Equipment and Material Procurement in a Post-Pandemic Era

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37th Annual

State Bar of Texas Construction Law Conference

March 7-8, 2024

Part I: The Procurement Problem Defined

The post-COVID-19 Pandemic era has magnified the challenges faced by general contractors when procuring equipment and materials. Now more than ever, general contractors fall victim to late deliveries, delinquent payments, price fluctuations, warranty issues, and heightened risks of loss and liability. These problems can stem from various sources of legal rights and obligations—such as construction contracts, purchase orders, the Uniform Commercial Code ("UCC"), and bargaining power disparities. This paper explores these sources and challenges they pose, including by touching on how they can manifest in contractual disputes and by providing potential solutions available to general contractors.

Take the following example. A project owner and general contractor execute a construction contract, containing a liquidated damages clause, for the construction of an airport terminal. Under the contract's terms, the general contractor must procure security scanning and X-ray equipment, which must be of a specific brand. The general contractor soon finds that the manufacturer of the specified brand refuses to guarantee a delivery date, providing only an estimate. In other words, if the general contractor wants that specific brand, it must be willing to risk waiting. The general contractor may have no choice but to agree to the manufacturer's terms.

Fast forward a few months. Because of supply chain issues, the manufacturer cannot deliver the equipment on time. The general contractor, therefore, cannot complete the project on time. The owner and traveling public cannot use the project for its intended purpose—doing so wouldn't be safe—so a project delay ensues. Now, the general contractor owes liquidated damages to the owner while potentially having no recourse against the manufacturer.

This is one of many scenarios that can easily arise in our post-pandemic era. All too often general contractors become stuck in the middle between project owners and manufacturers/suppliers. On the one hand, the general contractor is subject to a contract with the project owner governed by common law. On the other hand, the general contractor is subject to a contract with the manufacturer/supplier governed by Article 2 of the UCC. Tension naturally exists between the two, as this paper will show.

The next section of this paper identifies parts of the UCC that are sources of problems for general contractors. Manufacturers and suppliers have become adept at using and modifying UCC provisions to the disadvantage of the general contractor.

Part II: Article 2 of the UCC as a Source of the Problem

The UCC, codified in Chapter 2 of Texas's Business and Commerce Code, governs the sales and purchases of goods in Texas. It is "liberally construed and applied to promote its underlying purposes and policies."[1] Those purposes and policies are "(1) to simplify, clarify and modernize the law governing commercial transactions; (2) to permit the continued expansion of commercial practices through

[1] Tex. Bus. & Com. § Code 1.103(a).

custom, usage and agreement of the parties; and (3) to make uniform law among the various jurisdictions."[2]

To that end, unless a specific provision of the UCC provides otherwise, the UCC "preempts principles of common law and equity that are inconsistent with either its provisions or its purposes and policies."[3] Common law principles are merely a complement to the UCC.[4]

To serve as a refresher on key UCC principles, relevant provisions are included below. These provisions are referenced throughout the paper and serve as useful context when examining the sample contractual language presented in Part III. In theory, the UCC's provisions are reasonable and beneficial to both parties in a transaction. Unfortunately, however, manufacturers and sellers are often able to modify the provisions listed below due to their bargaining power. Thus, general contractors should be familiar with what these provisions say so they can identify when manufacturers and sellers disclaim, replace, or modify the provisions.

An appropriate starting place for general contractors is to understand what constitutes acceptance and satisfactory performance under the UCC. Relevant UCC provisions include:

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[2] *Id.*

[3] Tex. Bus. & Com. Code § 1.103 cmt. 2.

[4] *Contractors Source, Inc. v. Amegy Bank Nat'l Ass'n*, 462 S.W.3d 128, 138 (Tex. App—Houston [1st Dist.] 2015, no pet.).

Tex. Bus. & Com. Code § 2.601. ***Buyer's Rights on Improper Delivery*** **(otherwise known as the "Perfect Tender" rule).**

Subject to the provisions of this chapter on breach in installment contracts (Section 2.612) and unless otherwise agreed under the sections on contractual limitations of remedy (Sections 7.18 and 2.719), if the goods or tender of delivery fail in any respect to the conform to the contract, the buyer may:

(1) reject the whole; or

(2) accept the whole; or

(3) accept any commercial unit or units and reject the rest.

Tex. Bus. & Com. Code § 2.602. ***Manner and Effect of Rightful Rejection.***

(a) Rejection of goods must be within a reasonable time after their delivery or tender. It is ineffective unless the buyer seasonably notifies the seller.

(b) Subject to the provisions of the two following sections on rejected goods (Sections 2.603 and 2.604),

(1) after rejection any exercise of ownership by the buyer with respect to any commercial unit is wrongful as against the seller; and

(2) if the buyer has before rejection taken physical possession of goods in which he does not have a security interest under the provisions of this chapter (Subsection (c) of Section 2.711), he is under a duty after rejection to hold them with reasonable care at the seller's disposition for a time sufficient to permit the seller to remove them; but

(3) the buyer has no further obligations with regards to goods rightfully rejected.

(c) the seller's rights with respect to goods wrongfully rejected are governed by the provisions of this chapter on Seller's remedies in general (Section 2.703).

Tex. Bus. & Com. Code § 2.606. ***What Constitutes Acceptance of Goods.***

(a) Acceptance of goods occurs when the buyer

(1) after a reasonable opportunity to inspect the goods signifies to the seller that the goods are conforming or that he will take or retain them in spite of their non-conformity; or

(2) fails to make an effective rejection (Subsection (a) of Section 2.602), but such acceptance does not occur until the buyer has had a reasonable opportunity to inspect them; or

(3) does any act inconsistent with the seller's ownership; but if such act is wrongful as against the seller it is an acceptance only if ratified by him.

