CONTRACTS 101

Presented by Rick Gover and Russ Leavitt, SET

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Paper-Lite

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The handout file for this seminar can be downloaded at:

www.firesprinkler.org/convention

Instructor

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Instructor
Russ is the Executive Chairman of Telgian Corporation. He is a graduate of the University of Nevada, Las Vegas, holds a Level IV certification from NICET in Fire Sprinkler Layout, and is a Certified Fire Protection Specialist. He is a licensed contractor with over 30 years of experience in the design, installation, and testing of fire protection systems. He currently serves on the NFPA Board of Directors and on a number of NFPA Technical Committees including NFPA 13. Russ is a long time seminar instructor for AFSA and is a senior instructor for NFPA's Professional Development Series. He has authored a number of articles and training materials including the AFSA study guide for NICET certification in Inspections and Testing and the AFSA on-line hydraulics course.

Construction Contracting Defined
- The allocation of risk to the party best prepared or most willing to assume the risk
- Subcontractors naturally:
  1. Accept risks associated with performance
  2. And, seek compensation for doing so

Assumptions of Law or Fact Can Lead to Unfavorable Results for Subcontractors

False Assumptions in Construction Contracts and Subcontracts.
Some common misconceptions:
1. The contract has to be fair.
2. A waiver of mechanic’s lien rights is not enforceable.
3. If sprinkler work is delayed by the general contractor, other subcontractors, designers or others, recovery of damages is usually a right.
4. Courts will not enforce an indemnification clause that makes me indemnify another party for its own negligence.
5. Pay-if-paid clauses are so wrong courts will not enforce them.
Assumptions of Law or Fact Can Lead to Unfavorable Results for Subcontractors

False Assumptions in Construction Contracts and Subcontracts.

Some common misconceptions (cont’d):

6. It cannot be required to perform sprinkler work not specifically shown in the design documents.
7. If a dispute is not promptly resolved, I can terminate performance and “walk off the job”.
8. Clauses in the prime contract are not binding on me unless they are specifically set forth in my subcontract.
9. If my payments are late, I can automatically quit working until they are made.
10. Liquidated damages are unenforceable unless there is a bonus for early completion.

Assumptions of Law or Fact Can Lead to Unfavorable Results for Subcontractors

The previous 10 assumptions are either false or wrong without contract language to make them correct.

The Subcontract

- Working document
- Sets forth the Rules of Engagement
- Allocates risk
Bid Evaluation Process
- GC typically evaluates
  - Price
  - Skill
  - Experience
  - Willingness to accept risk

1st Rule of Risk Assumption
- Read the subcontract
- Understand the risks being assumed
- Obtain legal advice as necessary

2nd Rule of Risk Assumption
- Try to negotiate away “killer clauses”
- Seek insurance for the risks assumed
3rd Rule of Risk Assumption
- Administer performance to avoid the consequences of the assumed risk

4th Rule of Risk Assumption
- Price your work accordingly
- Apply lessons learned to future projects

Problem Areas and Killer Clauses
What is a “killer clause”?
- Contract provisions that impose financial risks beyond your control
Problem Areas & Killer Clauses

Six of the most common clauses:
- Scope of Work
- Flow-through
- Contingent Payment
- Indemnification & Hold Harmless
- Waiver of Lien Rights & Periodic Releases
- Time of Performance & Delay Damages

The Scope of Work Clause

- Contract documents
  - What about your bid? Try to include it as a contract document.
  - What is in and what is out - Exclusions
  - In accordance with the contract documents and specifications (All or only those defining your work?)
  - Specific v. General

The Scope of Work Clause

- Beware of scope modifiers
  1. “inferable”
  2. “indicated”
  3. “contemplated”

You are not a mind reader!
The Scope of Work Clause

- Avoid catchall language
  1. “and other related items”
  2. “all work incidental thereto”
  3. “all work inferable”

Remember – Subcontract trumps everything

Limit your scope to what you bid. Be as specific as possible.

