WEBINAR

MANAGING RISKS

WHEN PROVIDING SUBCONTRACTED DESIGN SERVICES

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ConstructionRisk

Arch

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PLA UNIVERSITY

NSM Insurance Group
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Today's Agenda

- PUA Overview
- Overview: Design-Build Risks
- Risk Management Lessons
- Q&A

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PUA Overview

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Learning Objectives

Design-build projects create unique risks for design subconsultants. We will discuss these risks, examine court decisions involving design professionals and explore ways to manage or reduce risks.

We'll cover:

- Why there is more risk when working as a design subconsultant to the design-builder
- Example claims scenarios against designers by design-builders
- Managing the risks associated with contract language
- Managing emerging risks in the design-build sector

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Overview: Design-Build Risks

The Professional Liability Claims Experience for Consulting Engineers in Design-Build (DB)

- What are the sources of professional liability claims against Consulting Engineers on DB projects?

Need For Industry Standards for Evaluation of Design Development Risk Claims

Factors to be considered include:

1. How much design development, detailing and prescription is furnished by the Owner and included in the RFP ("Bridging documents")
2. The Owner's approach to design and related risk allocation (e.g., DSC)
3. Disclaimers and non-reliance provisions in the RFP as to preliminary design risk; and defense and indemnification obligations as to Owner-furnished preliminary design defects

Need For Industry Standards for Evaluation of Design Development Risk Claims (cont.)

4. The extent and reasonableness of validation and verification (investigation, studies, etc.) expected or required of the Design-Builder and/or its Consulting Engineer with respect to the Owner-furnished preliminary design (or related reports or information)
5. The standard of care in the DB Contract as to compliance with preliminary design (warranty?), and the extent of flow-down to the Engineer, and conflict with the Engineer's insurable standard of care obligation
6. Compatibility between Owner's preliminary design and other Owner-furnished information, investigations, etc. (e.g., subsurface); and how risk is allocated in those other respects?

Need For Industry Standards for Evaluation of Design Development Risk Claims (cont.)

7. The scope of services and professional standard of care reasonably expected of the Engineer in evaluating bridging documents, verifying Owner-furnished information, and in preparing its preliminary design;
8. Can design development contingency to be priced in the DB Proposal?
9. What is the contractual (legal) significance of the Owner's acceptance of the Design-Builder's Technical Proposal

Roles and Risks of DB Project Participants

Design-Builder:

- Aggressive bid pricing
- No design development contingency
- Pre-award design and investigation/verification services (scope is too limited)
- Unreasonable risk allocation (e.g., Quantity overrun contractual liability) and heightened standard of care contractual terms
- Insistence on payment withholding and back-charge provisions that diminish or negate otherwise available professional liability insurance coverage

Design-Builder's Pricing Should Include Design Development Contingency

- Design development progression following contract award
- Optimistic, aggressive bid (proposal) design assumptions may not be accepted by the Owner
- Owner preferences, regulatory interpretations, delay in third-party approvals may impact design development process
- Non-negligent errors, omissions or other deficiencies in proposal design or design development services that need correction

How Much Contingency?

- "A number of experts testified concerning industry standards regarding the amount of contingency that a contractor should include when bidding a design/build project; consensus seemed to be that cost increases in the range of 10% should be expected. It is unnecessary for the court to find as a fact what the proper percentage for contingency was in this case; indeed, an appropriate contingency is undoubtedly dependent on the project and the amount of time available to the engineering team to advance toward a final design before bid submission. All of the experts, however, agreed, and the court finds, that in design/build projects weights, complexities and therefore construction costs invariably increase after the contract is awarded as design development proceeds to the final approved-by-owner construction design."
- The Middlesex Corporation, Inc. v. Fay, Spofford & Thorndike, Inc., Commonwealth of Massachusetts, Superior Court, Civil Action 15-02992-BLS1, Memorandum of Decision, June 28, 2019, pp. 13-14.

Design-Build Risk Management Lesson 1

Joint Ventures and Teaming Agreements

What Are Teaming Agreements?

- Agreement reflects parties' intent that if the Owner awards a contract to the prime contractor, then the prime contractor will enter into a subcontract with the other team member, and the teaming agreement often allocates the types and amounts of work to be done by each party
- One of the reasons teaming agreements are used is that they avoid the need for the parties to negotiate a detailed subcontract agreement that they may end up not needing if their proposal is not successful — but beware of state law in this regard

Joint Venture: A Special Purpose Entity

- Viewed As a Partnership/Fiduciary relationship
- Sharing of Loses and Profits
- Management Committee
- Joint and Several Liability

Teaming Agreement Unenforceable

- A federal district court decision holding a teaming agreement between two contractors unenforceable under Virginia law raises questions about the usefulness of these commonly employed agreements

- Cyberlock Consulting, Inc. v. Information Experts, Inc., F.Supp.2d (2013), 2013 U.S. Dist. LEXIS 49092, 2013 WL 1395742, affirmed 2014.