(b) Acceptance of a part of any commercial unit is acceptance of that entire unit.

Tex. Bus. & Com. Code § 2.607. ***Effect of Acceptance; Notice of Breach; Burden of Establishing Breach After Acceptance; Notice of Claim or Litigation to Person Answerable Over.***

(a) The buyer must pay at the contract rate for any goods accepted.

(b) Acceptance of goods by the buyer precludes rejection of the goods accepted and if made with knowledge of a non-conformity cannot be revoked because of it unless the acceptance was on the reasonable assumption that the non-conformity would be seasonably cured but acceptance does not of itself impair any other remedy provided by this chapter for non-conformity.

(c) Where a tender has been accepted

(1) the buyer must within a reasonable time after he discovers or should have discovered any breach notify the seller of breach or be barred from any remedy; and

(2) if the claim is one for infringement or the like (Subsection (c) of Section 2.312) and the buyer is sued as a result of such a breach he must so notify the seller within a reasonable time after he receives notice of the litigation or be barred from any remedy over for liability established by the litigation.

(d) The burden is on the buyer to establish any breach with respect to the goods accepted.

(e) Where the buyer is sued for breach of a warranty or other obligation for which his seller is answerable over

(1) he may give his seller written notice of the litigation. If the notice states that the seller may come in and defend and that if the seller does not do so he will be bound in any action against him by his buyer by any determination of fact common to the two litigations, then unless the seller after seasonable receipt of the notice does come in and defend he is so bound.

(2) if the claim is one for infringement or the like (Subsection (c) of Section 2.312) the original seller may demand in writing that his buyer turn over to him control of the litigation including settlement or else be barred from any remedy over and if he also agrees to bear all expense and to satisfy any adverse judgment, then unless the buyer after seasonable receipt of the demand does turn over control the buyer is so barred.

(f) The provisions of Subsections (c), (d) and (e) apply to any obligation of a buyer to hold the seller harmless against infringement or the like (Subsection (c) of Section 2.312).

Turning now to the UCC's warranty provisions, these provisions at times can also present problems for general contractors. While beneficial in theory, these warranty provisions often become toothless after being modified or disclaimed by manufacturers and suppliers:

Tex. Bus. & Com. Code § 2.312. *Warranty of Title Against Infringement; Buyer's Obligation Against Infringement.*

(a) Subject to Subsection (b) there is in a contract for sale a warranty by the seller that

(1) the title conveyed shall be good, and its transfer rightful; and

(2) the goods shall be delivered free from any security interest or other lien or encumbrance of which the buyer at the time of contracting has no knowledge.

(b) A warranty under Subsection (a) will be excluded or modified only by specific language or by circumstances which give the buyer reason to know that the person selling does not claim title in himself or that he is purporting to sell only such right or title as he or a third person may have.

(c) Unless otherwise agreed a seller who is a merchant regularly dealing in goods of the kind warrants that the goods shall be delivered free of the rightful claim of any third person by way of infringement or the like but a buyer who furnishes specifications to the seller must hold the seller harmless against any such claim which arises out of compliance with the specifications.

Tex. Bus. & Com. Code § 2.313. *Express Warranties by Affirmation, Promise, Description, Sample.*

(a) Express warranties by the seller are created as follows:

(1) Any affirmation of fact or promise made by the seller to the buyer which relates to the goods and becomes part of the basis of the bargain creates an express warranty that the goods shall conform to the affirmation or promise.

(2) Any description of the goods which is made part of the basis of the bargain creates an express warranty that the goods shall conform to the description.

(3) Any sample or model which is made part of the basis of the bargain creates an express warranty that the whole of the goods shall conform to the sample or model.

(b) It is not necessary to the creation of an express warranty that the seller use formal words such as "warrant" or "guarantee" or that he have a specific intention to make a warranty, but an affirmation merely of the value of the goods or a statement purporting to be merely the seller's opinion or commendation of the goods does not create a warranty.

Tex. Bus. & Com. Code § 2.314. *Implied Warranty: Merchantability; Usage of Trade.*

(a) Unless excluded or modified (Section 2.316), a warranty that the goods shall be merchantable is implied in a contract for their sale if the seller is a merchant with respect to goods of that kind. Under this section the serving for value of food or drink to be consumed either on the premises or elsewhere is a sale.

(b) Goods to be merchantable must be at least such as

(1) pass without objection in the trade under the contract description; and

(2) in the case of fungible goods, are of fair average quality within the description; and

(3) are fit for the ordinary purposes for which such goods are used; and

(4) run, within the variations permitted by the agreement, of even kind, quality and quantity within each unit and among all units involved; and

(5) are adequately contained, packaged, and labeled as the agreement may require; and

(6) conform to the promises or affirmations of fact made on the container or label if any.

(c) Unless excluded or modified (Section 2.316) other implied warranties may arise from course of dealing or usage of trade.

Tex. Bus. & Com. Code § 2.315. *Implied Warranty: Fitness for Particular Purpose.*

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

Tex. Bus. & Com. Code § 2.316. *Exclusion or Modification of Warranties.*

(a) Words or conduct relevant to the creation of an express warranty and words or conduct tending to negate or limit warranty shall be construed wherever reasonable as consistent with each other; but subject to the provisions of this chapter on parol or extrinsic evidence (Section 2.202) negation or limitation is inoperative to the extent that such construction is unreasonable.

