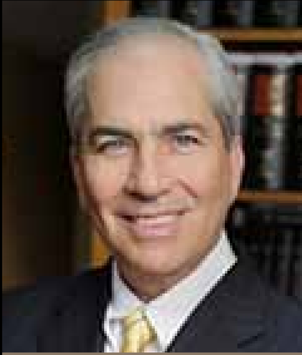

# Oral Contracts in the Construction Context – Hope Springs Eternal

LEGAL LOG

**BY HENRY L. GOLDBERG, MANAGING PARTNER, GOLDBERG AND CONNOLLY AND STA LEGAL COUNSEL**

A New York appellate court recently has held that a subcontractor was, in fact, entitled to compensation for work done pursuant to an oral agreement. The case involved a masonry subcontractor on a School Construction Authority ("SCA") project. During the course of the project it became clear that additional masonry work would be needed beyond the original scope of the subcontract. The subcontractor submitted a written proposal to the contractor for this work in the amount of $498,000.

In response, the contractor issued a "letter of intent" to enter into a subcontract with the subcontractor, pending SCA approval. When the contractor sought SCA approval, the SCA decided to attempt to negotiate directly with the subcontractor to perform the extra work as a change order, and for a lesser amount. The SCA attempted to negotiate despite the fact that the subcontractor's estimate fell within the SCA's engineer's estimate for the cost of the work. The subcontractor refused to budge on either the price or its demand for a new contract covering the additional work.

Despite the lack of a formal agreement, the contractor ordered the subcontractor to perform the work. The subcontractor went on to complete the work despite the lack of any formal agreement with the SCA or the contractor.

The court held, preliminarily, that the "letter of intent" was not binding upon the contractor due to the letter being contingent on SCA approval which was never received. However, the court also went on to hold that in spite of the lack of a formal agreement, the contractor had accepted the subcontractor's written proposal to perform the work for $498,000 through its "acquiescent conduct."

Citing well established New York contract law, the court stated: "In determining whether the parties entered into a contractual agreement and what were its terms, it is necessary to look, rather, to the objective manifestations of the intent of the parties as gathered by their expressed words and deeds"

Specifically, the appellate court found the following factors that supported its finding: the subcontractor continually demanded a new contract, not a change order; the subcontractor continually demanded the same price; the contractor admitted that the subcontractor's price was comparable to the SCA's estimate of the cost; the contractor's project manager testified that he was "comfortable with the dollar figure"; the contractor retained the plaintiff's first requisition (for 25% of the work), which contained the $498,000 price, without noting its non-acceptance of this price; and the contractor's sworn affidavit submitted to the SCA claiming $498,000 as the "fair and reasonable value" of the subcontractor's additional work.

All of these facts led the court to the conclusion that the contractor's direction to the subcontractor to perform the work was "an objective manifestation of assent to its price." Accordingly, the court awarded the subcontractor $498,000, the full value of the orally "agreed to" price.

continued on page 10

continued from page 8

**G&C Commentary**

This case presents a scenario that is all too familiar to subcontractors, namely, being directed to perform work without a formal contract or change order being properly in place. More often than not, these situations turn out badly for the subcontractor, who often winds up receiving far less than the actual value of his work. After all, a service already performed isn't worth as much after all leverage is lost.

While this case can certainly provide some cover for subcontractors who perform work in the absence of a signed written agreement, it should be read more as a cautionary tale. Letters of intent and similar communications from a general contractor are generally not binding. An agreement to agree is not a contract. It is imperative that subcontractors receive clear, non-contingent writings when they are directed to perform work. Such writing must specify the scope, price and other material terms of the agreement so that the subcontractor will have a binding contract.

The facts of this case were unique. If any one of these unique factors cited by the appellate court did not exist, the result might have been very different. The best advice here is to learn from this case, but not rely on it.

Finally, both the trial court and the affirming appellate court clearly wanted the subcontractor paid for its extensive work. The work was done and the general contractor and subcontractor had agreed to the price. The unexpressed truth is that a half million dollar windfall to the general contractor would have been the only alternative result. The courts were not going to countenance the general contractor receiving the work for free. This time the subcontractor was lucky, but running one's subcontracting business should not be based on such good fortune. Make certain you don't get ahead of the paperwork: sign first, work later!