CCIFP Study Group

Legal – Chapter 6

6.01 – Introduction

1. Major legal topics present in the construction industry
2. Identify potential risks
3. Minimize those risks
4. Know when to seek legal counsel

6.02 – The Contract

0. Miscellaneous items
    a. Who is the owner
        i. Public – Federal or state
        ii. Private
    b. Contract structure
        i. Design-bid-build
        ii. Design-build
        iii. Integrative
    c. Contract payment structure
        i. Fixed price
        ii. Cost plus fee
        iii. Cost plus fee with guaranteed maximum
        iv. Unit price
        v. Time & materials
1. Contract documents – all documents that the parties identify. Can include but are not limited to the contract, general conditions, tech specs, drawings
    a. Differences between documents
        i. Pay careful attention at the contract formation stage for differences between documents
        ii. Contractor needs to inform architect of error or defects ASAP
    b. Plans & Specs
        i. Owner warrants to the contractor the fitness of the plans and specs
        ii. Patent defect – not obvious to bidder that plans & specs are impossible
        iii. Performance specs – contractor determines the method to meet the requirements
        iv. Design specs – contractor must follow the detailed specs exactly
2. Remedy Clauses
    a. Compensation for extra work
        i. Change orders – written notice to the owner before work done
    b. Legal remedies for breach of contract
3. Scheduling provisions
4. Exculpatory & indemnification provisions
    a. Exculpatory – excuse the owner from responsibility for increased costs
        i. Shift burden to contractor
        ii. Contractor can include in subcontractor contracts

        iii. Contractor should try and get these out of the contract
    b. Indemnification – hold the owner and architect harmless from claims by 3rd parties
        i. Shift risk to the contractor
        ii. Usually for personal injury
        iii. Contractor can obtain insurance via rider to the builder's risk policy or a general liability policy
5. Bonding & Insurance - Requirements for bonding & insurance are generally specified in the contract
6. Cost of performance, course of dealings, usage of trade
    a. Contract interpretation related to disagreements
    b. Generally followed in the courts in the order listed
    c. Course of performance – interpretation of contract before controversy arises
    d. Course of dealing – interpretation of requirements by looking at other contracts or dealings with same person(s)
    e. Usage of trade – How is the issue generally handled in that trade/industry
7. External factors that affect performance
    a. Force majeure – act of God
        i. Each party should bear the cost(s) as neither is responsible
    b. Also called "excusable delay" clauses
8. Dispute resolution
    a. Alternate mechanisms to litigation and arbitration
        i. Independent Decision Maker (IDM)
        ii. Mitigation
        iii. Mediation
    b. Resolution in the field – most cost-effective and least stressful
    c. Dispute clauses
        i. Included in the 2007 iteration of the AIA 201 form contract
        ii. Designates the architect as the IDM unless otherwise noted
    d. Legal options in the absence of dispute clauses
        i. Litigation
        ii. Sue for breach of contract
        iii. Contractor can stop work if owner make fraudulent or intentional misrepresentation of material fact

<u>6.03 – Subcontractors</u>

1. General contractor will enter into contractors with specialty trade contractors
2. Contract is governed by GC contract with the owner
3. Work must be done consistent with the GC/owner contract plans and specifications
4. Pay-if-paid and pay-when-paid clauses if states allow

<u>6.04 – Statutes</u>

1. State law that governs arbitration or litigation is important to know
    a. Contract may specify locale of litigation or arbitration
    b. If silent, generally is jurisdiction that has the most significant relationship with the contract

<u>6.05 – Case Law</u>

1. Just as important as statutory law
2. Varies by jurisdiction

6.06 – Local Codes and Regulations

1. Need to comply with these provisions as well
2. Ignorance is no excuse

6.07 – Labor Relations

1. Labor law
    a. Davis-Bacon Act – must pay prevailing wage on federal contacts
    b. Important that subs comply with labor laws as well
2. Prehire agreements
    a. Allows a contactor to enter agreement with union(s) that state contractor will only hire union employees
3. Hot Cargo Agreements
    a. Means that contractor will only hire subs that hire union employees

