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CONTRACT CLAUSES TO WATCH OUT FOR

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Association of Women Contractors

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Presentation Roadmap

- What's in your subcontract?
- Terms to look for in your subcontract.
 - Indemnity
 - Notice Provisions
 - No Price Escalation Clauses
 - No Damage for Delay
 - Suspension & Termination
 - Contingent Pay Clauses
- Q&A

What's in your subcontract?

- Your bid is accepted and you are awarded the job.
- You receive a copy of a blank subcontract form.
- Do you know what is in your contract?

What's in your subcontract?

- Almost every subcontract will contain a flow down clause.
- Example: AIA A401 – 2017.

§ 1.1 The Subcontract Documents consist of (1) this Agreement; (2) the Prime Contract, consisting of the Agreement between the Owner and Contractor and the other Contract Documents enumerated therein . . .

* * *

§ 1.3 Except to the extent of a conflict with a specific term or condition contained in the Subcontract Documents, the General Conditions governing this Subcontract shall be the AIA Document A201-2017, General Conditions of the Contract for Construction.

What's in your subcontract?

- Many important provisions won't actually appear in your subcontract.
- Look at the prime contract and other documents incorporated by reference.
 - Tip: Ask for unredacted copy of GC contract with Owner.
- If you have leverage, ensure your subcontract agreement controls in case of a conflict with the GC contract.
- Ensure any lower-tier subcontractors sign corresponding agreements containing flow-down language.

What's in your subcontract?

- It is incumbent on the subcontractor to carefully review the contract before signing.
- Negotiate allocation of risk on private contracts during the contracting process following award of the subcontract.
- Public contracts are much more difficult to negotiate from a practical perspective.
- You cannot negotiate or change the terms of your contract after you've signed it.

Terms to look for in your subcontract

- Indemnity
- Notice Provisions
- No Price Escalation Clauses
- No Damage for Delay
- Suspension & Termination
- Contingent Pay Clauses

Indemnity

- Scope of indemnity determines your proportion of potential liability for claims, losses and expenses.
- Negotiate to minimize indemnity at least to the extent of your proportionate liability.

Indemnity - Example

- AIA § A401 4.7.1 To the fullest extent permitted by law, the Subcontractor shall indemnify and hold harmless the Owner, Contractor, Architect, Architect's consultants, and agents and employees of any of them from claims, damages, losses, and expenses, including but not limited to attorney's fees, arising out of or resulting from performance of Subcontractor's Work under this Subcontract...attributable to bodily injury, sickness, disease or death, or to injury to or destruction of tangible property (other than the Work itself)...
- A broadly drafted indemnity clause can make the subcontractor fully responsible for the indemnity even if the a portion of the fault is attributable to the GC or Owner.

Notice Provisions

- Carefully following the requirements of the notice provisions preserves the contractor's ability to seek a change order or bring a claim.
- Two main components of notice
 - Timing
 - Means of Transmission
- Consequences of noncompliance

Notice Provisions – Timing

- Two possibilities
 - Certain number of days from the event giving rise to the notice OR
 - In time for the contractor to notify the owner
 - AIA A401§ 5.3. The Subcontractor shall make all Claims promptly to the Contractor for additional cost, extensions of time and damages for delays, or other causes in accordance with the Subcontract Documents. A Claim which will affect or become part of a Claim which the Contractor is required to make under the Prime Contract within a specified time period or in a specified manner shall be made in sufficient time to permit the Contractor to satisfy the requirements of the Prime Contract. Such Claims shall be received by the Contractor not less than two working days preceding the time by which the Contractor's Claim must be made. Failure of the Subcontractor to make such a timely Claim shall bind the Subcontractor to the same consequences as those to which the Contractor is bound.

