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Negotiating a contract?

Try this checklist

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The contract negotiation process is an opportunity for parties to clearly communicate expectations and allocate risk. Contracting parties must have a full appreciation of the issues involved in the negotiation process, their interrelationships and their relative importance to the end result — a successful project.

The following checklist presents some of the issues that should always be considered in any contract. The list is not exhaustive since every project has unique considerations and modifications.

Most of the following items are addressed in standard Associated General Contractor, American Institute of Architects and Engineers Joint Contract Document Committee contract forms. While these forms are meant to balance the interests of the contracting parties, a number of the clauses that are acceptable to general contractors are rejected by owners and vice-versa.

1. Consequential damages

Contractors prefer to retain the waiver of consequential damages contained in the standard form. Owners, on the other hand, prefer to remove the waiver, particularly where there are potentially large impacts from construction delays, such as additional rental costs, construction financing, lost revenues and similar damages. As a compromise, contractors may agree to liquidated damages in place of risking actual damage claims.

2. Order of precedence

Most contracts consist of multiple documents that may conflict or be ambiguous. An order of precedence should be included in the contract to provide direction in the event of an inconsistency between the documents. Owners may also include language requiring that, in the event of ambiguity or inconsistency, the greater number or better quality shall govern.

3. Limitations periods

Most standard contract forms include when limitations periods on claims will start and for how long they will run. The standard forms usually have shorter limitations periods than those allowed by law. As a result, owners strike these provisions, whereas contractors prefer they remain.

4. Change orders/claims

Contracts generally require timely notice of changed conditions, preclude claims without written notice, and place limitations on contract adjustments and remedies. Contractors do not favor these provisions, whereas owners often require them. These provisions, including what constitutes timely notice, must be fair and practical for the type of project. Unreasonable notice provisions and overly broad limitations on remedies will be closely scrutinized and may be deemed unenforceable by a court. Many states have statutes addressing contractual damage or claim limitations.

5. Dispute resolution

The standard form contracts generally call for mediation followed by arbitration. Both contractors and owners generally accept mediation requirements. While contractors generally favor arbitration, most owners do not. Arbitration is best applied to small claims and may prove to be expensive for larger, complicated matters. The contract must provide for arbitration, since it cannot be compelled without mutual agreement. Consolidation of disputes should also be addressed.

6. Insurance and bonds

Insurance limits should be specified in the contracts, and proof of the types and amounts of coverage should be required. The financial ability of the contractor should be considered by the owner, as most commercial general liability insurance covers damages resulting from the contractor's work, but not the contractor's faulty workmanship. As a result of this lack of insurance coverage, owners may require payment and performance bonds, particularly if there

is any question of contractor insolvency or the project is risky enough to cause the contractor to go bankrupt. Condominium projects may be uninsurable.

7. Indemnification

Contractors want to limit their liability to negligence, while owners want them to be responsible for any fault. Owners will often require a waiver of any statutory immunities.

8. Time/schedule, float

Owners want no extensions for concurrent delays and won't allow extra time if a contractor doesn't complete a job within schedule. Owners also generally specify they own any float in the schedule. If not otherwise defined, any schedule float benefits the party using it first. Owners generally require detailed schedules that are regularly updated, which can assist in claims analysis.

9. Errors and omissions

Standard forms do not allow contractors to charge or recover for work that doesn't meet the design or laws, codes and ordinances. Most owners also disallow costs of errors or omissions resulting from the ignorance of a particular worker.

10. Design ownership

The parties should consider limitations on subsequent uses of the design, ownership and the right to obtain and use electronic media. This is of particular concern where a contract is terminated before project completion.

11. Choice of law/venue

If out-of-state parties or projects are involved, specify venue and which state law applies to the contract. The standard forms generally set venue and choice of law as that of the project locale. These issues are particularly important to statutes of limitations/repose and any statutes relevant to insurance, indemnity and limitations of liability.

12. Warranties

Contractors desire to have any warranties limit other legal remedies, while owners demand warranties in addition to those remedies.

13. Termination

The standard contract forms allow profit to be paid on the unfinished portion of the project for a termination for convenience. Owners often strike this provision, limiting profit to work completed.

14. Submittals

Although processing submittals is a significant administrative burden for the contractor, owners often require submittals for components incorporated into the work. The contract should clearly identify submittal requirements to ensure that the owner's expectations are met and the contractor has considered the cost and schedule ramifications associated with them.

15. Retainage

Owners often require retainage as additional security to complete the project and/or remedy defective work. In negotiating for reduction or elimination of retainage, contractors may successfully argue that owners are always "ahead of the game" from a financial perspective because the work always precedes the billings and related payments.

16. Prior occupancy

The parties should consider whether or not prior occupancy of all or a portion of the work will occur and whether it will constitute acceptance, the start of warranty periods, assumption of site safety responsibilities, or a waiver of any rights or obligations. Insurance concerns must also be addressed.

17. Liens

The lien provisions of the standard form contracts generally are acceptable to both contractors and owners. Owners often ensure that lien provisions are subordinate to any bank financing obtained by them.

18. Integration clause

This clause states the written contract represents the entire agreement, supersedes all prior negotiations and agreements, and may only be amended in writing. By limiting the contract to what is written, the integration clause can limit subsequent disputes concerning whether other documents and communications are part of the contract.

19. Waiver of subrogation

A waiver of subrogation is an agreement that the party paying the claim will not seek reimbursement from another party, even if the second party is at fault, to the extent that insurance covers the loss. Waivers of subrogation apply to

commercial general liability insurance claims, but not to workers' compensation or professional liability insurance. Also, these provisions may conflict with many current insurance forms.

There are many other contract provisions that are potentially significant to any particular project. As always, a common-sense, practical approach to contract analysis and negotiation is imperative to ensure the expectations of both contracting parties are met.

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