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Percentage of the exam: 11% (22 Questions)
Chapter(s) of "The Book:" Volume 1, Chapter 6, sections 6.02-.04, .12-.14, .20 & .23

6.02 The Contract

Contractors spend a lot of time with the technical aspects of the job i.e. estimating and technical specifications, however must pay equal attention to the nontechnical portions of the contract which may contain provisions relating to the following:

- (1) Inspection;
- (2) Coordination;
- (3) Assumption of risks related to the scope of work, such as unforeseen subsurface conditions, changes, and damages for delays;
- (4) Risks related to other project concerns such as safety precautions, changes, or the indemnification of the owner and design professionals and insurance requirements; and
- (5) Time frames for compliance.

Other clauses may include the following:

- Manner of payment for contract work and change orders;
- Timing and manner of presentation of claims

All of these provisions can create economic consequences often overlooked during the bidding process and could mean the difference between a profitable or a financially disastrous job.

*****NOTE: Government agencies and private enterprises who do a lot of construction contracting will use contracts that will place as much risk that is legally permissible on the contractor.**

[1] Contract Documents

The contract documents consist of all documents that the parties identify as those that establish the descriptions of the obligations between them. Most construction contracts include the following documents:

- Contract
- General conditions
- Technical specifications
- Drawings

Contract documents may also include the following:

- Supplemental general conditions
- Special conditions
- Addenda
- Modifications
- Other documents the parties agree are part of the contract

*****NOTE: Bid invitation documents should not be ignored as they sometimes contain crucial contract terms.**

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The contractor should make sure the executed contract contains all drawings and specifications referenced by type, date and number with revisions identified as part of the basic agreement or not. They should be assembled in one place and initialed by both parties.

[a] Difference Between Documents

It is not unusual for the contract drawings to depict one particular type of construction, while the contract specifications describe a different type of construction. These differences should be resolved prior to contract signing.

- Any obvious differences should be called to the attention of the architect in writing and finalized in writing.
- Many contracts contain a requirement to notify the architect of any errors or defects in the drawings and specifications.

** Even if this is not specifically required by the contract, the contractor may be legally obligated to do so.*

Provisions outlining assumption of responsibilities and risks should also be reviewed.

- The contractor should not assume risks it did not intend to and avoid or negotiate removal of risk assumption clauses.

Ex. Clause that contractor has examined the plans and specs and accepts all risks as to defects regarding these.

[b] Plans and Specifications

A general legal principle is that the owner implicitly warrants to the contractor the fitness of the plans and specs.

- The owner can institute a legal action against the design professional for defects.
- Since the contractor has no contract with the design professional, the contractor must make claims against the owner for defects.

There are two important exceptions to the general legal principle mentioned above:

- (1) Patent defect - if it is obvious that performance according to the plans and specs would be impossible

** These should be called to the owner's attention at bidding and the contractor may be legally bound to do so.*

- (2) If any of the specifications are *performance specifications* as opposed to *design specifications*.

(a) Performance specs - the design professional sets certain requirements and asks the contractor to determine the product or construction method to meet those requirements

(b) Design specs - the design professional has already made these selection and the contractor is to follow them

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[2] Remedy Clauses

Remedy clauses fall into two main categories:

- (1) Compensation for extra work which address situations in which
 - (a) the contractor is directed to perform work different from the plans and specs
 - (b) the worksite conditions are not as anticipated in the plans and specs

** Some of these clauses limit or exclude compensation for overhead and profit.*
- (2) Limits or prohibits the normal legal remedies of the parties that are available as a matter of law in the event of a breach of contract

** May also include limitations on the time periods within which legal remedies may be pursued.*

*****NOTE: Particular attention should be paid to the notice provisions in the contract.**

[3] Scheduling Provisions

The contractor should be certain that the contractor's performance be in accordance time requirements

- Contract completion date needs to be reviewed for appropriateness
- Liquidated damages provisions must be reviewed

[4] Exculpatory and Indemnification Provisions

Clauses that excuse the owner from responsibility for increased cost resulting from various unforeseen circumstances.

These clauses may include those that exculpate the owner and architect from paying increased cost resulting from their own acts and omissions during the course of the contract.