Notice Provisions – Transmission Requirements

- 14.1.1 Except as otherwise provided in Section 14.4.1, where the Subcontract Documents require one party to notify or give notice to the other party, such notice shall be provided in writing to the designated representative of the party to whom the notice is address and shall be deemed to have been duly served if delivered in person, by mail, by courier, or by electronic transmission if a method for electronic notice is set forth in Section 14.4.3.
- 14.4.2 **Notice of Claims** shall be provided in writing and shall be deemed to have been duly served **only** if delivered to the designated representative of the party to whom the notice is addressed by certified or registered mail, or by courier providing proof of delivery.

Notice Provisions – Transmission Requirements

- EJCDC C-700 Standard General Conditions
- 18.01.A. Whenever any provision of the Contract Documents requires the giving of written notice, it will be deemed to have been validly given if:
 1. delivered in person, by a commercial courier service or otherwise, to the individual or to a member of the firm or to an officer of the corporation for which it is intended; or
 2. delivered at or sent by registered or certified mail, postage prepaid, to the last business address known to the sender of the notice.

Notice Provisions – Transmission Requirements

- Failure to send notice by the required means can be dispositive.
- *E.G. Borough of Brentwood v. Plavchak Constr. Co., Inc.*, No. 872 WDA 2017, 2018 WL 3582534 (Pa. Super. Ct. July 26, 2018)
 - Contractor sent notice of claim by email
 - Contractor argued that the email claim was effective
 - Court disagreed, stating that “[i]f the parties had wished only to ensure successful conveyance of information, there would have been no need to include the foregoing language in the contract.”
 - *Claim was barred*

Notice Provisions – Consequences of Noncompliance

- Varies by state – strict compliance vs notice prejudice.
- Minnesota tends towards strict compliance.

No Price Escalation Clauses

- Recent development in response to delays in obtaining materials, supply chain disruptions, and labor shortages.
- Limit or eliminate relief available under contract to recover damages caused by cost increases.
- Contractor will likely be strictly held to prices and schedules provided in bid.

No Price Escalation - Example

- AIA § 7.1.4 For proposed changes in the Work the costs shall be determined as provided under this Subsection 7.1.4. The Contractor shall submit an itemized list of quantities with the applicable unit costs and extended price for each, in such form and detail as required by the Construction Manager/Architect.
- AIA § 7.1.4 provides detailed requirements for change orders involving material cost changes.

No Price Escalation - Example

8.5 Notwithstanding any provision herein or in the Contract Documents to the contrary, in no event shall changes to the cost to Subcontractor of or for materials, labor or other items give rise to, or entitle Subcontractor to be eligible for, an adjustment to the Contract Amount hereunder. Both parties covenant and agree that the Contract Amount stated above was a material inducement for Contractor executing this Agreement with Subcontractor, and in no event shall the increase of material or labor costs to Subcontractor be deemed an event of force majeure such that Subcontractor is entitled to an adjustment to the Contract Amount. Furthermore, in the event Subcontractor orders materials after the execution of this Agreement, in no event shall Contractor be liable or responsible for any increases to the cost of said materials after the date of execution of this Agreement. Subcontractor shall bear all liability for material price increases after execution of this Agreement.

No Price Escalation - Negotiation

- Requires bargaining leverage and coordination with GC and Owner.
 - Private vs. public projects
- Know what types of risks are not acceptable to your business.
- Cannot re-negotiate terms of agreement after contracting process has concluded.
 - Tip: Force majeure clauses are an ineffective defense against no price escalation clauses in contracts arising in times of disruption.

No Damage for Delay

- Typical No Damage for Delay (“NDFD”) Clauses
- Dangers of NDFD clauses
- Enforceability of NDFD clauses
- Exceptions to NDFD clauses

Typical No Damage for Delay Clauses

Notwithstanding anything to the contrary in the Contract Documents, an extension in the Contract Time, to the extent permitted shall be the sole remedy of the Contractor for any

- (i) delay in the commencement, prosecution, or completion of the Work,
- (ii) hindrance or obstruction in the performance of the Work,
- (iii) loss of productivity, or
- (iv) other similar claims (collectively referred to in this Subparagraph as “Delays”)

whether or not such Delays are foreseeable, within the contemplation of the parties, or caused by the acts of the Owner or its agents. In no event shall the Contractor be entitled to any compensation or recovery of any damages, in connection with any Delay, including, without limitation, consequential damages, lost opportunity costs, impact damages, or other similar remuneration.

