

THE ACADEMY OF ELECTRICAL CONTRACTING

Paper Presented by

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Are Contract Documents Really Found Under Cabbage Leaves?

April 1986

ARE CONTRACT DOCUMENTS REALLY FOUND UNDER CABBAGE LEAVES?

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Everyone knows that contract documents are not delivered by storks, because there are few storks but an abundance of contract documents in America. In fact the genesis of most contract documents other than technical specifications in Divisions 2 through 16 is unknown to most people. How many of the contracts you have signed over the years have you or your attorney helped write? General conditions and supplementary conditions appear with the drawings and specifications when bids are solicited. Contractor-subcontractor agreement forms are likely to appear only after costs have been estimated and bids submitted even though the terms of these agreements have a profound effect on costs. More often than not, you see subcontract agreements after they have been filled in by your customer and you get the strong feeling that if you do not want to sign them the way they are, one of your competitors will.

Some contract documents seem to have so many "gene defects" that one wonders whether they were the product of any normal process or were, in fact, found under a cabbage leaf where they had sprung up like toadstools. References to contract documents in this paper will be to the general and supplementary conditions, owner-contractor agreements and subcontract agreements and not to the technical specifications or plans. Although the drawings and technical specifications tell you what

has to be done, the other documents tell what will happen if you or others don't do it right.

Being optimists, contractors and estimators generally assume at the time of taking off a job that everything will go fine and that the main costs to be reckoned with are those incurred in complying with the drawings and technical specifications. Unfortunately, however, construction projects are often ruled by Murphy's Law--"If anything can go wrong, it will." All sorts of potential costs lurk in the convoluted verbiage of general and supplementary conditions, which may get too little attention at estimating time. This is understandable; whether many of these costs ever occur, and in what magnitude, will be determined largely by future and apparently unforeseeable events. Under the law, however, you may be liable for damages to others or not relieved from damages to your firm for events that you or another bidder could have contemplated at the time of entering into the contract. The probable intent of the two parties to the agreement may be judged on how a reasonably intelligent person who is knowledgeable of the normal usage of words in the trade and surrounding circumstances at the time of bidding would read the contract documents as a whole. This is probably some place between the thinking of the optimistic estimator and a believer that Murphy's Law always applies.

Contract documents should promote harmonious and efficient cooperation to accomplish the objectives of both parties and not to entrap the unwary. In practice, however, carelessly worded language and ambiguities often do entrap one party or the other because the parties were unknowingly far apart in their

contemplation of what the words meant when the job was bid and the contract signed. The fact is, contract documents did not spring up like toadstools and they were not discovered under cabbage leaves. At some time or another, most of them were meticulously crafted by someone with the intention either to promote harmony or to gain advantage for one party over the other. When craftsmanship is not evident, it is probably because the writers either did not really understand construction or tried to "improve" on some tested standard form which did not give them all the advantages they wanted.

The Business Roundtable's Construction Industry Cost Effectiveness Project Report on "Contractual Arrangements" urges owners, who have the most say about the wording of contract documents, to allocate risk according to the party's relative ability to control the factors that create risks. Obviously, the party best able to mitigate damages will then have an incentive to do so and can judge the magnitude of the unmitigated risk. No matter what the incentive to the other party, there is little he can do if the causative factors are beyond his control.

EXCULPATORY CLAUSES

By excusing one party from liability he could control by dumping it on the other, exculpatory clauses are examples of improper risk allocation. Contract documents that contain them are not only unfair, they are uneconomic. Bidders who have to guess at the possible cost of risks over which they have no control will have to include significant contingency factors in their bids, and these bid additions will cost the other party even if the event does not occur. Moreover, courts and

arbitrators may refuse to impose exculpatory clauses unless it is clear that the victim knew explicitly what he was signing.

Indemnity or hold harmless clauses are often exculpatory because they excuse one party from consequences for his acts by requiring the other party to indemnify him from all loss, even if negligence of the party being indemnified were wholly, or in large part, the cause of the damage. Repetition or strengthening of indemnity clauses in subcontracts and sub-subcontracts passes the liability down to the last party that contracts to do any work on the project. Prudent contractors and subcontractors make sure that their insurance agents see the contracts they want to sign and provide adequate contractual liability insurance. In the future, however, contractual liability insurance against the risks of broad form--and perhaps even intermediate form--indemnity clauses may be difficult to obtain.

No-damage-for-delay clauses are gaining in popularity with owners who are alarmed when they find that damages for delays caused by design errors and omissions, excessive change orders, owner interference, and other problems over which someone besides the contractor has control can be excessively costly. When delays caused by the owner exceed those that could reasonably have been contemplated when bidding, courts may refuse to impose the clause. The owner stands a risk of paying twice: first in cushioned bid prices, and second in losing the case in court.

"Scope" documents may state that the contract documents indicate the general scope of the project but do not necessarily indicate or describe all work required for full performance and completion. The contractor is contractually required to furnish

all items required for the proper execution and completion of the work, and the decision of the architect as to the work included within the scope of the document is final and binding.