(b) Subject to Subsection (c), to exclude or modify the implied warranty of merchantability or any part of it the language must mention merchantability and in case of a writing must be conspicuous, and to exclude or modify any implied warranty of fitness the exclusion must be by a writing and conspicuous. Language to exclude all implied warranties of fitness is sufficient if it states, for example, that "There are no warranties which extend beyond the description on the face hereof."

(c) Notwithstanding Subsection (b)

(1) unless the circumstances indicate otherwise, all implied warranties are excluded by expressions like "as is", "with all faults" or other language which in common understanding calls the buyer's attention to the exclusion of warranties and makes plain that there is no implied warranty; and

(2) when the buyer before entering into the contract has examined the goods or the sample or model as fully as he desired or has refused to examine the goods there is no implied warranty with regard to defects which an examination ought in the circumstances to have revealed to him; and

(3) an implied warranty can also be excluded or modified by course of dealing or course of performance or usage of trade.

(d) Remedies for breach of warranty can be limited in accordance with the provisions of this chapter on liquidation or limitation of damages and on contractual modification of remedy (Sections 2.718 and 2.719).

(e) The implied warranties of merchantability and fitness shall not be applicable to the furnishing of human blood, blood plasma, or other human tissue or organs from a blood bank or reservoir of such other tissues or organs. Such blood, blood plasma or tissue or organs shall not for the purpose of this Title be considered commodities subject to sale or barter, but shall be considered as medical services.

(f) The implied warranties of merchantability and fitness do not apply to the sale or barter of livestock or its unborn young.

Tex. Bus. & Com. Code § 2.317. *Cumulation and Conflict of Warranties Express or Implied.*

Warranties whether express or implied shall be construed as consistent with each other and as cumulative, but if such construction is unreasonable the intention of the parties shall determine which warranty is dominant. In ascertaining that intention the following rules apply:

(1) Exact or technical specifications displace an inconsistent sample or model or general language of description.

(2) A sample from an existing bulk displaces inconsistent general language of description.

(3) Express warranties displace inconsistent implied warranties other than an implied warranty of fitness for a particular purpose.

Moving on from warranty provisions, the UCC also contains provisions on the risk of loss. Manufacturers and suppliers are often keen to modify the following provisions:

Tex. Bus. & Com. Code § 2.509. Risk of Loss in the Absence of Breach.

(a) Where the contract requires or authorizes the seller to ship the goods by carrier

(1) if it does not require him to deliver them at a particular destination, the risk of loss passes to the buyer when the goods are duly delivered to the carrier even though the shipment is under reservation (Section 2.505); but

(2) if it does require him to deliver them at a particular destination and the goods are there duly tendered while in the possession of the carrier, the risk of loss passes to the buyer when the goods are there duly so tendered as to enable the buyer to take delivery.

(b) Where the goods are held by a bailee to be delivered without being moved, the risk of loss passes to the buyer

(1) on the buyer's receipt of possession or control of a negotiable document of title covering the goods; or

(2) on acknowledgment by the bailee of the buyer's right to possession of the goods; or

(3) after the buyer's receipt of possession or control of a non-negotiable document of title or other written direction to deliver, as provided in Subsection (d)(2) of Section 2.503.

(c) In any case not within Subsection (a) or (b), the risk of loss passes to the buyer on his receipt of the goods if the seller is a merchant; otherwise the risk passes to the buyer on tender of delivery.

(d) The provisions of this section are subject to contrary agreement of the parties and to the provisions of this chapter on sale on approval (Section 2.327) and on effect of breach on risk of loss (Section 2.510).

Tex. Bus. & Com. Code § 2.510. *Effect of Breach on Risk of Loss.*

(a) Where a tender or delivery of goods so fails to conform to the contract as to give a right of rejection the risk of their loss remains on the seller until cure or acceptance.

(b) Where the buyer rightfully revokes acceptance he may to the extent of any deficiency in his effective insurance coverage treat the risk of loss as having rested on the seller from the beginning.

(c) Where the buyer as to conforming goods already identified to the contract for sale repudiates or is otherwise in breach before risk of their loss has passed to him, the seller may to the extent of any deficiency in his effective insurance coverage treat the risk of loss as resting on the buyer for a commercially reasonable time.

Turning now to the issue of shipping terms, manufacturers and sellers will also use their material supply agreements and purchase order forms to impose favorable shipping conditions that may be to the detriment of a general contractor. The UCC includes the following provisions on shipping:

Tex. Bus. & Com. Code § 2.319. *F.O.B. and F.A.S. Terms.*

(a) Unless otherwise agreed the term F.O.B. (which means "free on board") at a named place, even though used only in connection with the stated price, is a delivery term under which

(1) when the term is F.O.B. the place of shipment, the seller must at that place ship the goods in the manner provided in this chapter (Section 2.504) and bear the expense and risk of putting them into the possession of the carrier; or

(2) when the term is F.O.B. the place of destination, the seller must at his own expense and risk transport the goods to that place and there tender delivery of them in the manner provided in this chapter (Section 2.503);

(3) when under either Subdivision (1) or (2) the term is also F.O.B. vessel, car or other vehicle, the seller must in addition at his own expense and risk load the goods on board. If the term is F.O.B. vessel the buyer must name the vessel and in an appropriate case the seller must comply with the provisions of this chapter on the form of bill of lading (Section 2.323).

