

Client-Favorable Contracts for Design and Construction

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Part I: Design

An owner contemplating the construction of a new facility may be surprised to learn that the owner is often the least protected of all the parties in the so-called standard contracts (such as those written by the American Institute of Architects) for architectural services and construction. A strong contract for the owner will clarify for all of the parties exactly what the rights, obligations, and expectations are for the owner, architect, and contractor. A strong contract will serve as a useful tool to prevent disputes later, and as a method of resolving those disputes when they arise. Although owners are often inclined to begin a business relationship on a friendly basis by avoiding confrontation, a robust negotiation of contract terms at the outset, led by an expert consultant or an attorney, will yield many benefits in keeping the project on track. Part I of this article takes a look at contracting with architects.

After developing a detailed facility program, the owner will usually be ready to contract with an architect (or engineer) for the design of the facility. The architect will want to limit its liability for errors and omissions, to avoid being tied to strict definitions of performance and time, and to have an unfettered right to payment. Most complaints from owners about their contracts with architects involve misunderstandings about deliverables, the right of the architect to fees for additional services, use of the drawings, and project cost overruns.

Following are some of the major issues that should be addressed in forming a contract with an architect along with suggested approaches.

Responsibilities of the Parties

- Many contracts will permit the architect to rely completely on information provided by the owner (or owner's consultants). This can lead to errors in the work. To avoid misunderstanding, require the architect to notify owner in writing if any such information is

Why would an institution use standard industry forms for contracts when they are written primarily to protect the other party? Start fresh to protect your institution's interests, and you may save very substantial sums avoiding unnecessary obligations and inappropriate additional fees.

unsuitable, improper or inaccurate, and, most importantly, prevent the architect from proceeding unless the owner confirms in writing how it wishes the architect to proceed.

- Many printed form contracts prevent the owner from changing its project budget, and require the owner to name a representative with complete decision-making authority. These requirements are often incompatible with the structure of institutional governance. Specify limitations on the authority of individuals, including the specific dollar amount authority given to specific employees and officers, and including which decisions will have to be referred to the institution's governing board.
- The AIA contracts give the architect certain rights with respect to the owner's legal, insurance, and accounting needs and services. The owner will normally not want to agree with a third party (the architect in this case) about such services.

The Architect

The "standard of care" is the legal standard to which the architect will be held if the architect is accused of negligence in the performance of its duties. The AIA contract will include the most basic standard.

- If you have hired the architect because of its special skills or the special nature of the project, consider requiring a higher standard. Make sure that the contract requires the architect's services and designs to be "in accordance with all applicable laws, codes, and regulations."
- Include detailed lists of requirements for each phase of the architect's services (schematic design, design development, construction documents, bidding and negotiation, and construction administration). For example, specify the scale of all of the drawings, at what point outline specs are developed, requirements for sections and elevations, what types of engineering services are included, and presentations before community groups.
- For any significant project, always require errors and omissions (professional malpractice) insurance from the Architect.

Drawings and Specifications

Many owners are surprised to learn that they do not own the drawings. When an architect is terminated, the owner may not have the right to use the drawings to finish the project until the owner complies with the architect's payment and other demands under the contract, even when the right to some payments is in dispute. Under the AIA contract, terminating the contract can actually terminate the owner's right to use the drawings.

- The owner should have the right to use the drawings and specs unless it is in default under the agreement in the payment of an *undisputed* amount. It is essential that the owner have the right to hire a substitute architect (without an adjudicated default by the architect) with the substitute architect having the right to use the drawings and specs to finish the project.
- It is perfectly legitimate to negotiate a

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provision which gives ownership of the drawings and specs to the owner.

Changes in Services

An architect's fees can significantly increase through claims from the architect that it is due additional compensation under the contract or by custom. Avoid later confusion by prohibiting increases in compensation for:

- "official interpretations" such as those by building officials. Require the architect to meet all codes and regulations, including interpretations enforced by field inspectors.
- a change in procurement method, such as from a hard bid to a negotiated price with the contractor.
- failure of performance by contractor, unless additional services are required by architect to re-bid or re-negotiate the contract, or the original time frame is substantially exceeded.
- any work performed by the architect for which a signed, written detailed approval is not obtained in advance from the owner.