6.08 – Labor Disputes

1. Organized picketing of the subcontractor
2. Jurisdictional disputes
3. Legal recourse
4. Nonunion operations
    a. Open shop – nonunion
    b. Right to work states – can't require union membership and/or dues as condition of employment
    c. Double-breasted operations – two separate companies, one union, one non-union; must have separate ownership

6.09 – Bidding and Estimating

1. Owner is not required to accept the lowest bid
2. Responsibility and responsiveness requirements generally include;
    a. Skill
    b. Integrity
    c. Experience
    d. Financial resources
3. Public sector projects may have contractors that "prequalify"
4. Responsive bids address all the matters in request for proposal (RFP)
5. Mistakes in bids – generally bidders can withdraw bids if;
    a. Magnitude of mistake is so large that awarding the contract on the erroneous bid price would be unconscionable?
    b. Does the mistake affect a material aspect of the contract?
    c. Did bidder exercise ordinary care in preparing the bid

    d. If the court grants relief will the petitioning bidder obtain an unfair competitive advantage over other bidders, which will adversely affect the competitive bidding process?
    e. Did the bidder notify the owner of the mistake soon after the bids were received or as soon as the mistake was discovered?
6. Mutual mistake
    a. Contract can either redrafted or rescinded

6.10 – Bankruptcy and Insolvency

1. Artful drafting and admin of contracts can minimize risk of non-payment

6.11 – Industry-Wide Specifications and Standards

1. If standards are used in contracts, contractor needs to obtain the most recent edition of the standards and review them
2. Examples include;
    a. American Society of Mechanical Engineers (ASME)
    b. American Society of Civil Engineers (ASCE)
    c. American National Standards Institute (ANSI)

6.12 – Warranties

1. Express warranties – Goods supplied will be from defects and services will be performed in accordance with the contract
    a. The Uniform Commercial Code's (UCC) Warranties
        i. Express warranty can be created without using the words "warranty" or "guarantee"
    b. Other express warranties
        i. Home-Owner Warranty program
2. Implied warranties – Do not arise from negotiations are not part of the contract's terms. They arise from operation of law
    a. Implied warranty of fitness
        i. Imposed on the sale of goods under the UCC
        ii. Goods sold fit for a particular purpose
    b. Implied warranty of merchantability
        i. Also imposed under the UCC
        ii. Requires that the goods sold be fit for ordinary purposes
        iii. Bulk items – bricks, paint, concrete, lumber
    c. Implied warranty of fitness for residential construction
        i. Court imposed
        ii. Rejection of *caveat emptor* doctrine – buyer beware
    d. Implied warranty in construction contracts
        i. Hybrid of fitness for goods and fitness for const in residential const
        ii. Based on:
            1. Contractor holds themselves to be competent to undertake the contract
            2. Owner has no expertise in the kind of work contemplated

            3. Owner furnishes no plans, designs, specs, details, or blueprints
            4. Owner indicates reliance on contractor's experience and skill after telling the contractor the specific purpose for which the building is being built
    e. Owner's warranty of Specifications
        i. *Spearin* doctrine – Provides that owner's impliedly warrant the accuracy of their plans and specifications
        ii. Exceptions
            1. If the contractor new that a defect in the plans & specs existed when the contract was signed
            2. If the contractor knows a defect exists and proceeds with construction
            3. Contractor fails to follow the plans and specs

