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A Practical Guide to Negotiating Tricky Clauses in Prime and Subcontracts

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Summary

- Essential contract negotiation strategies for construction projects are explained, focusing on risk allocation and important contractual clauses.
- Perspectives from owners, contractors, and subcontractors illustrate the negotiation process and highlight differing priorities.
- Best practices and actionable tips are provided to help parties reach balanced and successful project agreements.

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Negotiating contracts from owner, contractor, and subcontractor perspectives can be a challenging endeavor as all parties have different goals and risk tolerance. As an attorney facilitating negotiations, it is important to understand all perspectives to best meet the two main goals of contract negotiations: minimizing your client's risk and getting the deal done. Often these two goals are at odds and it is essential to know where and how to compromise to ensure the deal is solidified and that your client is accepting only reasonable and manageable risk. In this article, we provide strategies, considerations, and best practices for attorneys who are negotiating construction agreements for design-bid-build (DBB) projects on behalf of owners, general contractors, and subcontractors, with a focus on often-negotiated areas of the contract. Because the parties to the relevant types of contracts have different goals, objectives, and risk mitigation tools, the headers below will identify toward which contracting party the guidance is directed.

As one would expect, there is inherent conflict in the objectives of owners, general contractors, and subcontractors as it relates to risk shifting. While the practical guidance below advises on risk avoidance and mitigation strategies, contracting parties often will find that they may not be able to negotiate the "perfect" contract owing to lack of leverage, business objectives (e.g., future opportunities becoming available as a result of taking on undesirable contract risk), and other situational circumstances. Each project team, in conjunction with legal counsel, must determine which positions are critical and which have room for compromise based on their unique circumstances, including insurance program coverages.

Note that this article does not address each and every type of "risky" contract provision. Rather, the authors have selected a set of clauses that, in their experience, are heavily negotiated because of the risk exposure each clause presents to the various parties and the common disputes that arise where the language in these clauses becomes critical. These clauses not only are often the source of conflict during contract negotiations, but also have many variations that practitioners consider to be "market" or "industry standard."

Scope of Work

Duty to Review Contract Documents

Construction agreements in the DBB context typically refer to the relevant set of documents (the agreement, general or other conditions to the agreement, modifications to the agreement (such as change orders), drawings, and specification) as Contract Documents. This term should be defined in the agreement, and a list of documents that the parties believe control their respective obligations and responsibilities should be specifically listed.

On large and/or complex projects, construction drawings and specifications and other relevant Contract Documents may be voluminous. It is typical that there may be some inconsistencies and/or conflicts between different Contract Documents; additionally, there may be gaps of information necessary to determine exactly what is required for construction.

Owner Perspective

By the time an owner is retaining a general contractor, the owner likely already has hired an architect and/or a team of design professionals; accordingly, a mostly complete set of drawings and specifications has likely been prepared. Typical owner/designer agreements do not allow for much, if any, recourse against the designers for the inconsistency/gap issues described above, unless they rise to the level of a breach of the designer's applicable standard of care. Additionally, most owners lack the requisite experience to themselves identify and/or address any potential conflicts, inconsistencies, and gaps among Contract Documents.

While the AIA A201 template provides that the general contractor must "carefully study and compare the various Contract Documents" before performance of the work, and "promptly report to the Architect any errors, omissions, or inconsistencies," it also provides that the "Contractor's review is made in the Contractor's capacity as a Contractor and not a design professional." [1]

Many owners prefer to heighten the contractor's standard for review, especially when the owner is not meaningfully involved in the details of design and construction. This can be accomplished many ways, depending on the owner's particular pain points. Some variations include requiring the contractor to

- Affirm it has reviewed the Contract Documents and can perform the work and provide a complete and operable project.
- Represent and guarantee that based on its review of the Contract Documents, the project can be built in a way consistent with the owner's goals and design intent.
- Examine the Contract Documents in conjunction with investigation of the existing conditions and applicable laws and raise any identified issues with the owner and/or designers.

General Contractor Perspective

Generally, the standard AIA language quoted above is deemed a reasonable assumption of risk for general contractors. A general contractor must review custom agreements and modifications to the standard AIA forms to make sure that the language does not require a peer review and that the general contractor is otherwise qualified to perform the contract scope. Contract language should be reviewed to ensure both the necessary tasks and the risks of the unknown are reflected in the contract price and covered to the extent possible by available insurance.

Additionally, the general contractor should review the Contract Documents to ensure it is not waiving its right to claim adjustments of time and money for issues within the Contract Documents due to failure to report them in a specific time or method to the owner/design team.

Subcontractor Perspective

As will be the case frequently in this article, as it relates to review of Contract Documents, subcontractors often will be stuck with whatever risk the general contractor assumed visà-vis the owner. Subcontractors should still make sure, however, that if the subcontract agreement flows down the terms of the prime contract, the subcontractor has reviewed the prime contract and all relevant Contract Documents. The subcontractor should be careful not to accept responsibility for design defects or higher responsibility for review of Contract Documents beyond that of a reasonable subcontractor unless the subcontractor's scope specifically includes design work. The subcontractor also should be careful to ensure that its responsibilities are limited to its scope of work in the subcontract agreement.

Like the general contractor, the subcontractor should review the subcontract, prime contract, and related documents to ensure the necessary tasks and risks of the unknown are reflected in the subcontract price and covered to the extent possible by available insurance. To the extent possible, the subcontractor should try to negotiate that the terms of the subcontract agreement take precedence over any conflicting prime contract terms to minimize exposure to clauses it might be bound to that it had no opportunity to negotiate.

Spearin *Doctrine*

The *Spearin* doctrine establishes an implied warranty that owner-provided plans and specifications are sufficient for the intended work. [2] If defective, the owner, not the contractor, bears the risk of resulting issues. However, the *Spearin* doctrine's application and the ability to contract around it vary by state, creating critical considerations for all parties.

Owner Perspective

For traditional DBB projects/contract, owners must recognize *Spearin* shifts liability to them for defective designs unless explicitly contracted out. For example, in Texas, prior to 2021 legislation, [3] contractors could be held liable for owner-furnished design defects, [4] an outlier now largely aligned with *Spearin* via statutory reform requiring notice of defects. [5]

To mitigate *Spearin* risk, owners can include clauses shifting design verification duties to contractors such as "Contractor shall verify all dimensions and conditions and assumes responsibility for design adequacy." However, courts require such disclaimers to be clear and specific. Ambiguous language may not override *Spearin*, leaving the owner liable. [6]

Not all states permit contracting around *Spearin*. California, for instance, upholds *Spearin* as a public policy matter, [7] prohibiting waivers in public contracts. Ohio, by contrast, allows express disclaimers. [8]

General Contractor Perspective

In DBB projects, the *Spearin* doctrine shields general contractors from liability for defective prescriptive specifications; however, accepting duties like "verifying constructability" can waive this protection.

In traditional DBB projects/contracts, the general contractor must precisely follow the owner-provided drawings and specifications. These owner-provided specifications are thus sometimes known as prescriptive specifications. Where the general contractor is providing design services and/or performing under a design-build contract, the specifications provided by the owner are known as performance specifications because they dictate the performance standards by which the contractor or design-builder must design and construct. Agreeing to comply with performance specifications (rather than traditional prescriptive specifications) opens up the general contractor to liability for defective design. [9]

Most states allow contracting around *Spearin* with explicit terms, [10] but states like California and Illinois do not allow such risk shifting on public projects. [11] In the Illinois court of appeals decision W.H. Lyman, a $675,000 claim evaporated because the general contractor improvised without approval and missed subsurface risks—proof that *Spearin*'s sword cuts both ways: follow the plans or pay the price. Finally, even where permissible, shifting design risk to contractors often increases bids and insurance costs because contractors price in the added liability.

Ohio courts have upheld express terms overriding *Spearin*. [12] and shifting risk from the owner to the general contractor. Similarly, in Pennsylvania, a general contractor could not invoke *Spearin* when a named window supplier failed because the contract's "approved equal" clause allowed for substitutions of materials; the court deemed that this clause created a performance specification—leaving the general contractor liable for its material choice. [13] General contractors straying from prescriptive specifications risk losing *Spearin*'s shield.

