



Results FirstSM

Learned: Drafting Construction Contracts From A Litigation Perspective

Mark Berry, Esq.

Two Types of Contracts Provisions

- The provision you agreed to
- The provision you wished you had agreed to

Lessons of Litigation

- Outcomes can turn on single word choice
- Language varies from the norm for a reason
- Faithful adherence to contractual provisions during project performance matters.
- No provision is interpreted in a vacuum.
 - Context matters
 - Circumstances of the project matter
 - Legal precedent is an unwritten term of your contract

Contract Formation

- Design Liability tweaks may chip away at *Spearin* doctrine (warranty of adequacy of design)
 - Perform all work "reasonably inferable from Contract document necessary to produce intended results"*
 - Instead: use "reasonably **discoverable** from Contract Documents to produce **indicated** results"
 - contractor should not determine design inferences or intent

Contract Formation – Design Liability

- Be mindful of state law – *Spearin* not universally recognized
- Texas Supreme Court rejects *Spearin* in *El Paso Field Servs. V. MasTec North America, Inc.* (Tex. 2012)
 - owner does not impliedly warrant plans and specifications
 - Must include positive, express warranty
 - No right of action against designer in Texas

Contract Formation - DSC

- **Site Investigation clauses may undermine expectation of differing site conditions risk**
 - "Inspected site and satisfied with condition of the work and the risks inherent therein"
 - Instead, refer to:
 - *Observable* conditions [excludes subsurface and covered]
 - *Foreseeable* risks
 - "Contractor has verified accuracy and completeness of reports and surveys provided by Owner"
 - Instead:
 - *"Contractor relies on the accuracy and completeness of information provided"*

Where *Spearin* not Followed

- The AIA solution
 - § 2.3.4.... The Contractor shall be entitled to rely on the accuracy of the information furnished by the Owner, but shall exercise proper precautions relating to the safe completion of the Work.
 - AIA A201, 2017 ed.

Contract Formation

Price Escalation – address tariffs directly

- Cost recovery highly unlikely under traditional impossibility/impracticability argument
- Not enough that escalation makes work unprofitable
- *Alcoa* decision – only in rare instance where entire contract was for delivery of material, and entire contract would be at significant loss, is relief available under impracticability argument
 - But, *Alcoa* arose from embargo, not lawfully imposed tariffs

Contract Formation- Price Escalation

- Change of law or change of taxes provisions may provide relief for tariff-related price increase
- On federal contracts, FAR 52.229-3 broadly permits cost recovery for changes in "federal excise taxes and duties."
- AIA A201 § 3.6, General Conditions of the Contract for Construction (2017) allows recovery for changes to "sales, consumer, use or similar tax."
 - question of whether the current steel and aluminum tariffs, enacted by executive order, constitute a change of tax remains unresolved.
 - BUT, current tariffs are by operation of an existing law, not new law.

Price Escalation – Going Forward

- Use a Material escalation clause
 - *ConsensusDocs 200.1 is excellent model provision*
 - Defines baseline for measuring price adjustment
 - Can be agreed price, or market index
 - States deadband of acceptable risk
 - Allows for delay due to delay availability
 - Requires downward adjustment in event of price reduction
- Provide time limitation on pricing
- Align risk with suppliers and subs

Contract Formation - Delay

- ***Force Majeure***

- Broadly define as "circumstances beyond contractor's control" then include specific, detailed examples
- Watch for language seeking to carve out of delays beyond contractor's control (e.g., other contractors)
- Define measure of "abnormal" weather (NOAA average, specify number of days)

Contract Formation - Payment

- ***Alignment of payment provisions upstream and downstream***
 - Statutory
 - Prompt Payment / Retainage /
 - Contingent Payment – Pay if Paid
 - Most states: freedom to contract, but decisions vary greatly on what qualifies as waiver, and whether temporal only
 - Cali: Invalid
 - Timing
 - Flow down the timing in Prime Contract to align cycles
 - Agree on schedule for review of payment and measure of payments/progress
 - Conform with payment certifications, provide form
 - Without clear alignment, disputes arise when withholding, determining status of work at time of termination, or evaluating work progress

Contract Formation - Payment

- ***Triggers*** - Identify triggers for right to stop work for non-payment
- ***Unpaid Wage Protections***
 - New statutes apply regardless of tier, impose 3x penalties and attorney fees
 - Statute require employer indemnity
 - Strategy: contractual indemnity, certified payrolls, payment bonds, personal guarantees in contract payment applications, lien waivers
 - close scrutiny

Integration Clauses

- Typical to Include
 - But be sure scope is properly defined
 - Capture agreed contractual assumptions
or
 - Attach proposal as exhibit to contract

Contract Formation - Termination

- Include requirement for written notice of specifics and reasonable period to cure after such notice of default.
- Never agree to allow take over of tools, equipment, machinery
- For termination for convenience, avoid clauses allowing subjective decision to terminate without adequate compensation
- Address warranty needs in event of default
- Assignability of subs

Contract Application – Default Termination

- ***Termination for Default***
 - Describe broadly ground for declaring default, but
 - Declaration does not waive other defaults
 - Define cure properly (cure or provision of acceptable plan)
 - Termination for Convenience if improper
 - Recovery of profit and overhead on unperformed work to deter against arbitrary termination
 - or Limit to Work performed and demobilization if upstream
 - Termination at or near substantial completion not recommended

