Use of Drones in Construction: New Rules and Legal Issues

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Advances in technology have made drones a sought after and cost efficient tool to monitor work on construction sites. Drones provide real-time data on job progress, can help identify quality issues, and acquire other useful information in an expeditious and cost-effective manner. Rather than flying planes or helicopters over a construction site for aerial photographs or video or otherwise have employees walk a site to document conditions, a drone equipped with a camera makes the process easier and significantly less expensive. Advents in technology allow today’s drones to be controlled via mobile devices connected to the internet, and positioned using autopilot navigation. Drones can also be used by the construction industry for, among other things, quality inspections,
ensuring that contractors and laborers are performing and meeting milestones, documenting deliveries and timing of deliveries, and tracking construction progress and scheduling.

Until recently, there was a lack of clarity regarding the permissibility and appropriateness of drone usage in the United States. Individual states and local governments have implemented laws governing drones, but there was only limited guidance provided by the federal government.

**FAA’s New Drone Operational Rules**

Earlier this summer, on June 21, 2016, the Department of Transportation’s Federal Aviation Administration (FAA) finalized the first operational rules for routine commercial use of small unmanned aircraft systems (the FAA's terminology for drones). These rules are contained within Title 14 of the Code of Federal Regulations (14 CFR) part 107 and are scheduled to become effective on August 29, 2016.

The new rules implemented by the FAA apply to all drones weighing less than 55 pounds that are being used for non-hobbyist or commercial purposes, but there are separate requirements for hobbyist or recreational use of drones. Under the new rules, the FAA has developed a variety of operational limitations that drone users must follow. By way of example:

- Drone users may not act as a remote pilot for more than one drone at one time, cannot operate from a moving aircraft, cannot operate from a moving vehicle (unless the operation is in a sparsely populated area), and cannot operate a drone if the user knows or has reason to know of any physical or mental condition that would interfere with the safe operation of the drone.

- Remote pilots for drones are required to conduct a preflight visual and operational inspection in order to ensure that the drone’s systems are functioning properly, including checking the control links between the controls and the drone.

- Drones are permitted to carry objects and transport property, subject to certain weight restrictions, provided that the object being carried can be
securely attached will not adversely affect the flight characteristics or controllability of the drone. There is, however, a prohibition against drones carrying any hazardous materials.

- Drone flights are limited to daytime use only, except for "civil twilight," which is considered 30 minutes before official sunrise or 30 minutes after official sunset during local time. However, in order to operate a drone during civil twilight, the drone must possess the appropriate anti-collision lighting.

- Drones may not operate over any persons not directly participating in the drone operation, may not operate under a covered structure, and may not operate inside a covered stationary vehicle.

- The drone must remain in the visual line of sight of the drone pilot in command and the person manipulating the flight controls. Alternatively, a visual observer can be designated to assist the drone operator in maintaining a visual line of sight. However, it is important to note that the rules require that either the drone operator or the visual observer must maintain a close enough visual line of sight unaided by devices such as first-person view cameras or other equipment.

- During operation, the drones maximum ground speed cannot exceed 100 mph (87 knots) and its maximum altitude cannot exceed 400 feet above ground level.

- Other operational rules included minimum weather visibility requirements, permissible use in certain classes of airspace, encounters with other aircrafts, restrictions on careless/reckless conduct, and the use of foreign drones.

Although the above provides a general synopsis of the FAA's new operational rules, there is also a process by which the FAA will waive certain of these requirements if the drone operator can demonstrate to the FAA that the appropriate safety measures will be utilized pursuant to a certificate of waiver.

**Licensure/Certification for Drone Pilots**

Additionally, included within the new rules is a certification requirement for drone operators. The drone operator must be at least 16 years old and possess a remote pilot certificate or be directly supervised by someone with such a certificate. In order to qualify for a remote pilot certificate, an individual must either (1) pass an initial aeronautical knowledge test at an FAA-approved knowledge testing center or (2) possess an existing
non-student Part 61 pilot certificate (as provided for in 14 CFR, part 61), complete a flight review within the previous 24 months, and take a drone online training course provided by the FAA. The Transportation Security Administration will also conduct a security background check of all remote pilot applications prior to issuance of a certificate.