General contractors can negotiate indemnity clauses to hold owners accountable for defective plans, as seen in J.L. Simmons, where a general contractor recovered costs for faulty pile foundation designs, preserving *Spearin*'s benefits via conditional subcontractor liability. [14] However, A.G. Cullen shows limits: In that case, the general contractor won delay costs for lead paint abatement (an owner omission), but not for supplier issues, underscoring the need for explicit terms. [15] In performance-specification contracts, where general contractors control design or means, *Spearin* offers no shield, and general contractors bear the risk—here, A.G. Cullen incurred $130,000+ in supplier delay costs due to its discretion. Missouri treats *Spearin* as a "shield" against liability and a "sword" for delay claims. [16]

Subcontractor Perspective

Subcontractors must meticulously review the prime contract and all incorporated documents to avoid assuming unintended liabilities. In *Fuller*, [17] subcontractors were forced to incur the price of union wage hikes when the labor costs outpaced the prime contract's fixed rates. [18] The general contractor was unable recover from the government due to a prime contract clause barring claims for excess wage payments, leaving subcontractors unpaid for increased costs of approximately $2.5 million.

Subcontractors should resist clauses shifting design or external cost risks (e.g., "Subcontractor warrants plan sufficiency" or "No claims for wage increases") unless compensated. In Washington, where *Spearin* is robust, [19] subcontractors can lean on the implied warranty unless overridden, but Fuller shows how explicit disclaimers can neuter protections. For protection, subcontractors should consider negotiating carve-outs like "Subcontractor shall not be liable for Owner-driven cost increases."

New York courts allow subcontractors to recover from general contractors for owner design defects under *Spearin*, [20] but only if the subcontractors did not assume the risk or contribute to the issue. In Fuller, the subcontractor's recovery hinged on the general contractor's claim, which failed due to the prime contract's wage clause—highlighting that *Spearin*'s shield does not extend to all cost overruns. Subcontractors in states like Ohio, where contracting around *Spearin* is permitted, [21] must be beware of such traps.

Standard of Care: Balancing Expectations and Liability

The standard of care defines the level of skill and diligence expected in performance of the work, typically that of a reasonably prudent contractor performing work of a similar nature and similar size in a similar location. Contract modifications can heighten or lower the standard of care, but legal and practical limits apply. In some jurisdictions, both an industry standard of care and a reasonable person standard of care can apply. [22]

Owner Perspective

Many owners require general contractors to provide "first-class," "best," "highest quality," and/or "top of the line" services and work. This language is used to heighten the standard of care to which the contractor is contractually required to perform. However, owners should be aware of the ways in which such language could backfire and ultimately limit owner recovery in the event of defective or deficient work. Specifically, courts may find that terms that elevate the standard of care operate as express warranties, which may then invalidate insurance coverage because professional policies often exclude guarantees beyond negligence. [23]

Additionally, heightened standard language could lead to unpredictable end results for the owner. For example, the contractor may argue that the "best" and "first class" language requires it to deviate from the prescriptive specifications. The parties to a construction agreement are typically seeking clarity and clear agreement between them. Rather than broadly heightening the standard of care as described above, for DBB projects, an owner should work with its design team to ensure the project designs reflect the owner's desired end result and that the contractor has properly bid, planned for, and ultimately installed that which has been designed.

Tellingly, the AIA A201-2017 does not contain any express standard-of-care language. The contractor is required to perform the work as set forth in and reasonably inferable from the Contract Documents, [24] in accordance with applicable laws, [25] of good quality and new (unless otherwise specified), [26] free from defects (except as inherent in the design), [27] and in conformance with the Contract Documents. [28]

General Contractor Perspective

General contractors should carefully review proposed language to avoid a heightened standard of care that could be virtually impossible to achieve. For example, language like "best efforts," "best care," and of a "first class contractor" could result in the general contractor breaching the agreement if its efforts and care are anything short of best. [29] Additionally, this type of language leads to ambiguity (which can lead to disputes) because these heightened standard of care goals are not defined. In practice, what constitutes best efforts compared to reasonable efforts?

While the AIA A201-2017 generally affords general contractors with a reasonable starting point for negotiations, one exception is the following language in Section 1.2.1 in bold:

> The intent of the Contract Documents is to include all items necessary for the proper execution and completion of the Work by the Contractor. The Contract Documents are complementary, and what is required by one shall be as binding as if required by all; performance by the Contractor shall be required only to the extent consistent with the Contract Documents **and reasonably inferable from them as being necessary to produce the indicated results.**

(Emphasis added.) General contractors may consider striking the portion above stating "as being necessary to produce the indicated results" because such language could be interpreted to require a performance standard (i.e., a deviation from a DBB contract's typical prescriptive standard).

With regard to the subcontract agreement, the general contractor often imposes on subcontractors a standard of care slightly higher than the one the prime contract imposes on the general contractor. For example, subcontractors are frequently required to include all things reasonably inferable from the plans and typical for their scope of work to help the general contractor avoid scope gaps. From a general contractor's perspective, subcontractors are often in the best position to understand the ins and outs of what is necessary to accomplish the subcontractor's scope of work.

Subcontractor Perspective

Similar to prime contract concerns relating to insurance coverage and a heightened standard of care, heightening the standard of care in subcontract agreements may have the same unintended effect. If found to create express warranties, heightened standard of care terms may nullify errors-and-omissions (E&O) coverage. [30] Instead, subcontractors should insist on specificity and details in the scope of work and other key contract requirements.

Subcontractors also should consider pushing back on a standard of care beyond what would be "reasonable" for a similarly situated subcontractor in the same specialty in the same area unless there are business reasons to take on the increased risk. While subcontractors are often stuck with flow down of a prime contract that they had no ability to negotiate, they should be mindful of taking on the risk of a heightened standard of care for all the reasons that apply to a general contractor.

Implications of "Sole Discretion"

A higher-tiered party will sometimes attempt to insert language into a construction contract giving it the unilateral ability to make certain decisions. Such language is generally included to state that the higher-tiered party, often the owner or general contractor, shall have “sole discretion” to make a decision if a certain event arises on the project. Typically, this language is most often seen in the following types of clauses: (1) reduction of retainage, (2) changes, (3) options when a contractor (or subcontractor) is in default, (4) passthrough claim,; (5) dispute resolution method, or (6) direct payment to subcontractor, sub-subcontractor, or supplier. By way of example, a clause may read: “Owner may, at its sole discretion, deduct from any payment due Contractor those costs and damages necessary to correct Contractor’s default or neglect.”

Owner Perspective

Owners can benefit from using “sole discretion” language in contracts for issues where the owner wants to avoid having to seek any approval or agreement from another party to the construction project. Owners should seek to implement “sole discretion” language when considering delay to and/or payment withholding/offset. However, the use of “sole discretion” also can lead to its own issues and problems. Owners are likely to get significant pushback from lower-tiered parties on issues where owners assert “sole discretion,” which can lead to more drawn-out negotiations and ill-will. Additionally, the term “sole discretion” can be ambiguous and open to interpretation if the contextual language is not clear. For example, if an owner makes a decision using its “sole discretion,” is that decision final or can it be contested in the claims process? If it can be contested, the use of “sole discretion” might not avoid litigation or other dispute resolution processes to resolve the issue. In balance, to avoid or minimize these issues, owners should use “sole discretion” language mindfully, avoid overuse, and be sure to have appropriate language clarifying the context in which the “sole discretion” is intended to avoid ambiguity.

General Contractor Perspective

General contractors should be cautious about accepting any language in the prime contract that gives owners “sole discretion” because it puts general contractors at high risk. Of course, the level of caution is dependent on over what the owner seeks to have “sole discretion.” For example, if the owner seeks “sole discretion” over a significant issue —i.e., substantial completion when failing to meet substantial completion subjects the general contractor to liquidated damages—the general contractor should not agree to allowing the owner “sole discretion.” If the owner insists on the “sole discretion” language for a significant issue in the contract, the general contractor should insert language to reduce its risk. One way to reduce the risk is to add language that the owner’s determination is subject to the claims provisions in the contract so that the owner’s unilateral decision is not binding, or to require that the discretion be exercised "reasonably" or "in accordance with reasonable commercial practices."

General contractors face similar considerations when using "sole discretion" language in subcontracts, and general contractors will have an additional subcontract consideration where the owner has inserted sole discretion language in the prime contract. If the owner successfully added "sole discretion" language for certain issues, the general contractor should consider including similar language in its subcontracts for those same issues or make any determination of those issues dependent on the owner's decision.

Subcontractor Perspective

Subcontractors, as the lower-tiered parties, often incur the brunt of any "sole discretion" language in the owner–general contractor prime contract or the subcontract. Subcontractors should be cautious about agreeing to any "sole discretion" language because such language could negatively impact their rights. To the extent the general contractor requires that language, the subcontractor should attempt to include language so that the general contractor's decision is not the final decision and can be subject to the claims process. Also, if the general contractor cites the prime contract as the reason for the language, the subcontractor should consider including language that links the general contractor's determination to the owner's determination.