<u>6.13 – State and Local Government Contacts</u>

1. May contain multiple prime contracts
2. Claim Requirements
    a. Exculpatory clauses
        i. No damage for delay clauses
        ii. Contractor cannot seek a claim for certain delays
    b. Liquidated damages
        i. Governmental agencies seek damages from contractor for delays
    c. Notice of Claim Requirements
3. Municipal Lien Laws
4. Bonding requirement
    a. Bid bond
        i. Guarantees the own that contractor will accept an perform the contract if the contract is awarded to the contractor
        ii. May be liable for more than bond face amount if difference between contractor's bid and next lowest bid exceeds the bond
    b. Performance bond
        i. Protects the owner if the contractor defaults
        ii. Surety will complete the project, pay another contractor to finish, or pay the owner the cost to complete
        iii. Also used between contractors and subs
    c. Payment bond
        i. Required on public sector jobs
        ii. Protects subs and suppliers if contractor fails to pay them
        iii. Also protects owner as long as sub and supplies don't file liens

<u>6.14 – Federal Government Contracts</u>

1. Government obligations and contractor's rights
2. General principles of competition and negotiation
3. Bid protests
4. Contact types- Generally fixed-price
5. Contract clauses

    a. Performance requirement clauses
    b. Payment clauses
    c. Adjustment clauses
    d. Socioeconomic clauses
6. Bonding and Sureties
7. Recovery from project delays
    a. Contract clauses
        i. Commencement, prosecution and completion of work
        ii. Suspension of work – establishes right to order a suspension of any part of the work for the government's convenience
    b. Compensable vs. non-compensable delays
        i. Excusable – not contractor's fault, non-compensable, extension of time to complete
        ii. Compensable delay – government's fault, extension of time to complete
    c. Eichleay Formula
        i. Recovery of compensable delays
        ii. Home office overhead allocation
            1. Contract billings / billings during contract period = Overhead %
            2. Overhead % X overhead during contract period = Allocated overhead
            3. Allocated overhead / days of contract = overhead per day
            4. Overhead per day X # of days delayed = Overhead due to delay

043 - A contractor has a claim for extended field overhead on a federal government contract. The contract billings were $10 million. The contractor's total billings during the contract period were $100 million. The contractor's total overhead costs during the contract period were $3 million. The contractor worked 1 year on the project. The government caused the contractor to be delayed by 60 days on this contract. Using the Eichleay formula, what is the contractor's claim for overhead due to the delay?

8. Acceleration
    a. If contractor is entitled to an excusable delay, a directive to complete the job on time is a constructive acceleration
    b. Denial of extension due to an excusable delay is equivalent to an acceleration order
    c. Elements of a constructive acceleration include:
        i. Excusable delay
        ii. Government knowledge of the delay
        iii. Government statement or act that may be construed as an acceleration order
        iv. Notice by the contractor to the government that the order constitutes a constructive change; and
        v. Additional costs for acceleration efforts
    d. The following are all considered acceleration orders:
        i. Threat to terminate for default because of an excusable delay
        ii. Request to accelerate

        iii. Gov't pressure to complete on schedule if coupled with a threat assess liquidated damages
        iv. Refusal to grant time extensions (to which the contractor is entitled) coupled with the assessment of liquidated damages
        v. NOTE – mere failure to grant an extension of time does NOT constitute acceleration
    e. If an acceleration order is issued the contractor is entitled to recover the costs resulting from acceleration
9. Contract Disputes Act and Disputes Clause
    a. Provides procedures for appealing the contracting officer's final decision
10. Equal Access to Justice Act and Recovery of Attorney's Fees
    a. Gov't sovereign immunity for liability for legal fees is waived
    b. Gov't become susceptible to the payment of legal fees to the prevailing party if it acts in bad faith
    c. Requires gov't to pay legal fees to the prevailing parties if net worth of individual is less than $2MM or corp/partnership is less than $7MM and under 500 employees
11. Subcontracting
    a. Notification and consent
    b. Flow-down of prime contract obligations
12. Terminations
    a. Termination for convenience
        i. Gov't can terminate contract for convenience
        ii. Contractor can recover certain costs
    b. Termination for default
        i. Gov't can terminate if contractor refuses or fails to prosecute the work with diligence to ensure completion on time

<u>6.15 – Claims</u>

1. Claim exists if a request for additional money or time has been rejected
2. Risks – Need to follow the language in the contract
3. Deficiencies in performance by the owner