Since the FAA will expectedly continue to update these rules as commercial drone operations expand, it is critical that businesses remain informed and up-to-date on new regulations, requirements, and standards. Additionally, drone operators will need to be cognizant of the new regulations to avoid potential civil and criminal penalties.

Insurance, Risk and Litigation Concerns

Since insurance considerations are important for every construction project, construction companies should ensure they have appropriate insurance coverage for drone operation in order to avoid gaps in coverage. Most, if not all, commercial general liability policies contain language which excludes an insurer's liability for "'bodily injury' or 'property damage' arising out of the ownership, maintenance, use or entrustment to others of any aircraft . . . owned or operated by or rented or loaned to any insured." Since a drone would seemingly qualify as an aircraft, or at a minimum, sophisticated insurers or coverage counsel could make such an argument to avoid coverage, construction companies that utilize drones should consider purchasing unmanned aircraft insurance or adding an unmanned aircraft liability endorsement to an existing commercial general liability policy.

Likewise, in light of the FAA's new rules, appropriate language should be included in agreements and subcontracts to address limits of drone operations, minimum insurance requirements, and ensuring compliance with drone pilot certification.

Privacy concerns is another issue that is typically front and center in the media when it comes to drone related issues, and is one which companies should consider addressing on the front end of construction projects to avoid potential claims from adjacent or nearby property owners.
Aside from pre-project planning, construction companies should also consider the impact drone usage may have on litigation. As a project tool, information obtained from drones is likely to result in requests for discovery should litigation arise and litigants may be expected to preserve any evidence obtained through the use of drones. Consequently, preservation of data obtained from drones or otherwise maintained on drones becomes a significant concern because the failure to preserve evidence may lead to assertions of spoliation of evidence, especially if parties are involved in a dispute at the time and are aware that litigation is likely or if litigation has already commenced. Separately, video and photographic documentation obtained from drones documenting project progress may assist litigants in proving their claims, assist experts in understanding claims, and assist judges, juries, and other fact-finders in evaluating claims and defenses. Like many other technological advances, there are benefits and drawbacks to the use of drones on construction projects from a litigation perspective.

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ConsensusDocs 752 and the Unique Aspects of Subcontracts on Federal Government Construction Projects

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Federal government construction contracts are unique. Unlike private owners, the U.S. government attempts to achieve a variety of public policies through the solicitation, award, and administration of its contracts. To do so, the government has developed distinctive regulations and contract clauses that govern federal construction projects. The obligations the government imposes require contractors to conform their subcontract terms accordingly. The ConsensusDocs 752 Standard Subcontract Agreement for Use on Federal Government Construction Projects addresses those concerns.

Mandatory Flow-Down Requirements

The Federal Acquisition Regulation (FAR) and certain federal agencies’ FAR supplements mandate that certain contract clauses contained in a prime contract must be flowed down into subcontracts. The regulations require contractors to incorporate
some of these clauses verbatim, while others must be flowed down in substance. Addressing flow-down requirements is complicated and time consuming.

ConsensusDocs 752 addresses these requirements in three ways. First, like most subcontracts on projects public and private, Section 2.4 incorporates the prime contract into the subcontract as one of the subcontract documents. Second, as is also common in many subcontracts, Section 3.1 obligates the subcontractor to assume toward the contractor the same duties that the contractor assumes toward the government under the prime contract. Third, in the most specific and direct way in which ConsensusDocs 752 addresses flow-down requirements, Exhibit H expressly obligates the subcontractor to abide by the provisions of the FAR and the agency FAR supplements that apply to the subcontract. Exhibit H then directs particular attention to a list of dozens of individual regulations and contract clauses that are authorized and possibly required to be applied to construction contracts and subcontracts. These regulations address public policies on ethics, safety, security, transparency, labor and employment, small-business participation, and prompt payment, among others.

