FORUM ON CONSTRUCTION LAW
Building the Best Construction Lawyers



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# UNDERCONSTRUCTION

## An Investigation in Sheep's Clothing: Multilateral Development Bank "Audits"

**Kathleen Hamann**

Enforcement actions against international construction companies have been on the rise in recent years, culminating in the headline-grabbing $3.5 billion joint U.S./Brazilian action against Odebrecht S.A. in late December 2016. Less prominently, however, enforcement actions against construction companies by the multilateral development banks ("MDBs" - such as the World Bank and the European Bank for Reconstruction and Development) have also risen sharply, and in many cases have been putting companies out of business. Here are some basics you should know in case you ever get a letter from an MDB saying you are about to be "audited."

### It's Not an Audit

The letter a company will receive launching this kind of investigation will usually say that the integrity office (as the enforcement arms are generally known) is conducting an "audit" of a particular project. This is unlike any audit you have ever experienced—because it is actually a full-blown investigation that in many ways resembles an investigation by traditional law enforcement. They will demand documents and access to your emails and financial records, they will interview your employees (with and without the company's permission or knowledge), they will try to get dirt on you from your competitors, they will show up on site unannounced, and they will treat everything you say as a potential admission or deliberate misrepresentation, even if you are just trying to help. Don't think of them as auditors—think of them more like the FBI.

### Their Jurisdiction is Broad

The MDBs have jurisdiction to investigate any individual or company that receives even a dime of the bank's money—*even if the company does not know it is MDB funded*. You can be a third-tier subcontractor, or think the government is funding the contract. You will nonetheless be subject to the procurement or consultant guidelines that are applicable to the loan the MDB made to the government. It is important to know the funder of every project you work on, even if you are not the prime.

### The Rules are Different—Companies have Far Fewer Rights in the Multilateral Development Bank Sanctions System

The sanctions systems of the MDBs operate under their own rules. No domestic legal system, not even the legal system where the MDB is headquartered, applies. That means there is no right to discovery, no right to interview (or cross-examine)

## IN THIS ISSUE



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witnesses, and in fact you might not even see the evidence of a violation until after a determination has been made to sanction you. They do not have to tell you what the allegations are, or even what they are investigating. In fact, the subject of an investigation has very few rights, basically only the minimums under international law, and sometimes those are not fully respected either. The investigators have diplomatic immunity and can travel basically anywhere and can interview anyone they think might have relevant information, including government officials. It is unlikely that the company under investigation will be able to do the same.

The investigators also can, and very often do, refer their allegations—no matter how unfounded or speculative—to domestic law enforcement where the conduct occurred as well as where the company is headquartered. Because this is a communication to a sovereign government, it is immune—the company that is the subject of the referral has no right to see it or to defend against the allegations it contains. This can cause significant adverse consequences, ranging from investigation and prosecution to "pocket" debarment (when a country effectively refuses to issue any further contracts on the basis of the MDB referral).

It is important to remember that these investigations are different, and should not be treated like an investigation by a domestic agency (like an Office of the Inspector General). The investigations are governed by international law, and the process is quite different from prior audits or investigations you may have experienced.

### Consequences can be Severe and Wide-Ranging

The primary punishment by the MDBs is debarment from contracts that an MDB funds. That is deceptively simple, however. If one of the five major multilateral development banks debars you for more than a year, the other four will *automatically* cross-debar you as well. There are also a number of governments—including India and the European Union—that will likely find you ineligible for contracts based on the debarment of an MDB, and virtually every country will at least take it into consideration. This can result in a multiplication of the impact of a sanction—to the point where companies that do a lot of development work cannot survive even a relatively short debarment period.

Unfortunately, unlike most domestic systems, the multilateral development banks do not have to take into account whether the sanction they are imposing will destroy the company, and they usually do not consider it. In the Odebrecht case, the penalties were reduced by both the Brazilian and U.S. Governments to ensure the company could continue to operate and that innocent third parties were not harmed, but the banks do not do the same. Brazil and the U.S. also considered the fine being paid in the other country. Not so with the MDBs—they may or may not consider penalties being imposed for the same conduct by other enforcement agencies, and they will not consider the impact on the company of multiple punishments. There is no such thing as "double jeopardy" in these systems, and conduct can be punished by the MDBs even if it has already been punished by a domestic government.

