The Half-Priced Contractor

by Sid Hymes

Recently, I was asked what a contractor could do after discovering that he underbid a job by 50%. Short of suicide, the answer depends on the nature and status of any contract as well as the type of error that led to the bad price.

Is There a Contract?

The first thing we need to know is whether there is already a contract between the owner and the half-priced contractor. Assuming that we're dealing with private parties (the rules change when the owner is a government agency), if no contract exists, then the contractor can usually just withdraw or correct the bid.

In the absence of a state law requiring a written contract, a contract can still arise either from a verbal offer and acceptance (see "Bid Acceptance Blues," 3/94), or from the parties conducting themselves as if a contract exists. For example, before accepting the low bid, the owner may have relied on it to decide to reject other contractors' prices. In legalese, this is called "detrimental reliance," and it means that the owner suffered harm by relying on the erroneous bid.

How Big a Mistake?

Assuming that an agreement exists, whether by the usual means or through detrimental reliance, merely making a mistake is not enough to allow a contractor to withdraw or rescind his or her bid. Contractors usually have to live with the consequences of carelessness. Courts have, however, allowed contractor mistakes to void a contract. The four questions a court will ask when considering such a case are:

- Is the mistake so great that enforcing the contract would be fundamentally unfair?
- Is the mistake a material (important) element of the contract?
- Did the contractor exercise "reasonable care" to avoid the mistake in the first place?
- Will allowing relief to the contractor seriously prejudice (harm) the owner?

As readers of this column know by now, how the courts apply these criteria depends on the circumstances. In the case of the amount of the error and its material nature, consider how two real-world examples resulted in different outcomes. In one case, a contractor failed to carry over an item from an estimate worksheet to the bid summary sheet. When the mistake was discovered, the contractor notified the owner immediately. The court allowed the contractor to rescind his bid because the mistake was clerical and involved 10% of the total price — over $9,000 on a $90,000 bid. According to the court, the contractor would have lost money, making it "fundamentally unfair" to have enforced the contract.

In another case, however, a $90,000 mistake was *not* considered material where the contract amount was $3.4 million. Here the court felt that the mistake, which was less than 3% of the contract, was neither material nor would it cause the contractor to fail to make a profit. Obviously, there is no dollar amount or percentage that guarantees one result or the other. In fact, in some cases, it has been necessary for the underbid amount to exceed one-third of the contract price for the contractor to get relief (see, "Who Pays When the Bid is Wrong?" 9/93).

Note also that in both instances, the contractor notified the owner of the error promptly. This quick action is required by virtually all courts as a prerequisite to relief. Had the contractor in the first case waited, or worse, begun the job before claiming the error, it is unlikely that he would have found a sympathetic ear at the courthouse.

What Kind of Mistake?

It's important to distinguish between different types of mistakes. Errors in judgment which lead to the low bid are generally not reversible. This means that if the contractor underestimates the amount of time or material it will take to perform the job, or if he completely forgets to price the second floor, he's out of luck and will have to live with the mistake. But where the contractor made a mathematical error that "slipped through the cracks" — even an error made repeatedly — relief may be possible. Often, this aspect of a case stands or falls on the notion of reasonable care.

In the case of the half-priced contractor I mentioned at the start of this column, the court would want to know how the mistaken price was arrived at. If the contractor used "Kentucky windage" to establish the price — "Call it 50 bucks a square foot" — he will probably get no relief. Similarly, if the discrepancy was noted by the owner or architect, the contractor confirmed the low bid amount, the bid was accepted, and *then* the contractor tried to bail, most courts would cite the theory of detrimental reliance and enforce the bid.

On the other hand, if the contractor was systematic in his estimating procedures but still managed to transpose some numbers or make some other clerical error, the court will be more sympathetic. In fact, if he left out the entire second floor through a clerical error — a misreading of a checklist, for example — the court may give relief.

Again, it's important that the error be brought to the attention of the owner promptly and before the work has started. Otherwise, the court will look to the fourth criterion — harm to the owner. Once too much time has passed or the project is underway, the owner has usually made commitments that would be adversely affected if the underbid price were rescinded. In cases like this, the courts have let contracts stand that were underbid by as much as 50%.

An Ounce of Prevention

So what about our guy? No matter how you slice it, a mistake of 50% will be expensive. Even if the court rules in favor of the half-priced contractor, there will be attorneys' fees to pay, as well as lost productivity for time spent preparing a case and defending it in court. It makes much more sense to avoid this problem in the first place. Here are some ways to protect yourself.

First, allow yourself enough time to study the plans and specs, and to prepare a bid, then allow more time to double-check the numbers. Using a computer to prepare your estimates will eliminate the math errors, and giving the bid the "smell test" will alert you to oversights and any errors in judgment. If you discover, for example, while calculating the completion date, that you've only included enough labor for eight weeks of work on a project you know is going to take you six months, it's time to go back into the estimate and find your mistake.

Second, if you still make a mistake, notify the owner promptly in writing as soon as you find it. Send notice by certified mail, UPS, Federal Express, or other means that will provide you with a receipt. In the notice, document any clerical or math errors, and explain how and why the errors occurred. If you've flat-out underestimated the job, the owner may let you off the hook; otherwise, however, you'll probably have to live with it. But be sure to ask a qualified construction lawyer in your area, because the rules vary from state to state.

Finally, use language like this in your own contract: "Contractor reserves the right to adjust the contract price to correct clerical or mathematical errors." There's no guarantee that this kind of language will work, but it probably won't hurt. Also, use the statutory rescission period (3 days as required by federal law) to review your bid for accuracy; if you find a "material" error, this is the time to take care of it.

Just so there is no misunderstanding, remember that the right of rescission doesn't work both ways — it only extends to the homeowner. But if you notify the owners that the project will cost $100,000 and not $50,000, they may bail out and save you the grief. And if they try to hold you to the contract with this knowledge before the project even gets going, you'll have a better chance of rescinding the agreement. Maybe.

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