



CONSTRUCTION LAW

Expert Analysis

Owner Friendly Modifications To Construction Forms

The American Institute of Architects (AIA) publishes a multitude of contract forms for use on construction projects.

While the AIA attempts to achieve a balance among the interests of owners, architects and contractors, there is a natural bias in favor of architects, which may also redound to the benefit of contractors. However, because of their widespread use, the forms are generally accepted by owners in order to avoid costly negotiations with architects and contractors.

While we endorse the use of AIA forms, we recommend fundamental modifications to protect the interests of the owner. In this article, we will suggest several modifications to the “Standard Form of Agreement Between Owner and Contractor for a Project of Limited Scope” (AIA Document A107-2007), which we believe will provide greater protections to the owner than exist under the form.

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The Contract Sum

The 2007 version of A107 provides for three types of pricing: stipulated sum, cost of the work plus the contractor’s fee, and cost of the work plus the contractor’s fee with a guaranteed maximum price. For the purpose of this article, we will view A107 as a stipulated sum agreement, and reserve the discussion of “cost plus” and “cost plus with GMP” types of agreements.

Having agreed to a stipulated sum, which should be based upon a complete set of construction plans and specifications, the form should be modified to contain a representation that the contractor represents and warrants that the work can be completed for the stipulated sum. Increases in the stipulated sum should be permitted only when procedures related to “changes” are followed. While A107 lays out those

procedures, additional language should be added confirming that no claim can be made for additional compensation unless a change order containing the actual cost of the change or a method for determining the cost is signed in advance by the owner and contractor. Provisions should also be made for the method to be used for determining the cost of the change (such as unit pricing) and the permissible markups for profit and overhead on account of the change.

In order to guard against the untimely submission of claims for changes, language should also be added confirming that late submission of claims constitutes a waiver by the contractor. Further, during the monthly requisition process, the contractor should represent, through its lien waiver, that only changes specifically identified in the waiver may be the subject of a claim. In the absence of listing the pending changes on the lien waiver, the contractor should be deemed to waive a claim for the change.

A107 has detailed procedures for periodic (usually monthly) applications for payment, but language should be

added confirming that lien waivers must accompany the applications for payment and that the owner, as well as the architect, can assert grounds for withholding payments requested. While A107 gives full authority to the architect to approve applications for payment and issue certificates for payment, we add the caveat that the certificate is subject to the approval of the owner. This provides added protection in the event of a disagreement regarding amounts due between the owner and the architect.

Regarding final payment, additional language is necessary providing for final waivers and releases of lien from the contractor and the subcontractors as well as documentation specified by the owner and the architect, such as warranties and operating manuals, “as built” drawings in CADD format and other documentation which may be appropriate as a condition precedent to final payment.

The Work

Numerous provisions throughout A107 identify the work and establish requirements to be met by the contractor for the performance of the work. Several owner friendly modifications should be made to A107 in this regard. For example, the contractor should be obligated to:

- Perform all work not only expressly required by the contract documents but all work which is reasonably inferable therefrom.
- Perform all related work made necessary by a visual inspection of the project.
- Perform work in accordance with the manufacturer’s instructions, industry standards and all applicable laws, rules and regulations where not expressly

stated in the contract documents.

- Notify the architect and owner where the contractor identifies a conflict or ambiguity in the contract documents.
- Accept full responsibility for all conditions at the project that may affect its performance and warrant that the performance of the work will be in conformity with all applicable codes, rules, regulations and ordinances.
- Maintain a full time construction supervisor to coordinate and supervise the work and hold regularly scheduled job meetings to be attended by the contractor, the subcontractors, the owner and the architect.

In regard to subcontractors, A107 should be modified to provide for the conditional assignment of the subcontracts to the owner, which assignment may be exercised in the case of a contractor default. Additionally, the owner should be permitted to communicate with the subcontractors to verify that payments have been appropriately made. A107 should also be modified to provide that the contractor will comply with the provisions of the Prompt Payment Act (Article 35-E of the New York General Business Law) regarding the timeliness of payments to subcontractors.