### There is No Redress or Appeal from the Decision of a Multilateral Development Bank Sanctions System

The immunity of the MDBs from any kind of sovereign nation is near absolute. The only option for challenging the decision of the integrity office is through the sanctions system, which generally consists of two levels (an officer who determines the sanction and a board who hears appeals of the sanction), and that is it. No other court can reverse the decision of the sanctions system, even if the integrity office violated its own rules or domestic laws. Nor can any government take action against the investigators, who enjoy diplomatic immunity, even if the violate local law or their own guidelines. In some systems, if the investigators in the integrity office engage in misconduct while conducting the investigation, the only redress is to report their misconduct—to the *integrity office*.

### What to Do Now

Conduct a review of contracts you know are MDB funded, or that might be MDB funded, to be sure you know which ones they are. Get familiar with the guidelines of the MDB's Procurement, Consultant, and Anti-Corruption Guidelines (the World Bank's Guidelines, which are fairly representative, are available at http://siteresources.worldbank.org/EXTOFFEVASUS/Resources/ WBGSanctionsProceduresJan2011.pdf, pages 38-39). Update your existing compliance program to ensure you have covered all the issues raised by the guidelines. Consider a risk assessment or review of your compliance system to prevent any issues, or to detect any issues you may already have—you are much better off if you find the issue first, as you can remediate it. If you identify a serious issue, most of the MDBs have voluntary disclosure programs that significantly reduces the sanction—or may eliminate the sanction all together—if you tell the MDB about the problem before they start investigating.

### What to Do if are Contacted by a Multilateral Development Bank Integrity Office

Unfortunately, you are probably already under investigation. Be cautious even if they say they just want assistance and are not investigating you—that may be true, but it might not be. If they say they just want

*Continued on page 6*

MESSAGE FROM CHAIR-ELECT

# "Making The Business Case For The Forum"

I am often asked by those unfamiliar with the Forum, "Why should I become a member of the Forum?" and "Why should I send my associates, and even partners, to Forum events?"

The membership question is an easy one to answer. If someone is already an ABA member, joining the Forum is a relatively modest monetary commitment at $60/year. And, the benefits received—including access to the membership directory, subscriptions to *The Construction Lawyer* and *Under Construction*, access to the Forum's Knowledge Base, and member discounts for programs and books (just to name a few)—far outweigh the cost.

Where the real "value" comes in, however, is in not just being a member, but actively partaking in everything the Forum has to offer—namely, networking at national meetings, writing and speaking opportunities on a national platform, and countless opportunities for leadership.

While involvement in the Forum and attending Forum programs may not seem like the most likely source of business, given the Forum's national and international reach, it unquestionably does. Many in-house counsel have told me that the first place they look for outside lawyers is the Forum directory, focusing primarily on names (and firm names) that are recognizable from their active participation in the Forum Divisions, Committees, Publications and/or at National Programs. It is unquestionable that the Forum has become the go-to place for identifying and retaining qualified construction counsel throughout the country and beyond.

We are also seeing more and more "clients", including but not limited to in-house counsel, at our meetings and are consistently looking for ways to attract more of them, not as business targets, but as active contributors to the overall mission of the Forum—namely, to "Build the Best Construction Lawyers." Of course, an added benefit is that these "clients" have the opportunity to not only learn about the latest developments in construction law, but to meet lawyers throughout the country and to hear them speak.

But opportunities don't always come directly from the potential clients. Business (or business opportunities) can also come from other lawyers. Over the years, the referrals I have received from other Forum members have more than paid for not only my membership in the Forum, but my attendance at national programs as well. It certainly made my participation an easier sell to both my practice group leader and firm managing partner.

And, in my private practice, I have found the Forum network to be invaluable for several reasons. When I need local counsel, my Forum contacts are the first place I look. Moreover, I can have a level of confidence that my Forum colleagues are knowledgeable in the industry, will serve the client well and will not try to poach my clients in the process.

The "business case" for the Forum extends beyond just the receipt of legal engagements. Indeed, the access to resources is often equally critical to a successful practice. The Forum network provides resources that may not exist within the ranks of my own Firm. It is like, if not better than, having an office in every jurisdiction in the country (and beyond). The amazing network of Forum resources is at our fingertips and can not only save us time, but make us more efficient, productive and valuable to our clients.

