



In the Board Room – Construction Contracts

September 27, 2023

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General Overview:

1. Introduction
2. The Importance of Planning
3. Delivery Methods
4. AIA Contract Documents
5. Contract Drafting
6. Additional Insights



The Importance of Planning



The Importance of Planning

“Before anything else, preparation is the key to success.”

– Alexander Graham Bell



The Importance of Planning

- Even before designing the project, you have to start planning.
- Important Questions:
 - What are we building?
 - What is the time?
 - How much are we spending?
 - Who are we building with?

But how do we know what we need?!



The Importance of Planning (cont.)

- RFP for initial design and scoping.
- You may receive solicitations and recommendations.
- An RFP may not be necessary if a county already knows its scope.



The Importance of Planning (cont.)

“Who are we building with?” is a key question:

- Preliminary planning may set expectations for future work.
- Business models challenges.
- What is the County locking itself into?
- Key point: Plan during the planning stage, but do not agree to agree later!



The Importance of Planning (cont.)

- Architectural programming: Establishing the parameters of the design and set the stage for the scope of work.
 - The overall extent of work.
 - Memorialized in plans, specifications and project requirements.
- Components:
 - Building site – what are the challenges?
 - What is the primary function? Any specific spaces that are statutorily required?
 - Types of spaces, requirements for adjacency to each other, and type of use.
 - Mechanical and electrical needs
 - Other special requirements



The Importance of Planning (cont.)

Enter the team...



Some Team Lessons From the Trenches

- Form an oversight committee – continuous oversight (NOT micromanagement) and learned expertise.
- Appoint an internal single point of contact responsible for contract administration and to serve as direct report to committee.
- Other team members:
 - Owner's Representative
 - Legal counsel



Other Lessons From the Trenches

- Understand that reference checks are difficult – you may not hear the whole story.
- Talk to other counties.
- Provide updates to county board members and the public educated about the process and next steps.



Project Delivery Methods



Project Delivery Overview:

- Definition: The process by which all the procedures and components of designing and building a facility are organized and put together in an agreement that results in a completed project.
- Key considerations:
 - Time
 - Cost
 - Quality
 - Scope
 - Function
 - Safety



Project Delivery Overview: Traditional - Architect Designs and Contractor Builds

1. Lineal approach: First comes the architect, then comes the contractor.
2. This method is not used often in commercial or institutional projects unless the project is very small. The main issue with this delivery method is that the risk of cost over-runs or schedule delays is mostly transferred to the owner.
 - Often plans and specifications are not as detailed as they should be resulting in the contractor issuing Requests for Information ("RFI") to the architect for clarification. The time to answer these RFIs slows the construction schedule.
 - The contractor may find that the plans and specifications are not constructible or require work that was not apparent when the project started. If the contractor is on a time and materials basis, this could cause the project cost to increase because of change orders. The architect is not liable for cost estimates that are not accurate unless the contract states otherwise.
 - Owner is oftentimes required to certify plans and specs.
3. One reason for using this delivery method is that the architect's and contractor's fees are often lower than in a construction manager delivery method.
4. This is the traditional project delivery method for public works and the easiest to fit in the competitive bidding laws – i.e., design, bid, build.



Project Delivery Method: Construction Manager

- Common Misconception is that there is only one variation of a CM relationship – there are actually two:
 - CM at Risk
 - Traditionally, CM is contracted with Owner
 - May have separate contract with Architect
 - CM delivers at a guaranteed maximum price (GMP)
 - Many other variations of the contractual relationship
 - Agency CM
 - CM *advises* owner in its contractual relationships with Architect and Contractor
 - CM is not at risk for the budget, the schedule or the performance of the work.
 - *Not a true delivery method*



Project Delivery Method: Construction Manager at Risk

Primary Benefit: Contractor/CM is involved from the beginning

- Since the contractor is involved with the design while it is being created, the contractor should have the opportunity to clarify its questions and suggest cheaper or faster ways to construct the project. If the contractor does its job, it will reduce or eliminate RFIs and Change Orders.
- The contractor, rather than the architect, develops costs estimates for the project as the design proceeds. The contractor usually has a better idea of cost than an architect. The contractor becomes bound to its cost estimates when it delivers a Guaranteed Maximum Price ("GMP") Contract.