Liability for Unforeseen Conditions/Differing Site Conditions

Unforeseen conditions and differing site conditions are often the cause of claims and disputes on a construction project. Unforeseen site conditions are conditions that are covered or otherwise latent or hidden and not reasonably ascertainable by the general contractor or subcontractor from the project documents or a site visit. Differing site conditions are conditions that are materially different than those shown on project documents and that could not be determined by a general contractor or subcontractor through a site visit and inspection. The owner is generally responsible for unforeseen/differing site conditions but will usually include language in the prime contract to limit its liability or push the risk of these conditions down to the general contractors. Similarly, general contractors often will attempt to push the risk down to subcontractors.

Owner Perspective

To the extent it can, an owner wants to make the general contractor responsible for knowing all conditions, seen or unseen, on the project site and to disallow price adjustments for conditions that the general contractor failed to take into consideration. This drastic position is not typically realistic. Owners should consider including a prime contract provision that requires the general contractor to accept the risk for any visible condition, conditions that the general contractor should be aware of at the property and that were "reasonably inferable" from the Contract Documents. The owner also should include language that requires the general contractor to provide notice when it discovers an alleged unforeseen condition or assume responsibility for the costs resulting from the unforeseen condition (see further discussion of notice requirements below). The owner should seek that such notice be required within three or seven days after discovery to permit the owner time to investigate and/or mitigate cost impact.

General Contractor Perspective

General contractors should have upfront discussions with owners about who is in the best position to obtain information about the property and understand the risk of potential unforeseen or differing site conditions. At the beginning of the project before construction activities commence, the owner is in the best position to discover conditions that are not visible on the property. The owner generally retains a geotechnical contractor to determine the suitability of subsurface conditions. Further, the owner generally contracts with the design team to prepare construction drawings and documents (unless the project is design-build). Because of this, the owner is in the best position to mitigate unseen risk prior to the general contractor commencing the construction work.

The general contractor is often in the best position to identify visible conditions or conditions that are reasonably ascertainable from the construction drawings and documents. For a balance, the general contractor should limit its risk to any visible conditions and conditions the general contractor could reasonably ascertain; general contractors should be wary of contract provisions that attempt to heighten a general contractor's investigative duties on the front end or shift risk of unforeseen conditions to the general contractor.

The AIA A201-2017 takes a reasonable position requiring the general contractor to notify the owner of an alleged unforeseen condition within 21 days:

> § 3.7.4 Concealed or Unknown Conditions. If the Contractor encounters conditions at the site that are (1) subsurface or otherwise concealed physical conditions that differ materially from those indicated in the Contract Documents or (2) unknown physical conditions of an unusual nature, that differ materially from those ordinarily found to exist and generally recognized as inherent in construction activities of the character provided for in the Contract Documents, the Contractor shall promptly provide notice to the Owner and the Architect before conditions are disturbed and in no event later than 21 days after first observance of the conditions. The

> Architect will promptly investigate such conditions and, if the Architect determines that they differ materially and cause an increase or decrease in the Contractor's cost of, or time required for, performance of any part of the Work, will recommend an equitable adjustment in the Contract Sum or Contract Time, or both. If the Architect determines that the conditions at the site are not materially different from those indicated in the Contract Documents and that no change in the terms of the Contract is justified, the Architect shall promptly notify the Owner and Contractor in writing, stating the reasons. If either party disputes the Architect's determination or recommendation, that party may proceed as provided in Article 15. [31]

Subcontractor Perspective

Subcontractors need to be especially careful about taking on responsibility for unforeseen conditions because they are the most likely party to discover the condition as the project proceeds. Subcontractors should not agree that a site visit or investigation coupled with a review of the Contract Documents is sufficient for the subcontractor to undertake responsibility for all site conditions, visible or unseen. Similar to general contractors, subcontractors should limit their responsibility to visible conditions or conditions reasonably ascertainable from the Contract Documents. Subcontractors also can agree that they will provide notice of any unforeseen or differing site condition promptly after it is discovered.

General contractors often try to include clauses similar to the below:

> Subcontractor has visited and examined the Premises and reviewed all physical conditions that could affect the Work. Through that review the Subcontractor has familiarized itself with all of the conditions affecting the Premises. Therefore, Subcontractor agrees that it shall not be entitled to a claim for any additional compensation or extension of time due to the existing conditions on the Premises.

Subcontractors should attempt to modify those clauses to limit their risk and responsibilities (see proposed bolded revisions below):

> Subcontractor has visited and **viewed** the Premises and reviewed all **reasonably visible** physical conditions **that are not concealed or otherwise obstructed from view** that could affect the Work. Through that

> review the Subcontractor has familiarized itself with all of these **reasonably visible** conditions affecting the Premises. Therefore, Subcontractor agrees that it shall not be entitled to a claim for any additional compensation or extension of time due to these **reasonably visible** existing conditions on the Premises.

Changes in the Work

Another area giving rise to frequent disputes and claims is changes in the project. Changes in the scope of work can arise from design changes, material or equipment changes, owner choices, schedule changes, and changes arising due to site conditions. Both what constitutes a change and what is allowed to be included in the requested change are potential areas for disagreement.

Limitations on Changes

Owner Perspective

Owners have a significant interest in controlling costs. Changes represent a significant risk for owners and, accordingly, an area where owners will want to exert some control. Owners should include prime contract language that defines what costs, markups, and associated schedule extensions can be included in change order proposals. Owners (and their lenders) are becoming more hands-on concerning what general contractors may include as costs within changes. For example, limitations on a general contractor’s profit and overhead for changes can control costs. Owners also may require detailed substantiating documents to justify requested costs and ensure that the general contractor only passes on the incremental additional cost attributable to the change.

General Contractor Perspective

General contractors will want to push back on any change order cost cap, particularly for overhead and profit. General contractors can agree to put a cap on their subcontractors’ overhead and profit, which will result in lower costs for the owner even if there is no cap on the general contractors’ overhead and profit. General contractors will want to make sure that the scope of work, clarifications, and qualifications are clearly defined so that any changes are clear. It is equally important for general contractors to ensure that their subcontracts cover every aspect of the prime contract scope of work. If the general contractor misses a portion of work, that is a scope gap, and the general contractor (i) will not be entitled to additional funds from the owner and (ii) will face a change order request from its subcontractor for additional work.

Subcontractor Perspective

Subcontractors, as the ones required to perform changed work, should make sure that their subcontracts contain language that provides them the ability to secure change orders, not perform changed work until the change orders are executed, avoid unreasonable limits on overhead and profit for change order work, and require that the general contractor pass their change order requests up to the owner in a timely manner (where the change stems from the owner). Subcontractors should make sure that their subcontracts clearly identify the scope of work, including qualifications and clarifications. Subcontractors must include any qualifications or clarifications in their proposals and make sure that proposal documents are explicitly incorporated by reference within the subcontract. A common subcontractor oversight is where a subcontract does not include proposal qualifications/clarifications; when a subcontractor then seeks a change for work that may have been qualified in the proposal, the subcontractor will not be entitled to that change. Subcontractors also should try to limit or remove language that only allows the subcontractor to obtain a change order where the owner approves the change order for the general contractor or that caps the amount recoverable for a change to that which the owner agrees to pay the general contractor.

Subcontractors should push back on a general contractor trying to limit overhead and profit, but subcontractors can consider agreeing to the same cap to which the general contractor agreed in the prime contract. Subcontractors should make sure that the language in their subcontracts allows change orders for general contractor–directed changes even if the general contractor is not entitled to a change order from the owner.

Obligation to Continue to Perform Work During Dispute

It is common for construction contract parties to dispute change orders. Most frequently, disputes arise over (1) the cost of the change order work, (2) additional time allowed due to the change order work, and (3) whether the work is actually a change. Because of the frequency of change requests on projects, most industry contract forms contain a clause requiring the general contractor and subcontractor to proceed with work even if there is a dispute over whether that work is a permitted change.

For federal projects, Federal Acquisition Regulation 52.233-1 states:

> (i) The Contractor shall proceed diligently with performance of this contract, pending final resolution of any request for relief, claim, appeal, or action

> arising under the contract, and comply with any decision of the Contracting Officer. [32]

This is similar to the requirements set forth in AIA A201-2017, Section 15.1.4.1, which states:

> Pending final resolution of a Claim, except as otherwise agreed in writing or as provided in Section 9.7 and Article 14, the Contractor shall proceed diligently with performance of the Contract and the Owner shall continue to make payments in accordance with the Contract Documents. [33]

Owner Perspective

For owners, time equals money. Owners want their projects completed on time, and costs for project delays can arise from many areas, including interest and costs on loans, inability to profit from the completed project (e.g., leasing spaces and collecting rents, or using the space as a business and collecting profits), and realizing the benefit of the completed project. Because of the various costs owners can incur for a delayed project, owners will seek contract language requiring general contractors to continue to work even when a dispute arises on the project. If a general contractor is able to stop work during a dispute, an owner would find itself in a challenging negotiation position because the length of the dispute discussion/work stoppage could extend the project completion time, costing the owner money.

