

ACC Houston Chapter August 2021

Construction Contracting After Covid



Speakers

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Agenda

- From a predominately Owner's perspective, discuss contracting issues with Architects using a typical AIA document as a reference.
- From a predominately Owner's perspective, discuss contracting issues with Contractors using a typical AIA series of documents as a reference.
- Discuss current issues related to the impacts of Covid-19
 - Price Escalations
 - Force Majeure
- Discuss Texas specific laws that affect construction contracts
 - Anti-indemnity
 - Responsibility for design defects - *NEW change in law
 - Choice of Law
 - Liquidated Damages

Contracting Methods

■ Design-Bid-Build

- Traditional approach – Architect designs, design is put out for bid, contractor builds

■ Construction Manager Agent/At Risk

- A “builder” is involved during design to aide in cost estimates for the design, constructability, value engineering.
 - Once design is finished if the “builder” becomes the “Contractor” then it is Construction Manager At Risk
 - Once design is finished if the “builder” becomes an “advisor” to the Owner because the Owner hires a separate contractor or enters into contracts with the trades directly, then it is Construction Manger Agent

■ Design-Build

- One firm is responsible for designing and building typically to a set of criteria.
- Sole source of responsibility.

Pricing Methods

- Lump Sum
 - Parties agree to an “all-in” fixed price to perform the contract.
- Cost Plus
 - Cost Plus a Fee up to a Guaranteed Maximum Price
 - Cost Plus a Fee with no GMP
- Unit Price (more associated with horizontal construction – roads, excavation, utilities, pipelines, etc.)

Pricing Methods

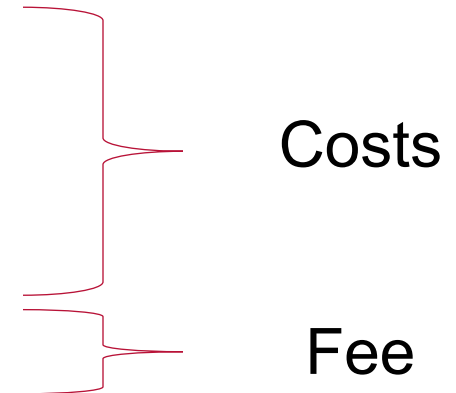
Lump Sum

- Labor
- Materials
- Overhead
- Profit
- Risk



Cost Plus a Fee

- Labor
- Materials
- Overhead
- Profit
- Contingency





Owner/Architect Agreement AIA-B101



Consultants

- Who should contract with consultants?
 - Geotech, Structural, MEP, Traffic, Code Compliance
- Pros: Owners may see potential cost savings by eliminating an Architect markup on these services.
 - Address this by controlling markup on these services instead.
- Cons: Owners lose the single source of responsibility for all design related issues.
 - In the event of a dispute or litigation this can be problematic
 - May also end up with design “scope gap” that the Owner gets stuck with.

Authority of the Architect

- The Architect is empowered during construction administration to do things that can affect a Contractor's right to make a request for a change order.
- May be prudent to limit the authority of the Architect to recommendations only, with the actual decision coming from the Owner's Representative.
- Exception might be on things that do not affect a change in time or cost.

Insurance and Indemnity

- Is there sufficient insurance?
- Are the right forms specified to give you the right Additional Insured status and a Waiver of Subrogation?
 - Note that the typical insurance policies grant these two “when required by written contract.”
- Does the indemnity clause comply with state law.
 - Many states limit to indemnity permissible in construction related contracts.
 - Many states limit the indemnity that can be required of Architects or Owners relating to design.
- Professional liability policies are typically “claims-made” policies.
 - Consider an extended reporting period or “tail”

Texas Construction Anti-Indemnity Act

■ Texas Construction Anti-Indemnity Act

- Does not tell you what you can have...tells you what you can not have.
- Can get broad form indemnity for bodily injury claims from contractor and lower tiers.
- Can only get limited indemnity for property damage and claims from third parties.
- Can't get around anti-indemnity act using Additional Insured coverage.
- Please note that many other states have anti-indemnity acts. Some permit broader indemnity IF it is covered by insurance. Assume nothing is "standard" across the jurisdictions.

