BY GEOFFREY A. BRYCE

HELPING PMs REDUCE THE IMPACT OF *Complex Legal Risk*

Construction projects often take unexpected detours and many end in expensive, time-consuming, and unpredictable litigation.

Whether you're the CFM of a developer, GC, subcontractor, supply house, or other service provider, one of the most important ways to reduce your legal exposure on projects is to help your PMs comprehend the fundamentals of the projects they manage.

The scope of this article will address some basic contract knowledge and common provisions for CFMs to use as a guide to help PMs reduce the impact of legal risks on their projects.

Contract Documents: The Fundamentals

The very first thing a PM can do to reduce legal risk is to simply read and understand the contract. While it may seem like common sense, oftentimes this is not done until after a problem arises. Instruct PMs to ask: Do I have all the contract documents? What exactly constitutes the contract documents? These questions are significant because those documents will define the responsibilities of the respective parties in any litigation.

Sometimes the contract is specific as to what it encompasses; other times it's ambiguous. If there is any uncertainty about what is included in the contract documents, then the PM should locate and read *all* applicable documents before the project begins. Then, if an issue is spotted, it can be addressed immediately.

If your company uses standard industry contracts (e.g., The American Institute of Architects (AIA), ConsensusDocs, and the Engineers Joint Contract Document Committee (EJCDC)), then your PM should understand how the legal responsibilities are allocated by such contracts.

Understand Flow-Down

Flow-down clauses exist in almost all trade contracts. Often, the GC will flow down the terms and conditions of the contract it has with the owner to its

subcontractors. In most states, these clauses are enforceable. A flow-down clause applies regardless of whether it is a traditional project delivery system (e.g., owner/GC/subcontractors/material suppliers) or other delivery system (e.g., construction managers and multiple prime contractors, etc.)

The purpose is to bind the subcontractors to the same terms and conditions as the GC. However, it is equally important that the subcontract requirements are aligned with the higher-tier contract requirements. Making sure this symmetry is in place before the project starts is critical. The time to find out that there is no symmetry is not after a dispute erupts.

To learn more about flow-down provisions for subcontractors, check out "A CFM's Guide to Drafting Sensible & Useful Subcontracts" by Kenneth B. Franklin, Joy T. Davis & Antony L. Sanacory in the January/February 2014 issue. For a perspective on how GCs can approach flow-down provisions, read "Protecting Your Company from a Rebounding Economy" by Scott G. Wolfe also in that issue.

Ensure the Contract Is Signed

In some instances, the timing of a contract's formation can have very serious consequences. Let's say a subcontractor submits a bid to a GC and the GC gives the subcontractor a verbal "go ahead" without signing the contract. Then, the subcontractor starts on the job and one of its employees gets hurt.

The injured employee sues the GC and owner, but the subcontractor and GC had not yet signed the contract. The GC and subcontractor argue about who is responsible to handle the claim. Is there an indemnity provision? Is there additional insured coverage? Both the GC and subcontractor's PMs should make sure the contract is signed and insurance requirements have been met before starting work.

Common Contract Terms & Conditions to Review with PMs

Now let's address the terms and conditions that frequently appear in litigation, including scope of work disputes, change orders, indemnity, no-damages-for-delay clauses, waiver of lien and claims clauses, pay-if-paid clauses, notice provisions, insurance, terminations, and disputes.

Scope of Work

Some of the biggest contract disputes involve the scope of work. While there may be architectural, structural, civil, and MPE drawings and specifications that accompany a project, that doesn't always mean that the scope of work is sufficiently defined. Many contracts incorporate by reference of other terms and conditions in the contract, which can increase the scope or complexity of the work.

If this additional scope of work was not addressed in bidding, then the contractor may have committed to a scope of work without accurately understanding the complexity (i.e., it may have underpriced the work). PMs should have a complete understanding of the scope of work before the project starts. The sooner scope of work questions are answered, the less likely disputes will arise later.