General Contractor Perspective

General contractors' primary interest on change orders is to be paid for the work performed. Contractors should push back on requirements to continue work during disputes, although that pushback is often futile. Instead, contractors can attempt to limit their risk. One way to limit the risk is to negotiate a cap on the amount of changes an owner can direct absent execution of an agreed change order and payment to the contractor. In 2023, Texas enacted legislation protecting contractors and subcontractors on private projects by allowing them to elect not to proceed with additional work directed by an owner if (1) the contractor or subcontractor has not received a written, fully executed change order for the owner-directed additional work and (2) the total actual or anticipated value of the additional work, plus any previous owner-directed additional work for which the contractor or subcontractor has not received a written, fully executed change order exceeds 10 percent of the contractor's or subcontractor's original contract amount. [34] The contractor or subcontractor electing not to proceed "is not responsible for damages associated with the election not to proceed." [35]

Another strategy is for contractors to include language requiring owners to pay a certain percentage of a disputed change order up front while reserving rights to dispute the amount later. Similarly, contractors can reserve rights to seek an adjustment of time arising from the changed work at a later date; however, general contractors must ensure that any such reservations are free from potentially conflicting language stating that a change order resolves "all claims" through a date certain. Executing this could waive the general contractor's rights to later seek additional compensation or time arising from the change.

A more complicated situation arises where there is disagreement about whether or not a change is one for which the general contractor is entitled to a price or time adjustment. In these situations, the general contractor should try to negotiate a similar agreement where the owner is required to pay a portion of the costs incurred and where both parties reserve their rights to dispute the validity of a change. Owners, however, typically do not like to make "advance" payments for work owners do not believe are changes and any such advance could be complicated if the project is funded through a loan or a title company is involved in payments. An alternative is to include a provision that allows for dispute resolution during the project in an expedited timeframe so there can be an adjudication of rights and payment to the general contractor (i.e., a project-specific mediator). Some form contracts provide for the architect to play this type of role, but typically general contractors will not want to have the architect be the interim decision-maker because of the architect's closer connection with the owner and the likelihood that disputed changes often arise from claims that the drawings and specifications were deficient.

The general contractors also will want to ensure that any obligation to continue work during disputes flows down to subcontracts requiring the subcontractors to perform during disputes.

Subcontractor Perspective

The subcontractor is typically the party that bears the burden of change order disputes because it is the party actually performing the work and incurring the majority of the additional costs. Subcontractors do not want to finance changed scope of work for the duration of the project because of a dispute. Accordingly, subcontractors should push back on a blanket requirement to continue work during a dispute and should push to require that a percentage of payment for the changed work be made while the final amount is negotiated, reserving rights for additional time due to changes and considering interim-dispute resolution if a dispute arises over whether certain portions of the work are changes to the subcontractor's scope. Like general contractors, subcontractors also must be wary of release language in changes that seeks to encompass scope greater than that of the change itself.

Subcontractors also will want to ensure that their subcontractors secure the same or better rights to refuse to perform change work as those set out in the prime contracts.

In addition, subcontractors should (1) guard against nonpayment because of any delay by the general contractor in submitting a proposed change order to the owner and (2) limit a general contractor's refusal to pay because it has not been paid by the owner. Consider the following language:

> Owner's payment to General Contractor for any Changes it orders or causes is a condition precedent to General Contractor's obligation to pay Subcontractor for such changes or alterations **provided that General Contractor has pursued payment of the changes from the Owner in a timely and good faith manner and has continued to provide Subcontractor with information on the status of the submitted changes and the opportunity to provide evidence of the entitlement to and amount of additional compensation due to the Change.**

Subcontractors also will want to clarify the difference between an owner-directed change and a general contractor–directed change to ensure that approval/payment by the owner is not a prerequisite for a general contractor–directed change. This protects the subcontractor against situations where the subcontractor is entitled to a change, but the general contractor may not be so entitled. Consider: "When a change is directed by Contractor instead of Owner, Contractor shall process and pay that change to Subcontractor within [__ days] or [a reasonable amount of time]."

Notice Requirements

Contractual notice requirements typically require a general contractor or subcontractor to provide written notice within a certain timeframe of any conditions discovered on a project that give rise to a claim by the contractor or subcontractor for additional money or time. Courts differ in their enforcement of notice provisions. Some courts view notice requirements liberally and focus on the purpose of the clause. [36] Other courts employ a stricter construction, finding that "written-notice-of-changed-conditions provisions" should be strictly enforced. [37]

Owner Perspective

Owners should seek strict notice requirements and enforce waiver provisions if contractors do not strictly adhere to those notice requirements. Generally, notice requirements exist to provide owners notice of conditions or circumstances that could result in a more expensive project or a project that will take longer to complete. By requiring timely notice of any conditions or circumstances for which a general contractor or subcontractor claims additional time or money, the owner can work to mitigate the impact or cost.

General Contractor Perspective

General contractors will want to ensure that notice provisions allow for sufficient time to provide notice to the owner and that subcontracts include subcontractor notice requirements that allow the general contractor time to comply with its own notice obligations to the owner. Similarly, general contractors should seek that subcontractors waive any claims if the subcontractors do not comply with subcontract notice requirements.

Subcontractor Perspective

Subcontractors are the most likely party to discover conditions or circumstances that give rise to a claim for increased cost or time. Because of this, subcontractors should make every effort to extend notice periods as far out as possible to ensure they have sufficient time to report such conditions (e.g., “as soon as reasonably practicable”) and try to eliminate any waiver language. If the prime contract contains a notice provision and a correlating waiver clause, it is unlikely that the general contractor will agree to eliminate these same provisions in the subcontract. Subcontractors should try to mitigate the impact of these clauses by making sure that the “notice” can be provided in different ways and is not a specific type of written notice. Subcontractors also should seek language that permits oral notice of changes, but best practices dictate that a written confirmation of such notice also be issued. Additionally, subcontractors should add language that waiver does not apply if the general contractor is not prejudiced by the subcontractor’s failure to strictly comply with the notice provision, e.g., “unless Contractor is not prejudiced or detrimentally impacted in any way as a result of Subcontractor’s failure.”

Risk Allocation

Flow-Down Provisions

Flow-down provisions are very typical in construction contracts for both private and public projects. Flow-down provisions may expressly specify provisions from a prime contract with which a subcontractor is required to comply or may generally obligate the subcontractor to the general contractor and owner in the same manner and extent the general contractor is obligated to the owner in the prime agreement. The purpose of flow-down provisions is, among other things, to ensure the subcontractor is contractually obligated to take steps necessary for the general contractor to meet its requirements (e.g., notice provisions for changes and claims) or to ensure that the owner and other parties are protected in the event the subcontractor is responsible for damages or liability (e.g., indemnity for third-party claims for personal injury or property damage).

Owner Perspective

Owners can ensure certain provisions exist in subcontract agreements by, among other ways, including a flow-down provision and affirmative obligation on the general contractor in the prime agreement, dictating the terms of the subcontract through a contractual right of review, or requiring a subcontractor rider that takes precedence over the general contractor's template language. Reputable subcontractors not only will be able to perform the project work as required but will have insurance coverage available in the event of an insured occurrence. To ensure an owner retains this benefit, an owner will want to make sure insurance requirements for subcontractors are specified in the prime contract and the requirements for the same are flowed down to all subcontracts. Additionally, owners should insist on subcontractors providing indemnity to the owner in the subcontract.

Other flow-down provisions that owners should consider include

- Provisions requiring the subcontract agreement to expressly provide that the owner is a third-party beneficiary under the subcontract agreement, which can allow the owner to directly enforce the subcontract.
- Provisions providing that the subcontract may be assigned from the general contractor to the owner, sometimes contingent on termination of the general contractor.
- Dispute resolution provisions, including venue and choice of law.
- Jobsite access, use, and safety rules.
- Requirements that are to be flowed down from agreements between the owner and the lender or the owner and the landlord.
- Hiring and discrimination representations.