** Contractors include these clauses in the contracts with their subcontractors as well to transfer risk.*

Common exculpatory clauses:

- (a) "inspection"/"familiarity of work" - worksite conditions
- (b) "no damage for delay" - various contracted parties

** These clauses should be negotiated out of the contract if possible.*

Indemnification clauses require the contractor to indemnify (i.e. "hold harmless) the owner and architect from claims by third parties.

- The contractor can obtain insurance to cover this risk by a contractual indemnification rider to the builder's risk or general liability policies.

[5] Bonding and Insurance Requirements

At the beginning of the project, the contractor should consider if the insurance required is sufficient to protect the contractor.

- Protections for design errors
- Protections against indemnifications clauses

[6] Course of Performance, Course of Dealing, and Usage of Trade

These clauses deal with interpretation of ambiguous contract provisions.

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- (a) Course of performance - relates to the interpretation of a contract provision before a controversy arises
- (b) Course of dealing - relates to the interpretation of a particular contract requirement by evaluating the interpretation of the same provision in previous contract or dealings between the same parties
- (c) Usage of trade - a general concept that relates to the way a particular trade or industry usually deals with the disputed contract language

The sale of goods is governed by the Uniform Commercial Code (UCC).

- The UCC can be applied to an entire subcontract if the major purchase of the contract is to supply materials.

[7] External Factors That May Affect Performance

These clauses have the effect of extending the time of performance for "acts of God" that include fires, embargo, labor disputes, wars, riots and weather conditions not reasonably anticipated. Recovery of cost for these acts is denied on the basis that each party should bear the costs they incur since neither party is responsible.

- Referred to as "force majeure" or "excusable delay" clauses

[8] Dispute Resolution

[a] Resolution in the Field

The most cost efficient and least stressful.

[b] Dispute Clauses

**See attachment*

[c] Legal Option in the Absence of Dispute Clauses

- (1) Suit for breach of contract
- (2) Stop work

6.03 Subcontracts

General contractors enter into subcontracts with trade contractors who perform areas of the work for which they have the specialized experience, knowledge, workmen, tools, equipment, or materials that are necessary for the contractor to perform the entire project. A subcontract is governed by the general contract's requirements.

6.04 Statutes

The state law that governs the arbitration or litigation may be the most important factor affecting the rights and liabilities of the various parties.

Contract form 1997 AIA Document No. A201 states that "the Contract shall be governed by

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the law of the place where the Project is located."

** Other contracts may state otherwise.*

State courts have almost unlimited jurisdiction over the parties to a construction project performed in that state. Federal courts are limited to federal district (trial level) court to hear matters in controversy. The basis for federal court jurisdiction is the diversity of the state citizenship of the disputants. For diversity jurisdiction to exist, two requirements must be met:

- (1) The controversy must exceed \$75,000 exclusive of interest and costs.
- (2) The parties must be citizens of different states, a state and a foreign country, or different states and a foreign country.

** Although a suit may be brought in federal court based on diversity, the court applies the law of the state in which it sits.*

Keep in mind:

- Certain contract provisions may violate statutory law in some states and not in others.
- States have different statutory provisions regarding the contractor's time frame to file a claim.
- The Miller Act applies in disputes with federal government agencies.
- The doctrine of sovereign immunity means that the government cannot be sued except to the extent it has expressly consented to be sued.

6.12 Warranties

A warranty is generally defined as an affirmation of fact, a representation, or a promise that a proposition or fact is true. Providing a warranty gives legally enforceable assurance of a product's quality or of a workman's performance for a certain period of time.

[1] Express Warranties

Most standard construction contracts include an express warranty by the contractor that the goods supplied will be free of defects and that the services performed will be in accordance with the contract.

Contract warranty assurances

**See attachment*

The UCC is an express warranty for the sale of goods out of a representation or an affirmation of fact or promise made by the buyer that is contractually binding.

** Each state is free to alter the provisions of the UCC.*

[b] Other express warranties

Home-Owner Warranty (HOW) - provides warranty protection that is furnished to the buyer of a new home through a contractor's enrollment in the program and the contractor's payment of a registration fee for each home that is registered in the program.

