

16 Contract Provisions You Need to Know

Make sure you understand these basic contract terms before venturing into your next project.

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In the AEC community, contractual agreements provide the structure and road map for successful, profitable projects. It is amazing, however, that project participants are often unaware of the actual contract terms.

Only by familiarity with, and frequent reference to, the actual contractual obligations can team members deliver the required contract services without voluntarily providing more or inadvertently providing less.

While each contract should be created based on the unique demands of each project, there are some key contractual issues that apply to virtually any engineering service agreement. Every engineer should be familiar with them.

1

SCOPE OF WORK.

This is the most important provision of any services agreement. More than any other provision, the scope of work statement defines the parties' expectations and establishes the parameters of the services to be provided. Accordingly, the scope of work should be as complete and detailed as possible. Ambiguity and open-ended descriptions should be avoided wherever possible.

To preserve the benefits of a properly drafted scope of work statement, the agreement should also state that no additional services will be provided absent a written amendment to the agreement signed by both parties. Such a provision avoids claims that additional services were promised but not delivered. However, such a provision requires diligence on the part of the engineer to make certain that any additional services are documented by a written amendment. Absent such a written amendment, the engineer may face claims that it is not entitled to payment for the services, regardless of whether they were actually provided.

2

CHANGE IN/ ADDITIONAL SERVICES.

A necessary corollary to defining the scope of services is defining when, how, and why the scope of services will change. In this regard, it is very important to provide as detailed a list as possible of those services that are not included in the basic agreement, as well as those services that will be treated as "additional." Such lists should be preceded by the words "including, but not limited to" as a means of making the list nonexclusive. Such changes are usually required to be in writing. The problem arises, however, when the project timing or owner delay does not allow for this process. Accordingly, additional services provisions should include a self-executing mechanism to avoid unnecessary delay. For example, the owner or prime consultant may be given a certain time period in which to object to additional services proposed by the engineer. If the owner does not respond, the owner will be deemed to have agreed to the change.

3

OWNER RIGHTS & RESPONSIBILITIES.

Generally, an engineering service agreement focuses on the obligations of the engineer. Often, the only obligation of the owner or prime consultant defined in the contract is the duty to pay for the services. Depending on the nature of the project, however, other rights and responsibilities of the owner or prime consultant should be identified. For example, what information is the owner or prime consultant expected to provide, and what right does the engineer have to rely on that information? Similarly, what is the extent of the owner's project input and authority, and when is that input to be provided? Consideration of these issues can be invaluable in clarifying the expectations of the parties and can greatly assist the engineer in providing a quality, cost-effective service.



6

STANDARD OF CARE.

Absent implied or express provisions to the contrary, engineers are required only to provide their services with the degree of skill and care ordinarily exercised by reputable practitioners of the profession practicing in the same locality under similar circumstances. Perfection is not typically required. However, engineers often expressly or impliedly increase the applicable standard of care. Frequently, clients attempt to include contractual language indicating that the services will be provided “in accordance with the highest professional skill and care,” or some similar language. While it is difficult to tell a client that such a provision is unacceptable, the engineer must recognize that such a provision may raise the standard of care to a level of near perfection. Such elevated standards of care may also create insurance coverage denials with respect to any liability arising out of the elevated standard of care.

In addition to express contractual language, the standard of care may be elevated by implication. In pursuing a project, engineers and others will frequently describe outstanding qualifications to provide services. Some clients would argue that such overtures elevate the engineer’s obligations beyond the ordinary standard of care. Avoid such implications by including in the agreement an integration clause, which provides that all representations and obligations are set forth in the written agreement. To make an integration clause effective, the proposal including the extraordinary representations should not be included in or incorporated by reference into the agreement.

Finally, engineers should approach contractual obligations to comply with “all applicable laws and codes” with great caution. Ideally, the specific code should be identified with the qualification that it is subject to the interpretation and authority of the applicable building official.

7

OWNERSHIP OF DOCUMENTS.