So, the next time you are trying to convince your practice group leader, your managing partner, or even your spouse/significant other, why they should support your involvement in the Forum, share this article with them, or just a few of my shorthand bullets:

- National / International Marketing and Networking Platform that reaches over 6,000 members located throughout the world;
- Speaking and Writing Opportunities to a National / International Audience;
- Networking Opportunities with clients and lawyers in other areas of the country who can be a source of business and referrals (and sometimes even job opportunities);
- Access to resources that may not exist (or are not easily reachable) within your own firm or practice (e.g., legal research, forms, expert recommendations, etc.);
- Leadership Opportunities;
- Discounted CLE focused on Construction Law and related topics; and
- Construction law publications and books that are either included in the membership cost or offered to members at a significantly discounted rate.

And that is just the "business case" for the Forum. Stay tuned next month for the "personal" case for involvement in the Forum! ■

**WENDY K. VENOIT**, Hinckley, Allen & Snyder LLP, Boston, MA

**2017 WRITING COMPETITION**

## Law Students: Submit Articles for the 2017 Writing Competition by June 5, 2017

The author of the first place submission receives: a cash prize of $2,000; travel expenses and registration to attend the next fall meeting of the ABA Forum on Construction Law (where a first prize plaque will be presented); a one-year membership in the Forum and recognition in both the Forum newsletter, *Under Construction*, and on the Forum's website. In addition to the first place winner, one or more authors may be judged a finalist and recognized with a plaque and in Forum publications.

For complete rules, visit http://www.americanbar.org/content/dam/aba/images/construction_industry/aba-const-forum-2016-17-writing-comp.pdf. All articles shall be submitted to Tamara Harrington (Tamara.Harrington@americanbar.org) and Marilyn Klinger (Marilyn.Klinger@sedgwicklaw.com) by email in Word format.

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- **Five Things Attorneys Should Know About Float** by Lee Schumacher, ARCADIS U.S., Hartford, CT

**Plus News From the Divisions!**

**COMING SOON**

## AIA A201-2017 Deskbook

The AIA Documents Committee is actively working to finalize an updated suite of Contract Documents for release in 2017. This forthcoming release will be the AIA's seventeenth edition of the standard form documents, and will mark the 130 year anniversary of the Documents Committee. These new form contract documents will be a focus of the AIA National Convention on April 27-29, 2017 in Orlando, Florida.

Please mark your calendars for the ABA Forum on Construction Law's Fall 2017 Meeting, Has It Really Been A Decade? The 2017 Updates To The AIA Contract Documents, on October 5-6, 2017 at the Westin Copley Hotel in Boston, Massachusetts to learn everything you need to know about the updated 2017 AIA contract suite.

Additionally, in time for the Fall 2017 Meeting, the ABA Forum on Construction will publish an updated A201 Deskbook discussing the changes in the A201 from the 2007 edition, analyzing how courts have interpreted these provisions, and providing practice pointers. This book is a must read for practitioners using the AIA contract suite and a fabulous addition to your reference library.

## 2017 Reserve Spending Program

The ABA Forum on Construction Law is conducting a Reserve Spending Program for the second year. The Forum will fund, starting in September 2017, innovative and extraordinary special projects that advance long term benefits or strategies of the Forum, particularly those that fit the Forum's Strategic Plan. In addition, we will fund a total of about $40,000 in innovative and extraordinary special projects that increase or provide supplemental member benefits.

The guidelines for the program and an application form and the Forum's Strategic Plan are available here:
**Application:** http://bit.ly/2jxg1iV
**Guidelines:** http://bit.ly/2k0eY7F

The Forum will accept applications until March 3, 2017. If you have questions regarding Reserve Spending Program, please contact Joseph Kovars (jkovars@bakerdonelson.com).

# Toil or Trouble: "Labor" Under the Federal Miller Act

**Karlee Starr Blank**

As construction attorneys, we are all familiar with the Miller Act, requiring prime contractors to furnish a payment bond "for the protection of all persons supplying labor and material in carrying out the work provided for in the contract for the use of each person."[1] We know who may bring suit under the Act: "[e]very person that has furnished labor or material in carrying out work provided for in a contract for which a payment bond is furnished."[2] We know the Miller Act "is highly remedial in nature" and "entitled to a liberal construction and application in order to properly effectuate the Congressional intent to protect those whose labor and materials go into public projects."[3] And we know that, under the Miller Act, claimants must comply with certain notice requirements (if applicable) and timely file suit.