While A107 has provisions relating to the correction of nonconforming work and provides for a one year warranty, the form should be modified to increase the warranty for a limited period of time following the performance of corrective work. It is also helpful to confirm that the one year warranty is not to the exclusion of the full six-year statute of limitations for the assertion of claims by the owner against the contractor for nonconforming work.

The Role of the Architect

As would be expected, A107 inserts the architect into the construction process in numerous ways and, in our view, goes too far. For example, the architect has the exclusive right to pass on amounts due the contractor under applications for payment. We modify these provisions by giving the owner the right of review and approval.

A107 also establishes the architect as the initial decision maker with respect to claims and disputes relating to the contract—including those involving an error or omission by the architect. This places the architect in an obvious conflict of interest position and we remove the concept of the architect as the initial decision maker. We also eliminate the requirement that the architect “certify” that sufficient cause exists for the owner to terminate the contractor for cause.

Time and Scheduling

A107 contains dates for the commencement and substantial completion of the project; however, an essential element missing from the form is the requirement that the contractor “accelerate” the work in the event specific milestone dates (e.g., erecting steel, closing in building, completing plumbing) are not met, by adding additional personnel or working overtime—all at the cost of the contractor. Rather than waiting until the end of the projected time period for construction to see that the schedule has not been met (and fight over liquidated or other delays damages), delays should be addressed during the course of the project, and lost time made up to enable the project to return to the schedule.

The importance of an acceleration

clause is highlighted by the mutual waiver of consequential damages contained in A107. Regarding the owner, damages for rental expenses, lost income and profit and financing costs are waived and the owner's best protection against delay damages is to prevent them by strictly enforcing the scheduling requirements. While the owner may seek to strike the waiver, most contractors and their counsel refuse to do so and, in certain cases, would prefer liquidated damages rather than be exposed to consequential damages. (Contractors also consider liquidated damages an anathema, leaving the owner with the protection of the acceleration clause and, of course, any actual damages incurred as a result of delay, such as additional fees to the architect because of the delay.)

Delays can also result from the actions or inactions of the owner or its architect, for whose acts the owner is responsible to the contractor. In order to guard against monetary claims for delay by the contractor against the owner, a "no damages for delay" provision should be included in the contract by limiting the contractor's remedy for delay exclusively to an extension of the contract time, not an increase in the contract sum. The mutual waiver of consequential damages also limits the contractor's ability to recover indirect expenses, such as home office overhead and lost profit as a result of owner delays.

Termination for Convenience

A107 contains a termination for convenience clause for the benefit of the owner, which eliminates the need to

prove cause and allows for an amicable parting of the ways. Of course, if this clause is exercised, the owner will have no recourse against the contractor for defaults which may have occurred relating to nonperformance and it may be problematical to recover damages for defective work.

A107, however, allows the contractor to recover unearned profit and overhead on work not executed. We strike this clause and provide that the contractor is paid for work performed, calculated in accordance with the existing schedule values (in order to avoid claims of quantum meruit). Where appropriate, we may allow for the recovery of demobilization costs the contractor may incur in terminating operations.

While the AIA attempts to achieve a balance among the interests of owners, architects and contractors, there is a natural bias in favor of architects, which may also rebound to the benefit of contractors.

Indemnity and Insurance

We depart entirely from A107 when it comes to indemnity and insurance by adding a separate rider. Regarding indemnity, we expand the provisions by including an indemnity covering economic losses arising from any breach of contract (which are not covered by insurance), such as fines, violations and mechanic's liens. We also provide for the recovery of attorney's fees incurred in connection with the enforcement of the indemnity.

Our insurance rider contains far more extensive provisions than recited in A107, including suggested coverages and limits and makes reference to current insurance industry forms. The rider, however, must be reviewed and approved by each owner's insurance consultant or broker, inasmuch as we believe counsel should not pass on final insurance coverage and limits required by an owner.

Conclusion

We have only touched on the major modifications to A107 but it should be apparent that, while A107 is a useful base, owners and their counsel should be prudent in its use.

Issues relating to cost, quality of work, time, the role of the architect, termination, and insurance and indemnity must be addressed in order to afford owners the greatest protection.