Teaming Agreement Unenforceable (cont.)

- The U.S. District Court for the Eastern District of Virginia granted summary judgment to Defendant who was resisting the enforcement of a teaming agreement after the parties were unable to reach agreement on a subcontract relating to a prime contract awarded by the government

- The court essentially agreed that the teaming agreement was a "mere [agreement] to agree in the future," and therefore unenforceable under Virginia law

Teaming Agreement Unenforceable (cont.)

- The court noted that the teaming agreement didn't include a detailed description of the work to be performed by the proposed subcontractor and didn't include as an exhibit the subcontract the parties would execute if the prime contract were awarded
- Court also noted the teaming agreement included a provision calling for termination of the agreement if there was a "failure of the parties to reach agreement on a subcontract after a reasonable period of good faith negotiations"

Case Study: Teaming Agreements

- Atacs Corp v. Trans World Communications, 155 F.3d 659 (3rd Cir. 1998)
- Subconsultant contributed significantly to obtaining design build contract
- Court found enforceable teaming agreement; however, relief was limited to amounts spent in solicitation effort and “the fair value of the subcontractor's contribution to the prime contractor's agreement”
- Lost profits were too speculative

Case Study: Teaming Agreements

- Trident Constr. Co. v. The Austin Co., 272 F.Supp.2d 566 (D.S.C. 2003)
- Preliminary discussions between Trident (subcontractor) and The Austin Company (general) but could not agree on price
- Agreement to agree was not enforceable

Design-Build Risk Management Lesson 2

Documenting the Agreement Between Parties

Battle of the Forms: What Terms Govern?

- On City of Savannah parking garage project, the design- builder and its engineering subconsultant litigated over what contract terms and conditions applied to the contract between them
- Engineer's Letter Proposal contained scope of services and a terms and conditions sheet
- Purchase Order (PO) by D-Bldr contained different terms and conditions (but also referenced the Engineer's proposal)
- Court found PO was the final form (counteroffer); the engineer did not object to it, but instead began its services

  - Batson-Cook Company v. TRC Worldwide Eng., (2011)

Letters of Intent: When are They Enforceable? (cont.)

- Developer sued Owner for breach of contract
- Owner moved for SJ, arguing:
  - There were unaccepted offers and counteroffers
  - There was no enforceable contract
  - Damage claims barred by Statute of Frauds
- Court found the LOI showed the parties intended to be bound by its terms "at the moment of acceptance, before the negotiation of more formalized agreements"
  - It may have been intended as an interim agreement, but it was intended to be binding nonetheless
- SJ denied and matter goes to jury for decision on merits
  - Erdman v. USMD of Arlington (2011 WL 1356920 (N.D. Tex, 2011)

Design-Build Risk Management Lesson 3

Establish the Standard of Care

Standard of Care for Preliminary Services

- “The Design-Builder acknowledges that the designs and information prepared by the Design Consultant under this Agreement are preliminary in nature, not complete and subject to design development and progression after award of the Project. Design-Builder shall include appropriate contingencies in its price to account for such variance and other risk factors with input to be provided by Design Consultant. Design-Builder will have sole responsibility for the preparation of the price proposal, including the calculation of unit prices and contingencies with input from Design Consultant. Design- Builder and Design Consultant will jointly estimate the bid quantities and will estimate the anticipated tolerance for each item. Any quantity information provided by the Designer is for information purposes only and the Design-Builder will be ultimately responsible for the determination of quantities to be included in the proposal and will determine the appropriate amount of contingency to be included in its proposal to cover variations in quantities and other risk factors. Design Consultant will consult with Design-Builder in this endeavor to the extent desired by Design-Builder.”

Design-Builder Unsuccessful in Suit Against Engineering Subconsultant for Cost Overruns

- Design-Builder sued its engineer subconsultant for costs allegedly attributed to errors in preliminary designs and cost/quantity estimates provided under the terms of a Teaming Agreement
- Design-Builder claimed that if the engineer had not breached the Teaming Agreement it would have bid more and made a greater profit
- Trial court found contractor was arguing preliminary plans prepared for bidding purposes should have been complete and accurate to the same extent as if they were one hundred percent final construction documents
- There was no evidence that the engineer failed to meet the standard of care for preliminary design documents and nothing suggested anything the engineer did caused the Project to be more expensive
- Middlesex Corp., v Fay, Spofford & Thorndike, Inc., 2019 WL 3552609, (Superior Court of Massachusetts, Suffolk County, 2019).