Ownership of design documents has become an increasing point of controversy. Such concerns are amplified by the proliferation of electronic design tools and owners’ frequent requests to receive and own electronic design documents. Whenever possible, the engineer should retain all ownership of its design documents, and simply grant the owner a limited license for use solely with respect to the project that is the subject of the contract. If the owner insists on ownership of the documents, the right to use those documents should be narrowly defined such that the documents may not be misused to the engineer’s jeopardy. The agreement should also provide that any electronic design documents are provided solely as a courtesy, with a disclaimer as to their future usefulness. Finally, any client rights to the engineer’s work product should be expressly contingent on payment of all fees and costs under the agreement.

8

ELECTRONIC COMMUNICATIONS.

Electronic communication has also substantially affected the way that project participants communicate. Although often treated in a casual way, an e-mail message becomes a “written direction” with the click of a button. Accordingly, the agreement should specifically identify the anticipated electronic communications, and specifically identify the reliability and authority of such communications. This is particularly true if the project includes a project Web site.

4

PARTIES TO THE AGREEMENT.

Although it seems obvious, the agreement should also carefully define the parties to the agreement. Such provisions are necessary to determine who is entitled to modify or control the terms of the agreement, who is obligated to make payment under the agreement, and who is entitled to claim the benefits of the services.

5

ASSIGNABILITY.

Provisions regarding each party’s right to assign the agreement may seem inconsequential, but may have significant ramifications for the engineer. For example, if the engineer structures its fee and approach to the project based on the assumption that it is dealing with a sophisticated and cooperative client, and the client later assigns the contract to a less sophisticated/cooperative party, the engineer may be left in a difficult position. Accordingly, the agreement should provide that the agreement is not assignable. If that approach is not workable, the agreement should provide that any assignment constitutes a change in scope with an appropriate change in compensation.

9

WARRANTIES & GUARANTEES.

A warranty is an express or implied promise or guarantee that services or a product will satisfy certain criteria. Express warranties and guarantees can arise in various forms. In addition to express warranties clearly set forth in the agreement, express warranties may also arise from a number of other sources, including (1) the description of the scope of work, (2) review of shop drawings and as-built drawings provided by the contractor, and (3) certifications of contract compliance and payment requests. Similarly, management of a project with a guaranteed maximum price may create an implied warranty that the price will not be exceeded. Accordingly, the agreement should state that the only warranties and/or guarantees established by the agreement are those expressly set forth and identified as such in the agreement.

10

LIMITATION OF LIABILITY.

Limitation of liability provisions seek to limit the engineer's potential liability to some finite amount proportionate to the benefit of the project. Although such provisions have been repeatedly attacked in the courts, the current law recognizes them as valid tools of risk allocation. To promote the effectiveness of limitation of liability clauses, they should be prominently set forth in the agreement such that the client can not claim surprise, mistake, or duress. Ideally, a limitation of liability clause limits the engineer's liability not just to the prime consultant and owner, but also to any contractors, suppliers, or other third parties. The limitation of liability should also exclude liability for consequential damages such as lost profits and loss of use.

11

INDEMNITY.

Indemnity is the companion to limitation of liability. An indemnity provision seeks to have one party indemnify the other for claims of liability asserted against the party to be indemnified. Often, clients will seek to have engineers indemnify them from all claims except those caused solely by the client. Obviously, such indemnity provisions carry tremendous risk in that they subject the engineer to substantial exposures beyond the risks the engineer can control. The preferable approach is a mutual indemnity provision requiring each party to indemnify the other to the extent they are negligent and thereby responsible for the subject matter of the claim. The indemnity provision should also clearly define who is covered by the indemnity provision.

12

INSURANCE.

Indemnity obligations are only as useful as the resources available to back them up. Accordingly, the engineer should recommend and require that all project participants have and maintain adequate insurance coverage. Furthermore, the engineer should seek to be included as an additional insured on all contractor insurance policies.

13

DISPUTE RESOLUTION PROVISIONS.