Examples

- **Specific Scope**
  - Subcontractor shall perform all fire sprinkler work as specified in Division __, pages ___ to ___ of the Specifications and/or as detailed on the following sheets of the plans prepared by ____________.

- **General (Broad Scope)**
  - Subcontractor shall perform all fire protection/ sprinkler work in accordance with the specifications and contract drawings (plans) together with all work inferable and/or required to produce a complete fire protection system in full compliance with all applicable codes and laws.

Flow-Through Clauses

Diagram:

- Owner
  - Prime Contract Obligations
    - Subcontract
Flow-Through Clause

“The Contract Documents for this Subcontract consist of every document between the Owner and Contractor . . . .

“Subcontractor agrees to be bound to Contractor by all of the terms of the Agreement between Contractor and Owner and by the Contract Documents and to assume toward Contractor all of the obligations and responsibilities that Contractor assumes towards Owner. All of the above documents are available upon request.”

Flow-Through Clause

- Contract documents always available but rarely requested by subcontractor
- Primary purpose is to maintain consistent contractual obligations, but can place added duties on subcontractors
- Try to limit clause to technical performance and to subcontract scope only

Flow Through Clause Revised

“Subcontractor agrees to be bound to Contractor by all of the terms of the Agreement between Contractor and Owner and by the Contract Documents and to assume toward Contractor all of the obligations and responsibilities pertaining to the Subcontractor’s work that Contractor assumes toward Owner, and Subcontractor shall have the same rights and remedies against Contractor as Contractor has against Owner.”
Contingent Payment Clauses

Pay If Paid

Pay When Paid

Contingent Payment Clauses

**PAY IF PAID**

Subcontractor paid only if contractor is paid

- Shifts risk of owner’s non-payment from general contractor to subcontractor
- Language used:
  - “Condition precedent”
  - “Subject to”
  - “Upon the condition”
  - “Subcontractor assumes the risk of non-payment by Owner”
Contingent Payment Clauses

"Pay WHEN Paid"

- Determines amount of payment only
- Subcontractor paid when contractor receives payment
- Contractor remains bound to pay subcontractor
- "Reasonable time" for payment if no time is specified

Typical Pay When Paid Clause

"Contractor shall pay Subcontractor within 7 days of Contractor’s receipt of payment from Owner."

Contingent Payment Legal Issues

- Unless clearly drafted, not favored by courts of most states
- Surety cannot use to defeat Miller Act claim
- Some states do not bar lien/bond claims
- Some states have voided CP clauses
Contingent Payment Final Thoughts
- Disputes & debate will continue
- Know the law where you work
- Is this a “deal breaker” for you?

Indemnification & Hold Harmless
What is indemnity?
- One party promises to safeguard or hold harmless another party from existing and/or future loss or liability

How Indemnity Works

HOW INDEMNITY WORKS

[Diagram showing how indemnity works]
Types of Indemnity Clauses

- **Broad** – Imposes entire risk of loss upon sub, even for GC's sole negligence (The goal for G.C.‘s.)
- **Intermediate** – Sub assumes all liability except for GC’s sole negligence
- **Limited** – Imposes liability only to extent of sub’s fault or negligence (The goal for Subs.)

Indemnity-Legal Perspective

- Strictly construed by majority of states
- Some states have anti-indemnity statutes
  - No indemnity for design professionals
  - No indemnity for sole negligence
- Express negligence & conspicuousness

Final Indemnity Considerations

What is your bottom line?
1. I’ll sign any clause to get a good job.
2. I’ll agree to it if I can insure it.
3. I draw the line at sole negligence.
4. I’ll indemnify for my negligence only.
5. I’ll indemnify for the negligence of others but only to the extent of my insurance coverage
Waiver of Mechanic’s Lien Rights
- Mechanic’s lien is a useful collection tool
- Requirements vary state to state
- Watch for blanket waiver of lien rights
- Several states permit waiver of lien rights
- This should be a deal breaker
- DO NOT DO IT!