The Teaming Agreement – Middlesex (Part 1)

- The Design/Builder acknowledges that as a design professional, the Engineer's performance of its service both pursuant to this Agreement and with regard to any services performed as part of a Subcontract for Design Services are subject to a professional standard of care
- The Design/Builder and Engineer agree that the applicable standard of care for the Engineer's services shall be that degree of skill and care normally exercised by practicing professional engineers performing similar services on similar projects under similar conditions
- No other representations or warranties, whether express or implied, shall be imputed to the Engineer's services …

Teaming Agreement – Middlesex (Part 2)

- The Engineer will provide its professional opinion regarding the Design/Builder's construction estimate for quantities and comment on specific items of potential quantity growth, but the Engineer shall not have risk associated with estimate quantities and/or construction pricing
- The Engineer will prepare its own independent estimate for use by the Design/Builder in making its assessment of quantities
- The Design/Builder acknowledges that such estimates are based upon only limited and conceptual design development derived from the contents and requirements of the RFP
- The Design/Builder shall verify quantities or other information furnished by the Engineer and shall use its knowledge and experience as a construction professional in developing its bid and pricing for the work, and shall include in such bid an appropriate degree of contingency for additional cost resulting from the post-award design development and finalization process

Design-Build Risk Management Lesson 4

Responsibility for Code Compliance

Responsibility for Legal Codes

- Tips vs. Hartland Developers, Inc. (1998):
  - Airplane hangar in San Antonio
  - Design-builder failed to meet fire code requirements for mezzanine
  - Court stated contractor gives implied warranty that codes would be met (see next slide)

Responsibility for Legal Codes

Court held:

- “Contractors, not owners, are in the best position to know about and comply with relevant building codes. Furthermore, buyers are not in the business of building; they are in the business of occupying. They rely on builders to furnish structures that can be occupied.”

Don’t Warrant Compliance with Laws and Codes

- Insert wording that the designers will “exercise the Standard of Care” to comply with laws and codes.”

- “Consultant shall exercise the standard of care to comply with requirements of all applicable codes, regulations, and current written interpretation thereof published and in effect during the Consultant’s services.”

Design-Build Risk Management Lesson 5

Differing Site Conditions Claims: Same Rules Apply on Design-Build Projects as Other Types of Projects

Differing Site Condition

- “An RFP stated that an expansive-soil report was ‘for preliminary information only….” The Design-Build contract required the contractor to conduct its own independent soil investigation.
- Court held: “That statement merely signals that the information might change (it is ‘preliminary’). It does not say that Metcalf bears the risk if the ‘preliminary information turns out to be inaccurate. We do not think that the language can fairly be taken to shift that risk to [Design-Builder], especially when read together with the other government pronouncements, much less when read against the longstanding background presumption against finding broad disclaimers ‘of liability for changed conditions.”
- Metcalf Construction Co. v. United States, (U.S Ct. of Appeals for the Federal Circuit, Case No. 2013-5041, Feb. 11, 2014).

DSC Claim Denied for Suspected UXOs

- Design-Builder that was awarded contract to remediate landfill on military base in Italy claimed entitlement to equitable adjustment for DSC based on
  - It suspected UXOs might be present
  - Work was delayed because government didn't issue a "War Bombs Reclamation Certification"
- ASBCA denied appeal from Contracting Officer's rejection of DSC claim
  - No UXO was actually found at the site
  - Design-Builder didn't prove "certification" was legally required or that Government had duty to evaluate risk

CEMES, ASBCA No. 56253, 11-1 BCA P 34640 (Dec. 2010)

Owners Are Including Contract Provisions Stating Design-Builder Cannot Rely on Owner-provided Data

- Be careful of contract language depriving the design-builder and its subconsultants of the right to reasonably rely upon owner provided information and data

Design-Builder Entitled to Recover on DSC Based on Conditions Differing from Soil Reports

- On underground parking garage project, the engineer subcontractor of Design-Builder incurred costs redesigning foundations due to soft clay differing from soil reports
- Owner denied Design-Builder claim, asserting:
  - Because soil reports showed clay, there could be no DSC based on clay
- Design-Builder prevailed (over $15 million plus $2 million attorney's fees)

Design-Builder Entitled to Recover on DSC Based on Conditions Differing from Soil Reports (cont.)

- Court's holding:
  - Jury could find DSC because the type and amount of clay could be deemed different from what was shown in the soil reports
  - Jury could find bad faith by City because City "rejected Batson–Cook's materially different conditions claim, simply because the [soil] reports had always indicated the presence of clay," and ignored the provisions for DSC claims for site conditions that "differed materially from the conditions indicated in the contract documents or from conditions ordinarily found to exist…."
  - Quantum meruit claim also allowed for matters beyond the contract

City of Savannah v Batson-Cook, 714 S.E.2d 242 (Ga. 2011)

Differing Site Condition Claims Are Not Eliminated by Design-Build Method

- RFP Technical Spec provided government survey and stated gravel material with certain grain sizes would be available on site for use of Design-Builder
- Design-Builder increased quantity of sub grade fill as a result of the survey errors
- Due to high moisture content and frozen materials in stockpiled materials, Design-Builder had to use different screening process – taking longer and required purchase of off-site borrow material
- Government denied change order – asserting that although stockpile contained excessive fines, “processing the pile and choices of screening procedures were Design-Builder’s responsibilities”
- Board Held: Entitled to Type I DSC – That being difference in Kr’s actual costs and what the cost would be if conditions had been as represented in the RFP

Haskell Corp., 06-2 BCA 33422 (2006)

Differing Site Conditions in Federal Government Contracting

- Metcalf v. United States (2014)
  - Government duty of good faith and fair dealing is held to mean more than merely not acting with bad faith and malice
  - Differing Site conditions claims cannot be denied with general disclaimers

Design-Build Risk Management Lesson 6

Contract Language Is Important

Ignore it at your own peril!