The HOW warranty provides a buyer with the following three levels of protection:

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- (1) For the first year, the contractor warrants the property against faulty workmanship or faulty materials.
- (2) For the second year, the warranty continues to provide protection against plumbing, heating, electrical and cooling systems defects, as well as against item in (3).
- (3) For the third year through tenth year, the warranty continues to cover major structural defects.

[2] Implied Warranties

Implied warranties do not arise from negotiations and are not part of the contract's terms. Implied warranties arise by operation of law.

[a] Implied Warranty of Fitness

Implied warranties are imposed on the sales of goods by the states' adoption of the Uniform Commercial code.

Section 2-315 of the UCC establishes the following implied warranty that goods sold are fit for a particular purpose:

"Where the seller at the time of contracting has reason to know any particular purpose for which the goods are required and the buyer is relying on the seller's skill or judgment to select or furnish suitable goods, there is unless excluded or modified under the next section (2-316) an implied warranty that the goods shall be fit for such purpose."

[b] Implied Warranty of Merchantability

This type of warranty states that goods will be salable if the seller is a merchant of the same kind of goods.

The UCC specifies, without limitation, the following minimum criteria for merchantability: The goods must be:

- Passed with objection in the trade under the contract description;
- Fit for the ordinary purposes for which these goods are used;
- Within the variations permitted by the agreement, of even kind, quality, and quantity within each unit and among all units;
- Adequately contained, packaged, and labeled as the agreement requires; and
- Conformed to any promises or affirmations of fact made on the container or label.

*****NOTE:** These types of warranties are not contingent upon the buyer's knowledge where implied warranties are. The most important difference between fitness and merchantability warranties is that a warranty of merchantability requires the goods sold be fit for ordinary purposes, and the warranty of fitness requires that the goods be fit for a particular purpose intended by the parties to the contract of sale.

[c] Implied Warranty of Fitness for Residential Construction

A builder implies warranty that a home is built and constructed in a reasonably workmanlike manner, fit for

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habitation, and fit for the intended purpose.

[d] Implied Warranty in Construction Contracts

- (1) The contractor holds themselves expressly or by implication to be competent to undertake the contract.
- (2) The owner has no particular expertise in the kind of work contemplated.
- (3) The owner furnishes no plans, designs, specifications, details, or blueprints.
- (4) The owner tacitly or specifically indicates its reliance on the contractor's expertise and skill after telling the contractor the specific purpose for which the building is intended.

[e] Owner's Warranty of Specifications

If a contractor is required to perform in accordance with the plans and specs, the contractor will have met the contractual obligations. If contractual adherence causes unforeseen costs, the contractor is entitled to recover those additional costs that result in a defect in the plans and specs, because a breach of an implied promise by the owner exists that the plans and specs can be followed successfully.

Three exceptions:

- (1) The contractor knew there were defects in the plans and specs at the time the contracts were signed.
- (2) The contractor knows a defect exists and proceeds with construction.
- (3) The contractor fails to follow the plans and specs.

6.13 State and Local Government Contracts

Bidding on public contracts must be in accordance with statutes containing certain procedural requirements. Furthermore, state and local laws often mandate that specific provisions be included in the contract.

[1] Multiple Prime Contractors

This arrangement places the owner in direct contractual relationship with all of the trade contractors to avoid the expense and profit of a general contractor's administration of the subcontracts.

[2] Claim Requirements

[a] Exculpatory Clauses

Public agencies often use "no damage for delay" provisions in their contracts.

[b] Liquidated Damages

Government bodies often insist on liquidated damages if that contractor has caused a delay.

[c] Notice of Claim Requirements

In order to determine a jurisdiction's specific requirements, the contractor must examine the contract and

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applicable statutes and regulations relating to the project.

[3] Multiple Lien Laws

Lien laws vary from state to state. On a public project, a lien does not attach to property, but to a government agency's funds.