FEDERAL CONTRACTS

Much as some contractors do not like to perform Federal work, it must be recognized that Form 23-A, the standard government construction contract, is a fair document and the genesis of innovations which are now taken for granted as being needed for economically sound contracts. It includes some clauses now taken for granted but once unprecedented: the differing site conditions clause which lets contractors build instead of gamble on what is unknown to everyone; constructive changes which give you the same benefits as a change order when the government's action requires unplanned actions; equitable adjustments for cost or time increases required for performance of any part of the work, whether or not changed. It was this last clause that opened the way for often successful claims for impact or ripple damages and unabsorbed or extended overhead. By contrast, some private contract documents allow only for reimbursement of changes ordered and not those caused by actions or inactions of the customer.

Robert A. Stone, Deputy Assistant Secretary of Defense, in a February 1982 memorandum to assistant secretaries of the Army, Navy and Air Force, stated the philosophy of the Department of Defense that led it to discontinue the routine use of retainage on construction projects:

"Interest on commercial construction loans remains high, and we must expect that the carrying cost on retained

payments will be included in contract bids. The current construction contract retainage practices are likely to add costs to our construction program, therefore, and do not necessarily improve the quality or utility of the project. By controlling retainage on our contracts, we should realize economic savings in Department of Defense construction.

* * *

"This policy on retainage must be complemented by prompt and positive final payment procedure after a contractor has completed all contract requirements. This should improve our perception as a preferred customer by the construction industry and tend to reduce our contract construction costs even more."

Undoubtedly, the thinking on eliminating "carrying costs" and improving contractors' perceptions of the Defense Department as a preferred customer led originally to the lack of use of exculpatory clauses and provision of such clauses as those pertaining to constructive changes, constructive acceleration, constructive suspension and differing site conditions.

AIA DOCUMENTS

Contract documents used in private and non-federal public construction are not as uniformly reasonable, but current AIA forms are. The American Institute of Architects has published AIA Document A201, General Conditions of the Contract for Construction, since 1911. The thirteenth edition was published in August of 1976, and the fourteenth is expected in December of 1986. AIA Document A401, Subcontract, Standard Form of Agreement

Between Contractor and Subcontractor, was first published in 1915, and the eleventh edition in 1978. The twelfth edition will be ready by December 1986. With motives similar to those of the government, the AIA makes a real effort to develop documents that are fair to the owner, contractor, and subcontractor alike. The architects on the AIA Documents Committee spend many hours with their attorneys and industry spokesmen in studying proposed changes submitted by organizations like NECA and the Associated Specialty Contractors, to decide on wording for A201, A401 and other documents. The goal is language that is unambiguous, efficient in its application, consistent with the common law of contracts and with the few applicable Federal and state statutes, and equitable. Since they are written by architects, some AIA documents do excuse architects from some liability they probably should have, but the effect is to shift risks to owners more than to contractors.

Because some electrical contractors are prime contractors using A201 and all are greatly affected by it through flow-through provisions to subcontracts, I have been greatly involved since 1974 in the development of the 1976 and 1986 editions of A201; the 1978 and 1986 editions of A401; the new A312 surety bond form; A511, Guide to Supplementary Conditions, and the Short Form Contract, A107. For the 1986 edition, we started collecting and evaluating proposals from contractors as long ago as 1980. On behalf of NECA and other ASC affiliates, the Associated Specialty Contractors, Inc. proposed 70 some changes from the 1976 edition of A201 and subsequently has proposed many changes to each of the various drafts prepared by

AIA. I have met several times with the Documents Committee to explain our positions and to "negotiate" mutually acceptable language. The groups that work most with the AIA are the Associated General Contractors, Associated Specialty Contractors, and American Subcontractors Association, the latter two meeting jointly and adopting a unified position with the AIA Documents Committee. Occasional meetings are also held by AIA with associations of surety companies, surety bond producers, insurance companies, and a joint committee of consulting engineering societies. Although no one gets everything he wants or prevents everything he doesn't want, the product of these efforts is as close to an industry consensus document as is possible to attain. The AIA tries diligently to earn the approval and endorsement of the contractors' associations.

BENEFITS OF STANDARDIZED DOCUMENTS

Standardized contract documents such as Form 23-A, A201 and A401 enable contractors, owners, and architects to know their rights and obligations, the deadlines for giving notices, provisions for change orders, disputes and many other matters without having to study the entire general conditions for every job. Legal precedents have already been established on some of the language so some litigation and arbitration will not be demanded by probable losers. Fewer mistakes due to ambiguities will be made with standard contracts. Associated Specialty Contractors or NECA are able to publish commentaries on AIA forms, calling particular attention to benefits and potential problem areas.

Some state contracting agencies use AIA documents even though

they may change them and reprint them under a different title, but contractors who have not become familiar with those documents do not have the same security of knowing they have studied the document before. Furthermore, some state governments take two or three years after a new standard form has been produced to start using it.