Indemnification Clause Required Indemnity for "All" Damages

- Black & Veatch ("B & V") to EPC a power plant
- Subcontracted combustion turbine installation
- "Foreign object damage" to a number of the compressor blades after start up (Cutoff bolt, a welding rod, and a half- moon shaped cut metal plate were found)
- B&V paid damages to owner and sued sub under indemnity clause for $1.5 million in direct costs to repair the damage, and another $2.1 million due to delays caused by the damage

Black & Veatch Construction, Inc. v. JH Kelly, LLC, 2011 WL 1706223 (U.S. District Court, D. Oregon, 2011

Indemnification Clause Required Indemnity for "All" Damages (cont.)

- Summary judgment for B&V, finding:
  - Indemnity language was broad enough to require indemnity for "any and all" damages, including delay damages
  - The waiver of consequential damages clause was inapplicable because that clause expressly excepted its applicability to obligations under the indemnity clause
  - No subcontractor right to recover contribution from Mitsubishi, the manufacturer, because not independently responsible by contract or tort for the damages

Liquidated Damages Enforceable Even Where Far Exceeding Actual Damages

- Miller Act claim filed against Dick Corp. by U.S. on behalf of subcontractor on design-build project at Pensacola Naval Air Station
- Dick made counter-claim against sub, arguing it was entitled to withhold payment, and anything owed was more than offset by Liquidated Damages Sub owed Contractor
- Sub argued LD provision unenforceable:
  - Navy didn't assess LDs against Contractor
  - It caused no delay to trigger the LDs
  - LDs are unconscionable penalty – far exceeding actual damages sustained.

U.S. v. Dick Corp., 2010 WL 4666747 (2010, N.D. Fla.)

Liquidated Damages Enforceable Even Where Far Exceeding Actual Damages (cont.)

- Court concluded although LDs were “far in excess” of the actual damages, it was not possible to ascertain at time parties entered into the contract what the actual damages would be
- Even if Dick could calculate part of its potential actual damages when entering contract, there were additional unascertainable factors
- The LDs were not “grossly disproportionate to damages that might reasonably be expected to follow… from delays”

Design-Builder Failed to Prove Liquidated Damages Amount was Arbitrary

- Coast Guard assessed LDs against design-builder that was late in performance and was terminated for default
- Contractor filed suit (and SJ motion) and argued the $ amount set for the LDs was unreasonable based on what was used on other projects and based on certain components such as government personnel and administrative costs being included
- Court denied SJ because:
  - Design-Builder did not prove that rate was unreasonable at time it was set by CO based on info available to the CO
  - Government personnel and admin costs can be included in rate
  - K-Con Building Systems, Inc. v. U.S., 97 Fed.Cl. 41 (2011)

Contractor Forfeits Recovery for Extra Work Performed without Approved Change Order

- Design-Builder had fixed-price contract to upgrade HVAC in college dorms
- Performed significant extra work due to unforeseen problems with existing system – with approval of CM
- University refused to pay anything other than original contract price because Change Order was never executed by Purchasing Department
- Court granted SJ for University, finding contractor did work without first getting approved change order
- No recovery for unjust enrichment or quantum meruit allowed

Mallory & Evans Contractors and Engrs v. Tuskegeee U., 2010 WL 5137580 (M.D. Ala., Dec 2010)

Design-Build Risk Management Lesson 7

Comply with Plans & Specifications — Even If You Wrote Them

Prescriptive Design Specs Versus Performance Specs

By Submitting Proposal in Response to RFP, Design-Builder Represents It Can Meet Performance Specifications

- RFP called for windows at Alaska base to meet blast requirements and also meet high thermal requirements
  - Design-Builder could not locate commercially available windows and had to custom build them instead
- Government denied change order (REA) for additional costs of windows
- Board HELD: Design-Builder represented it could meet the performance specifications by submitting its proposal
  - Failure to adequately investigate availability of windows was Design-Builder risk

Strand Hunt Construction, Inc., ASBCA 55,671 (2008)

What If It's Impossible to Meet Performance Specs?

- When Design-Builder argues it should be excused from guarantee due to impossibility to meet the performance requirements, courts consider:
  - Contract terms
  - Relative knowledge of parties regarding specs

- Design-Builder agreed to meet performance requirements tied into state air quality standards and warranted it would bear cost of all corrective measures until continuous compliance was achieved
  - Court found Design-Builder expressly warranted it could provide satisfactory precipitator and thus assumed risk of impossibility

Colorado-Ute V. Envirotech, 524 FSupp 152 (D.Colo 1981)

Impossibility as a Defense (cont.)

