

LAW SEMINARS INTERNATIONAL
CONSTRUCTION LAW

PRIMARY CONTRACTS
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- I. Introduction
- A. Primary contracts define basic relationship in any construction project: owner and contractor
 - B. Generally documents complex because
 - 1. Process of construction is complex
 - 2. Dollars are usually large for what's produced, a significant investment for the owner and significant financial stake for contractor
 - C. While contract is between owner and contractor, are other interested parties who must be considered in negotiating contract, especially
 - 1. Architect
 - 2. Most important, sources of financing—debt and equity
 - a. Must be sure that construction contract is financeable
 - b. Financing approvals add another layer of complexity to the process
 - D. Several fundamental issues addressed in primary contract
 - 1. Scope of work to be done by contractor: usually defined by reference to construction plans and specifications prepared by architect
 - 2. Amount to be paid to contractor for performing work
 - 3. Time for performance—dollars involved and consequences for delay (lost income, sales) make this important in most contracts
 - 4. What takes up a lot of document space and what the lawyers spend a lot of time negotiating—what happens when things don't go as planned: who bears the risk and pays the cost
- II. Varying types of contractual relationships between contractor and owner
- A. Fixed price—contractor agrees to complete construction project for specified amount of money
 - B. Cost plus fee—payment for construction based solely (with variations) on costs incurred by contractor, with contractor receiving fee for work. Contractor is responsible to owner for completion of work.
 - C. Cost plus fee with guaranteed maximum price (GMP)—same as cost plus fee, except contractor agrees that cost to owner won't exceed a specified amount—the guaranteed maximum price (GMP).
 - D. Construction management—is no general contractor, construction manager supervises and coordinates construction for a fee, but costs and risks are all borne by owner

III. Forms of contracts

- A. Most construction contracts for projects of any size start with American Institute of Architects (AIA) forms
- B. AIA has a form that fits each of the categories in II above
- C. All contracts also include the "General Conditions"—which are a very large number of contract terms that are incorporated by reference in each of these forms
 - 1. Easy to treat as boilerplate, but worthy of negotiation in all deals
- D. General approach—as befitting an architectural group, protective of the architect—but otherwise a generally not unfair document. That doesn't mean it should be signed without change in any deal.

IV. Contract provisions: impossible to discuss every important contract document issue in available time, but will touch on highlights of portions above

- A. The Work—AIA term for the work the contractor is to do under the contract
 - 1. Definition of Work is essence of performance
 - 2. Contained essentially in drawings (pictorial representations of work) and specifications (verbal requirements)
 - 3. Level of detail of drawings is beyond lawyer's scope, but whichever side you represent, your client (as if they didn't know) has to be sure that drawings are as complete and detailed as possible.
 - 4. Infinite number of disputes arise over what's included in drawings (and is included in Work) and what's not (and is an addition to the Work)
 - 5. Lawyer at least wants to be sure that list of drawings attached to contract or referred to in contract complete and accurate (correctly dated version, etc.)
 - 6. Shop drawings
 - a. Because the architectural drawings can't possibly show all details of the Work, contractor (usually via subcontractors) have to prepare drawings (shop drawings) showing particular details
 - b. Some shop drawings to adapt to variations in field conditions
 - c. Critical question—whose responsibility to be sure that shop drawings match up with design
 - d. AIA form—as you would expect—protects architect by making it contractor's responsibility to tell architect of any variation in shop drawings from architectural drawings
 - e. On behalf of contractor, would try to negotiate change so that he's responsible for items within his scope—essentially, field measurements and field conditions—and not for overall conformance of shop drawings with architectural drawings
 - f. On behalf of owner, assuming above change for contractor, would need to be sure architect is prepared to accept broader responsibility
- B. The Contract Sum
 - 1. AIA term is the Contract Sum—the amount to be paid the contractor for the Work provided in the contract

2. For fixed price (stipulated sum) contract, not much to negotiate in terms of documentation/language
3. When contractor is entitled to be paid on a cost plus fee basis, then a lot to talk about—what's included in the cost of the work?
 - a. Amounts paid to subcontractors per their subcontracts
 - (1) Makes the owner the financial party in interest regarding the subcontracts
 - (2) Owner's lawyer would want all subcontracts to be approved by the owner. Contractor probably doesn't care if no GMP
 - (a) Of course, could be other terms than price—such as a fixed schedule—that would make contractor care about identity of subs, but those are similar to considerations if there is a GMP (see below)
 - (3) When GMP, have very different interests
 - (a) Contractor has to be worried about being stuck with
 - (i) a subcontractor who won't perform and stick him with costs that will make him exceed his max
 - (ii) a subcontractor that owner wants that will cost him more
 - (b) Owner is more concerned about lower price
 - (c) Standard form provides that the Contractor is entitled to an increase in the GMP if Owner wants a sub that is higher cost
 - (d) If I'm representing contractor, I want right to pick subs, especially on major trades, without exception—that's the consideration for the GMP. Not even satisfied with standard form language, because quoted price from sub doesn't cover other performance issues. Owner's counsel may disagree because of cost-savings opportunity if use cheaper sub.
 - ((1)) In fairness to owner, contractor's strength may be a factor here
 - b. Contractor's own costs
 - (1) If contractor runs own trades, will include labor and materials
 - (2) On-site supervisory personnel
 - (a) Usually, on-site supervisory personnel are an included cost
 - (b) Prudent owner will want some definition and limitation on how many and cost, perhaps even specific identity (by name or by job classification with rates)
 - (c) GMP situation makes this less of a concern for the owner, because if the contractor thinks he needs

more supervision, the owner has some protection, at least on the high side

- (3) Off-site supervisory personnel usually not included (standard exclusion in contract form), so if supposed to be included, need to spell out

C. Contract time

1. Can be as important as contract sum to both parties
 - a. Difference with contract sum—unless contract provides for liquidated damages, can be hard to measure exact cost to owner (and therefore damage for which contractor is liable) of being late
2. Want to be sure time is carefully defined—contractor wants to be sure that measuring start date fits with reality.

D. Things don't go according to plan—change orders

1. Inevitable that in something as complex as a construction project, some things don't go according to plan
2. Responsibility for any resulting increases in cost and delays in time wrapped into the change order process
3. Has impact regardless of how contract sum computed, although most impact where fixed price or GMP
4. Usually, disputes arise on change orders over whether included in original scope of work—not much contract language can do to prevent/resolve these disputes
5. Contract language affects process
 - a. How to compute amount due contractor if no agreement
 - b. Construction change directives by owner—unilateral direction to proceed without agreement on what contractor entitled to
 - (1) In this case, especially want method of computation provided
 - c. Important to owner and contractor both that work go forward before agreement on amount in order to keep job going

E. Termination

1. For cause termination by both parties for failure to perform
 - a. May want to negotiate “cause” or notice and right to cure, but generally not controversial
2. Owner's right to terminate for “convenience”
 - a. Owner typically has right to terminate for convenience—without any cause at all
 - b. Typical formulation is to allow contractor to recover for work in place and fee attributable to that work if cost plus or portion of payment for work in place if fixed price
 - c. Work of contractor, especially if doesn't run any of own trades, generally front-loaded, so standard formulation doesn't always make contractor whole—issue for negotiation