts, or omissions. See *Zachry*, No. 12-0772, 2014 Tex. LEXIS 768, at *40-41.

Second, a contractual provision exempting a party from contract liability for harm caused intentionally or recklessly is typically unenforceable on public policy grounds. The court found this case consistent with cases where pre-injury waivers of future liability for gross negligence are void as against public policy. The court noted that its conclusion was supported by lower courts in Texas and 28 other U.S. jurisdictions. See *Zachry*, No. 12-0772, 2014 Tex. LEXIS 768, at *41-44.

Further, while the Port argued that the cases in other jurisdictions were distinguishable because those jurisdictions recognize a party's duty of good faith in performing a contract and Texas does not, the court flatly rejected this argument. The "law need not impose a duty of good faith on a party to prohibit him from attempting to escape liability for his future, deliberate, wrongful conduct." *Zachry*, No. 12-0772, 2014 Tex. LEXIS 768, at *43. The Port also maintained that failing to

¹ See, e.g., *Green Int'l, Inc. v. Solis*, 951 S.W.2d 384, 387 (Tex. 1997); *Shintech Inc. v. Group Constructors, Inc.*, 688 S.W.2d 144, 148 (Tex. App.—Houston [14th Dist.] 1985, no writ); *City of Houston v. R.F. Ball Constr. Co.*, 570 S.W.2d 75, 80 (Tex. Civ. App.—Houston [14th Dist.] 1978, writ ref'd n.r.e.).

enforce a no-delay-damages provision is in derogation of the freedom to contract and that Zachry was a sophisticated company. But, the court found that a contractual provision can violate public policy and “the law’s protection against intentional injury is not limited to the helpless.” *Id.*

Implications for Contractors and Owners

At bottom, the Texas Supreme Court affirmed that while parties are generally free to draft their contracts as they see fit, they cannot immunize themselves from deliberate and wrongful conduct. The extension of this rule outside of tort liability and into the construction context is important for both owners and contractors.

For contractors, the decision gives teeth to the recognized exceptions involving no-delay-damages provisions in Texas. Notably, several of these exceptions likely raise fact issues that may be difficult to defeat on summary judgment. For example, a Texas state court may have difficulty deciding as a matter of law whether an owner engaged in “willful and unreasoning actions” or “arbitrary and capricious acts.” Savvy plaintiff’s lawyers may be able to create triable issues of fact that otherwise may have been disposed of on summary judgment.

For owners, they need to be tuned in to all of these factors and their involvement in the project, not only during contract negotiations, but also throughout the course of the engagement. For example, if there is a scope of work change, owners need to be upfront with any concerns and careful in how they approach further changes that increase time and expenses. In short, to attempt to protect themselves, owners need to think about ways their decisions and conduct may arguably fit into one of the five exceptions and render the no-delay-damages provision unenforceable.

Conclusion

The court’s decision highlights the need for owners to monitor their own conduct throughout a project and the potential for additional remedies for contractors where an owner

actively drives a project in a direction that ultimately requires additional time and money.

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