General Contractor Perspective

As an initial matter, the general contractor should always review the prime contract obligations for flow-down provisions and ensure the relevant subcontract agreements are compliant with the same. Additionally, even if not expressly required, the general contractor should draft the subcontract agreement in a way that ensures consistency of dispute resolution forum, venue, and choice of law in case a dispute arises involving both the owner and a subcontractor.

The general contractor may choose to flow down the necessary provisions without providing a copy of the prime contract by specifically including language in the subcontract that covers the obligations/requirements from the prime contract; however, the general contractor can run the risk of improperly or incompletely drafting the clause in a way that adequately achieves the necessary flow-down. If the general contractor does not want to share a redacted copy of the prime agreement, it must be diligent about clearly identifying flow-down requirements in the subcontract.

Alternatively, the general contractor can provide the subcontractor a redacted copy of the prime agreement and achieve the flow-down by referencing the flow-down clause of the prime contract by (i) referencing the clauses to be flowed down from the prime contract and (ii) more generally, stating that the subcontractor is being bound to the contractor in the same manner and to the same extent that the contractor is bound and obligated to the owner under the prime contract.

If the general contractor seeks to flow down the provisions by providing a copy of the prime contract, it is recommended that the agreement is actually provided to the subcontractor rather than requiring the subcontractor to request the agreement. Actual provision of the prime contract ensures the subcontractor has a fair opportunity to review and understand the relevant flow-down provisions.

Subcontractor Perspective

Subcontractors must make sure that they have an opportunity to review and understand the relevant requirements flowed down from the prime contract and should request a copy of the relevant prime contract and other Contract Documents. While, at the time of review, it is unlikely a subcontractor will be able to bring about a change to the prime contract, the subcontractor should review the requirements to make sure it understands the risks presented and available insurance and has priced its work adequately to account for such requirements.

Subcontractors also should consider negotiating language allowing them to obtain the benefits and rights of the general contractor as to the owner in addition to just adopting the general contractor’s responsibilities and obligations as to the owner. This arrangement is not typically prohibited by the prime contract and could provide the subcontractor with benefits commensurate with those enjoyed by the general contractor.

Cybersecurity and Cyber Fraud: Emerging Risks in Construction Contracting

The FBI's 2023 Internet Crime Report flags construction as a Business Email Compromise (BEC) bullseye, with $2.9 billion in industry losses screaming for action. [38] Contracts often lag behind these risks, leaving liability unclear.

Owner Perspective

Owners can take on major risks if their electronic systems let fraudsters in, especially when contractors lean on the owner's electronically communicated instructions in good faith. The Erie Parkway Bridge project provides a cautionary example. In 2015, the Town of Erie, Colorado, was the victim of a BEC scam in which scammers posing as a contractor tricked the Town of Erie into wiring a $1.016 million payment to the scammer's account. [39] While the Town of Erie had cybersecurity insurance in place at the time of the scam, the relevant insurers were hesitant to pay out against the policy, forcing the Town to litigate to obtain recovery. [40] UCC § 4A-202 shields banks if the owner authorizes the wire, so owners do not have a source of recovery from the financial institution itself. [41]

While owners can attempt to pass on the risk of BEC scams to general contractors, many contractors do not have the insurance available or financial wherewithal to take on such risks. Nonetheless, it is likely to be increasingly common for owners to contractually pass on liability to general contractors for the risks associated with cyberfraud and BEC scams. It is yet unclear what the "market" standard will be for the shifting of such risk; in the meantime, owners should ensure they are adequately insured and are requiring affirmative steps to avoid scams, such as multifactor authentication for payment changes. Owners also should understand that many insurers are initially denying claims for BEC scams and that they should be prepared for what may be a drawn-out recovery process against insurance. [42]

General Contractor Perspective

General contractors are also frequent targets of BEC scams, as subcontractor payments flow through them. In 2 Hail, a BEC scammer hacked into a subcontractor's email account and scammed a general contractor into wiring $54,985 to the scammer account. [43] In that case, even though the subcontractor was found to have inadequate protections against email hacking, the general contractor was responsible for the risk of double payment. [44]

General contractors may consider contractual waiver and/or disclaimer language in their subcontracts and/or putting procedures in place to authenticate subcontractor payments. However, subcontractors are generally undercapitalized, and most are unlikely to be able to weather the risk of cyberfraud uncertainty without drastically increasing their margins. General contractors also may consider obtaining insurance protection for such situations and putting in place stringent procedures for payment and changes to payment methods.

Further, if the general contractor's cybersecurity or cyberfraud situation stems from abusive domain name registrations like cybersquatting, the most efficient and effective tool may be through a Uniform Domain Name Dispute Resolution Policy (UDRP) action through an approved dispute resolution service provider. These proceedings are typically faster than a traditional court proceeding and may be a good tool if the fraud stems from cybersquatting.

Subcontractor Perspective

Subcontractors also may consider obtaining computer fraud and other relevant insurance to protect them from electronic scammer risks. While in the case highlighted above, a general contractor was responsible to pay despite the root cause being the hacking of the subcontractor, this is not yet the law in Colorado or other states. Subcontractors should resist contractual provisions shifting liability of BEC scamming to them unless they are able to obtain adequate insurance and should consider UDRP actions where cybersquatting is in play.

Subguard/Subcontractor Bonds

Subcontractor default insurance (SDI), also referred to as Subguard® (the name coined by Zurich Insurance Company for their SDI product), is an insurance policy that protects general contractors from financial losses due to subcontractor defaults. In contrast, a subcontractor bond is generally comprised of two separate bonds, a payment bond and a performance bond (P&P bonds), issued by a surety where the surety assures the obligee (usually the general contractor for subcontractor bonds) that the principal (the subcontractor) will perform its contractual obligations and pay all of its subcontractors and suppliers. Subcontractor bonds are not insurance, and if the surety must pay or complete the subcontractor's work, the surety will look to the subcontractor (and often individual owners of the subcontractor entities who signed a guarantee) for reimbursement.

Owner Perspective

The owner's interest with Subguard or P&P bonds is the same: what cost will be passed up to the owner for these products and what benefits the owner derives from these products. Owners do not necessarily receive a direct benefit from either Subguard or P&P bonds, but owners obtain an indirect benefit because these products provide a layer of protection for the general contractor that could help the project stay on time and on budget if there is a significant subcontractor default. Ultimately, the general contractor will be responsible to the owner for any subcontractor default, so the owner will want transparency as to the costs and rights bestowed by these products. The owner also will want clarity on who invokes these claims and when they are invoked. For example, are there other buckets of funds that can be used rather than Subguard or P&P bonds such as contingency or savings deduction? The owner should undertake an analysis of the costs and benefits of these products before agreeing to utilize them on a project.

General Contractor Perspective

The general contractor undoubtedly receives the primary direct benefit from Subguard or subcontractor P&P bonds by obtaining financial security to see the project to completion and remove the risk of project impacts due to subcontractor defaults. However, SDI can be expensive, so it is important that general contractors weigh the benefits of cost savings of a particular subcontractor against the risk of default. P&P bonds are a cost-effective alternative for the general contractor because the cost is paid by the subcontractor (and even if the subcontractor passes that cost on to the general contractor, it is less expensive than Subguard). The risk with P&P bonds is that they are not insurance policies, and sureties may make claims on the bonds if the subcontractor provides a defense to the claimed default or nonpayment.

Subcontractor Perspective

Subcontractors typically do not have a say in whether the general contractor procures SDI. Subcontractors generally do not want to provide P&P bonds and will try to eliminate any requirement to provide those bonds. For public projects, it is more likely that subcontractors will have to provide P&P bonds because general contractors are required to provide bonds as part of their contracting package and often will require the same from their subcontractors to manage risk and ensure project completion. For private projects, subcontractors should try to eliminate any requirement for P&P bonds. If there is a subcontractor default on the project and the subcontractor's surety must make payments under the P&P bonds, the surety usually will seek payment from the subcontractor, and often the subcontractor's principals and owners if they signed a guarantee, for those funds.

Contingency

At its broadest definition, contingency on a construction project is a sum of money set aside in the project budget to cover unforeseen costs or changes that might arise during the project. There are different types of contingencies and many ways that contingency can be utilized and incorporated. The two main types of contingencies are owner contingency and contractor contingency. Owner contingency is a reserve of funds controlled by the owner for unforeseen costs or changes. This allows the owner to control the funds. Contractor contingency is a sum set aside for the general contractor to use for unexpected expenses on the project, such as material price fluctuations, labor shortages, or errors in the work. This allows general contractors to mitigate risks. Depending on the agreement, there may be a “shared savings clause” that sets out how any remaining contingency funds will be allocated between owner and general contractor. Generally, having a well-defined contingency plan provides more financial security and flexibility to navigate the many uncertainties that arise in construction projects.