(b) Unless otherwise agreed the term F.A.S. vessel (which means "free alongside") at a named port, even though used only in connection with the stated price, is a delivery term under which the seller must

(1) at his own expense and risk deliver the goods alongside the vessel in the manner usual in that port or on a dock designated and provided by the buyer; and

(2) obtain and tender a receipt for the goods in exchange for which the carrier is under a duty to issue a bill of lading.

(c) Unless otherwise agreed in any case falling within Subsection (a)(1) or (3) or Subsection (b) the buyer must seasonably give any needed instructions for making delivery, including when the term is F.A.S. or F.O.B. the loading berth of the vessel and in an appropriate case its name and sailing date. The seller may treat the failure of needed instructions as a failure of cooperation under this chapter (Section 2.311). He may also at his option move the goods in any reasonable manner preparatory to delivery or shipment.

(d) Under the term F.O.B. vessel or F.A.S. unless otherwise agreed the buyer must make payment against tender of the required documents and the seller may not tender nor the buyer demand delivery of the goods in substitution for the documents.

Tex. Bus. & Com. Code § 2.308. *Absence of Specified Place for Delivery.*

Unless otherwise agreed

(1) the place for delivery of goods is the seller's place of business or if he has none his residence; but

(2) in a contract for sale of identified goods which to the knowledge of the parties at the time of contracting are in some other place, that place is the place for their delivery; and

(3) documents of title may be delivered through customary banking channels.

Tex. Bus. & Com. Code § 2.309. *Absence of Specific Time Provisions; Notice of Termination.*

(a) The time for shipment or delivery or any other action under a contract if not provided in this chapter or agreed upon shall be a reasonable time.

(b) Where the contract provides for successive performances but is indefinite in duration it is valid for a reasonable time but unless otherwise agreed may be terminated at any time by either party.

(c) Termination of a contract by one party except on the happening of an agreed event requires that reasonable notification be received by the other party and an agreement dispensing with notification is invalid if its operation would be unconscionable.

Tex. Bus. & Com. Code § 2.504. *Shipment by Seller.*

Where the seller is required or authorized to send the goods to the buyer and the contract does not require him to deliver them at a particular destination, then unless otherwise agreed he must

(1) put the goods in the possession of such a carrier and make such a contract for their transportation as may be reasonable having regard to the nature of the goods and other circumstances of the case; and

(2) obtain and promptly deliver or tender in due form any document necessary to enable the buyer to obtain possession of the goods or otherwise required by the agreement or by usage of trade; and

(3) promptly notify the buyer of the shipment.

Failure to notify the buyer under Subdivision (3) or to make a proper contract under Subdivision (1) is a ground for rejection only if material delay or loss ensues.

Moving on from the issue of shipment, perhaps the most notable about the UCC are its "gap-filling" terms. For example, should a general contractor and manufacturer/seller leave the price term open in a contract for goods, the UCC provides:

Tex. Bus. & Com. Code § 2.305. *Open Price Term.*

(a) The parties if they so intend can conclude a contract for sale even though the price is not settled. In such a case the price is a reasonable price at the time for delivery if

(1) nothing is said as to price; or

(2) the price is left to be agreed by the parties and they fail to agree; or

(3) the price is to be fixed in terms of some agreed market or other standard as set or recorded by a third person or agency and it is not so set or recorded.

(b) A price to be fixed by the seller or by the buyer means a price for him to fix in good faith.

(c) When a price left to be fixed otherwise than by agreement of the parties fails to be fixed through fault of one party the other may at his option treat the contract as cancelled or himself fix a reasonable price.

(d) Where, however, the parties intend not to be bound unless the price be fixed or agreed and it is not fixed or agreed there is no contract. In such a case the buyer must return any goods already received or if unable so to do must pay their reasonable value at the time of delivery and the seller must return any portion of the price paid on account.

Shifting gears from "gap-filling" terms, the UCC provides the following on excuse by the failure of presupposed conditions:

Tex. Bus. & Com. Code § 2.615. *Excuse by Failure of Presupposed Condition.*

Except so far as a seller may have assumed a greater obligation and subject to the preceding section on substituted performance:

(1) Delay in delivery or non-delivery in whole or in part by a seller who complies with Subdivisions (2) and (3) is not a breach of his duty under a contract for sale if performance as agreed has been made impracticable by the occurrence of a contingency the non-occurrence of which was a basic assumption on which the contract was made or by compliance in good faith with any applicable foreign or domestic governmental regulation or order whether or not it later proves to be invalid.

(2) Where the causes mentioned in Subdivision (1) affect only a part of the seller's capacity to perform, he must allocate production and deliveries among his customers but may at his option include regular customers not then under contract as well as his own requirements for further manufacture. He may so allocate in any manner which is fair and reasonable.

(3) The seller must notify the buyer seasonably that there will be delay or non-delivery and, when allocation is required under Subdivision (2), of the estimated quota thus made available for the buyer.

Finally, general contractors need to be aware of their remedies under the UCC. The primary remedy available for buyers is "cover," and the UCC provides as follows:

Tex. Bus. & Com. Code § 2.712. *"Cover"; Buyer's Procurement of Substitute Goods.*

(a) After a breach within the preceding section the buyer may "cover" by making in good faith and without unreasonable delay any reasonable purchase of or contract to purchase goods in substitution for those due from the seller.

(b) The buyer may recover from the seller as damages the difference between the cost of cover and the contract price together with any incidental or consequential damages as hereinafter defined (Section 2.715), but less expenses saved in consequence of the seller's breach.

(c) Failure of the buyer to effect cover within this section does not bar him from any other remedy.