- Design-Builder in this case asserted that Owner failed to provide design temperature and flue-gas volume required by contract
- Court found Design-Builder made express warranty that it would provide satisfactory equipment and assumed the risk of impossibility
- Court found this to be sale of goods under the Uniform Commercial Code (UCC) as well — and with that a warranty for fitness of the goods for their intended purpose

Design vs. Performance Specifications

- If Owner includes design details in its bridging documents, these will be binding on the Design-Builder
  - When responding to Design-Build solicitation, need to understand which aspects of concept documents developed by owner are discretionary and which are not
  - Electrical specs in solicitation described conduit size and characteristics as well as details of supports for the raceways

Dillingham Constr. v. U.S., 33 Fed.Cl. 495 (1995)

Design v. Performance Specifications (cont.)

- Dillingham's electrical sub wanted to use metal clad cable instead of raceways
- Owner rejected this proposal. When sub installed supports differing from those specified, the owner required them to be removed and replaced
- The sub submitted a $600,000 claim for extra costs to comply with these requirements. Argued specs were "performance" based — providing "general guidelines" giving sub "wide latitude" to interpret
- Court found specs were "design" specs that gave sub no flexibility to deviate

Design-Builder Cannot Substitute Plywood Siding for Prefinished Polyvinyl Hardwood That Was Specified

- A drawing submitted with Design-Builder's proposal showed Polyvinyl Fluoride Coated Hardwood (PVF) Siding. This was consistent with another section of the specs
- After contract award, Design-Builder asserted it intended to use T-111 plywood siding as permitted by one of the spec sections
- Government refused to allow the plywood – which it called unauthorized substitution
- Board HELD: Specifications did not allow use of plywood. Even if there was ambiguity, government made it clear during negotiations it wanted PVF siding and that is what the approved contract incorporated by way of the technical specs

C&L Construction, 78-2 BCA 13516.

Design-Builder Not Permitted to Substitute Steel Lighting Fixture for Aluminum that it Included in Technical Proposal

- Government spec for renovation of buildings called for a Type A1 Fixture, recessed mounted, two by four, made of rolled steel to produce 50 foot-candle illumination
- Design-Builder proposal submitted a catalog cut of a specific company and model fixture made with “extruded aluminum”
- Government accepted proposal and later rejected Design-Builder’s attempt to substitute different fixtures made of steel because “inferior in quality and look” to the fixtures included with the Design-Builder’s technical proposal.

Sherman Smoot Corp., 03-1 BCA 32073 (2002)

Design-Builder Not Permitted to Substitute Steel Lighting Fixture for Aluminum That It Included in Technical Proposal (cont.)

- Design-Builder argued it was entitled to furnish the less expensive steel fixture pursuant to FAR 52.236-5 Material and Workmanship
- Board HELD: There is no legal authority to support the Design-Builder's argument that when a brand name is offered by Design-Builder and incorporated into Contract, the FAR clause would allow Design-Builder to use of substitute product of the same standard of quality in accordance with that clause

Design-Builder Must Build What It Included in Technical Proposal – Can't Later Require Govt. to Accept Different Site Plan

- Government has authority to reject Design-Builder revised site planning as nonconforming, where plan differed from design that was submitted with best and final offer (BAFO)
- And this was regardless of whether Design-Builder could show that its revised plan would give government a better or more economical and best use of its site
- Board HELD: If site plan proposals included in the technical proposal with the BAFO resulted in excessive work, the government had the right to insist of the site plan it wanted, and that was included in the BAFO by the Design-Builder

Sea Crest Construction, 59 Fed. Cl., 473 (2004).

Kr. Must Remove Underground Duct Bank for Electric and Install it Overhead as Shown in Govt. Specs

- RFP included drawings for the installation of electrical conduits – showing them installed overhead, hanging either exposed from utility racks or hidden above a drop ceiling
- Notes on the drawings stated they were “diagrammatic”
- Diagrammatic notes stated Kr to avoid interference with other trades and Kr had some flexibility in how to do that
- Problem: Kr found electric couldn’t be installed exactly as depicted and also couldn’t avoid interference with other trades
- Kr solution: Installed electric underground

Blake Constr. v. U.S., 987 F.ed 743 (Fed. Cir. 1993)

Kr Must Remove Underground Duct Bank for Electric and Install It Overhead as Shown in Govt Specs (cont.)