A contractual contingency clause, among other things, should (i) set a contingency budget (typically a percentage of the cost of the work), (ii) set out the procedure to assess the contingency funds, and (iii) define the purposes for which the contingency may be used. [45]

Contingencies are generally subject to significant negotiations between the owner and general contractor.

Owner Perspective

The owner should carefully consider how they want to utilize contingency funds on the project. Some key considerations are

- Whether to include contingency as part of the contract sum or make contingency additional to the contract sum.
- Whether the owner should address what the contingency funds may be applied towards in the contract. For example, if there is a change due to an unforeseen condition, is that a change to the prime contract resulting in an increase in the contract price or is that paid out of contingency funds? What are the parameters? Who decides?
- Whether to apply savings to unused contingency funds with a portion to be paid to the contractor (a shared savings clause). Providing for shared savings could incentivize the contractor not to use up the entire contingency funds budget.

General Contractor Perspective

General contractors will want to push for a contractor contingency so they have control over how the money is spent. From the general contractor perspective, a contingency clause will be only for the contractor's use, not the owner's, and identifies all the costs that may be paid from the fund, including (i) scope yet to be finally designed; (ii) missed scope or estimating errors; (iii) labor and material cost escalations; (iv) acceleration expenses; (v) costs incurred to correct defective, damaged, or nonconforming work; (vi) general conditions overruns; and (vii) costs associated with subcontractor defaults. [46]

Further, general contractors should ensure that contingency funds are not applied to work that would otherwise be a change order. This is particularly important where the general contractor receives any remaining contingency funds or a percentage of remaining contingency funds. The general contractor should try to negotiate control of the contingency with updates to the owner and parameters to ensure that contingency does not substitute for changed work. The general contractor will want to negotiate for more control and less opportunities for the owner to delay or say no to the use of contingency funds. The general contractor also will want to be sure it gets some percentage of unused contingency.

Subcontractor Perspective

Subcontractors do not have any say in contingencies adopted between the owner and general contractor, and contingencies are not typically added to subcontracts. If unforeseen conditions or other unanticipated work arises for the subcontractor, it should get a change order from the general contractor for that changed work. Subcontractors can benefit from contractor contingency funds when unexpected site conditions require additional labor or materials, and the general contractor is more willing to pay for these unexpected conditions when there is money set aside to do so. Additionally, subcontractors can have allowances for areas where the final price of certain selections is subject to change.

Damages

Addressing damages in the construction contract helps protect the interests of all parties and provides clarity in the event of a dispute. Construction projects typically involve substantial investments, tight timelines, and complex coordination, all of which may create delays that lead to substantial financial losses. By clearly defining the types of damages, such as consequential or liquidated, the contract sets expectations and helps avoid lengthy legal battles.

Consequential Damages

Consequential damages are contract damages that flow from a breach but are indirect losses resulting from the breach of the contract. Although it is now fairly common practice to include consequential damages waiver provisions in construction contracts, such provisions were uncommon before the 1992 Supreme Court of New Jersey's decision in Perini Corporation v. Greate Bay Hotel & Casino, Inc. [47] That case drew considerable attention because lost profits awarded to the casino were significantly disproportionate to the construction manager's fee. In Perini, an arbitrator awarded the Sands Hotel and Casino more than $14.5 million in damages for lost profits against its construction manager (whose management fee was $600,000) because the construction manager failed to complete an ornamental façade intended to attract people to the casino. The construction manager, among other arguments, argued that the award was unfair because the award was significantly greater than its fee. [48]

The court held that the construction manager was well aware of the high stakes involved in the casino-construction industry and nevertheless agreed to the contract's damages provision. [49] Perini highlights how what seems like a relatively minor element of the entire project could be the difference in millions of dollars in consequential damages.

Many standard form agreements call for a mutual waiver of consequential damages. For example, Section 15.1.7 of the A201-2017 provides a mutual waiver of consequential damages as between the owner and general contractor.

§ 15.1.7 Waiver of Claims for Consequential Damages

The Contractor and Owner waive Claims against each other for consequential damages arising out of or relating to this Contract. This mutual waiver includes

1. damages incurred by the Owner for rental expenses, for losses of use, income, profit, financing, business and reputation, and for loss of management or employee productivity or of the services of such persons;and

2. damages incurred by the Contractor for principal office expenses including the compensation of personnel stationed there, for losses of financing, business and reputation, and for loss of profit, except anticipated profit arising directly from the Work.

This mutual waiver is applicable, without limitation, to all consequential damages due to either party's termination in accordance with Article 14. Nothing contained in this Section 15.1.7 shall be deemed to preclude assessment of liquidated damages, when applicable, in accordance with the requirements of the Contract Documents.

Although it is common for contract forms to include a mutual waiver of consequential damages, owners should assess the use of consequential damages on a project-by-project basis.

Owner Perspective

Owners should consider the potential losses (i.e., tenant relocation costs, insurance coverages, lost rent, and revenue) and determine whether they should be accounted for in the contract. Additionally, owners should be cautious of waiving consequential damages that could arise out of a third-party indemnity claim. For example, if a third party makes a claim against the owner due to the contractor's work, the owner may not want a waiver of the consequential damages provision to prevent it from passing on to the contractor any consequential damages suffered by the third party.

General Contractor Perspective

Unlike owners, general contractors are less likely to suffer consequential damages but may have a higher risk of owing consequential damages to the owner. Accordingly, it is typically in the contractor's interest to insist on a mutual waiver for consequential damages. If an owner is unwilling to waive consequential damages, the general contractor may consider drafting a waiver with exclusions to limit its liability for consequential damages. This could include a grace period before the owner assesses delay or exclusions for certain delays, claims, or losses. For example, the contractor may consider including an exclusion to the consequential damages for third-party claims, such as claims that could be brought by the owner's tenants, who may be affected by delay.

Subcontractor Perspective

Like general contractors, subcontractors are unlikely to suffer consequential damages. Subcontractors should review the subcontract to determine whether there is a waiver of consequential damages provision. It is common for subcontracts to include a unilateral waiver of consequential damages where the subcontractor waives its right to recover consequential damages from the contractor but remains liable for the consequential damages of the general contractor and owner. Subcontractors should consider including a mutual waiver of consequential damages provision between the subcontractor and general contractor, with the exception that it will be liable for its proportional share of consequential damages assessed by the owner and paid by the general contractor due to the subcontractor's fault.

Warranty and Corrective Work

In recent years, there has been significant interest in the relationship between warranty provisions and latent defects. The term "latent defects" refers to defects that are not discoverable through reasonably prudent inspection. [50] A latent defect discovered after the expiration of an express warranty period could reinstate the warranty if the warranty provision is not clear that the parties do not intend for the warranty to apply to defects discovered after the expiration of the warranty period. Generally, a defect claim accrues when defective work is completed, even if the defect is not immediately discovered. [51] However, the "discovery rule" can toll the accrual of a defect claim until the defect is discovered or reasonably should have been discovered, potentially extending a warranty period and the statute of limitations, or, more significantly, the applicable statute of repose. [52] If a defect is inherently undiscoverable and the evidence of injury is objectively verifiable, exposure to claims can be extended significantly, and the uncertainty of risk is broadened. [53]

Owner Perspective

The AIA A201-2017 addresses warranty under Section 3.5 generally but does not specify the duration of the warranty, or the owner's right to correct defective work if the contractor fails to do so. The owner should consider including a provision that requires the contractor to cure (or commence and diligently continue curing) within a certain time. The owner also should consider language that allows it to resolve the warranty item or corrective work at the cost of the contractor if it fails to comply with the warranty and/or corrective work obligations. Lastly, the owner should consider including the right to back charge, withhold payment, and offset payment.

General Contractor Perspective

General contractors should fully understand the warranty provision. General contractors should be wary of broad warranty requirements, including, without limitation, warranty provisions that do not define the warranty duration, require the general contractor to do warranty work that it did not provide, and warranty continued operations. Additionally, general contractors should require a reasonable notice and opportunity to cure period prior to being responsible for damages. The warranty provision also should address what the general contractor must do to cure the defect, such as replacing or repairing the work with the same or like materials. Allowing replacement with like materials can provide the general contractor with needed flexibility when a particular material or piece of equipment becomes unavailable due to limited supply or trade restrictions.

Subcontractor Perspective

Subcontractors should review the prime contract in conjunction with the warranty obligations under the subcontract to determine whether the obligations under the subcontract exceed the requirements under the prime contract. Like the general contractor, the subcontractor should include language in the subcontract that allows it to correct the work before the contractor or owner can take over the correction of the work or back charge the costs of correction.