The UCC provisions serve as a mere baseline. In an ideal world, a general contractor enjoys the protections the UCC offers. However, because of bargaining power disparities, manufacturers and sellers are often able to alter the UCC's terms to create their own favorable conditions that can leave general contractors in a bind.

Part III: How Manufacturers/Suppliers Alter the UCC's Terms

General contractors often rely on a commercial form such as a purchase order, invoice, or quotation as the only agreement that exists between them and the manufacturer/seller. Contractors can find themselves in a tough spot if they treat a commercial form too casually and fail to properly consider the implications of the printed terms, which can subsequently become an enforceable contract.

Manufacturers and suppliers often draft their commercial forms to take advantage of UCC terms that work to their benefit and alter/avoid the UCC terms that benefit the contractor. As the global economy continues to grapple with labor shortages, supply chain disruptions, and elevated prices, it is more important than ever for contractors to understand not only the "gap-filler" provisions of the UCC, but also the pitfalls that may be contained in commercial forms drafted by shrewd sellers. Contractors may be able to avoid the implications of such provisions (discussed in Section V), but the first step is recognizing them.

Common UCC provisions altered by sellers to their advantage involve **acceptance and satisfactory performance**. Standard UCC provisions protect a buyer who receives non-conforming goods, but a manufacturer/seller might avoid some of those protections by including language in a purchase order acknowledgement or confirmation similar to the following:

> Buyer shall inspect the Goods within _______ days of receipt ("Inspection Period"). Buyer will be deemed to have accepted the Goods unless it notifies Seller in writing of any Nonconforming Goods during the Inspection Period and furnishes such written evidence or other documentation as required by Seller. "Nonconforming Goods" means only the following: (i) product shipped is different than identified in this Agreement; or (ii) product's label or packaging incorrectly identifies its contents.
>
> If Buyer timely notifies Seller of any Nonconforming Goods, Seller shall, in its sole discretion, (i) replace such Nonconforming Goods with conforming Goods, or (ii) credit or refund the Price for such Nonconforming Goods. Buyer shall ship, at its expense and risk of loss, the Nonconforming Goods to Seller's facility located at _________. If Seller exercises its option to replace Nonconforming Goods, Seller shall, after receiving Buyer's shipment of Nonconforming Goods, ship to Buyer, at Buyer's expense and risk of loss, the replaced Goods to the Delivery Point.
>
> Buyer acknowledges and agrees that the remedies set forth above are Buyer's exclusive remedies for the delivery of Nonconforming Goods.

The pro-seller provision above aims to override the UCC's default rule that the buyer must reject nonconforming goods within a "reasonable time after delivery" by establishing a deadline during which the buyer must complete its inspection and notify the seller of any non-conformity. It also introduces additional, non-UCC requirements concerning how notice of non-conformity must be given by the buyer and how non-conforming goods that are rightfully rejected must be handled by the buyer. Importantly, the provision also introduces a pro-seller definition of non-conforming goods, thereby altering the perfect tender rule of Tex. Bus. & Com. Code § 2.601. Finally, the exclusive replacement remedies are also an end-run around the additional remedies provided to the buyer under the UCC.

Warranties are another area that is often addressed by sellers in their quotes or invoices to the detriment of contractors. As described in Section II above, the UCC contains implied warranties of merchantability and fitness for particular purpose that can be invoked by a contractor who receives goods that ultimately prove to be defective or nonconforming. Given the high costs that can be imposed as a result of breaches of warranties, a well-worded disclaimer can greatly assist a seller in managing its own costs and risk. To avoid the UCC warranties, a seller might include language similar to the following:

> Seller warrants to Buyer that for a period of _______ from the date of shipment of the Goods ("Warranty Period"), such Goods will materially conform to the specifications set forth in Exhibit A/Seller's published specifications in effect as of the date of this Agreement and will be free from material defects in material and workmanship.
>
> EXCEPT FOR THE WARRANTY SET FORTH ABOVE, SELLER MAKES NO WARRANTY WHATSOEVER WITH RESPECT TO THE GOODS, INCLUDING ANY (i) WARRANTY OF MERCHANTABILITY; OR (ii) WARRANTY OF FITNESS FOR A PARTICULAR PURPOSE WHETHER

> EXPRESS OR IMPLIED BY LAW, COURSE OF DEALING, COURSE OF PERFORMANCE, USAGE OF TRADE, OR OTHERWISE.
>
> Seller shall not be liable for a breach of the warranty set forth above unless: (i) Buyer gives written notice of the defect, reasonably described, to Seller within _____ days of the time when Buyer discovers or ought to have discovered the defect; (ii) Seller is given a reasonable opportunity after receiving the notice to examine such Goods and Buyer (if requested to do so by Seller) returns such Goods to Seller's place of business at Seller's cost for the examination to take place there; and (iii) Seller reasonably verifies Buyer's claim that the Goods are defective.
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> Subject to the above, with respect to any such Goods during the Warranty Period, Seller shall, in its sole discretion, either: (i) repair or replace such Goods (or the defective part) or (ii) credit or refund the price of such Goods at the pro rata contract rate provided that, if Seller so requests, Buyer shall, at Seller's expense, return such Goods to Seller.
>
> THE REMEDIES SET FORTH ABOVE SHALL BE THE BUYER'S SOLE AND EXCLUSIVE REMEDY AND SELLER'S ENTIRE LIABILITY FOR ANY BREACH OF THE LIMITED WARRANTY SET FORTH ABOVE.