- Government required contractor to remove underground duct bank and install where specified

- Court Held: Where there is a combination of design specs and performance specs, the contractor must meet the design specs
- Great description of difference in design and perf specs

No REA for Kr where Roofing Spec was Either Patently Ambiguous or Latently Ambiguous

- Specs for roof repair called for “light-weight concrete” but in other sections called it “asphaltic concrete”
- Kr bid sought to use less expensive – and government rejected it
- Board Held: The ambiguity in the spec was apparent If it was deemed patent, the Kr had duty to inquire and failed to do so
  - If its was “latent” and not discovered until after contract was awarded, Kr must prove how it priced its bid with the less expensive material. It failed to do so

MCSD Construction, 91-2 BCA 23986 (1991).

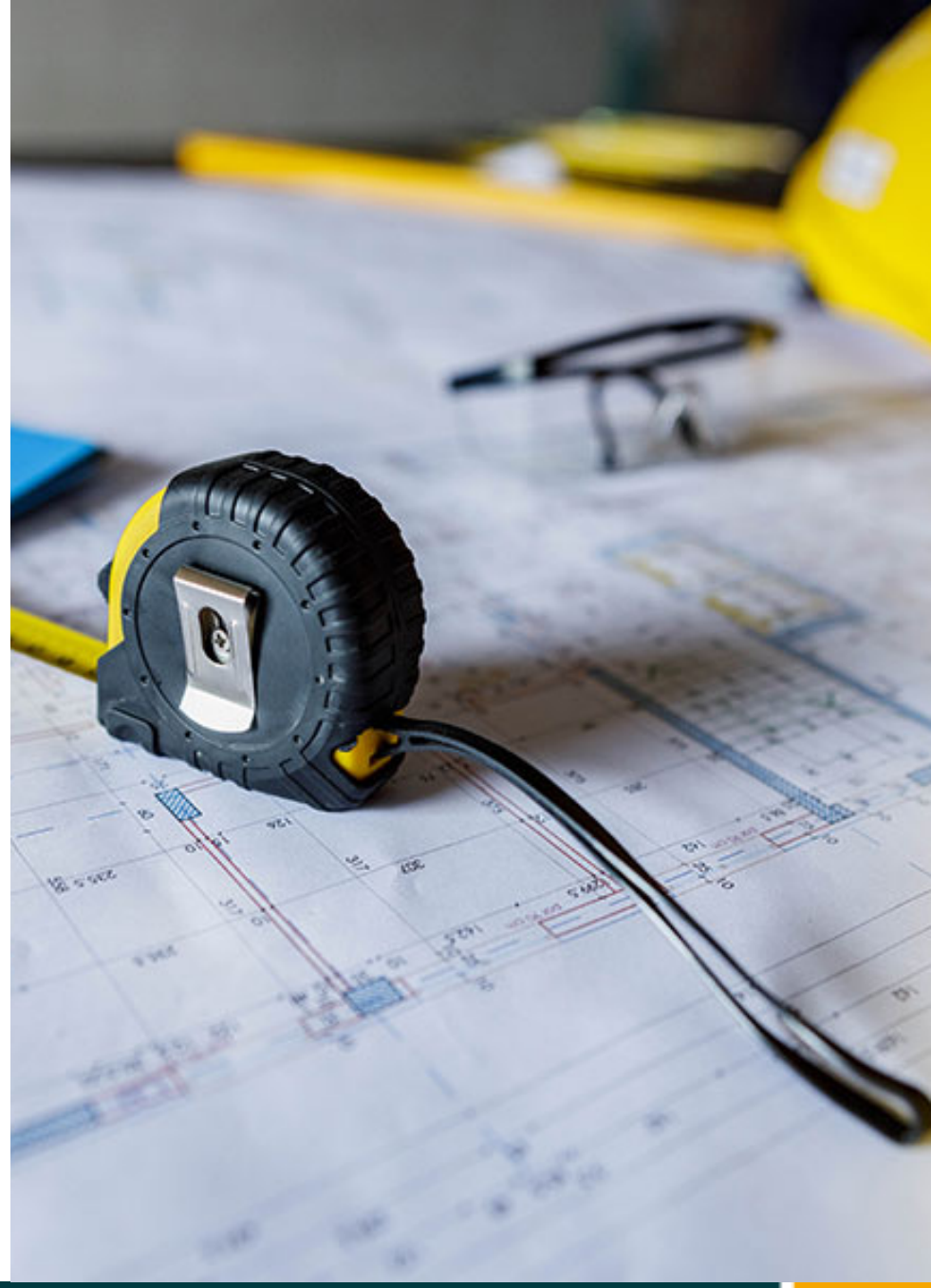
Design-Build Risk Management Lesson 8

Owner’s Implied Warranty of the “Bridging Specs”

Contractor Entitled to Rely on "Bridging" Specifications Provided by Owner

- RFP for medical clinic stated government's preliminary design could be used in preparing proposals, but that successful bidder must verify the design details during the design phase
- Turned out the initial design for steel was not adequate and Design-Builder had to increase amount of structural steel as well as rebar steel in concrete

M.A. Mortenson, Co., 93 BCA 26,189 (1993).



Contractor Entitled to Rely on "Bridging" Specifications Provided by Owner (cont.)