■ Why the distinction? Worker's Compensation/Action Over

■ Also be aware of the Texas Oilfield Anti-Indemnity Act for other types of construction contracts (well or mine service)

- Texas Construction Anti-Indemnity Act DOES NOT APPLY IF the Texas Oilfield Anti-Indemnity Act does.

Correction of Errors

- Obligate the Architect as a part of the Basic Compensation to provide design and construction administration services required to correct:
 - Errors
 - Omissions
 - Inconsistencies
 - Lack of Coordination
 - Other similar issues with the project design or other services provided by the Architect and its Consultants

Coordination

- Architect should be responsible for coordinating all design regardless of whether it comes from the Architect, Architect's subconsultants or the Owner's consultants.

Intellectual Property

- Who owns the design? When?
 - AIA approach is Architect owns it and Owner gets rights when everything is fully paid.
 - Better approach is for Owner to own the design as it is paid for.
 - Why?

Specifications

- Are the Architect's provided specifications consistent with the design intent?
 - Energy Efficiency

Warranty Walk

- Consider having the Architect walk the project at the 11 month mark to help the Owner put together a comprehensive warranty claim.
 - May be able to include as part of Basic Services
- Consider having Architect provide construction administration for the corrective work as an Additional Service

Reimbursable Expenses

- Current Language includes some items that should be stricken
 - Long distance services, dedicated data and communications service, teleconferences
 - Postage, handling and delivery
 - If required by Owner, and with the Owner's prior written approval, the Architect's consultants' expenses of professional liability insurance dedicated exclusively to this Project, or the expense of additional insurance coverage or limits in excess of that normally maintained by the Architect's consultants.
 - Other similar Project-related expenses
- Reimbursable Expenses should have a cap and be included in the budget.
- Cap can be exceeded only with prior written consent of Owner
- Some mark-up is reasonable for the administrative burden, but the markup should be a low number.

Coordination

- Architect should be responsible for coordinating all design regardless of whether it comes from the Architect, Architect's subconsultants or the Owner's consultants.



Owner/Contractor Agreement AIA-A101, AIA-A201



Scope of Work

- Scope is one of the most important parts. It describes what you are going to get.
- Do not incorporate the Contractors proposal as a general rule.
- Scope should be to build per the plans and specifications as well as those things reasonably inferable therefrom.
- Clarifications and Assumptions (more potential on a remodel)
 - Contractor's sometimes include these.
 - Generally ok if these are limited to true assumptions about the physical conditions of the project but not legal terms
 - i.e. "Assume that existing electrical panels can be re-used." NOT "Assume that Contractor has no indemnity obligations."

Limitations of Liability

- Limits of Liability
 - To available insurance?

- Waiver of Consequential Damages
 - Mutual waivers are not equal. Owner's consequential damages are usually greater.
 - A consequential damage is one that flows from the breach, but not necessarily.
 - Additional rent expense, storage expense, relocation expenses would likely be consequential damages.

Insurance and Indemnity

- Is there sufficient insurance?
- Are the right forms specified to give you Additional Insured status and a Waiver of Subrogation?
- Does the indemnity clause comply with state law.
 - Many states limit to indemnity permissible in construction related contracts.
- Have you contractually limited the type of exclusions permissible in Contractors insurance?
 - Explosion, Collapse, Underground
 - Residential
 - EIFS?
 - Asbestos?

Schedule of Values

- Not front loaded
 - Fair representation of the work items
 - Not to be used to value change orders
 - Subject to Architect and Owner approval
-
- Consider whether to permit breaking out of insurance, bonding, etc. so that those items or a portion thereof can be paid on the front end.