Schedule

A well-structured construction schedule is a critical component of a successful construction project. The project schedule outlines the sequence of tasks and sets timelines, helping ensure the timely completion of the project. Without a well-maintained schedule, projects are more likely to experience delays, budget overruns, and miscommunications, which can compromise timely completion of the work and lead to significant damages.

Changes to the Schedule

The construction schedule outlines how the contractor is completing the project on time and within the owner's budget. The project schedule measures the contractor's progress during construction and identifies delays. Construction schedules are not standardized and can vary in format, content, and purpose. [54] Section 3.10.1 of the AIA A201-2017 addresses the project schedule generally.

> **§ 3.10.1** The Contractor, promptly after being awarded the Contract, shall submit for the Owner's and Architect's information a Contractor's construction schedule for the Work. The schedule shall contain detail appropriate for the Project, including (1) the date of commencement of the Work, interim schedule milestone dates, and the date of Substantial Completion; (2) an apportionment of the Work by construction activity; and (3) the time required for completion of each portion of the Work. The schedule shall provide for the orderly progression of the Work to completion and shall not exceed time limits current under the Contract Documents. The schedule shall be revised at appropriate intervals as required by the conditions of the Work and Project.

Unfortunately, the most common construction contract forms provide little guidance to the parties other than to state that the contractor is required to prepare and update a schedule. [55]

Owner Perspective

Delays to the construction schedule will inevitably occur, and since owners are generally less involved in the day-to-day construction activities, they rely on the contractor to keep them up to date with the project status. The contract should define which schedules must be provided and how often they must be provided, and the contract should outline what the contractor must do when it becomes aware of a delay, e.g., provide written notice when a delay has or is likely to occur. In addition to addressing requirements specific to the schedule itself, owners may want to address how changes to the schedule affect the contract sum. Owners also should consider whether to factor potential delay events into the schedule, namely, weather delays.

Contractor Perspective

Contractors typically will want to be in control of the schedule and to have the ability to modify it. The owner's exertion of control over the schedule may hinder the contractor's ability to timely complete the project or mitigate delay. When negotiating the contract, contractors should be wary of providing the owner with too much control over the schedule and how much backup information it must provide to the owner to support changes to the schedule. In addition to considering the owner–contractor relationship, general contractors must address the schedule in the subcontract. Subcontractors often want control over their work but may fail to understand how their schedule factors into the schedule for the entire project. Accordingly, general contractors should be in control of the schedule for the subcontract work, and the subcontract should include provisions that allow the general contractor adequate flexibility appropriate for the project and anticipated challenges.

Subcontractor Perspective

Subcontractors should review the prime contract to understand the schedule requirements' flow-down effects. Additionally, subcontractors should weigh the amount of control the general contractor has over the subcontractor's schedule and should consider including provisions in the subcontract that would limit the general contractor's ability to make changes to the schedule and that would allow the subcontractor to receive an increase in the subcontract sum as a result of the general contractor's changes.

Delay Damages

Delays to a construction project's completion date occur frequently across projects. When they occur, delays lead to claims for time-related damages. These claims are usually highly contentious and result in significant legal costs for the parties involved. Assessing delay claims requires categorizing each delay event as either nonexcusable or excusable and determining which events are compensable. [56] To categorize delays into the foregoing categories, the party seeking delay damages must demonstrate that the delay was compensable.

Owner Perspective

Aside from the liquidated damages provision in AIA contract forms, the forms do not address specific details regarding the types of delays that are compensable to the owner. Accordingly, the owner should clearly outline when it is entitled to delay damages in the contract. The owner also should be clear as to what damages it will seek (e.g., liquidated damages or actual damages, but not both). Generally, a liquidated damages clause is the owner's exclusive remedy for delay. [57] In addition to addressing when it is entitled to delay damages, the owner should address when the contract is (or is not) entitled to delay damages. While Section 8.3 of the A201-2017 describes events that entitle the contractor to an extension of time, and Section 15.1 of the A201-2017 addresses the contractor's obligation to provide notice, the owner should consider including language in the contract that specifically outlines when the contractor must provide notice and what information must be included in the notice.

General Contractor Perspective

Although contractors should keep in mind that documentation is often the key to recovery, general contractors may want to limit their obligation to provide notices of claims to the owner. The general contractor also should ensure that the contract describes the types of damage for which it may be liable. While delay damages are often looked down on by general contractors, they may be preferable to actual damages because they are predictable, and contractors can manage around them. Additionally, the general contractor should include language in the contract addressing when it is entitled to delay damages. Ideally, general contractors will want additional money and time on all delays not caused by it or those for whom it is responsible. Alternatively, the general contractor would want to seek additional money and time for delays caused by the owner, as well as for all other delays not caused by it or those for whom it is responsible.

In addition to addressing the owner-contractor relationship, the general contractor has to consider the delay damages in its subcontracts. Typically, general contractors will only want to provide relief to the subcontractor when it is allowed relief under the prime contract. Accordingly, the general contractor should be cautious of permitting the subcontractor to recover for anything that is not recoverable by the general contractor under the prime contract.

Subcontractor Perspective

Subcontractors should understand their liability for delay damages under the prime contract and the subcontract. Understanding that general contractors typically limit the subcontractor's right to recovery to the extent the general contractor receives recovery under the prime contract, the subcontractor should consider addressing the scenario in which it has suffered delay damages due to the general contractor's fault and the general contractor is not entitled to relief under the prime contract. The subcontractor should consider including a provision in the subcontract that entitles it to additional compensation and an extension of time if the contractor is at fault, regardless of whether the contractor receives compensation or an extension of time from the owner. Essentially, the subcontractor should ensure that it is not absorbing the effects of the contractor's fault.

Force Majeure

Force majeure events are generally considered exceptionally rare occurrences, and force majeure provisions have historically been a lower-priority negotiation item. However, in recent years, force majeure provisions have become a hot topic during contract negotiation. The opinion of what constitutes a force majeure event now varies significantly. Following the COVID-19 pandemic, we have seen more creative force majeure provisions.

Owner Perspective

When an owner is providing the contract form, the owner should decide whether to define what constitutes a force majeure event, what is not a force majeure event, or whether to avoid addressing the topic at all. While addressing what is or is not a force majeure event from the onset of negotiation may resolve the possibility of ambiguities, it also opens the door for the contractor to provide heavy-handed provisions. On the other hand, omitting a force majeure event from your contract form may create ambiguities later on. Assuming the contract includes a force majeure provision, the owner should consider offering an extension of time only. If costs are on the table, the owner could consider avoiding provisions that grant the contractor profit from the force majeure event. Owners also should consider including contract provisions that require the contractor to mitigate the effect of the force majeure event.

General Contractor Perspective

Whether escalation, pandemics, tariffs, or labor shortages, contractors typically do not price to take on the risk of unknowns. Contractors should clarify upon what assumptions the contract sum is based and what types of scenarios might lead to entitlement for change orders. Typically, the contractor is able to pass material risk onto the owner and labor risk onto the subcontractors.

Subcontractor Perspective

Subcontractors should consider the effects of the force majeure provision in the prime contract and whether there is a force majeure provision in the subcontract.

Float

Float is the amount of time an activity can be delayed without affecting the project's completion date. [58] When float exists, an excusable delay will first erode the float before resulting in a critical-path impact to the project, and courts will erode float before awarding delay damages. However, most standard contract forms, like the AIA, do not define float in the contract. If the contract is silent on float, the party who uses the float first gets the benefit of the floa.t. [59]

Owner Perspective

Owners should consider defining float in the contract and when and how it can be used. For example, float could be defined as "the difference between the time available to accomplish an activity and the estimated time required and as determined by the most recently updated schedule." If the contract fails to specify who owns the float or to prohibit the contractor from finishing the work early, the contractor is free to use the float. Owners should consider requiring the contractor to provide details regarding the project schedule and how the float is used.

General Contractor Perspective

While the owner may not hinder, obstruct, or delay the contractor's use of float, if float is not defined, conversely, the contractor would not be able to stop the owner from using float. Accordingly, it is beneficial for the general contractor to negotiate float in the contract. General contractors should understand how float is to be used in connection with the critical path and delays.

Subcontractor Perspective

Subcontractors are unlikely to have any ownership of float. However, it is important for subcontractors to understand how the use of float could impact their schedule and right to extensions of time in the event of a delay.