This type of warranty-limiting language is permitted by Texas law, and it significantly decreases the protections offered to buyers under the UCC. The warranties of merchantability and fitness for purpose are excluded, express warranties are limited by time and the required actions of the buyer, and the remedies of the buyer in the event of a breach are substantially reduced from those offered by the UCC.

A third area that is ripe for contractor/buyer hazards involves shipment **delays and the risk of loss.** The timing of transferring title and risk of loss from the seller to the buyer can vary greatly depending on the terms and conditions of the sale documents. Similarly, the risk of delays caused by supply shortages and supply chain disruptions can be shifted by clever language included by sellers. The following are examples of terms that contractors should strive to avoid:

> The goods will be delivered within a reasonable time after the date of this Agreement, subject to availability of finished Goods. Seller shall not be liable for any delays, loss, or damage in transit.
>
> Seller shall deliver the Goods to [SELLER'S LOCATION] (the "Delivery Point") using Seller's standard methods for packaging and shipping such Goods. Buyer shall take delivery of the Goods within __________days of Seller's written notice that the Goods have been delivered to the Delivery Point.
>
> Seller may, in its sole discretion, without liability or penalty, make partial shipments of Goods to Buyer. Each shipment will constitute a separate sale, and Buyer shall pay for the units shipped whether such shipment is in whole or partial fulfillment of the quantity purchased under this Agreement.
>
> If for any reason Buyer fails to accept delivery of any of the Goods on the date fixed pursuant to Seller's notice that the Goods have been delivered at the Delivery Point, or if Seller is unable to deliver the Goods at the Delivery Point on such date because Buyer has not provided appropriate instructions, documents, licenses, or authorizations: (i) risk of loss to the Goods shall pass to Buyer; (ii) the Goods shall be deemed to have been delivered; and (iii) Seller, at its option, may store the Goods until Buyer picks them up, whereupon Buyer shall be liable for all related costs and expenses (including, without limitation, storage and insurance).

This type of language reflects the default provision of the UCC, which states that the time for delivery is a "reasonable time," and it provides the seller with more flexibility than a specific delivery date. The above language also reflects the default position of the UCC, which states that unless otherwise agreed by the parties, the place of delivery is the seller's place of business, and it affords the seller the least amount of responsibility and risk. All costs and risks involved in transporting the goods from the seller's premises to the desired destination are shifted to the buyer. Importantly, the language above provides the seller with flexibility to tender delivery in installments. Otherwise, the UCC's gap-filler provision states that tender of the ordered goods must take place in a single delivery, and it enables the buyer to reject the goods if the delivery did not take place in one shipment. By stating that each shipment is a separate sale, the buyer arguably has no termination right if the seller breaches with respect to only one shipment. Moreover, if the delivery point is the seller's location, the seller can avoid any storage and transportation costs arising from the buyer's failure to accept delivery.

Force Majeure is another area where contractors need to be attentive. In today's environment of more frequent supply chain disruptions, *force majeure* provisions are more important than ever. A seller will typically want to have a broad *force majeure* clause that allows its performance to be excused in a variety of circumstances beyond its control. A seller will also want to include a "catch all" provision that does not limit the *force majeure* events to only those listed. Catch all language ensures that when unexpected events prevent a seller from performing timely under an agreement (or performing at all), the seller will not be liable for damages. The following is an example of a pro-seller provision:

> Force Majeure. Any delay or failure of Seller to perform its obligations under this Agreement will be excused to the extent that the delay or failure was caused directly by an event beyond such Party's control, without such Party's fault or negligence and that by its nature could not have been foreseen by such Party or, if it could have been foreseen, was unavoidable (which events may include natural disasters, embargoes, explosions, riots, wars, acts of terrorism, strikes, labor stoppages or slowdowns or other industrial disturbances, and shortage of adequate power or transportation facilities).

The term above is drafted as a wholly unilateral provision, and the buyer's principal obligation, that of making payment for the goods, is not included among the excused obligations. Mistaken assumptions about future events or worsening economic conditions are expressly listed as a *force majeure*, and the seller is now excused from performance merely because it proved difficult, burdensome, or economically disadvantageous.

Part IV: How Construction Contracts Differ from Manufacturer/Supplier Purchase Orders' Terms and Conditions

Construction contracts predominantly involve the provision of labor and services by the general contractor. Therefore, unlike the purchase and sale of goods, the UCC does not typically apply to construction contracts. Instead, common law principally applies, which is a body of law derived from judicial decisions and precedents. The legal rights and responsibilities dictated by common law can be very different from the legal obligations provided by the UCC, and they can also differ substantially from the terms and conditions contained in sales documents. To avoid being stuck in the middle or surprised, general contractors need to be aware of some of the most notable differences between the UCC and common law.

In general, common law requires more definiteness than the UCC. Under the UCC, a contractual obligation may arise even if the agreement between the buyer and seller has open terms. As long as the parties intend to make a contract, and the court can find a reasonably certain basis for giving an appropriate remedy, then a contract is deemed to have been formed. For example, under the UCC, if a sales contract says nothing about price, or if it permits the parties to agree on price but they fail to agree, then the UCC will "plug" the open term with a "reasonable price at the time for delivery." The same is true concerning the particulars of performance, which can be left to one party to be dictated in good faith. In sharp contrast, at common law, a contract that fails to specify a material term like price or performance will almost always fail. Consequently, a general contractor must be aware of its need for specificity on the one hand and its vulnerability to lack of specificity on the other, which can give rise to exposure and be fertile ground for disputes.