But what don't we readily know about the Miller Act? Or stated differently, are there any requirements or limitations under the Miller Act that we might inadvertently overlook?

## "Labor" under the Miller Act

You receive a call from your client—a prime contractor on a multi-million dollar construction project for the Department of Defense—that was just served with a first-tier subcontractor's Complaint, which includes a Miller Act payment-bond claim for its work on the project. Your client asks you whether the subcontractor's claim complies with the Miller Act, and you determine that the subcontractor has met all notice, timeliness, and venue requirements, concluding that the Miller Act count appears to state a prima facie claim for relief. But what did you miss?

In your haste, you have taken for granted that the subcontractor actually "performed labor" for which a claim may be made under the Miller Act. To determine whether a subcontractor has stated a prima facie payment-bond claim, you should always ask about the *type of work* the subcontractor performed. The subcontractor's claim turns on whether it performed "labor" as that term is used in the Miller Act. Despite the ostensibly inclusive language in the Miller Act—requiring a bond "for the protection of all persons supplying labor . . . in carrying out the work"—and the Supreme Court's pronouncement that courts should liberally construe the Miller Act remedy "to protect those whose labor goes into public projects," several federal courts have found limits on the type of work constituting "labor" under the Miller Act.

## Furnishing Labor for a Contract: Evaluating the Sufficiency of a Claim for Unpaid Work

With respect to its allegations about labor, to determine whether the subcontractor has sufficiently pleaded a claim for its unpaid work under the Miller Act, confirm that such work (1) was performed "in the prosecution of work provided for in a contract for which a payment bond is furnished" and (2) qualifies as "labor" within the meaning of the Miller Act.

### *(1) Was the work performed "in the prosecution of [the contract]"?*

Work is performed "in the prosecution [of the contract]" when it adds value to the project and is called for within the scope of work for the project.[4] The federal appellate courts generally agree that neither warranty work nor corrective work[5] satisfies this requirement. To bring itself within the Miller Act, the subcontractor must show that its work was "performed . . . in connection with the completion of the project and not for the purpose of correcting defects."[6]

### *(2) Was such work "labor"?*

Assuming the work was performed "in prosecution of the contract," next determine whether the work qualifies as "labor" under the Miller Act. To answer this question, begin with the following general rule: If the subcontractor did not "toil" at the project site, its Miller Act claim may be in trouble.

The word "toil" was first invoked as the test for labor in 1982. That year, the United States District Court for the Southern District of Ohio noted that, despite the Act's remedial purpose, there are limits to just how liberally courts may construe the Miller Act, holding that "the Act is not to be applied so as to impose wholesale liability on payment bonds."[7] This ruling stemmed from the court's construction of "labor" under the Miller Act. The court reached two main conclusions:

1. While caselaw interpreting "labor" is relatively sparse, the word has been construed to include *physical toil*.[8]
2. Federal caselaw has adopted an admittedly narrow definition of the term "labor" under the Miller Act.[9]

This decision is important because it expressed a limitation to the Supreme Court's mandate for courts to liberally construe and apply the Miller Act, and recognized that the few decisions defining "labor" defined it narrowly.

In 2017, as in 1982, federal caselaw interpreting the word "labor" is relatively sparse. The Eighth Circuit was the first federal appellate court to address this question, holding in 1992 that "labor" means physical labor and not work involving "technical and professional skill and

judgment."[10] The Fourth Circuit piggybacked on that decision, concluding that professionals only perform "labor" to the extent they perform "skilled professional work which involves actual superintending, supervision, or inspection *at the job site*."[11]

Here are examples of other courts finding that work either does not qualify as "labor" or constitutes "labor" only to the extent it involves some on-site physical toil.

- **Project Management.** "[T]he on-site supervisory work of a project manager falls within the purview of the Miller Act if such a superintendent did some physical labor at the job site or might have been called upon to do some on-site manual work in the regular course of his job."[12]
- **Project Administration.** "Living on the job site and performing routine office maintenance [e.g., cleaning the office and bathrooms; negotiating contracts; determining change orders; preparing bid proposals] is not enough to constitute labor that went towards completing the construction job."[13]
- **Contract Administration.** "Paying invoices, reviewing proposals, and supervising hiring are *clerical* or *administrative tasks* which, even if performed at the job site, do not involve the physical toil or manual work necessary to bring them within the scope of the Miller Act."[14]

In each of these situations, if—within one year before the subcontractor files its Complaint—it was not on the project site, physically toiling, the subcontractor might not have performed "labor" under the Miller Act.