[4] Bonding Requirements

Three types of bonds;

- (1) Bid bond - guarantees the owner that contractor will accept and perform the contract if the contract is awarded to the contractor.
- (2) Performance bond - protects the owner (or the general contractor) if the contractor defaults.
- (3) Payment bond - required on public projects, protects the subcontractors and suppliers if the contractor fails to make the required payments.

6.14 Federal Government Contracts

*****ALERT*** - READ THIS CHAPTER THOROUGHLY!!!!**

[1] Government Obligations and Contractor's Rights

- In nongovernmental contracting, there is "apparent authority."
- In government contracting there must be actual authority. These are vested agency heads called "contracting officers."

Sovereign immunity - the government or sovereign) is not responsible to its actions except if it has expressly consented to be sued.

"Sovereign Acts" - the government is not required to provide an equitable adjustment for changes or delays and is not required to provide damages for breach of contract if it acts in its governmental rather than proprietary capacity.

- A sovereign act would occur if the government, for public health and safety reasons, permitted water to escape from a dam after heavy rains, even though it could delay or impede the work of a contractor on another project. An equitable adjustment would not be required in this case.
- A proprietary act would be if the government permitted water to escape from the same dam in or to facilitate work on another project and, thus, that act delayed repair work on the dam. This event would be a compensable delay to the dam work.

[2] General Principles of Completion and Negotiation

Federal government statutes require that federal procurements be awarded on the basis of full and open competition.

Sealed-bid requirements are required if:

- time permits
- the award is to be made on the basis of price and other price related factors

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- it is not necessary to conduct discussion with the bidders
- a reasonable expectation exists of receiving more than one sealed bid

Exceptions:

- "small business set aside program"
- If the government's best interest to have a sole source of procurement.

[3]Bid protests

A protest can be made either to the Government Accountability Office (GAO), headed by the Comptroller General, or to the Court of Federal Claims.

[4] Contract Types

- (1) Fixed Price - the contractor bears the risk of increased cost of performance and the benefits of decreased costs of performance
- (2) Variable quantities - unit prices for parts of performance
- (3) Indefinite-quantities contract - for supplies and materials
- (4) Cost reimbursement contracts - the contractor is paid for allowable and allocable costs on the basis of the regulations in the Federal Acquisition Regulation (FAR).
- (5) Design-build

[5] Contract Clauses

*****ALERT*** - READ THIS SECTION THOROUGHLY!!!!**

Categories:

- Performance
- Payment
- Adjustment
- Socioeconomic
- Delay
- Disputes procedure
- Termination

[6] Bonding and Sureties

Miller Act - requires a payment bond in any construction, alteration or repair of public building or public sector contract in excess of \$100,000.

[7] Recoveries for Project Delays

[a] Contract Clauses

- "commencement, prosecution and completion of work" requires commencement of work within a certain number of calendar days following the date the contractor receives the notice to proceed.

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- "liquidated damages" requires the contractor pays an amount for each day of delay if the contractor fails to complete the work by the time periods established in the contract
- "suspension of work" establishes the right of the contracting officer to order a suspension, delay, or interruption of any part of the work for the government's convenience.

[b] Compensable Versus Noncompensable Delays

- An excusable delay is one that is not the contractor's fault. The contractor is not held to liquidated damages and is entitled to only an extension of time
- A compensable delay is one that is caused by the government.

[c] The Eichleay Formula

**See attachment*

[8] Acceleration

Elements of a constructive acceleration:

- (1) Excusable delay
- (2) Governmental knowledge of the delay
- (3) Government statement or act that may be construed as an acceleration order
- (4) Notice by the contractor to the government that the order constitutes a constructive change
- (5) Additional costs for acceleration efforts

The following have all been held to be sufficiently coercive to constitute an acceleration order:

- (1) A threat to terminate for default because of an excusable delay
 - (2) A request to accelerate
 - (3) Government pressure to complete on schedule if coupled with a threat to assess liquidated damages
- The refusal to grant time extension (to which the contractor is entitled) coupled with the assessment of liquidated damages.

[9] Contract Disputes Act and Disputes Clause

The standard government contract disputes clause provides a procedure for filing claims with the contracting officer and for obtaining final decision from the contracting officer. The Contract Disputes Act of 1978 provides the procedures and jurisdictional bases for appeal of the contracting officer's final decision.