Dangers of NDFD Clauses

- “No damage for delay” clause shifts the risk of delay costs from owners to contractors, even when the owner causes the delay.
- Flow down clause shifts the risk of delay from contractors to subcontractors.
- Only remedy for delay is to seek a time extension.

Dangers of NDFD Clauses

- GC failures that increase risk to subcontractors:
 - GC fails to seek time extension or seeks insufficient time extension from owner.
 - GC doesn't follow proper protocol (i.e. notice requirements) under contract to seek time extension.
- Is owner required to grant time extension if subcontract contains NDFD clause?

NDFD – Enforceability

- Private Contracts
 - Legal but strictly construed.
- Public Contracts.
 - Prohibited
 - “Any clause in a public works contract that waives, releases, or extinguishes the rights of a contractor to seek recovery for costs or damages, or seek an equitable adjustment, for delays, disruption, or acceleration in performing the contract is void and unenforceable if the delay, disruption, or acceleration is caused by acts of the contracting public entity or persons acting on behalf of the public entity for which the public entity is legally responsible.” Minn. Stat. §15.411.

NDFD – Acceleration and Disruption

- Acceleration and disruption claims might not be subject to NDFD provisions.
- For example, if the NDFD clause only mentions delay damages, a Contractor should be able to recover if it can legitimately characterize its damage claim as one for acceleration or disruption rather than for delay.

NDFD – Best Practices

- Know who has to ask for time extension and what is required for requesting additional time
- If you have to submit request for time – do it ASAP
- How much time do you need? Make sure to ask for enough time.

Suspension & Termination

- Generally
- What rights accrue to subcontractors in the event of suspension?
- What rights accrue to subcontractors in the event of termination?
- Recovery
- Assignment
- Best Practices

Suspension & Termination

- Most subcontracts allow the contractor or owner to suspend and/or terminate the contract if certain criteria are met.
 - For convenience or
 - For cause
- Minnesota law requires the terminating party to strictly comply with the termination clause in the contract.

Suspension – what rights accrue?

- If suspension is for extended duration – can terminate contract.
- A201 General Conditions to the Prime Contract gives the Contractor the right to terminate the Contract if it is suspended more than 120 days:
 - “The Contractor may terminate the Contract if, through no act or fault of the Contractor or a Subcontract . . . repeated suspensions, delays or interruptions of the entire Work by the Owner as described in Section 14.3 constitute in the aggregate . . . 120 days in any 365-day period, whichever is less.” Section 14.1.2.
- The Subcontract incorporates the Prime Contract:
 - “The Subcontractor shall be bound to the Contractor by all terms and conditions of this Subcontract and, except as otherwise provided herein, by all terms and conditions of the Prime Contract between the Owner and Contractor which is incorporated by reference into this Subcontract and is an integral part of this Subcontract.” (Subcontract Section 1.0).

What happens after Termination?

- Termination for cause
 - GC's damages against subcontractor include cost to complete work and subcontractor will be responsible for damages above subcontract price.
- Termination for convenience
 - Subcontractor is owed payment for work performed through date of termination, including materials procured and delivered, profit/overhead recovery varies by contract.

Suspension & Termination – Assignment

- What happens if the GC is terminated?
 - Subcontracts assigned to a new GC
 - Or temporarily assumed by the Owner
 - Subcontractor may have new opportunity to negotiate terms
- Example: AIA A201.