Contractors should review each prime contract with the federal government to identify flow-down requirements specific to that project. In an environment of ever-increasing regulation, new requirements arise from time to time. The monetary thresholds triggering application of certain clauses can also change. Additionally, while some provisions are required by law to be flowed down, a particular agency or contracting officer might include additional flow-down requirements in any particular contract.

**Advisable Flow-Down and Coordination Considerations**

In addition to the mandatory flow-down requirements, other unique aspects of prime contracts with the federal government should be coordinated in subcontracts on federal projects. Incorporation of the prime contract into the subcontract and the subcontractor’s express assumption toward the contractor of the contractor’s duties to the owner both begin to address this concern. But it is wise to directly harmonize certain issues in subcontracts for the sake of emphasis and clarity and in order to mitigate the potential for disputes about ambiguities, conflicts, or inconsistencies among the contract documents. The following are just a few examples of this concern.

**The Buy American Act**

The Buy American Act requires contractors to use domestic construction materials on federal projects within the United States unless circumstances justify an exception. Most construction materials are provided and installed by subcontractors, and so contractors must ensure that its subcontractors and their suppliers comply with the Act’s requirements. Section 3.7.2 of ConsensusDocs 752 provides an example:

3.7.2 By executing this Agreement, Subcontractor represents and warrants that it has reviewed the provisions of the Subcontract Documents governing the country of origin for materials and equipment furnished by or on behalf of Subcontractor, which are commonly referred to as “Buy American Act” requirements, and that any materials or
equipment furnished by Subcontractor, its Subsubcontractors, or vendors, at any tier, will comply with the applicable Buy American Act requirements.

**Termination For Convenience**

Federal construction contracts contain the Termination for Convenience of the Government clause found in FAR 52.249-2 (Alternate I). If a contract is terminated for the government’s convenience, the contractor’s right to include in its settlement proposal to the government any amount awarded to a subcontractor in a final judgment for the subcontractor’s lost profits is conditioned upon the contractor’s reasonable effort to include in the subcontract a termination-for-convenience provision similar to the FAR clause. ConsensusDocs 752 contains such a provision in Section 10.4.

**Prompt Payment**

The Prompt Payment Act governs the timing of payments to subcontractors on federal projects. Contractors must pay subcontractors within seven days of receiving payment for the subcontractor’s work. Unlike the prompt-payment statutes in some states, the federal Act cannot be avoided by contract.

Article 8 of ConsensusDocs 752 begins with this acknowledgement in Section 8.1: “The payment provisions of this contract are governed by certain provisions in 31 U.S.C. Section 3901 et seq. (The Federal Prompt Pay Act).” Article 8 then sets forth detailed payment procedures compliant with the Act.

**Governing Law**

In the absence of a subcontract provision stating that the contract will be interpreted in accordance with the law of federal government contracts, arbitrators or courts will typically apply the law of the applicable state to interpret subcontracts. That law is not always in line with the interpretation of contracts by the Boards of Contract Appeals, the Court of Federal Claims, and the Court of Appeals for the Federal Circuit. This can lead to inconsistent results for contractors. Again, ConsensusDocs 752 addresses this issue.

12.1 GOVERNING LAW The Parties agree that regardless of the location of the Subcontract Work, this Subcontract shall be interpreted and all substantive issues presented for mediation, arbitration, dispute, claim, litigation, or other effort at resolution shall be determined in accordance with the federal law of government contracts including decisions enunciated by federal judicial bodies, boards of contract appeal, and quasi-judicial agencies of the federal government. To the extent that the federal law of government contracts is not dispositive, the laws of the state in which the Work is to be primarily performed shall apply.

**Concluding Thought**

Contracting with the federal government is simply different than with private commercial owners. Contractors should not use or rely on the same subcontracts used on private projects (or, for that matter, on state or local public projects) when working on federal
projects. From payment procedures to socio-economic programs like Buy-American requirements, labor and employment standards, and providing opportunities for small-business participation, subcontracts on federal projects must be tailored to comply with governing regulations to ensure successful performance.