Payments

Owners are often dismayed to learn that the architect is due a payment even when such payment puts the owner's position in jeopardy. Depending on the circumstance, the owner should be able to withhold a payment completely, or a portion of a payment needed to cover the problem. Contract with the architect to give the owner the right to withhold payment when:

- the architect is in breach or default under the contract.
- any part of such payment is attributable to services which were not performed in accordance with the contract.
- the architect has failed to make payments promptly to its consultants for services for which the owner has already paid the architect.
- the owner has paid the architect for more of its services than have actually been completed. For example, when the owner has paid the Architect 75% of its fee allocated for preparing the drawings, but the drawings are only 50% complete.

Project Budgeting

The best course of action is to require a real cost estimate (rather than mere opinions) from the architect if a consultant has not

been engaged specifically for that purpose. At The University of Texas System, we required the architect to employ and pay a recognized and specialized company, acceptable to the owner, to prepare detailed construction cost estimates of the construction project, in a form acceptable to the owner, following the Construction Specifications Institute (CSI) format.

The estimates were submitted with plans and specifications when submitted for review at the completion of the Design Development phase and at various stages of completion of the Construction Documents. The owner has little recourse with the architect for contractor prices which exceed the budget unless interim cost estimates are obtained *and* the contract requires corrective action from the architect.

- If a construction cost estimate at the end of design development or construction documents indicate a cost which exceeds the budget, then require the architect to revise the project scope or quality to lower the cost below the owner's budget without an increase in fee.

Conclusion

By following the simple contracting guidelines above, and by seeking the advice of an expert consultant or attorney to negotiate and draft actual contract terms, an owner can do much to ensure a smoother relationship with its architect, and to avoid unnecessary expense and delay.

Part II: Construction

Part I of this article discussed how to form a contract with an architect which protects the institution's interests. In Part II of this article, we will look at major issues in forming a contract with a general contractor or construction manager. This article will refer to both types of contracting companies as "contractor" in this article.

Most printed form construction contracts, including those promulgated by societies of design professionals, tend to favor the design professional and the contractor, but not the owner. The institution will want to ensure that the project is delivered on time with a minimum of claims for extra costs. The contractor will want maximum latitude in obtaining extensions of time, and in the right to increase the price charged to the institution for the project.

There are two basic types of construction contracts. One is a *stipulated sum* or *lump sum* contract. The other type is a *cost plus a fee with a guaranteed maximum price*, or *GMP*, for short. The GMP contract present special issues which are discussed separately below. Following are some of the major issues which should be addressed in forming a contract with a contractor along with suggested approaches.

The Contractor's Reliance On The Drawings

Where does the architect's responsibility for design end and the contractor's responsibility for a finished product begin? What happens when the contractor encounters something not shown in the drawings?

- Although the institution does not want the contractor to deviate from the drawings and specifications, it also wants the contractor to extrapolate from the drawings and specs so that the institution receives a finished, functioning product. Even the most complete drawings and specs will not include every conceivable detail and instruction. Most construction contracts, therefore, require the contractor to build what is "reasonably inferable" from the drawings and specs. Unfortunately, this term is rarely defined. The institution will want to define the term to ensure that it requires the contractor to include all material and equipment required for the proper installation of each item or system, and any material and equipment needed to make a complete operating installation.
- Most construction contracts attempt to address what happens when the contractor encounters something unexpected. These situations are commonly called "unexpected conditions" or "differing site conditions." On new construction, they are usually a result of underground discoveries. These conditions are of two types: (1) those that are represented inaccurately or misleadingly in the drawings and specs, and (2) those that could not have been reasonably foreseen. It is difficult for an owner to protect itself against claims based on Type 2 conditions. The owner can, however, include some protection against Type 1 claims by requiring the contractor to warrant that it has visited the site, and that it has conducted its own general

investigation. The contractor should be required to agree that it will thoroughly review the drawings and specs and that it will bring any inaccuracies and inconsistencies to the institution's attention in writing *before* proceeding. Note that overly broad contract exclusions of claims for unexpected conditions may cause contractors to pad their pricing with hidden contingencies.