- Court declined to enforce contract clause that stated the Design-Builder was "to verify and validate the accuracy of the preliminary design information"
- Court found Design-Builder's duty to verify design was only after award – not during bidding
- Court said contract docs didn't say "the information was to be used at the proposer's risk"

Can Rely on Bridging Spec Design Details to Complete Final Design to Meet Performance Specifications

- RFP for the design-build of a ship for the Navy included:
  - Preliminary structural design details concerning steel.
  - Language requiring Design-Builder to do own calculations and prepare final design to meet performance requirements of ship – including certain vibration limits
- D-Bldr determined it was necessary to substantially alter the amount and size of the steel to avoid excessive vibration
- Govt. denied change order (REA) to pay Design-Builder additional costs

Bethlehem Steel Corp., 72-1 BCA 9, 186 (1971)

Can Rely on Bridging Spec Design Details to Complete Final Design to Meet Performance Specifications (cont.)

- Board HELD:
- “Where performance specifications are accompanied by detailed drawings, absent effective disclaimer, the contractor has the right to rely on the drawings ‘for adequate detail to meet the performance requirements without substantial change or redesign.’"

Bethlehem Steel Corp., 72-1 BCA 9, 186 (1971)

Where Govt Drawings of Existing Building Conditions Were Inaccurate, Design-Builder Required to Verify Actual Conditions

- RFP for design-build sprinkler contract included "background" drawings of existing conditions of a VA Hospital
- RFP required Design-Builder to verify all information provided by govt.
- After award, Design-Builder learned drawings were inaccurate and it had to perform a complete field survey of the hospital.
  - Design-Builder said it had only intended to "spot check" the drawings against conditions

Fire Security Systems, Inc., 02-2BCA 31,977 (1999).

Where Govt. Drawings of Existing Building Conditions Were Inaccurate, Design-Builder Required to Verify Actual Conditions (cont.)

- Govt. denied change order (REA) for extra costs of doing field survey
- Board HELD: Design-Builder not entitled to recover since the work was not “extra” but was already included in contract
  - Contract required Kr to “verify” not merely “spot check”

Where Govt Drawings of Existing Building Conditions Were Inaccurate, Design-Builder Required to Verify Actual Conditions (cont.)

Court found:

- "As a 'design and build contractor,' [the contractor] assumed a far greater responsibility for preparation of drawings than would a contractor that was constructing entirely with the use of prescriptive drawings and specifications.
- [The government-furnished drawings] were not intended to superseded the design/build contractor's independent obligation to verify the accuracy of each room's dimensions…."

Fire Security Systems, Inc., 02-2BCA 31,977 (1999).

Owner Liable to Design-Builder

- Owner liability is limited because not coordinating work of or resolving disputes between the designer and contractor
- If owner becomes involved in everyday decisions or acts in supervisory role, its liability to the Design-Builder may be comparable to its liability to contractor in traditional contract setting
  - Where owner became involved in design process by increasing size of facility and modifying mechanical and electrical systems
  - It was found to be in de facto partnership with Design-Builder and found interferences by owner to be breach of contract

Armour & Company v. Scott, (W.D.Pa. 1972)

Design-Build Risk Management Lesson 9

Bidder Must Seek Clarification of Ambiguities in Contract Doc & Specs

Design-Builder Must Ask About Obvious Conflicts in Specs

- RFP contained conflicting requirements regarding use of aluminum or steel for ventilation registers, grilles and diffusers
- Govt. required more expensive materials than D-Bldr said it intended to use
- Govt. denied change order (REA) – asserting even if the specification could be read to allow either or both materials, the discrepancy was "patent" and because Design-Builder failed to inquire about what material was required, it can't take advantage of the discrepancy to use the less expensive material

United Excel Corp., 04-1 BCA 32485 (2003).

Design-Builder Must Ask About Obvious Conflicts in Specs (cont.)

- Board HELD: The rule pertaining to patent conflict applies to design-build projects just as to other projects

  - "… The case law indicates that a design build contract shifts risk to a contractor that a final design will be more costly than the bid price to build and that the traditional rules of fixed price contract interpretation still obtain."

United Excel Corp., 04-1 BCA 32485 (2003).

Design-Build Risk Management Lesson 10

Indemnification & Defense Obligations Can Be Costly

Indemnity, LoL and Insurance Can Be Tied Together and Claim Release Enforced

- EPC contract limited Design-Builder liability to CGL insurance proceeds
- Indemnity clause stated Owner would “release, defend, indemnify and hold harmless” the contractors to extent insurance did not cover loss
- Explosions occurred 2 and 3 years after contract execution

National Union Fire Ins. V. John Zink Co., 2010 WL 4523760 (Tex. 2010)

Indemnity, LoL and Insurance Can Be Tied Together and Claim Release Enforced (cont.)