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**False Claims Act - Implied False Certification Theory of Liability Recently Defined by Supreme Court Should Be a Concern for Contractors**

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On June 16, 2016, the U.S. Supreme Court ruled in the matter of *Universal Health Services, Inc. v. United States ex rel. Escobar*, 136 S. Ct. 1989 (2016), changing the legal landscape for False Claims Act qui tam claims concerning the implied false certification theory of liability. This article will discuss the *Escobar* holding and examine relevant considerations for contractors in light of this ruling.

In *Escobar*, a teenage patient received counseling under Massachusetts’ Medicare program at a mental health facility, Arbour Counseling Services, which is owned and operated by a subsidiary of Universal Health Services, Inc. As part of the counseling process, the staff at Universal diagnosed the patient and prescribed medication. The patient had an adverse reaction to the medication and subsequently died of a seizure. It was later determined that four out of the five Universal employees that treated the patient were not properly licensed to provide mental health counseling, prescribe medications or offer counseling services without supervision. Specifically, the person who diagnosed the patient had her psychologist license application rejected by Massachusetts, and the person who prescribed the medication was actually a nurse who lacked authority to prescribe medication without supervision, in violation of 130 Code Mass. Regs. § 429.22, et seq. *Escobar*, 136 S. Ct. at 1997-98.

During this time frame, Universal submitted requests for payment to the government for its personnel under Massachusetts’ Medicare program. Universal submitted these payment requests despite its knowledge that its personnel was improperly classified under the billing codes used by Universal.

**The False Claims Act Claim**
In 31 U.S.C. § 3730(b)(1) it states, “A person may bring a civil action for a violation of section 3729 for the person and for the United States Government. The action shall be brought in the name of the Government.” These suits are referred to as “qui tam” suits. Further, 31 U.S.C. § 3729(a) provides, “any person who knowingly presents, or causes to be presented, a false or fraudulent claim for payment or approval . . . is liable to the United States Government for a civil penalty of not less than $5,000 and not more than $10,000,¹ . . . plus 3 times the amount of damages which the Government sustains because of the act of that person.”

Under the above provisions, the respondents in Escobar brought a qui tam suit, alleging that Universal had violated the False Claims Act and defrauded the government in billing for services that were not properly rendered as described in the billings, while failing to disclose serious breaches related to Massachusetts’ Medicare program. The respondents asserted that the government would not have reimbursed the claims had it known that it was billed for mental health services that were performed by unlicensed and unsupervised staff. Escobar, 136 S. Ct. at 1997-98.

Universal filed a motion for summary judgment to dismiss the respondents’ claims. The district court granted Universal’s motion “because none of the regulations violated by Universal was a condition of payment.” The U.S. Court of Appeals for the First Circuit reversed, holding that “every submission of a claim implicitly represents compliance with relevant regulations, and that any undisclosed violation of a precondition of payment (whether or not expressly identified as such) renders a claim ‘false or fraudulent.’” The First Circuit also held that the “regulations themselves provided conclusive evidence that compliance was a material consideration of payment.” Id. at 1998.

The U.S. Supreme Court rejected both the holding of the district court and the holding of the First Circuit and remanded to the district court for further determination of the matter utilizing the new standard for implied certification claims under the False Claims Act. Id. at 2004.

New Standard for Implied False Certification Claims

The Court in Escobar held:

[T]he implied false certification theory can, at least in some circumstances, provide a basis for liability. By punishing defendants who submit “false or fraudulent claims,” the False Claims Act encompasses claims that make fraudulent misrepresentations, which include certain misleading omissions. When, as here, a defendant makes representations in submitting a claim but omits its violations of statutory, regulatory, or contractual requirements, those omissions can be a basis for liability if they render the defendant’s

¹ The government revised the penalties in 2015 via 28 C.F.R § 85.3(a)(9) to a minimum of $10,781 and a maximum of $21,563 per occurrence.
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representations misleading with respect to the goods or services provided.

Id. at 1999 (emphasis added).