<u>6.16 – Delays</u>

1. Non-excusable vs. excusable delay
2. Compensable vs. non-compensable
3. Excusable – non-compensable delay
    a. Only an extension of time is awarded, and no compensation is paid
    b. Acts of God (force majeure)
4. Excusable – compensable delay
    a. Owner caused and contract does not contain a "no damage for delay" clause
5. Non-excusable delay
    a. Delay due to contractor's fault or negligence

<u>6.17 – Acceleration</u>

1. Owner's order to complete the project sooner than the contract requires

2. See §6.14[8]

6.18 – Changed Conditions

1. Also called differing site condition
2. Materially different subsurface or work site
3. Examples:
    a. Buried artificial obstacle such as a rubbish pit or abandoned building foundation
    b. Different and harder rock formation than the contractor expected
    c. Unknown aquifer
    d. Impermeable soil strata that create site flooding during construction
4. Contractor not entitled to recover for a changed condition unless contract permits recovery or can prove contract documents misrepresented the site conditions

6.19 – Changes to the Scope of Work

1. Change orders must be approved by all parties
2. See §24 for detailed analysis

6.20 – Nonpayment or Late Payment

1. Ability to compel payment
    a. Making payments is the owner's primary obligation
    b. Ability to obtain payment should be contractor's central focus in determining whether to enter into a contract.
    c. Pay-if-paid and Pay-when-paid contracts for subs (certain states)
2. Owner's ability to pay
    a. Public sector contracts this is a non-issue
3. Private Owners
    a. Sometimes required to demonstrate they have sufficient money to pay for the contract
4. Mechanics Lien Remedies
    a. State law requirements
    b. Permit contractor or sub to file lien against the property they constructed or provided materials
5. Subcontractors claims and payments
    a. Federal contacts – Miller Act requires contractor post a payment bond to ensure subs get paid
    b. State contracts – same but called Little Miller Acts
    c. Private work – owner may require contractor to have a payment bond
    d. Can also file a mechanics lien

6.21 – Deficiencies in Contractor Performance

1. Breaches of contract by the contractor
    a. Material breaches – Owner can recover monetary damages and/or terminate the contract
    b. Minor/immaterial breaches – owner has right to recover monetary damages
    c. Contracts may specify the differences between material and minor breaches
2. Default Mechanisms

    a. Two types
        i. Minor – compel contractor to fix or pay to have it fixed
        ii. Major – compel cost recover or terminate contract
3. Owner's Damages for Breach of Contract
    a. Right to recover damages vary and depend on the circumstances
    b. Actual damages
    c. Consequential damages
        i. Damages that do not ordinarily flow from a breach of contract
        ii. Usually not recoverable unless the contractor knew or should have known the owner would suffer losses due to the breach
        iii. They can include:
            1. Financing costs
            2. Overhead
            3. Loss of anticipated profits
            4. Attorney's fees
            5. Interest on a damage claim
            6. Loss of business reputation
4. Punitive damages
    a. Rarely recoverable
5. Liquidated damages
    a. Very common in construction contracts
    b. Penalty for not completed on time – can be per day fee
6. Other grounds for recovery
7. Other Owner's claims
8. Owner's claims against third parties

<u>6.22 – Avoidance of Litigation</u>

1. Economics in litigation
2. Controlling litigation cost
    a. In-house resources
    b. Budgeting legal services
    c. Value of settlement

<u>6.23 – Alternatives to Litigation</u>

1. Arbitration
    a. Traditionally most common alternative
    b. More easily manipulated than litigation
2. Mediation
    a. Non-binding
    b. Encourages cooperation and compromise
3. Mini-trial
    a. Attorneys present cases to the two CFO's
    b. CFO's reach a settlement
4. Creativity in the Resolution of Construction Disputes

6.24 – Legal Services

1. Most effective use of legal services are before they are needed or as soon as an issue arises