To: New Jersey Law Revision Commission
From: Wendy Llewellyn
Re: Imputing Negligence to a City - N.J.S. 40A:11-1 to -39 (*City of Perth Amboy v. Interstate Indus. Corp.*)
Date: September 10, 2018

M E M O R A N D U M

Executive Summary

In *City of Perth Amboy v. Interstate Industrial Corp.*,[1] the Appellate Division considered whether a contractor's negligence could be imputed to the City of Perth Amboy ("the City"), thereby precluding the enforcement of an exculpatory clause as per a 2001 amendment to N.J.S. 40A:11-19 stating that it is against public policy to limit a contractor's remedy to an extension of time for a "contracting unit's" negligence, bad faith, active interference, tortious conduct, or other reasons uncontemplated by the parties.[2]

The Appellate Division determined 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 that because the City itself was not found to be negligent, the exculpatory clause was enforceable.[3]

Background

The City awarded contracts to multiple contractors for the construction of a municipal complex.[4] The contractors included Michael Zemsky, A.I.A., Architects & Planners (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.[5] Among other provisions, TAK's contract contained a provision waiving delay damages for costs arising from Imperial's direction, and also 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.[6]

After the project very quickly fell behind schedule, and there were multiple disputes over who was at fault, and multiple claims and counterclaims regarding terminations of contracts,

[1] *City of Perth Amboy v. Interstate Indus. Corp*., 2017 WL 2152738 (App. Div. 2017).
[2] *Id.* at *11.
[3] *Id.* at *11-12.
[4] *Id.* at *1.
[5] *Id.*
[6] *Id.*

defaults, and delay damages.[7] The trial court entered final judgment for $221,074.41 in favor of the City against Interstate, judgment for Safeco for $927,547.38 against the City, and judgments of no cause on Safeco's counterclaim for improper termination of TAK and delay damages against the City.[8] 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" and that although contractor Zemsky was negligent, the City's belief that Zemsky was acting properly, though misplaced, was not based on bad faith or unfair dealing, and therefore the exculpatory clause limiting TAK's remedy to an extension of time was enforceable, not against public policy, and TAK was not entitled to delay damages.[9]

Safeco argued on appeal, among other issues, that the judge should have awarded TAK pre-judgment interest on the contract balance as well as delay damages, despite the contract's exculpatory clause, as Zemsky's negligence should have been imputed to the City, making the exculpatory clause unenforceable under N.J.S. 40A:11-19.[10]

The Appellate Division rejected the trial court's reasoning on this last issue, but affirmed the trial court's judgment upholding the enforceability 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.[11]

The relevant portion of the statute says:

> Any contract made pursuant to P.L.1971, c. 198 (C.40A11-1 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.1071, 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 uncontemplated 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 assignees or legal representatives with whom a contract with a contracting unit is made.[12]

[7] *Id.* at *2-*4.
[8] *Id.* at *3.
[9] *Id.* at *10.
[10] *Id.* at *11.
[11] *Id.* at *12.
[12] N.J.S. 40A:11-19.

The Appellate Division noted that the statutory language declaring as void and unenforceable provisions that limit a contractor's remedy to an extension of time for delays due to a contracting unit's negligence, bad faith, active interference, tortious conduct, or other reasons uncontemplated by the parties, was added by a 2001 amendment.[13] In first looking to the plain language of the statute, the Appellate Division noted that "contracting unit" is defined in N.J.S. 40A:11-2(1) as a county, municipality, and certain local governmental boards, commissions, authorities, and agencies, and that "[t]he definition does not include the agents or independent contractors of the 'contracting unit.'"[14]

The Appellate Division then looked to the Assembly sponsor's statement that accompanied the 2001 amendment, noting that it "described the amendment as 'allow[ing] contractors to submit claims of delay *caused by the contracting unit* to the contracting unit for consideration,'"[15] and that the amendment's purpose "was 'to create an incentive for the contracting unit to work cooperatively with the contractor to resolve project issues in a timely manner.'"[16]

The Appellate Division also noted that the 2001 amendment to N.J.S. 40A:11-19 was modeled on language in a 1994 enactment amending N.J.S. 2A:58B-3, which disallowed exculpatory clauses in contracts with state agencies that barred delay damages that arose from a state agency's "negligence, bad faith, active interference, or other tortious conduct,"[17] and that this 1994 amendment also contained a provision that "expressly restricted delay damage claims against a state agency based on the imputed negligence of an agent: '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*.'"[18] The Appellate Division went on to note that the Senate sponsor's statement that accompanied the N.J.S. 2A58B-3 amendment reiterated that the prohibition of clauses barring delay damage claims "applies solely to the public entity's use of these clauses to exculpate its own negligence or intentional tort[i]ous acts but does not allow a contractor to impute the sole negligence of third parties to the public entity."[19]

The Appellate Division determined that because the negligence of third parties could not be imputed to the City, and the City itself was not independently negligent, nor did the City engage in any other behavior that under N.J.S. 40A:11-19 would render the exculpatory clause

[13] *Interstate*, 2017 WL 2152738 at *11.
[14] *Id.* (citing N.J.S. 40A:11-2(1)).
[15] *Id.* at *12 (quoting *Sponsor's Statement to A. 2913* (Nov. 9, 2000) (emphasis added)).
[16] *Id.* (quoting *Sponsor's Statement to A. 2913* (Nov. 9, 2000)).
[17] *Id.* (quoting N.J.S. 2A:58b-3(b)).
[18] *Id.* (quoting N.J.S. 2A:58B-3(c) (emphasis added); L. 1994, c. 80, § 1(c)).
[19] *Id.* (quoting *Sponsor's Statement to S. 977* (May 5, 1994)).

unenforceable, the exculpatory clause was enforceable and barred claims for delay damages that were caused by the negligence of Zemsky or other contractors.[20]

Although the Appellate Division reached its decision by looking at the language of N.J.S. 40A:11-19, it also examined not only to the legislative history of N.J.S. 40A:11-19 itself, but also to the statute and amendment, along with the legislative history, of N.J.S. 2A:58B-3(b) and (c), upon which N.J.S. 40A:11-10 was modeled. It is noted that the amendment on which the statute at issue was modeled includes express language indicating that the negligence of third parties was not to be imputed to the state, but there is no such express language in N.J.S. 40A:11-19 indicating the negligence of third parties is not to be imputed to the "contracting unit," defined under N.J.S. 40A:11-2(1) as a county, municipality, and certain local governmental boards, commissions, authorities, and agencies.[21]

Conclusion

Staff seeks authorization to engage in further research and outreach in order to determine whether adding language to N.J.S. 40A:11-19 and/or N.J.S. 40A:11-2(1) would be useful to clarify the law in this area consistent with the intent of the Legislature.

[20] *Id.* (citing N.J.S. 40A:11-19).
[21] *Id.* at *11.