Schedule and Delays

- Require critical path schedules
- Contractor gets more time but not more money?
- Contractor gets more time if they can show impact to critical path?
- What relief does contractor get if there is a concurrent delay?
- Require timely notice of claims.
- Have the option to require the contractor to accelerate for a cost, if they are overcoming an Owner caused delay.
- Contractor should timely provide a recovery schedule to demonstrate how they will overcome delays.
- Require Contractor to provide the schedule in native format, rather than just a paper schedule so that you can examine for potential tricks
 - i.e. Logic is broken, durations are shortened to show project is back on schedule, etc.

Substantial Completion

- Are there special requirements for Substantial Completion?
- Is a Certificate of Occupancy enough?
- Any other approvals required before you can use the project for its intended purpose?
 - Best to describe the requirements needed.

Liquidated Damages

- Must be a reasonable approximation of actual damages.
- Do not use a chart based on contract amount.
- Must perform the math on the front end.
- If Liquidated Damages are unenforceable you can still recover actual damages.
- Liquidated Damages must not be a penalty
 - I've seen LD's increase between Substantial Completion and Final Completion...????
- Texas is a “look back” state.
- Other states may not be “look back” states.
- What about liquidated damages between substantial and final completion?

Liquidated Damages

Holland PAGE et al., Petitioners, v. TRAVIS-WILLIAMSON COUNTY WATER
CONTROL AND IMPROVEMENT DISTRICT No. 1, Respondent.

No. A-9136.

Supreme Court of Texas.

May 8, 1963.

This rule is applicable to a construction contract such as we have in the present case. Where the owner has taken possession and is using the object of the contract for its intended purpose before the expiration of the number of working days provided for in the contract, there is no delay for which liquidated damages may be awarded. **After the date of occupancy the owner is entitled only to his actual damages.** Collier v. Betterton, supra. Liquidated damages were properly denied in this case.

Liquidated Damages

IN THE SUPREME COURT OF TEXAS

=====
No. 18-0228
=====

ATRIUM MEDICAL CENTER, LP AND TEXAS HEALTHCARE ALLIANCE LLC,
PETITIONERS,

v.

HOUSTON RED C LLC D/B/A IMAGEFIRST HEALTHCARE LAUNDRY SPECIALISTS,
RESPONDENT

=====
ON PETITION FOR REVIEW FROM THE
COURT OF APPEALS FOR THE FOURTEENTH DISTRICT OF TEXAS
=====

Argued November 5, 2019

JUSTICE BLAND delivered the opinion of the Court.

A properly designed liquidated damages provision, however, may still operate as a penalty due to unanticipated events arising during the life of a contract. Thus, we observed in *Phillips* that courts must also examine whether “the actual damages incurred were much less” than the liquidated damages imposed, measured at the time of the breach.²²

When a contract’s damages estimate proves inaccurate, and a significant difference exists between actual and liquidated damages, a court must not enforce the provision. Applying this rule in *FPL Energy, LLC v. TXU Portfolio Mgmt. Co.*, we held that the “unacceptable disparity” between damages assessed under the contract (approximately \$29 million) and actual damages (approximately \$6 million) made the liquidated damages provision unenforceable.²³ At the time of contracting, damages from a breach in that case “were difficult to estimate” and the liquidated damages provision “on [its] face, reasonably forecast damages.”²⁴ Nonetheless, we held the provision unenforceable because it “operate[d] with no rational relationship to actual damages.”²⁵

Retainage

- Retainage laws vary by state
- Know whether you are increasing your risk.
- Example:
 - In Texas if you agree to withhold less than 10% or have an early release of retainage you increase potential exposure for the Owner.
 - Some states may have limits on retainage that differ. Some states may only have 10% retainage until 50% of the project is complete and then change
 - Some states, like Louisiana (last time I dealt with this issue) require you to put retainage in an interest bearing account.