Schedule

Projects which are behind schedule are a perennial frustration. What can be done to more closely monitor the contractor's on-time performance?

- Require the contractor to submit a detailed schedule prior to being permitted to commence construction. At The University of Texas System, we required the contractor to create and maintain the schedule using an industry standard software package which The University of Texas System specified. This allowed the University in-house project management team to view and manipulate the schedule in their copy of the software.
- The schedule should show times of commencement and completion for each subcontractor, required activity sequences and durations, contract document packages, completion dates, owner contract document package review periods, project building permits acquisition time requirements, construction contract bid dates, processing of shop drawings and samples, owner-provided items, and long lead items.
- For large projects, insist on a "critical path" schedule rather than a bar graph schedule indicating task durations only.
- Require the contractor to update the schedule at least monthly; twice monthly for large projects.
- Most importantly, require the contractor to bring tasks lagging behind schedule to your attention and to *recommend action*.

Claims

Ranking right up there with projects that are behind schedule, as trouble for an institution, are claims for extra time and money.

- The key to controlling claims is to include a strict provision mandating that the contractor submit the claim within a certain number of days (usually about 20) after the conditions giving rise to the claim are known to the contractor. The institution will find it harder to defend itself when it is sandbagged at the end of the job with stale claims. The contract should require every claim to be supported in detail. The supporting data should, at a minimum, include a description of the facts, the legal and contractual basis for the claim, how the facts warrant compensation, and detailed pricing data supporting the amount claimed.

Housekeeping

- Your contract should require the contractor's on-site superintendent to keep daily logs showing, at a minimum, date, weather, subcontractors on the job, number of workers, and status of construction. The logs should be available to the institution for inspection upon demand and should be kept by the contractor for three years after the project is finished. These logs may prove invaluable to the institution in defending itself against a claim.
- Many institutions are surprised to find that their construction contract does not give them a specific right to force the contractor (or a subcontractor) to remove a particular worker. The institution should have the right to require the removal of a worker if, in the institution's opinion, the worker has engaged in inappropriate, offensive, vulgar, or disruptive behavior or speech, including lewd or sexually harassing behavior or speech.

GMP Contracts

GMP contracts present special problems for the unwary institution. In the typical GMP contract, the contractor charges the institution the actual amount of its costs for labor and material plus a mark-up percentage (e.g., six percent). The contractor agrees that it will absorb any costs once the total cost for the project exceeds a guaranteed maximum price.

- Carefully define exactly what types of costs can be charged to the

institution. Avoid provisions that allow contractors to pass on legal costs, home office overhead, costs resulting from subcontractor bankruptcies, consequences of a failure to maintain insurance, contractual indemnification expenses, liquidated damages, or unlimited travel and living expenses. Limit the contractor's performance of subcontract work to general conditions work unless the contractor openly competes with subcontractors for the work and the institution selects the contractor to perform the subcontract work. This prevents abuse on the part of the contractor resulting from the contractor inflating the cost of its work in its role as a subcontractor and then passing it on to the institution as an allowed project expense.

- Payment for stored materials should be limited to situations in which the materials are stored in a bonded warehouse, the materials are insured, the institution has the right to inspect the materials, and the materials are covered by the contractor's payment and performance bonds.
- Require the contractor to submit payrolls and subcontractor/supplier invoices and payrolls each month to support its application for payment.

Conclusion

By following the simple contracting guidelines above, and by seeking the advice of an expert consultant or attorney to negotiate and draft actual contract terms, a institution can do much to ensure that a project is built on time and within budget, and that unnecessary litigation is avoided.

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