Change Orders

Change orders are like mini-contracts. There is usually some additional scope of work that was not originally part of the project that is added to (or in some cases subtracted from) the overall scope of work. Many states require different articulations of elements to prove-up a change order.

For any change order, PMs should always read the contract to understand what work was originally required. If a PM receives a verbal request for additional or overtime work, but the contract requires change orders or overtime to be in writing, then the PM must confirm the request in writing. The PM can send an e-mail that states: "On (date), Joe said we should do X. We agreed that we would do X for Y price and it would have no effect on the scheduled completion date of our work."

For more information change orders, read "Practical Recommendations for Documenting & Demonstrating Extra Work Costs" by Frank E. Riggs in the May/June 2009 issue.

Indemnity

It's important to know who you are indemnifying and for what. Traditionally, if Party A indemnifies Party B for A's negligence, then the indemnity agreement is broadly construed. On the other hand, if Party A agrees to indemnify Party B for B's own negligence, then the indemnity agreement is narrowly construed. Many state statutes specifically prohibit the latter form of indemnity.

The CFM can assist the PM by finding out the indemnity rules in the state where the project is located or what law governs the contract. The subcontractor may be indemnifying the GC for its own negligence – a legal risk of which the PM must be aware. The PM should take extra precaution in executing the work because the company's risk of something going wrong increases substantially.

For more on indemnity clauses, read "Indemnification: One Leg of Contract Risk Management" by Jeffrey S. Ammon in the May/June 2013 issue.

No-Damages-for-Delay

One clause that appears as a supplement to many contracts is the no-damages-for-delay clause. Since this can sometimes be a difficult clause to spot, the CFM can assist the PM by requiring a verification that no such clause exists in the contract or that the subcontractor did not strike it out in the bidding process.

Regardless of which side of this clause your company takes, it is important to know whether this clause is operative for the project.

Additionally, there are a number of exceptions to this clause (e.g., bad faith, unreasonable duration of delay, delay not within the contemplation of the parties at time of contracting, inexcusable negligence of design professional); state law will dictate which exceptions, if any, will apply.

For more information about no-damages-for-delay, check out "Rules for Surviving No Damages for Delay" by Frank E. Riggs & Jonathan Y. Yi in the May/June 2013 issue.

Waiver of Liens & Claims

In the payment process, there is typically a waiver of lien rights. It's critical for PMs to consider the scope of the waiver as many lien waiver statements now contain an additional waiver of any claims to date. If your contract requires a waiver of liens and a waiver of claims, what happens if you have a claim? When filling out the application, attempt to strike out the waiver of claims language. If the removal of this clause results in the contractor not getting paid, then identify the timing of your lien rights and follow the contract's dispute clause.

Pay-If-Paid

Another area where CFMs can assist PMs is in understanding pay-if-paid and pay-when-paid clauses. PMs should know the difference between the two and whether or not they are enforced in that project's state, or the enforceability of these provisions if there is a choice of law clause. These clauses are the subject of many court cases and much literature, so it's necessary for the PM to know which clause applies and which clause is enforceable.

For more on this topic, read "Pay-If-Paid Clauses: How You Can Protect Your Company" by Susan L. McGreevy in the May/June 2013 issue.

Notice

In many standard industry contracts there are specific notice requirements that, if not met, would terminate the contractor's right to seek additional compensation for a claim or time to complete the work. Examples of notice events include differing site and project conditions, when a claim arises, delays, and jobsite accidents.

Most standardized industry contracts have notice provisions, but they are not strictly enforced by all courts. It is recommended the PM know which notice provisions are in the contract and when notice must be sent.

Delays

CFMs can also assist PMs in avoiding delays altogether. Asking a few simple questions at the front end of a project, such as the ones listed below, may be helpful in meeting the project timing requirements:

- How many man-hours are we going to need to complete this project?
- What trades are we going to use to accomplish this job?
- What does the project management structure look like?
- Do we have enough in-house skill to complete the project?
- How tight is the schedule?