Claims

- Require timely notice
- Limit what can be recovered on Claims
- These should not be a profit center for the Contractor
- No indirect or consequential damages permitted
- Damages recoverable are limited to extra costs specifically shown to have been directly caused by a proven wrong.

Termination for Convenience

- Preserve a safe way out
- No lost profit on unperformed work
- Acceptable work performed to date plus direct and unavoidable costs incurred as a result of the termination
 - Restocking fees
 - Cancellation fees
 - Demobilization
- But Termination damages should not exceed the total project amount.
- Consider removing the “Termination Fee” concept

Choice of Law

- Please understand that Choice of Law elections in construction contracts may not be enforceable.
- Many states have statutes like Texas that require local law to apply:
- Texas Business & Commerce Code 272.001

If a construction contract or an agreement collateral to or affecting the construction contract contains a provision making the contract or agreement or any conflict arising under the contract or agreement subject to another state's law, litigation in the courts of another state, or arbitration in another state, that provision is voidable by a party obligated by the contract or agreement to perform the work that is the subject of the construction contract.

- Your best chance around this is an arbitration clause referencing the Federal Arbitration Act.



Current Issues – Post? COVID-19



Price Escalations

- There have been noted price escalations in many building materials since the start of 2021
- Some have tapered off, some have not, they are expected to, but there is no consensus on when.
- Owner's should consider a price fluctuation clause NOT a price escalation clause.
 - i.e. If Owner takes the risk of prices going up, shouldn't they get the benefit of prices going down?
- Biggest two challenges
 - How do you measure price escalations?
 - Indexes
 - Invoices
 - How do you know that charges are really price escalations and not covering up mistakes.

Force Majeure

- Most Force Majeure clauses, whether they include pandemics or not, are not written very well to account for pandemics.
- Accordingly your old form, is probably not good anymore.
- Most Force Majeure clauses focus on the unforeseen. The difficult with this pandemic, is that is not unforeseen. Nevertheless people probably can not price in the risk.
- Force Majeure clauses should be adjusted to specify that the unforeseen aspect relates to a project impact.
- Some Force Majeure clauses make reference to impacts to the physical location of where the project is happening (i.e. a hurricane blowing through town). What if an outbreak or government order shuts down a manufacturing facility 1000 miles away where your equipment is being manufactured.
- Force Majeure clauses differ and must be carefully considered.

COVID-19

- Many other contract clauses focus on causes of things, delays, damages, etc.
- What if an electrician shows up on the job with Covid-19 and gets others sick?
 - Are they the cause?
 - What if the Owner's Representative was asymptomatic and gave the electrician Covid-19? Now who is the cause? How can we really tell where it came from?
 - We also know that people following protocols and who are vaccinated have ended up with Covid-19.
 - I.e. Its not a matter of negligence or not caring, or not being safe.
- Better approach is to focus on requiring proper protocols. If someone is not following protocols, address it but don't try to implement COVID-19 contractual provisions with remedies based on who gets sick, because it will probably not work.

Liability for Defective Design

- Until recently, Texas law followed a case called *Lonergan* which essentially makes a contractor responsible if they are unable to construct a project properly due to a defective design, unless stated otherwise in the contract.
- The concept was that the contractor impliedly warrants that the plans are sufficient and suitable.
- The rest of the country follows a federal case called *Spearin*, which puts the responsibility on the Owner. It is the Owner that has the relationship with the Architect, not the contractor.

Liability for Defective Design

- NEW to TEXAS: Effective September 1, 2021 (i.e. VERY SOON)
- SB 219
- “A contractor is not responsible for the consequences of design defects in and may not warranty the accuracy, adequacy, sufficiency, or suitability of plans, specifications, or other design documents provided to the contractor by a person other than the contractor’s agents, contractors, fabricators, or suppliers, or its consultants, of any tier.”
- There is much more to this than what is reported above. So you will have to read the actual statute for a more thorough understanding.

Locations

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