### Practice Pointers: "Labor" and the Miller Act

When evaluating the sufficiency of a Miller Act payment-bond claim, always ask whether the subcontractor performed work "provided for in the contract" that qualifies as "labor" under federal caselaw. The subcontractor's failure to perform qualifying "labor" destroys its Miller Act claim. ■

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### Endnotes

1. 40 U.S.C. § 3131(b)(2) (2006).
2. *Id.* § 3133(b)(1).
3. *Clifford F. MacEvoy Co. v. U.S. ex rel. Calvin Tomkins Co.*, 322 U.S. 102, 107 (1944).
4. *Innovative Metals Co. v. Sw. Sheet Metal of NC, LLC*, 2015 U.S. Dist. LEXIS 55301 at *7 (E.D.N.C. Apr. 28, 2015) ("'The applicable legal test' . . . is 'whether the work was performed . . . as a part of the original contract,' as opposed to being 'for the purpose of correcting defects, or making repairs following inspection of the project.'") (internal citations omitted).
5. *See U.S. ex rel. Interstate Mech. Contractors, Inc. v. Int'l Fid. Ins. Co.*, 200 F.3d 456, 460 (6th Cir. 2000) ("The majority of circuits . . . have held that remedial or corrective work or materials, or inspection of work already completed, falls outside the meaning of 'labor' or 'materials' under [the Miller Act].").
6. *U.S. ex rel. Olson v. W.H. Cates Constr., Co.*, 972 F.2d 987, 991 (8th Cir. 1992) (quoting *U.S. ex rel. Austin v. W. Elec. Co.*, 337 F.2d 568, 572—73 n. 12 (9th Cir. 1964)).
7. *U.S. ex rel. Naberhaus-Burke, Inc. v. Butt & Head, Inc.*, 535 F. Supp. 1155, 1157—58 (S.D. Ohio 1982).
8. *Id.* at 1158 (emphasis added).
9. *Id.* at 1160.
10. *W.H. Cates Constr., Co.*, 972 F.2d at 990—91.
11. *U.S. ex rel. Barber-Colman Co. v. U.S. Fid. & Guar. Co.*, 19 F.3d 1431 (4th Cir. 1994) (unpublished table decision) (emphasis added).
12. *W.H. Cates Constr., Co.*, 972 F.2d at 990.
13. *U.S. ex rel. Shannon v. Fed. Ins. Co.*, 2006 U.S. Dist. LEXIS 56509, *13—14 (D. Miss. Aug. 11, 2006) *aff'd*, 251 F. App'x 269 (5th Cir. Sept. 4, 2007) (unpublished).
14. *U.S. ex rel. Constructors, Inc. v. Gulf Ins. Co.*, 313 F. Supp. 2d 593, 597 (E.D. Va. 2004) (emphasis added).

## *An Investigation in Sheep's Clothing: Multilateral Development Bank "Audits"*

*Continued from page 2*

to conduct some interviews and do not discuss with senior executives or the general counsel the specific nature of their inquiry, insist on receiving that information in writing before agreeing to interviews. Be cooperative in tone, at least in the early stages, but remember you do have some rights. Call outside counsel with experience specifically with the MDBs investigative arms, preferably one that has significant familiarity with international law—this may be particularly important in these cases, because in many countries communications with in-house counsel is not protected from disclosure, but communications with outside counsel nearly always is protected. Ensure that outside counsel is on the ground with you when the investigators arrive, and stays with the investigators for the duration. Do not allow your employees to be interviewed without outside counsel present, and do not give the investigators direct access to your records. And brace yourself—you might be in for a bumpy ride. ■

**KATHLEEN HAMANN**, Pierce Atwood LLP, Washington D.C.

# A Primer for Outside Counsel Working with In-House Government Attorneys

**Kristen M. Rectenwald**

Serving as in-house counsel for the government is interesting and intellectually stimulating. Although the landscape in a governmental practice is necessarily political, the opportunities to hone a particular craft are endless for an attorney unafraid to work hard, consistently expand her knowledge base and creatively problem solve. In addition to providing legal counsel regarding large commercial transactions, an in-house government attorney is likely to counsel her client on numerous further matters, including regulatory compliance and legal questions related to procurement, the legislative process, contract development, dispute resolution, risk management, open records requests and media and public concerns.