For many large, complex projects (e.g., power plants, industrial projects, large multi-use structures), there are many more questions.

Liens

Although it seems fundamental, there are situations where the contractor does not know the basics of what lien law applies to the project. The PM should know the basics of the lien law of the state in which the project is located. Most state lien laws are strictly enforced and a poor timing provision or a failure to give proper notice may result in the lien being unenforceable.

Bonds

In most public works projects (and in some private projects) the contracting entity will require the GC, construction manager, or design/builder to furnish payment and performance bonds. Many of these bonds have notice requirements and timing mechanisms for triggering their application. It is important for the PM to understand what triggers those bonds and what to do in the event that circumstances require notice to the surety.

Insurance

Regardless of whether you are an owner, developer, GC, construction manager, subcontractor, or material supplier, understanding your insurance rights and obligations is a must. If the contract between an owner and GC requires that the GC name the owner as an additional insured, then the

GC is responsible for ensuring that the coverages required by the contract are actually supplied by its insurance carrier.

Often, the matching of the coverages with the contract is not always uniform. The PM must confirm that the coverages are consistent with the contract to ensure all requirements have been met. There have been situations where the contractor did not check the coverages, was found to have breached the contract, and was left responsible for the missing coverage.

Similarly, let's assume a contract requires certain coverages and the subcontractor fails to provide the coverage. The project concludes but a jobsite accident case is ongoing after completion. Suddenly, the GC wants the insurance coverage required by the contract and the subcontractor says, "We don't have it." Some courts may rule that the GC waived the contract coverage by waiting too late to assert it, thus the GC's insurance would apply.

Termination

Generally, two kinds of termination exist: one for default and one for convenience. The PM should have some basic understanding of the difference. In many instances, notice must be given prior to termination.

For example, if the GC seeks to terminate a subcontractor for failing to supply enough workers on a job, then it must give that subcontractor several days' written notice so that the subcontractor has an opportunity to cure the lack of manpower. A failure to give a cure notice could mean the GC breached the contract by wrongfully terminating the subcontractor, so after suit is filed, the termination – no matter how justified – is wrongful, and the terminating contractor then faces exposure for breaching the contract.

Disputes

Most PMs know the difference between arbitration and litigation. When reviewing the contract, the PM should know the dispute resolution method so that the procedures identified in the dispute clause are properly followed. Most contracts require some form of mediation before the arbitration begins or suit is filed. In some contracts, the claim must first be referred to the design professional for determination even before mediation is triggered. A failure to follow that step may result in the claim being rejected.

To learn more about dispute resolution, be sure to read "Dispute Resolution Provisions in Construction Contracts" by Antony L. Sanacory in the September/October 2012 issue.

Conclusion

The responsibilities of PMs are many. When they understand the legal framework of a project, PMs are better equipped to spot and address potential legal issues. Early intervention helps reduce the cost and potentially adverse consequences of a developing litigation matter. To keep up with the changing and evolving laws, continuing education is a must. ■

GEOFFREY A. BRYCE is Managing Partner of Bryce, Downey & Lenkov, LLC in Chicago, IL, where he represents developers, owners, facility management companies, architects, GCs, subcontractors, engineers, and material suppliers.

Geoff's litigation practice includes product liability, mechanics liens, insurance coverage, personal injury, property damage, real estate, bankruptcy, breach of contract, restrictive covenant, architectural/engineering malpractice, breach of surety agreement, and delay claims.

He has presented at numerous industry conferences on such topics as change orders, claims, and claims management. A member of CFMA's Chicago Chapter, Geoff also belongs to the ABA, AGC, and AIA. He earned a BA in Marketing and System Analysis from University of Toledo, MS in Taxation from DePaul University in Chicago, IL, and a JD from John Marshall Law School in Chicago, IL.

Phone: 312-377-1501, ext. 121
E-Mail: gbryce@bdlfirm.com
Website: www.bdlfirm.com