Another important difference between common law and the UCC is known as the "mirror image doctrine." At common law, if the acceptance differs from the offer, no contract results.[5] In other words, if the acceptance does not exactly mirror the offer, then there is no valid, enforceable contract between the parties. If the offer is amended, there can be no acceptance, but the terms can be renegotiated. An agreement is only reached when a new offer is accepted without modifications. Under the UCC, if a party receives an offer and adds additional terms or conditions, the new terms are construed as offers and are automatically incorporated into the contract between the buyer and seller unless the offer expressly limits acceptance to the terms of the offer, the new terms materially alter the offer or notice of rejection of the new

[5] *See*, *Amedisys, Inc. v. Kingwood Home Health Care, LLC,* 437 S.W.3d 507, 514 (Tex.2014).

terms is given within a reasonable time.[6] A general contractor must be cognizant of these rules and ensure that any additional terms written on the back of a quotation or acknowledgment of a purchase order, for example, are properly reviewed and acceptable.

Under common law, a contract can only be modified if there is additional consideration or benefit given for the modification.[7] For example, if a construction contract is modified to increase the scope of work, additional consideration would typically be provided by way of an increase in the contract price. However, a UCC contract can be modified on agreement of the parties without any additional consideration.[8] Similarly, a contract under the UCC can be discharged – freeing both parties of their contractual obligations – without an exchange of consideration.[9] Moreover, if the contract is impracticable or impossible to complete or too expensive or too difficult through no fault of the performing party, the obligations are excused.[10] A court must look at the circumstances and decide whether performance is impracticable enough to discharge the obligation.[11] For instance, if the parties agree on a price based upon current market conditions, but events beyond anyone's control

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[6] Tex. Bus. & Com. Code § 2.207

[7] *See, Med. Imaging Sols. Group, Inc. of Tex. v. Westlake Surgical, LP,* 554 S.W.3d 152, 161 (Tex.App.--San Antonio 2018, no pet.).

[8] Tex. Bus. & Com. Code § 2.209(1).

[9] Tex. Bus. & Com. Code § 1.306.

[10] Tex. Bus. & Com. Code § 2.615.

[11] *See, PPG Indus., Inc. v. Shell Oil Co.*, 919 F.2d 17, 18-19 (5th Cir. 1990).

cause costs to skyrocket, a party may try to cancel the contract based upon impracticability. In contrast, under Texas common law, an "Act of God" is technically not an excuse for non-performance unless the parties have agreed otherwise.[12] A general contractor must be aware of the differences in legal responsibilities to avoid getting stuck in the middle, potentially in a dispute both with an owner and a manufacturer/supplier.

Another crucial difference between common law and UCC involves the degree of performance that is acceptable. As detailed in Section II above, under the UCC, a buyer can insist on exact performance from the seller, and the buyer has the option of rejecting any goods that are not a "perfect tender." Texas common law is different and provides more flexibility in the context of construction contracts, in that it applies the "substantial performance doctrine." Substantial performance arises when one party has deviated slightly from the conditions of the contract, but those deviations have not materially detracted from the other party's benefit.[13] In this situation, the other party has substantially received the benefit it expected, and is, therefore, bound to perform under the contract. If a party can demonstrate that it has, in substance, satisfied its obligations in the contract and there are only slight deficiencies or very minor deviations, then the substantial performance bar is met.[14] Although it may

[12] *See, Valero Transmission Co. v. Mitchell Energy Corp.,* 743 S.W.2d 658, 663 (Tex.App. – Houston [1st Dist.] 1987, no writ).

[13] *See, Turner, Collie & Braden, Inc. v. Brookhollow, Inc.,* 642 S.W.2d 160, 165 (Tex. 1982).

[14] *Id.*

work to their benefit, general contractors should nonetheless be aware that the performance criteria in contracts for the sale of goods can be substantially more rigid than the criteria applied by the common law to a construction contract.

Other significant differences exist between the UCC and common law, such as the applicable warranties addressed in Section III above; the damages available to a buyer for breach of contract, which under the UCC are generally limited to the difference between the contract price and the market price plus incidentals; and the requirements for privity of contract, which are much more flexible under the UCC than at common law.

Part V: How General Contractors Can Manage Risk Through Terms and Conditions in Purchase Orders or Supply Agreements

Many of the risks faced by general contractors associated with purchase agreements can be reduced through an awareness of the legal rights, obligations, and remedies available under the UCC. The risks can also be mitigated by using well-reasoned terms and conditions in purchase orders and supply agreements that counter any unfavorable provisions written in by sellers and provide helpful protections to general contractors when procuring equipment and materials.

First and foremost, a general contractor can strive to transfer all of the risks and obligations the contractor is assuming toward the owner in the prime contract with respect to manufacturer or supplier equipment or materials, to the manufacturer or supplier by express agreement. Such a risk transfer term is commonly referred to as “flow down” provision.

If such a term cannot be obtained, contractors should recognize and attempt to disclaim unfair or unbalanced terms and conditions written into sales documents by sellers and manufacturers, like the ones described in Section III above. When, as is commonly the case, a buyer and seller both attach their respective standard terms and conditions to purchase orders, invoices and confirmations, ambiguity can arise regarding which party’s terms apply. In such a situation, the UCC’s “battle of the forms” rules will determine the provisions that make up the agreement. A buyer can improve its chances of winning the battle of the forms with two key statements. First, the buyer should expressly disclaim the seller’s terms and conditions in its purchase order terms. Second, the buyer should include a statement in the purchase order or supply agreement that the seller accepts the buyer’s terms by acknowledging and fulfilling the order.