Of course, no one ever enters into a contract expecting it to result in litigation. However, the original contract is the best opportunity to create a mechanism to cost-effectively resolve any eventual claims. Mediation and arbitration are the two alternative dispute resolution provisions most often used to manage claims. The effective use of either approach depends on the project, the parties, and the type of claim. For example, an engineer should seek to avoid becoming involved in a larger dispute that only remotely or tangentially relates to their services or to any dispute resolution forum that would not resolve all claims involving the engineer in a single action.

14

LIMITATION OF THIRD-PARTY RELIANCE.

Recently, one of the greatest sources of claims against engineers and other design professionals has come from third-party strangers to the contract. Typically, such claims arise either from a party who has received a copy of the project documents and somehow came to rely on them, or from a party who believes they were an intended beneficiary of the services. To prevent and/or defeat such claims, the agreement should expressly identify the intended beneficiaries of the services and provide that the services are not to be used or relied on by any other party without the express written consent of the affected engineer.

15

CONSISTENCY WITH OTHER AGREEMENTS.

Finally, once the engineer has negotiated an appropriate agreement, the engineer should make certain that contractual obligations of other project participants are consistent with that agreement. This concern really proceeds in two directions. First, the engineer should make certain that any obligation or risk it has undertaken is appropriately allocated or transferred to any subconsultants or subcontractors retained by the engineer. Predictably, architects retaining engineers will do the same. Accordingly, engineers should be wary when incorporating the terms of a prime consultant into their own subconsulting agreement. Before doing so, the prime agreement should be reviewed in detail to make certain that it does not establish any unanticipated and/or unacceptable risks. Second, the obligations should be consistent with other project participants, such as owner-retained consultants, contractors, and suppliers.

16**PAYMENT TERMS.**

Engineering service agreements often provide that the engineer is to be paid after the architect has been paid by the owner. Such a provision puts an engineer in a helpless secondary position without ordinary tools of recourse for payment. Such provisions may often be unenforceable as contrary to lien laws. A preferable approach is to provide that payment is due upon receipt of the invoice, but not late until after the architect has been paid by the owner. This approach will generally preserve the engineer's lien rights and other collection remedies.



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PERFORMANCE OF THE CONTRACT

The execution of the contract finally gives relevance and meaning to the contract. Before execution, it is just words. After execution, it becomes the controlling authority establishing the engineer's rights and responsibilities on the project. Nevertheless, it is not unusual for project participants to be in the dark about contract terms. This is a mistake, and it is one you do not want to pay the price for making. ■

How to Succeed on Projects With Precarious Contract Terms

Just as perfection in design and construction is a rarity, so is the perfect design agreement. It is a human enterprise subject to competing positions, competing leverage, preconceived biases and, ultimately, compromise. It is also rare that any agreement can fully anticipate all that can, and inevitably does, happen on any construction project.

While insurance companies and attorneys extol a vast array of contractual advice favorable to the design professional, owners and contractors have their own attorneys and advisors promoting contractual provisions equally or more favorable to their constituents. As a result, nearly any design agreement is either going to include provisions adverse to the design professional or exclude other provisions that could not be resolved into an agreement. It is the simple reality of business today.

Given this reality, many (or most) design professionals take one of two dramatically different approaches once the agreement has been executed. Some deliver the contract to their accounting department or otherwise file it away in the hope that they will never actually have to confront those imperfect and uncomfortable positions. Others seek to strategically identify and manage the imperfect provisions and omissions with the hope that proactive management will lead to project success

and client satisfaction, as opposed to any contentions and/or costly legal debate regarding the subject provisions. For obvious reasons, the latter approach is the preferred model.

Successfully managing such variables is greatly aided by doing so within the context of an operating model. Use IROPE as your guide.

- **Issues:** Identify the issues of concern arising from both the undesirable clauses, as well as those omitted from the agreement.
- **Risks:** Identify the potential risks and, especially, the consequences arising from the issues identified in step one.
- **Options:** List and map the potential options to manage and minimize the risks and consequences. Inevitably, some may be implemented in conjunction with one another, while others may be inconsistent and require an election.
- **Plan:** From the available options, establish a plan to proactively manage (or at least closely monitor) each issue.
- **Execute:** Implement and follow the plan consistently through the project with adaptation as possible and necessary to deal with the competing issues.