Project Delivery Method: Construction Manager at Risk (cont.)

- The owner is better protected from cost overruns by the GMP and has leverage to cause the contractor to put more workers on the project if it is behind schedule.
- If the contractor and architect work together as envisioned by this platform, then the extra costs of fees may be offset by having the project come in on-time and within budget. In any case, the risk to the owner of cost over-runs is significantly reduced.
- BEWARE: This project delivery method does not fit nicely in the competitive bidding laws – great care must be taken to ensure compliance (i.e., TALK TO YOUR CORPORATION COUNSEL!!)
- Remember: *“The object of the game is to mitigate risks as much as possible.”*
 - *Contract terms are essential.*



Project Delivery Method: Design-Build

- Growing in popularity – especially on larger projects.
- Under this method, the Owner engages one entity to act as architect and contractor.
- The primary advantage to this method is the single point of contact to which the Owner can turn with issues.
- The primary disadvantage is the “all eggs in one basket” syndrome. There is a lack of checks and balances – if the single point of contact fails, the project fails.
- This project delivery method is NOT ALLOWED under Wisconsin bidding laws unless the entire project is competitively bid or statutorily authorized.
 - Alternative: Design-build, but structure the contract to meet bidding laws.



AIA Contract Documents



AIA Documents: Overview

- Series of contract documents intended to work together.
- The AIA document used will be determined by the project delivery method and parties involved.
- **WARNING:** AIA documents appear easy, but are filled with ambiguities and loopholes.



AIA Documents: Famous Quotes

- “These are never modified!”
- “This is standard. Having your lawyer review will waste time and cost you more money.”
- “These have been around since 1911!”
- “Why make it so difficult? Use the form!”



AIA Documents: General Points

- Generally, the AIA documents are favorable first to the Architect, next the Construction Contractor, and finally the Owner.
- Reality: Complicated documents and intended to work in conjunction with other AIA documents.
- All AIA documents can be modified.
- All revisions should be shown, available when using AIA software.
- Key point: Early review and contract planning is essential.



AIA Document Examples: A-Series – Owner and Contractor

A101: Standard form of agreement between Owner and Contractor where the basis of payment is a stipulated sum

- Used when price is stipulated sum (fixed price)

A102: Agreement between Owner and Contractor where payment is cost of work plus a fee with a GMP

- Typically used on large projects requiring a guaranteed maximum price where payment is based on Contractor's cost of the work plus a fee

A103: Agreement between Owner and Contractor where basis of payment is cost of work plus a fee without a GMP

- Used on large projects where the cost is not fully known at commencement of construction



AIA Document Examples: A-Series - Owner and Contractor (cont.)

A105: Shared form agreement between Owner and Contractor

- Used on smaller, less complex commercial projects
- Lump sum/stipulated sum/fixed price

A121: Agreement between Owner and Contractor when work is provided under multiple work orders

- Used when Contractor's scope of work will be specified subsequently with one or more work orders

A133: Agreement between Owner and Construction Manager as Constructor (basis of payment cost of the work plus a fee with a GMP)

- Used on projects where Construction Manager serves as advisor to the Owner and assumes financial responsibility for construction of the project
- GMP Amendment is key



AIA Document Examples: A-Series - Owner and Contractor (cont.)

A201: General conditions of the contract for construction

- Sets the rights, responsibilities and relationships of the Owner, Contractor and Architect.
- Incorporated and referenced into other agreements.
- Used as an umbrella document over the project.
- Key document.



AIA Document Examples: B-Series - Owner and Architect

B101: Agreement between Owner and Architect

- Services divided into basic, supplemental and additional services.
- Can be used with a variety of compensation methods, including percentage of budget for construction and stipulated sum.