§ 5.4.1 Each subcontract agreement for a portion of the Work is assigned by the Contractor to the Owner, provided that

.1 assignment is effective only **after termination of the Contract by the Owner for cause** pursuant to Section 14.2 and only for those subcontract agreements that the Owner accepts by notifying the Subcontractor and Contractor; and

.2 assignment is subject to the prior rights of the surety, if any, obligated under bond relating to the Contract.

When the Owner accepts the assignment of a subcontract agreement, the **Owner assumes the Contractor's rights and obligations under the subcontract.**

§ 5.4.2 Upon such assignment, if the Work has been suspended for more than 30 days, the Subcontractor's compensation shall be equitably adjusted for increases in cost resulting from the suspension.

Suspension & Termination – Best Practices

- Know your available recovery.
 - Reason for suspension or termination may dictate what you can recover.
- Document work performed and cost of work in real time so that if terminated, documentation is in place to seek value of all work performed to date.

Contingent Pay Clauses

- Typical contingent pay clauses
 - Pay-When-Paid
 - Pay-If-Paid
- Dangers of contingent pay clauses

Contingent Pay Clauses

- General Contractor typically bears the risk of the owner's insolvency or inability to pay for the project.
 - Minn. Stat. § 337.10, subd. 3, provides that a construction contract "shall be deemed to require the prime contractor and all subcontractors to promptly pay any subcontractor or material supplier contract within ten days of receipt by the party responsible for payment of undisputed services provided by the party requesting payment."
- GC's attempt to shift the risk of non-payment to subcontractors through contingent pay clauses.
- Two common types of contingent pay clauses:
 - Pay-When-Paid
 - Pay-If-Paid

Pay-When-Paid

- A typical pay-when-paid clause:

“Final payment including all retention becomes due and payable within 30 days after Architects’ certification of final payment. At all times the Subcontractor shall be paid to the extent that the Contractor has been paid on the Subcontractor’s account.”

- Minnesota courts generally interpret a clause like this to outline the **timing** of payments to a subcontractor, rather than excuse an unpaid contractor from its payment obligation to its subcontractors altogether.
- If the clause does not specifically state a time for payment, the courts often require that payment be made within a “reasonable” amount of time.

Pay-If-Paid

- To relieve a GC of its obligation to pay its subcontractor *unless and until it is paid by the owner*, the subcontract must **unequivocally and unambiguously** create a condition precedent to payment.
- IE – the subcontract must explicitly state that payment from owner is a requirement for the contractor to have a payment obligation to the subcontractor.

Pay-If-Paid

- The ACG Standard Subcontract Agreement Form (1996 version), Rider B-55 conditional payment clause, which states, in part:
 1. Irrespective of any term or inference to the contrary in the Subcontract, Contractor and Subcontractor expressly agree that the Owner's payment to Contractor on the Subcontractor's account is an **absolute condition precedent** to Contractor's obligation to pay Subcontractor any progress or final payment pursuant to the Subcontract, except to the extent Subcontractor establishes that the Owner's failure to make payment to Contractor was caused by the fault of the Contractor.

* * *
 3. Subcontractor expressly agrees that it retains the risk of the Owner's insolvency or inability to pay for Subcontractor's Work, and such risk is not transferred to Contractor under the Subcontract.

Dangers of Contingent Pay Clauses

- Delays payment
 - Plan for delayed payments
 - Could affect other jobs

Important Statutory Provisions

- Mechanic's lien expires 120 days after last date of work under Minn. Stat. § 514.08, subd. 1.
- Subcontractors have right to prompt payment for undisputed services within 10 days of the GC's receipt of payment from Owner under Minn. Stat. § 337.10, subd. 3, and prevailing party is entitled to 18% interest and attorney's fees.
- Retainage cannot exceed 5% and retainage must be released no later than 60 days after substantial completion under Minn. Stat. § 337.10, subd. 4.

Questions?

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The logo for Fabyanske Westra Hart & Thomson is a dark blue square containing the firm's name in white, uppercase, sans-serif font. The text is arranged in four lines: "FABYANSKE", "WESTRA", "HART &", and "THOMSON".

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