Contract Remedies

- ***Consequential Damages***

- Broadly waive generically, and include specific nonexhaustive list tied to nature of project
- Failure to define at risk of narrow construction
 - Are delay costs consequential? Lost rental income?
- *Alternatively:*
 - place limitation of liability cap specific to consequentials, or total cap
 - Limit to insured claims
 - LDs in lieu of consequential for lost profits
- *Sands Casino*: \$600K CM contract resulted in \$14M arbitral award, upheld by court. (*Perini Corp. v. Greater Bay Hotel & Casino, Inc.*, 610 A.2d 364, 129 N.J. 479 (1992))

Contract Remedies

- ***Indemnity***
 - Broad – covers other party's sole negligence
 - Intermediate – covers other party's partial negligence
 - Limited – covers only own negligence

Indemnity – Drafting Tips

- Limit obligations assumed in indemnity to risks that are insurable
- Make sure have authority over case management
- Insist on limited, or at least intermediate, form of indemnity
- If limited or intermediate, require reimbursement of defense costs to extent Owner is found at fault

Anti-Indemnity Statutes May Alter Expectations

- *Uniwest Constr. v. Amtech Elevator, 280 Va. 428 (2010)*
 - Applied Virginia's anti-idemnification statute *Va. Code §11-4.1*, which render void and unenforceable indemnity provision seeking indemnity "caused by or resulting solely from the negligence" of indemnitee
 - Clause:
"if any claim be made or asserted, whether or not such claims are based upon the negligence of Uniwest...Amtech agrees to indemnify and save harmless Uniwest from any and all such claims"

Anti-Indemnity Operation under *UniWest*

- Despite invalidity of subcontract's indemnity provision, Court found the flow down clause to require indemnity, because prime contract contained valid AIA indemnity clause
- Court rejected sub's argument that specific Subcontract provision prevailed over the prime contract provision, because the subcontract provisions "was void *ab initio* and thus could not have excluded" the provision

Post - Uniwest

- Similar provisions struck down, despite effort to limit scope:

"To fullest extent permitted by law, the Subcontractor shall indemnify and hold harmless the Contractor but only to the extent caused in whole or in part by the negligent acts or omissions of the Subcontractor regardless of whether or not such a claim...is caused in part by a party indemnified hereinunder"

Supchak v. Fuller Constr. Corp, 86 Va. Cir 517 (2013)(claim in equitable indemnity may survive)

Contract Remedies – Dispute Clauses

- ***Choice of Law /Venue***

- Statutory requirement of law of locale (16+ states)
- Preemption of chosen locale where contradicts Project law
- Statutory requirement for venue of locale (preempted by FAA)
- US Supreme Court, *Atlantic Marine (2013)*: *federal courts will enforce forum selection clauses in “all but most exceptional cases”*

Contract Remedies – Alignment of Choice of Law

- ***Specification of differing Choice of Law provisions in Prime and Subcontract can lead to unexpected consequences***
 - Different statutes of limitations/repose
 - Different statutory prohibitions on clauses (indemnity, pay when paid)
 - Decisions vary on whether dispute clauses flow down
 - Forum, law choices frequently circumvented through bond actions

Contract Remedies - SOL

- ***Statutes of Limitation and Repose***

- Alignment of law

- Often, subcontracts and supplier agreement written in Prime's home state
 - But what is repose is shorter than the law of project? No recourse for owner's claim (ex. *20 years in one state vs. 5 years in neighboring state*)

- ***Overcoming statute of limitations***

Virginia: limitations statute does not prevent actions for indemnity, provided the parties negotiated a clear and enforceable indemnity provision. *Hensel Phelps v. Thompson Masonry*, 292 Va. 695 (2016)

Statute of Limitations/Repose – *Hensel Phelps*

- State brought claim 13 years after completion of \$15M student fitness center at VT.
- GC settled with state for \$3M, subs refused to participate in settlement
- GC sued subs for breach and common law indemnity
- Subs asserted 5 year statute of limitations
- GC says flow down provisions waived SOL

Statute of Limitations/ Repose – Hensel Phelps

- But Prime K was silent on waiver – endless limitations period for state arises by statute, but not referenced in Prime or Subcontract
- Court: waiver of statute of limitations must be expressed in writing
- GC further argued that two accruals applied – one for breach of contract, and one for breach of indemnity – with accrual of indemnity upon payment of claim
- But GC indemnity claim was void for violating anti-indemnity statute, and court rejected argument that warranty and payment provisions, requiring reimbursement for costs incurred by GC, created a separate indemnity.
- ***Lesson Learned:*** need express SOL waiver & valid indemnity

Contract Remedies – Dispute Clauses

- ***Arbitration***

- Flow Down requirements of prime K to permit consolidation, uniformity of law and proceeding
- Unilateral election
 - unenforceable in some states (e.g. Md. – unenforceable for lack of consideration)
 - FAA says validity determined by state law
 - Why agree to let adversary decide?
- Scope of Authority
 - Incorporate AAA rules, expressly provide that arbitrator to decide jurisdiction. Otherwise may end up in court in attempt to avoid arbitration
- Statute of Limitations
 - Expressly incorporate if desired, otherwise not applicable

Arbitration clauses

- Limits on discovery period
- Limits on depositions
- Looks for one-way attorney fees/costs for prevailing party.
- Prevailing party not easily defined, often to subjective view of arbitrator. Be careful what you wish for.

General Litigation Avoidance Tips

- Can provisions be reasonably complied with?
- Are notice provisions clear and workable?
- Will unfair or inequitable provisions backfire?
- Are damages provisions clear?
- Are contract documents and order of precedence clearly defined?
- Are general standards understood?
- Are your terms consistent with the law of project?