If a claim is greater than \$100,000, it must be certified under the terms of the dispute clause and the Contract Disputes Act.

The contracting officer is required to render a decision within 60 days of the claim or to notify the contractor of the date by which the contracting officer will make a decision.

[10] Equal Access to Justice Act and Recovery of Attorney's Fees

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The federal government is protected from liability for legal fees by the concept of sovereign immunity to suit. Until the Equal Access to Justice Act was passed, recovery of legal fees against the government was limited to a few situations covered by statute, and government contractors could not generally recover legal fees

Two effects of the Equal Access to Justice act;

- (1) The government's sovereign immunity for liability of legal fees is expressly waived.
- (2) The government becomes susceptible to the payment of legal fees to the prevailing party if it acts in bad faith.

[11] Subcontracting

[a] Notification and Consent

The government's consent to subcontracts is generally required if the subcontract work is complex, the dollar value is substantial, or the government's interest is not adequately protected by completion. Consent to subcontracts is not required under prime contracts that are firm-fixed-price or fixed-price with economic price adjustment provisions.

[b] Flow-Down of Prime Contract Obligations

The prime contractor must be assured that their subcontractors are bound to all obligations under the prime contract to the government.

[12] Terminations

[a] Termination for Convenience

In exchange for the right to terminate for convenience, the contractor is entitled to the following:

- (1) The cost of all contract work performed before the effective date of the notice of termination plus a profit on those costs
- (2) The cost of settling and paying claims arising out of the termination
- (3) The reasonable costs of preservation and protection of the property subsequent to the termination
- (4) Any other reasonable costs and settlement expenses incidental to the termination.

[b] Termination for Default

The government may terminate the contract for default if the contractor refuses or fails to prosecute the work with the diligence to ensure its completion on time or if the contractor fails to complete the work on time.

The government is entitled to take over and complete the work. The government is entitled to recover from the contractor the excess costs of having the work completed as well as any liquidated damages.

6.20 Nonpayment or Late Payment

Making those payments required by a contract is an owner's primary obligation, and the owner's failure to make them

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without a reason is justified by the law normally constitutes a material breach of the contract.

[1] Ability to Compel Payment

Many contracts include a clause in subcontracts that subcontractor will be paid if and when the general contractor is paid. Some states enforce these clauses and some don't. Action against the general contractor's payment bond may be a remedy for the contractor.

[2] Owner's ability to pay

In public sector contracts, contractors have the justifiable expectation that the owner has adequate funds available for the work to be performed.

[3] Private Owners

AIA Document No. A201 deals with the request of the contractor for the owner to provide evidence of the owner's ability to pay.

[4] Mechanics Lien Remedies

Most states have a mechanics lien statute that permits a contractor, subcontractor, or materialman to file a lien against the property that they have constructed or for which they have provided materials. The Property is the security for the payment of any debt incurred by the parties who have made improvements to the property.

[6] Subcontractors Claims and Payments

The further a contractor is from the source of the problem, the more likely the contractor will have difficulty in collecting payment. The subcontractor has the opportunity and the obligation to understand the mechanics lien laws so that the subcontractor can make a claim if necessary.

6.23 Alternatives to Litigation

Third-party resolution of disputes may not require litigation.

[1] Arbitration

Arbitrators or judges determine the prevailing party in a dispute. This is generally considered faster and less expensive than litigation.

[2] Mediation

A professional mediator or team of professional mediators is actively engaged in the process of attempting to bring about a settlement to a dispute. Mediators do not make judgments but encourage the parties both independently and in joint sessions to come to an agreement.

[3] The "Mini-trial"

A shortened proceeding that is usually conducted in the presence of the chief financial officers of the two disputing

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parties and their attorney's. This process is based on the assumption that if both chief financial officers listen to each side's testimony, reason will prevail and a settlement will be reached.

[4] Creativity in the Resolution of Construction Disputes

If confronted with a legal entanglement that could cost substantial amounts of money, every disputant and their attorney should consider the necessity to limit the amount of expenditure and to create proposals and opportunities in which a just and prudent procedure can be established.