A general contractor should also strive to ensure that it is able to recover a full complement of damages in the event of a breach by the seller. A full recovery is especially important in the current economic environment because of the numerous issues that can result from material and labor shortages. If a seller is unable to deliver the product requested, and the general contractor experiences losses as a result of not being able to fulfill its contractual obligations under the prime construction contract, being able to have a claim against the seller can help ensure that the contractor does not bear the entire brunt of the seller’s non-performance. For example, a general contractor should seek to ensure that the seller's terms and conditions do not exclude recovery of consequential damages—damages that are not directly caused by a given breach, such as lost profits or interest. Moreover, a mutual damage disclaimer may appear to provide a fair approach, but such "mutuality" generally benefits the seller. A buyer's primary obligation under the purchase contract is usually to pay, whereas the seller is responsible for the majority of the obligations. For this reason, when possible, a buyer should avoid agreeing to terms that limit any of the parties' recoverable damages. If consequential damages are excluded by the seller, the buyer should seek carve-outs for any indemnification obligations, and if possible, for losses arising from the seller's intentional or grossly negligent acts (See Section VI, infra).

In todays' unpredictable supply chain environment, the ability to rely on timely delivery is crucial for a general contractor. A purchase order should specify that the contractor is involved in a time-sensitive industry, and that time and quantity are "of the essence." A "time is of the essence" clause should provide that it is the seller's responsibility to ensure both time and quantity terms are met using any means necessary (e.g., expedited delivery, extra inventory, etc.) to ensure the delivery date and required volumes. The failure of a buyer to include a "time is of the essence" clause may provide the seller the opportunity to justify its late delivery or argue that it is not a material breach. The supply agreement should also include a right to cancel a purchase order if the supplier has not delivered the ordered goods by the scheduled or agreed delivery date for the order. Buyers should also consider adding a requirement for notice to their purchase agreements. The provision should state that when a seller becomes aware of a potential delay in delivery or increase in price for equipment or materials, the seller must give notice within a specific time and in a specific form.

A purchase order/supply agreement should also specify the buyer's inspection rights, including when and where the inspection may take place and by whom. The provision should give inspection rights to the buyer as well as authorized personnel, and the supplier should be expected to provide any assistance necessary and cooperate with the inspection process. A general contractor/buyer should also specify its right to cancel, suspend or modify a binding purchase order for obvious delivery issues, such as wrong deliveries or if there are frequent, consistent and minor errors and defects that breach the agreement.

As explained in Section III above, *force majeure* provisions typically benefit the seller, but a buyer can draft a *force majeure* provision to its advantage and protection. The provision should be very explicit as to the events that trigger excused performance, like "Acts of God" – events of nature over which the seller has no control. Events for which the seller should ordinarily bear the risk, such as labor or material shortages, should be expressly excluded from the provision. Moreover, a buyer can limit a seller's ability to use catchall language to excuse its responsibility for a risk not explicitly covered in the provision.

A general contractor should strive to include strong warranties in the purchase order agreement. A buyer should have the seller warrant that its goods are free from defects, meet the buyer's specifications, are merchantable, and are fit for their intended purpose. To help protect against a breach of warranty by a seller, a buyer should provide for available remedies in the warranty terms, such as requiring the seller to repair or replace the goods or, at buyer's sole option, offer a refund for the price of the goods. In addition to this remedy provision, a buyer should consider including an indemnity provision that requires the seller to reimburse the general contractor for any costs flowing from a breach of the warranties by the seller.

Part VI: How General Contractors and Purchasers Can Manage Risk through Negotiations with Project Owners

General contractors and purchasers can manage the risk associated with procuring equipment and materials in a variety of ways. It is incumbent on general contractors to negotiate with project owners to create fair and reasonable terms in the prime construction contract that appropriately allocate the risk general contractors face when procuring equipment and materials. Put simply, managing risk should be a top priority of a general contractor when negotiating a prime construction contract.

One way for general contractors to avoid the risks identified above is to negotiate a construction contract in which the owner is responsible for procuring specific equipment or materials. By placing the duty on the owner to procure specific equipment or materials, a general contractor is minimizing its risk of facing liquidated damages or consequential damages under the construction contract should delays in procurement arise. To be sure, a general contractor can be expected to procure common construction materials. But for extraordinary materials or equipment a project owner wants to incorporate into a project, general contractors may be wise to place the burden of procurement on the project owner.

For key items of equipment or material that the owner will not procure, a general contractor should seek to understand, before agreeing to any terms, the extent to which the prime contract and the terms and conditions of the manufacturers/suppliers of such items materially expose the contractor to risk to the owner that will not be transferred to or accepted by the manufacturer/supplier. With such an understanding, the contractor can strive to negotiate exceptions or limitations on its liability to owners. If the risk cannot be fairly allocated by agreement, the contractor should consider liquidating the risk into its pricing in the form of a premium, or in a worst case scenario, passing on the work. An extra premium paid to the general contractor, in addition to improving anticipated reward for performing the work, may allow the general contractor to obtain a stronger builder's risk insurance policy, for example, further quelling concerns about risk exposure the general contractor may face under the terms and conditions of the manufacturer or supplier.

In sum, general contractors are often caught in the middle between a construction contract with an owner and a contract for the sale of goods with a manufacturer/seller. The two contracts are governed by different rules and problems can naturally arise as between the two. To manage the risks general contractors face in this situation, they must be aware of potential pitfalls and be proactive in their negotiations with both project owners and manufacturers/sellers. By doing so, the likelihood of agreement to reasonable terms—beneficial to all parties—increases, and the risk of loss and disputes decreases.