AIA Document Examples: B-Series - Owner and Architect (cont.)

B105: Agreement between Owner and Architect.

- Used on small projects.

B121: Master agreement between Owner and Architect who is providing multiple services under multiple service orders.

- This establishes a master agreement with multiple service orders.

B132: Agreement between Owner and Architect with Construction Manager as advisor.

- This contract is used between Owner and Architect on large projects when Construction Manager is an advisor.



AIA Document Examples: B-Series - Owner and Architect (cont.)

B133: Standard form of agreement between Owner and Architect with Contractor as Constructor.

- Most frequently used in CM at Risk, GMP projects.
- Defines Architect's traditional scope of services for design and construction contract administration.

B201: Standard form for Architect's service for design and construction contract administration.



Contract Considerations



Remember: *“The object of the game is to mitigate risk as much as possible.”*

The devil is in the details...



Key terms to mitigate risk:

- Indemnification provisions
- What is a “change order”?
- Who is contracting with subs?
- Contingency fund usage and control
- “Profits” upon termination

Other key drafting considerations for on-budget and on-time delivery...



1. Controlling bids from subcontractors to bring a project in below the GMP

- A contractor may win a bid with the lowest Guaranteed Maximum Bid but it has a financial interest in bringing a project in as close to that GMP as possible, rather than under it, because its fee is often a percentage of the cost of the work.
- Under the standard AIA contract, the contractor has complete control of the subcontracting bid process. Much, if not all, of the work might be done by a subcontractor. Contractors usually have favorite subs and might have hidden financial arrangements with them (for example, allowing them to bid higher on one project to get a lower bid on another project or “trade contractors”). Bids might come in at a price the contractor wants. The contractor usually gets a mark-up on the cost of the subcontractors work.



1. Controlling bids from subcontractors to bring a project in below the GMP (cont.)

- Modify the contract to require sealed bids from multiple contractors that are given directly to the owner. Specify the amount of mark-up the contractor may receive on the subcontractor's invoice. Require that no contractor fee be taken on the mark-up.
- Practical suggestion: The review of the bids by an owner's representative may reduce your cost if you do not have an experienced in-house facilities group who know material and labor costs. The rep may find that all of the bids are above market and recommend a sub that can do the work for less.



2. Controlling the cost of self-performed work

- The contractor may self-perform work rather than have a subcontractor do it (for example, installing dry-wall).
- The standard AIA contract allows the contractor to self-perform work at a cost that is not subject to competitive bidding. This allows the contractor to make self-performed work a profit center with inflated costs for the work.
- Require the contractor to bid on self-performed work with other subs in the sealed bid process.



3. Controlling the cost of contractor supplied rental equipment

- It is typical for a contractor to supply the project with equipment that it owns and charge a rental rate for the equipment. This is another profit-center for the contractor.
- The standard AIA contract allows the contractor to charge whatever it wants.
- There are many modifications that must be made to this section to control costs. One common modification is to tie the contractor's rental rates to the AED (Associated Equipment Distributors) Green Book of national rental rates for equipment.



4. Controlling the Cost of Change Orders

- Change Orders are not always bad!
- Change Orders modify the scope of work that is being done and may increase the GMP and extend the construction schedule.
- The standard AIA contract has no real controls on the cost of a Change Order. Change Orders are probably the single most popular way for a contractor to increase the agreed upon GMP. It is a substantial profit center. Contractors can inflate the cost of labor and materials and take substantial mark-ups.
 - Warning: Other contract options and processes result in a Change Order.
- Limit the contractor's mark-up on Change Orders.
- Create a process for reviewing and approving change orders.



4. Controlling the Cost of Change Orders (cont.)

- Practical Tip No. 1: Pay careful attention to what has the effect of a “change order” in the contract.
- Practical Tip No. 2: Planning! More time spent in the pre-construction phase with actions such as team meetings with HVAC, electrical and other major subcontractors tend to significantly reduce the amount of Change Orders encountered during construction.
- Practical Tip No. 3: An owner should have the clarifications and assumptions in the GMP amendment professionally reviewed to avoid Change Orders during construction for items the owner thought were included.