SUBCONTRACTS

Subcontract agreements are an entirely different matter. Although A401 is fair, excellent, widely used and, in fact, is the third biggest seller in the AIA's inventory, with over 100,000 copies a year being sold, the AGC recommends against its use, and some general contractors instinctively suspect it because it has the AIA's name on it.

In the last 10 years, long and strenuous negotiations of ASC, ASA, and AGC to develop a contracting industry standard subcontract form resulted twice in committee agreements which AGC refused to ratify and a stalemate--particularly over payment terms--in the last effort. Twice after these negotiations failed, AGC published a unilateral form, the most recent being AGC Form 600, which ASC and ASA have criticized in a commentary. Form 600 contains numerous exculpatory and inequitable clauses. Of course, AGC is well aware of the fact that many subcontractors will sign such agreements, often without changing them, regardless of ASC commentaries. The general contractor has a vastly superior bargaining position when he has the job and the price has been set, while the subcontractors are trying to get the job they have spent a great deal of money and time estimating.

As flawed as it is, AGC Form 600 is considerably better than most of the subcontract forms developed by individual contractors and by various AGC chapters. A research project in Pennsylvania several years ago for a master's degree thesis revealed considerably more use of A401's and 1966 AGC-ASC subcontract agreements (also known as AGC-CMSCI agreements) than the AGC subcontract form then in use. But individual general contractors' forms were prevalent.

Lack of knowledge when bidding of the terms that the successful general contractor will want in the subcontract is a real problem. Probably at no other commercial venture are people thus shooting in the dark hoping to hit the target before it hits them to the extent of subcontractors' bidding. True, the subcontractor has a right to negotiate on the terms of the subcontract or to refuse to sign it. Legally, a subcontractor is obligated to perform at the amount bid if the general contractor used the bid in preparing the general bid, but this would not likely be construed by a court or arbitrator as requiring a subcontractor to sign any contract the general contractor demanded and perform the work at the bid price. It could fairly safely be assumed that this obligation would not require the subcontractor to agree to more onerous terms of a subcontract agreement than the terms in the owner-contractor agreement available to the subcontractor when bidding.

ASC recommends substitution of A401 for unfair subcontracts offered by general contractors, including AGC Form 600. The 1966 AGC-ASC form, which is still recognized by ASC and has never been abrogated by AGC, is another good substitution. A third

arrangement is to attach the type of addendum included in the commentary on Form 600 published by ASC and ASA which modifies the terms of Form 600. A similar addendum could be used for any other undesirable subcontract form. If the general contractor accepts the addendum, it amends the agreement he has proffered; and if he puts it in his file and directs you to proceed with the job without rejecting the addendum in writing, it is still binding.

Individually, general contractors are often more willing to accept changes in their proposed subcontract documents than might be expected. Frequently they use contract documents that were developed by someone else and may even have the impression that some of the legal-sounding language harmful to subcontractors is necessary to make it a legal document. If a general contractor likes a particular subcontractor's price and performance, he might well accept wording changes proposed by that subcontractor, especially if the proposals are made about the time the subcontractor needs to be brought onto the job.

There is little chance that another standard subcontract form that is acceptable both to NECA and its chapters and to the AGC and its chapters can ever be negotiated. The main sticking point is the payment clause. General contractors' associations want payment clauses that are exculpatory, requiring the contractor to pay the subcontractor only if and after the general contractor has been paid. With such a conditional payment clause, the subcontractor's payment may often be delayed because of disputes between the owner and the general contractor having nothing to do with the subcontract.

Although many general contractors accept their responsibility to pay their subcontractors on time, they are concerned about a mandatory requirement that they "bank the job," and the problems that could cause them in the event of an owner default. Furthermore, those general contractors who accept this responsibility seriously and might be willing to put it into their own individual contract forms are unable or unwilling to convince enough of their fellow AGC members, particularly broker-type general contractors, to accept unconditional payment language in standard subcontract forms. The corollary is that although individual electrical contractors might be willing to sign agreements with certain general contractors doing work for known owners that contain conditional payment clauses, it would not be appropriate for NECA or ASC to agree that such clauses are acceptable for universal use in standard agreements. Somewhat ambiguous payment language is often interpreted by courts favorably to subcontractors because of the common law rule that controversies over ambiguous language will be settled against the proposer of the agreement form, usually the general contractor. If it were a standard form to which ASC or NECA were a party, we would be equally responsible for the ambiguity, and this rule would no longer apply.

Contract documents are a means to an end, but not the end. General conditions are often almost ignored when everything is harmonious and going smoothly. It is only when claims and disputes arise that recourse to the language is necessary, and at that time the agreement language can become more important than the language of the technical specifications. Every contractor

and subcontractor, estimator, and project manager should be thoroughly conversant with the contract documents used to bid and administer projects. The ASC Contract Documents book provides helpful guidance, and a new edition will be published when the new AIA documents have been released. Read what your rights and obligations are, and decide whether you can afford to sign the contract. Exculpatory clauses should be discussed with your insurance agent or an attorney before you sign an agreement containing them. Murphy's Law does not always work when you've made the right preparations.