In Escobar, Universal knowingly submitted payment applications that listed specific billing codes corresponding to certified and licensed personnel, where those individuals were not certified or licensed, thus misleading the government into paying the invoices. Id. at 1997. The Escobar Court clarified that the claims in the matter related to more than just demands for payment and that “representations that state the truth only so far as its goes, while omitting critical qualifying information[,] can be actionable misrepresentations.” Id. at 2000.

A critical determination in the new Escobar standard is whether the statements made qualify as actionable misrepresentations. The Court in Escobar provided examples of some statements that create actionable misrepresentations to guide future litigation. When a seller of property reveals that there are two new roads near a property for sale, but fails to disclose that a third potential road might bisect the property, the seller has omitted key information that would “materially affect the value of the purchase.” Id. (citing Junius Const. Co. v. Cohen, 257 N.Y. 393, 400 (1931)). An applicant for a position at a college makes actionable misrepresentations when his résumé lists prior jobs and then retirement, but fails to disclose that his “retirement” involved time in prison for a $12 million bank fraud. Id. (citing Sarvis v. Vermont State Coll., 172 Vt. 76, 78, 80-82 (2001)). Both of these examples point to the need for the misrepresentation to affect the basic value of the goods or services to be provided in order to be an actionable misrepresentation.

The Escobar Court also held a critical factor was that the “misrepresentation about compliance with a statutory, regulatory, or contractual requirement must be material to the Government’s payment decision in order to be actionable under the False Claims Act.” Id. at 1996 (emphasis added). The Court also held that liability is not limited to cases where the requirements involved were expressly designated as conditions of payment. Id. at 2001. To assist in interpreting this standard, the Court provided an example of a material misrepresentation. When a contract involves the supply of guns, and the contract does not state that the guns must actually shoot, but the supplier knows that the government routinely rescinds contracts if the guns do not shoot, the supplier has “actual knowledge” of the materiality of that requirement. Further, the seller’s failure to appreciate the materiality of that condition would amount to “deliberate ignorance” or “reckless disregard” of the falsity of the information. Id. at 2001-02. The Court also cited to United States ex. rel. Marcus v. Hess, where two contractors violated a non-collusion bidding requirement and withheld that information. This was implicit false certification because the government would not have funded the subsequent payments had it known of the violation. Id. at 2003 (citing Marcus, 317 U.S. 5379, 543 (1943)).

In the construction context, misstatements concerning the types of materials supplied or the qualifications of the individuals whose labor is billed could implicate this implied
false certification theory of the False Claims Act. For example, consider a construction contract that calls for a specific material or equipment that is required to meet specified quality or regulatory requirements. If the contractor knowingly supplies a different and lesser quality item and then bills the government per the schedule of values including the originally specified item, then the contractor may be liable for implicitly submitting a false claim. Where a design-build contract calls for engineering or oversight services to be performed by a licensed engineer, or where a construction management contract calls for licensed or certified personnel to perform services, and where the contractor supplies unlicensed or uncertified personnel for the positions involved, an implied false certification claim is possible. Another example is a time and material construction contract that specifies categories of workers, depending on specific worker classifications and training levels. If the contractor provides labor that does not meet those specified classifications within the contract (e.g., supplying apprentice labor and billing for journeymen), and the contractor submits billing for personnel based on the classifications that do not match the personnel qualifications, the contractor is potentially liable for an implied false certification claim.

In all of these possible scenarios posed above, contractors need to be vigilant in verifying that the labor or materials supplied by the contractor or its subcontractors do in fact meet the specifications and/or regulatory requirements for any project. Otherwise, the contractor could be exposed to significant per act penalties and treble damages under the False Claims Act. Should any of these issues arise, a contractor should seek assistance in resolving the matter at the earliest time to avoid or minimize the potential penalties.

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**Project of the Month**

A. Chester Redshaw Elementary School, New Brunswick, NJ

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You need to include: Project name, Contracts Used, Name of the Owner, Name of the Developer, Name of the Project Design Professional, Name of the Project Contractor, a Project Description, a short Testimonial, and a Project Photo.

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