Given the volume and complexity of most governmental construction programs, as well as specific legal inquiries that invariably arise during the departmental client's day-to-day operations, in-house government law departments may require the expertise and assistance of outside counsel. The following list, which is by no means exhaustive, includes several key points to consider when engaged as outside counsel by an in-house governmental law department.

*Provide A Government Rate and Review your Bill.*

Leadership within the governmental law department is aware that highly qualified, particular legal expertise is not inexpensive. However, every department within a governmental body functions within a budget that is vetted internally and, most importantly, by the public. Be prepared to provide a government rate for services. In most cases, it will be required.

Following your retention, remain mindful that legal invoices are reviewed, in many cases by more than one attorney. Before submitting a bill, spend time reviewing the applicable government guidelines regarding acceptable charges and take heed. For example, disclose use of a new attorney in your firm, not previously identified in the initial engagement, prior to listing such individual on an invoice. Another rule of thumb is to consider how an invoice could be perceived publicly. Legal invoices are subject to disclosure. Keep in mind that each invoice, or that portion not subject to redaction, is available for public inspection.

*Be Aware of Ethical Restrictions.*

Prior to initiating representation, review ethical obligations that could impact you or your client. In-house government attorneys who work with outside counsel are restricted from accepting gifts or other courtesies customary in the private sector. Every government in-house attorney-client will certainly appreciate outside counsel who independently recognizes, and respects, ethical restrictions.

*Diversity is Appreciated.*

Most governmental law departments strive to achieve a culture of diversity and inclusion where unique insight and innovative solutions are brought together by attorneys of varied backgrounds. In-house government attorneys welcome the opportunity to work with outside counsel who value diversity and approach problems from different perspectives. Initiatives within your firm to promote diversity and inclusion will likely be noted and appreciated.

*Maintain Awareness.*

Be mindful that in-house government attorneys must remain attentive to discussion of potential disputes, open procurements and details regarding future projects. Collegial discussion of a unique legal question surrounding a future project is not possible without potentially disclosing an upcoming opportunity. Therefore, it is important to remain aware and sensitive to in-house government attorneys' limitations for information sharing.

*Communication is Key.*

Although able and learned, outside counsel should remain aware that he is not always cognizant of political initiatives or policy concerns. Prior to an in depth hypothetical discussion with opposing counsel, contact the in-house government attorney client. She is always in the best position to provide advice on the speed at which a transaction can be approved; the change, or lack thereof, in an internal policy; or why a particular "rule" is in place. It is imperative that outside counsel work closely with the governmental law department. To that end, communication is paramount.

Additionally, written communication, even from outside counsel, is not always privileged. Review relevant legal authority regarding open records and reconsider the decision to send that funny email. Depending on the situation, perhaps you can discuss the legal issues over a phone conversation instead of creating an open record. ■

*The opinions expressed here are solely those of the author.*

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UNDERCONSTRUCTION

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# 2017 ANNUAL MEETING
## APRIL 20—22, 2017 WASHINGTON D.C.

In light of the many changes in the last decade that impact the delivery of legal services, our Annual Meeting will focus on the hurdles facing all of us advising clients in the Construction Industry. Both inside and outside counsel will gain insights into industry trends and practical takeaways. Some of the highlights of our program will include:

- Recognizing and responding to cyber security risks
- Managing Complex litigation and leveraging recent rule changes to help control the cost of litigation
- Insights into the changing role of insurance for construction projects
- Ethical considerations to ensure protection of privileged communications between in-house counsel and business partners

### And the Forum is More than just CLE—Meet your Colleagues and Join in the Fun, too!

- National Museum of African American History and Culture—Welcome Reception
- Diversity Breakfast with Senator Maggie Hassan—Former Governor and Current Senator from NH
- Monuments and Memorials Segway Tour by day and Monuments by Moonlight Tour
- Mount Vernon Boat Tour

Register at http://ambar.org/FCLAnnual17