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Back to your Regular Programming: Construction Contracts – What is the Critical Path?

In these strange times, it is good to go back to basics, the "nuts and bolts" in mitigating common risks on a construction project. This is NOT intended to be an extensive article about every possible risk in a construction contract, but just a reminder of the basic construction contract risks that every party in a construction project should review. That holds especially true for construction contracts in this post COVID-19 world that is rapidly speeding up with multiple layers of risks, like price escalation due to the skyrocketing lumber prices.

Managing risks can be handled not only by sound business and construction practices (like estimating and scheduling) but also by careful contract preparation and review. One basic concept I like to emphasize with my clients is that any potential project risk should be anticipated by the parties to determine which party is in the best position to control that accept of risk and responsibility. For example, an owner will want to allocate the risk that someone is hurt by construction operations to the contractor, who is arguably in the best position to provide a safe work site. A contractor will want to allocate the risk of design errors to the owner, who often holds the contract with the architect and therefore is in a better position to address and minimize these losses. These are just a few of the many types of risks that a construction contract should address in a fair and balanced manner, so that the parties know in advance who is responsible for what risk.

Here are some of the "critical path" clauses to review in your next construction contract:

1. **Scope of Work**: The definition of what is (and what is not) included in the Scope of the *Work* is of critical importance. In the end, the Owner wants to ensure that the Project meets its specified needs and performance criteria, but must depend on others—the architect and contractor—to define the details and requirements to get the Owner the end result. The problem created by an ambiguous or incomplete description of the *Work* occurs when the Owner interprets the Scope of Work more broadly than does the Contractor. The battle will be fought during the course of the project when the Owner and Architect refuse to grant the Contractor a Change Order for what the Contractor believes is additional work, for which additional compensation is due.

2. **Indemnity**: This is often the most reviewed and negotiated clause in any construction contract. The basic explanation of an indemnity clause is that it requires one party to pay for

losses incurred by the other party and defend the other party against claims for such losses. The issue always becomes indemnifying and defending a party for a claim or loss caused by their own negligence. Most states have laws that address this issue and Texas is no exception. In short, the Texas Insurance Code ("anti-indemnity statute") makes a provision in a construction contract void and unenforceable to the extent that it requires a party to indemnify or defend a party against claims caused by the negligence or other fault of the party seeking indemnity. There is are exceptions contained in the anti-indemnity statute, but the major one that I see discussed during a contract negotiation is the exception in the statute relating to bodily injury or death. Specifically, the statute does not apply to a provision in a construction contract that requires a person to indemnify or defend another party to the construction contract against a claim for the bodily injury or death of an ***employee of the indemnitor, its agent, or its subcontractor of any tier***. In other words, the bodily injury exception allows indemnification even when the indemnitee is negligent, even solely negligent. Indemnification provisions that do not comply with the statute may be unenforceable, but the indemnity clauses are typically modified to the fullest extent permitted—particularly with respect to the bodily injury exception. The best way to mitigate indemnity risk is through insurance.

3. **Changes**: Changes in the work of the project (the "work") are an inevitable part of a construction project. Changes can be occasioned by unanticipated weather, differing site conditions, design errors or omissions, installation problems or errors, coordination problems in the work (for example, the parts of the work do not fit together as shown on the plans), or simply changes to the owner's program that necessitate a change in the project. It is important to manage changes carefully and consistently. Review the contractual requirements for making a timely and proper claim for a change. Many contracts have very specific requirements for what is required to make a claim for a change or any increase in costs within a specific time period and by a specific delivery method (certified mail). Do not assume you can send an email or text. Failure to adhere to the requirements to submit a change order or a claim for extra work could result in waiver of such claims.

4. **Suspension of Work**: As the Owner, many times there are provisions that address the situations where an Owner can suspend the project. However, as a contractor it is often silent unless you are using an unmodified AIA form of contract. Be specific as to who has the right to suspend, the notice required and the additional time and costs due to such suspension.

5. **Delays**: Especially in today's environment, there are delays in almost every construction project. Some delays are not the Contractor's or Owner's fault, like those caused by adverse weather, natural disasters, and the like. Generally, such delays are said to be "excusable." Other delays could have been prevented by the Contractor and are said to be "inexcusable." For example, adverse weather is generally considered an excusable, but many times is a non-compensable delay. An example of a compensable delay (the contractor gets extra money) would be where the owner actively interferes with the contractor's work or where the plans and specifications are defective, except on a design-

build project, where the design-builder is responsible for the accuracy of the plans and specifications. The construction contract should specify what delays are excusable and compensable, what delays are excusable but non-compensable, and what delays are inexcusable.

6. **Termination:** Most construction contracts give the owner the right to terminate the contract for convenience (without cause). In such case, the contractor is usually entitled to payment for work performed to date, plus additional termination expenses (but not profit on work not performed). Many construction contracts only address termination for convenience by the owner and default by the contractor. If a contractor wants the right to terminate the contract due COVID-19, future contracts should appropriately account for such termination rights. There are also termination for default requirements and notice should be required in order to cure any default prior to the right to terminate.

7. **Dispute Resolution**: It is important to read and understand the requirements to submit a dispute to dispute resolution under the contract. For example, is mediation required as a condition to litigation or arbitration? Many industry forms require mediation prior to submitting a claim to litigation or arbitration. The contract can be very specific as to the method of dispute resolution, the timing and location, the mediator or arbitrator requirements and important matters that govern the submission of a claim to dispute resolution. Do not wait until there is a dispute to determine that those may be and negotiate as required to be fair to both parties.

This is not a comprehensive list and every contract will require a full analysis to address potential issues.

For more information, please contact Mike Cortez.