5. Controlling the cost of “general requirements”

- General Requirements are the cost of items needed for the construction process (portable toilets, fencing, etc.) and the cost of supervisory personnel. It is also a profit center.
- The standard AIA contract puts no limits on General Requirements. It is not bid out and the contractor can increase the cost during construction.
- General Requirements should be fixed as a lump sum when the GMP Amendment is signed.
- Practical Tip: Do not permit additional General Requirements to be added to Change Orders unless it can be demonstrated that the Change Order actually increases the cost of the General Requirements.



6. Controlling the cost of the dispute resolution process

- The standard AIA contract requires the parties to refer the dispute to the Initial Decision Maker, then enter into non-binding mediation, with the American Arbitration Association as the default mediator, and, if that fails, to binding arbitration, with the American Arbitration Association as the default arbitrator.
- This process is so long, so unfavorable and so expensive to the owner as to prevent most owners from starting it and to give up on claims. The contractor, on the other hand, merely has to stop working if the owner fails to make payments to enforce its claims. No owner can afford a stoppage of the work.
- The standard dispute resolution provisions may be modified in any AIA contract.



6. Controlling the cost of the dispute resolution process (cont.)

- The entire section should be deleted and provisions should be inserted allowing the owner to choose litigation.
- Be careful of arbitration provisions.
- Practical tip: Require the litigation to be held in the circuit court of your county.



7. Controlling the use of the plans and specifications

- The architect owns the plans and specifications it develops for a project in the standard AIA contract. The contract provides that the owner must use the same architect if it renovates the building in the future or the owner cannot use the plans and specifications and cannot update them. The owner cannot easily choose the best architect for the renovation under these terms.
- Obtain a permanent license to do what the owner wants (regardless of any payment to the architect) and delete the requirement that the same architect must be used if the plans and specifications will be modified.
- Practical tip: Always require a record set of plans and specifications from the architect when the work is done. These are updated to show all of the modifications to the documents that were made during construction. It is essential to have the record drawings to guide future work on the building safely and with a minimum of cost.



8. Obtain builders risk insurance that conforms to the contract

- The standard AIA contract requires the owner to obtain builder's risk insurance and, if the owner doesn't do so, the contractor will obtain it and charge the cost to the owner. Builder's risk insurance will pay for damage to the building by such causes as fire, regardless of how the fire started. It permits the project to proceed since it pays for the repairs. Otherwise, the project could be stalled for years while the matter is litigated.
- The contract requires the insurance to be maintained until the later of final payment or until no one working on the project (contractor, subs, etc.) has a financial interest. These requirements are often at odds with the insurance owners carry. Revise the contract to conform to the coverage requirements of the owner's policy. Otherwise, the owner could be liable to pay for an uninsured loss.
- Practical tip: Sometimes an owner's existing policies of insurance allow the addition of builder's risk for all projects undertaken by the owner so an owner does not have to insure each project separately.



9. Be aware of consequential damage clauses

- Consequential damages are the damages an owner incurs in addition to the costs of repairing or replacing damaged property. For example, if a new building will not open on time because of the contractor's negligence, the owner may have to rent interim space, pay movers, install temporary wiring and IT equipment, etc.
- The standard AIA contract transfers the cost of consequential damages arising because of the contractor's negligence to the owner. Although consequential damages are much rarer than direct damages, if it happens it is very difficult to explain to an owner's constituency why they are paying for a contractor's negligence.
- Modify the provision so that damages are not waived by the owner.
- Practical tip: Sometimes it's acceptable to cap the damages to the limits of the contractor's insurance. Obtain expert advice to make these modifications.



10. The contract form and timing

- AIA is not the only option but be wary of other options.
- When to enter into the contract may be a challenge.
 - Planning?
 - Preliminary design?
 - Construction?



Additional Comment



Questions?



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