Periodic Lien Releases
- Partial lien waivers = standard practice
- Intended purpose
  - Release rights/claims for amount paid
- Often drafted to effect a broader release of:
  - Right to receive payment for extra work
  - Obligation to pay for work performed for which payment not yet due
  - Delay, interference & impact claims

Periodic Lien Releases
- Forms often incorporated into subcontract
- Understand scope of release
- Limit scope to amount being paid
  - “…to the extent of payment received.”
- Qualify type of claims being released
  - “…except for unresolved claims, retainage…”
Time of Performance & Delays

Three Common Issues -

1. Liquidated Damages
2. “No Damages for Delay”
3. Scheduling

Liquidated Damages
- Common in prime contract
- Used when damages difficult to prove
- Must be reasonable estimate of actual damages
- Unenforceable if penalty for nonperformance
- Depending on amount, may pose less risk than actual damages

No Damages for Delay Clause
- General Rule
  - Contractors can recover actual damages based on delay and hindrance caused by an upstream party
- Delayed subcontractor must prove:
  - Work was delayed or hindered;
  - Suffered damages due to the delay or hindrance; and
  - Contractor was responsible for the act or omission which caused the delay or hindrance
No Damages for Delay Clause

- **Subcontractors Beware!** – Frequently inserted into contracts
- Limits remedy to time extension
- Fair Notice Requirements **may not apply**
- Be cautious of hidden provisions
- Give notice of delaying event & document

Exceptions to Clause

Awareness & exceptions may be your only defense

1. Delays not intended or contemplated by the parties
2. Delays resulting from fraud, misrepresentation, or other bad faith
3. Delays which have extended such an unreasonable length of time that the party delayed would have been justified in abandoning the contract
4. Delays not within the specifically enumerated delays to which the clause applies

Typical Contract Provision

"Should Subcontractor's Work be suspended, delayed, accelerated or impacted by the acts or omissions of the Contractor, Owner, Architect or other subcontractors, Subcontractor shall be entitled to a time extension as its sole remedy and only to the extent Contractor receives same from Owner."
Favorable Alternative

"Should Subcontractor’s Work be suspended, delayed, accelerated or impacted by the acts or omissions of the Contractor, Owner, Architect or other subcontractors, Subcontractor shall be entitled to an equitable adjustment of the Subcontract price and a reasonable extension of time for performance of its work."

Scheduling

- Killer Combination
  1. Allow GC to modify schedule at will
  2. Sub agrees to meet modified schedule
  3. Sub accepts “no damage for delay” clause

- Exceeds risk priced or contemplated

Typical Schedule Clause

"Subcontractor acknowledges receipt of Contractor’s schedule and agrees to perform in accordance with it and any future amendments. Subcontractor shall perform its work at the time and in the manner directed by Contractor."
Alternative Schedule Clause

“Subcontractor has reviewed and agrees to perform in accordance with Contractor’s schedule and any future, mutually agreeable amendments. Subcontractor shall provide input for schedule modifications as required.”

Notice of Delay

If your work is delayed for reasons beyond your reasonable control, give written notice and request a time extension. If in doubt, give timely notice. Do not lose the right to defend a delay claim for lack of notice and time extension request.

Final Considerations

- Give and take in negotiations
- Get legal advice
- Read the entire contract before signing.
- Understand your money and risk positions
- Certain risks must be tolerated and priced
- There will be problems
- Jobsite staff must know the subcontract
Final Considerations

Risk in construction contracting may be:
1. Assumed;
2. Avoided;
3. Transferred; or
4. Reduced in careful performance and documentation

It’s up to you to define the “deal breakers”. You are a contractor – not a gambler (or are you?)

CONCLUSION

Questions & Answers

- Evaluations: Paper or Mobile Device
  - Attendee ID#: 5-digit number located on your badge
  - Paper: SEMINAR ID# 00458
  - Mobile Device:
    - Use Guidebook App to submit evaluation, or
    - QR Scan application on your mobile device to scan the QR code (below right) before leaving.

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