Endnotes

1. Am. Inst. of Architects, AIA Document A201-2007, § 3.2.2.

2. United States v. Spearin, 248 U.S. 132, 133 (1918).

3. S.B. 219, 87th Leg. (Tex. 2021).

4. El Paso Field Servs., L.P. v. MasTec N. Am., Inc., 389 S.W.3d 802 (Tex. 2012).

5. Tex. Bus. & Com. Code Ann. § 17.505 (West).

6. BAE Sys. Ordnance Sys., Inc. v. Fluor Fed. Sols., LLC, No. 7:20-CV-587, 2022 WL 969773, at *1 (W.D. Va. Mar. 30, 2022), *opinion vacated in part on reconsideration*, 2022 WL 21810167 (W.D. Va. Dec. 9, 2022).

7. Souza & McCue Constr. Co. v. Super. Ct. of San Benito Cnty., 370 P.2d 338, 339 (Cal. 1962).

8. Dugan & Meyers Constr. Co., Inc. v. Ohio Dep't of Admin. Servs., 864 N.E.2d 68, 74 (Ohio 2007).

9. *See* AIA Document A201-2017, § 3.12.10.1; Crabtree Atkins, Gorham & Nudelman, *Delegated Design: When a Contractor Is More Than Just a Contractor*, ABA F. on Constr. L., 2025 Annual Meeting, Plenary 3.

10. *Dugan & Meyers*, 864 N.E.2d 68; Fla. Bd. of Regents v. Mycon Corp., 651 So. 2d 149 (Fla. 1st Dist. Ct. App. 1995); Tex. Bus. & Com. Code § 17.505.

11. *Souza & McCue*, 370 P.2d 338; W.H. Lyman Constr. Co. v. Vill. of Gurnee, 475 N.E.2d 273 (Ill. App. 1985).

12. *Dugan & Meyers*, 864 N.E.2d at 74.

13. A.G. Cullen Constr., Inc. v. State Sys. of Higher Educ., 898 A.2d 1145 (Pa. Commw. Ct. 2006).

14. J.L. Simmons Co. v. United States, 304 F.2d 886 (Ct. Cl. 1962).

15. *A.G. Cullen Constr.*, 898 A.2d 1145.

16. Penzel Constr. Co., Inc. v. Jackson R-2 Sch. Dist., 544 S.W.3d 214 (Mo. Ct. App. 2017).

17. George A. Fuller Co. v. United States, 69 F. Supp. 768 (Ct. Cl. 1946).

18. While *Fuller* does not cite *Spearin*, its wage adjustment mechanism mirrors *Spearin*'s logic (owner adjusts for its changes), but the disclaimer flips it.

19. King Cnty. v. Walsh Constr. Co. II, LLC, 532 P.3d 182, 186 (Wash. Ct. App. 2023), *review denied*, 537 P.3d 1037 (Wash. 2023).

20. *George A. Fuller Co.*, 69 F. Supp. at 769.

21. *See* Dugan & Meyers Constr. Co., Inc. v. Ohio Dep't of Admin. Servs., 864 N.E.2d 68, 69 (Ohio 2007).

22. First United Methodist Church of Ozark v. Harness Roofing, Inc., 474 S.W.3d 892, 897 (Ark. Ct. App. 2015) (holding that contractors are held to both the standard of care of the contracting industry as well as to the standard of care of a reasonably prudent person, and that the more exacting standard will control).

23. *See* ISO Form CG 22 43, Exclusion—Contractual Liability (2019); Travelers Indem. Co. v. Miller Bldg. Corp., 142 F. App'x 147 (4th Cir. 2005).

24. AIA Document A201-2017, § 1.2.1.

25. *Id.* §§ 3.7.2, 10.2.2.

26. *Id.* § 3.5.1

27. *Id.*

28. *Id.*

29. *See* Gary Berman & Stephen A. Hess, "Scope of Work, Standards of Care and Changes: Five Problem Areas and How to Work Around Them," ABA F. on the Constr. Indus. Fall Meeting 31 (2006).

30. *See* Travelers Indem. Co. v. Miller Bldg. Corp., 142 F. App'x 147, 150 (4th Cir. 2005) (subcontractor's defective fill wasn't an "occurrence"); *see also* ISO Form CG 00 09 (2019).

31. AIA Document A201-2017, § 3.7.4.

32. FAR 52.233-1.

33. AIA Document A201-2017, § 15.1.4.1.

34. Tex. Prop. Code Ann. § 28.0091 (Unsigned Change Order).

35. *Id.*

36. *See, e.g.*, Brinderson Corp. v. Hampton Rds. Sanitation Dist., 825 F.2d 41, 44 (4th Cir. 1987); Nippo Corp./Int'l Bridge Corp. v. Amec Earth & Env't, Inc., 2011 U.S. Dist. LEXIS 108273, at *27 (E. Pa. Sept. 21, 2011).

37. *See, e.g.*, Razorback Contractors of Kan., Inc. v. Bd. of Cnty. Comm'rs, 43 Kan. App. 2d 527, 536 (2010); Perini Corp. v. City of New York, 18 F. Supp. 2d 287 (S.D.N.Y. 1998); Cecio Brothers, Inc. v. Greenwich, 156 Conn. 561 (1968); Starks Mech., Inc. v. New Albany-Floyd, 854 N.E.2d 936 (Ind. App. 2006); Mike M. Johnson, Inc. v. Spokane Cnty., 150 Wash. 2d 375 (2003); Rissler & McMurry v. Sheridan Area Water, 929 P.2d 1228 (Wyo. 1996); Ida Grove Roofing v. City of Storm Lake, 378 N.W.2d 313 (Iowa App. 1985); Foster Wheeler Enviresponse v. Franklin Cnty. Convention Facilities Auth., 78 Ohio St. 3d 353 (1997).

38. Fed. Bureau of Investigation, Internet Crime Report 2023, https://www.ic3.gov/annualreport/reports/2023_ic3report.pdf.

39. *[Archived] Progress in Recovering Losses from 2019 Fraud Scheme*, Town of Erie (Aug. 23, 2023), https://www.erieco.gov/CivicAlerts.aspx?AID=2932&ARC=4614.

40. *Id.*

41. U.C.C. § 4A-202(b) (Am. L. Inst. & Unif. L. Comm'n 1977).

42. *See, e.g.*, Am. Tooling Ctr., Inc. v. Travelers Cas. & Sur. Co. of Am., No. 17-2014, 895 F.3d 455 (6th Cir. 2018) (holding that a claim for amounts paid to a BEC scammer were covered under Computer Fraud coverage and not barred by any exclusion).

43. 2 Hail, Inc. v. Beaver Builders, LLC, 2017 Colo. Dist. LEXIS 1294 (Nov. 29, 2017).

44. *Id.*

45. Sklyer Santomartino, *The Contractor's Contingency: What Contractors and Construction Managers Need to Know and Be Wary of*, ConsensusDocs (Nov. 3, 2023), https://www.consensusdocs.org/news/the-contractors-contingency-what-contractors-and-construction-managers-need-to-know-and-be-wary-of/.

46. *Id.*

47. 129 N.J. 479 (1992).

48. *Id.*

49. *Id.*

50. Gupta v. Ritter Homes, Inc., 646 S.W.2d 168 (Tex. 1983).

51. Murphy v. Campbell, 964 S.W.2d 265, 270 (Tex. 1997).

52. HECI Expl. Co. v. Neel, 982 S.W.2d 881, 886 (Tex. 1998).

53. Cosgrove v. Cade, 468 S.W.3d 32, 36 (Tex. 2015); Via Net v. TIG Ins. Co., 211 S.W.3d 310, 315 (Tex. 2006).

54. *See* Steven S. Pinnell, *Construction Scheduling Disputes: Proving Entitlement*, 12 Constr. Law., Jan. 1992, at 18, 19.

55. *See* AIA Document A201-2017, § 3.10 (General Conditions).

56. W. Stephen Dale & Robert M. D'Onofrio, Construction Schedule Delays §§ 1:2–1:4 (2023).

57. 15 Philip L. Bruner & Patrick J. O'Conner Jr., Bruner & O'Conner on Construction Law § 15:82 (2009). *See also* George C. Baldwin, *The A, B, C's of Liquidated Damages* at 7, Constr. L. Conf. (1999) ("An owner will not be able to collect both liquidated damages and other delay damages, if the [liquidated damages] clause covers delay. Neither will the owner be permitted to choose whether to pursue actual or liquidated damages once the breach has occurred. Its election occurs when the clause is placed in the contract.").

58. Dale & D'Onofrio, *supra* note 56, § 2:10.

59. Williams Enter., Inc. v. Strait Mfg. & Welding, Inc., 728 F. Supp. 12 (D.D.C. 1990), *aff'd in part, remanded in part on other grounds*, 938 F.2d 230 (D.C. Cir. 1991).

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