- Owner and its Insurers argued that because the LoL/ waiver/release/indemnity was executed PRIOR to the explosions, it did not apply to claims for damages from the later explosions

- Held: Since the alleged negligence of contractors was on work performed prior to the waiver/release being signed, damages arising out of the negligent work was released even though explosions and damages had not yet occurred

- What matters is when the negligence occurred, not when the damages materialized

Indemnity, LoL and Insurance Can Be Tied Together (cont.)

- In enforcing the release provision, the court explained:
  - "Valero and Kellogg are sophisticated entities, replete with learned counsel…They negotiated their working relationship over the course of almost three years with Kellogg submitting several proposals for Valero's review….Valero, having bargaining power equal to Kellogg's, agreed to the exculpatory clause in this contract. Valero possessed resources necessary to ascertain and understand the rights it held….Valero, of its own accord, negotiated those rights away."

Limitation of Liability Enforced

- Limit of Liability clause enforced to limit Design-Builder's liability to $332,000 to its client, Unocal, for breach of contract damages where client claimed that an eight-month delay in project completion was caused by Design-Builder's failures

- Court concluded that Unocal was experienced with such contracts and voluntarily acquiesced to the Limit of Liability clause — that Unocal was "a giant and sophisticated company" and there was no evidence of an unequal bargaining position

Union Oil v. John Brown (N.D. Ill. 1995)

Limitation of Liability — Cover all Causes of Action

- Courts strictly construe Limit of Liability clause
  - Clause provided: “The Owner agrees to limit Engineer’s liability to Owner and to all Construction Contractors and Subcontractors on the Project, due to Engineer’s professional negligent acts, errors and omissions, such that the total aggregate liability of the Engineer to those named shall not exceed $50,000 or the Engineer’s total fee for services rendered on the project, whichever is greater.”
  - Failure of A/E to timely submit plans to government agency resulted in loss of $338,935 in EPA grant funds
  - Court found LoL was only for negligence claims
  - This was breach of contract and court refused to limit damages

Wm Graham v. Cave City,289 Ark. 105, 709 S.W. 94 (1986).

Limitation of Liability — Cover all Causes of Action (cont.)

Clause provided:

- "The Owner agrees to limit Engineer's liability to Owner and to all Construction Contractors and Subcontractors on the Project, due to Engineer's professional negligent acts, errors and omissions, such that the total aggregate liability of the Engineer to those named shall not exceed $50,000 or the Engineer's total fee for services rendered on the project, whichever is greater."

Wm Graham v. Cave City,289 Ark. 105, 709 S.W.94 (1986).

Limitation of Liability

- To the fullest extent permitted by law, the total liability, in the aggregate, of Consultant and its officers, directors, partners, employees, agents, and Subconsultants, to Client, and anyone claiming through or under Client, for any claims, losses, costs, or damages whatsoever arising out of, resulting from or in any way relating to this Project or Contract, from any cause or causes, including but not limited to tort (including negligence and professional errors and omissions), strict liability, breach of contract, or breach of warranty shall not exceed the total compensation received by Consultant or $XXX,000, whichever is greater.

Mutual Waiver of Consequential Damages

- Consultant and Client waive all consequential or special damages, including, but not limited to, loss of use, profits, revenue, business opportunity, or production, for claims, disputes, or other matters arising out of or relating to the Contract or the services provided by Consultant, regardless of whether such claim or dispute is based upon breach of contract, willful misconduct or negligent act or omission of either of them or their employees, agents, subconsultants, or other legal theory, even if the affected party has knowledge of the possibility of such damages. This mutual waiver shall survive termination or completion of this Contract.

Design-Build Risk Management Lesson 11

Designer Becomes Liable to Contractor

Designer Liable to Contractor

- D/B contracted to design and fabricate storage.
  - subcontracted steel design to an engineer
- Engineer miscalculations caused structure collapse
- Engineer liable for injuries because of duty to create design imposing no unreasonable danger to those implementing it

Mudgett v. Marshall, 574 A.2d 867

DP Liable to Kr for Cost Overruns

- A/E breached implied warranty that its design was sufficient to enable Kr to adequately price bid for design-build proposal
  - Kr relied on drawings and specs prepared by A/E per oral contract to be used for bidding the job
  - Maddox v. The Benham Group, 88 F.3d 592
- Kr relied on A/E's drawings in preparing its guaranteed maximum price (GMP) proposal to owner. The drawings had major defects, requiring substantial changes — increasing project cost and causing delay. A/E held liable for costs
  - Skidmore, Owings & Merrill, 1997 Wash. App. LEXIS 1505

Subcontractor Relationships

- Notice requirements for Changes or Claims must be strictly followed
  - Sub was precluded from recovering on delay claims because failed to comply with the subcontract's notice requirements
  - Port Chester Elec. Constr Corp. v. HBE Corp. (S.D. NY 1995)
  - Lead JV partner had duty to submit a claim to project owner from its partner in a timely manner
  - Ahtna, Inc. v. Ebasco, 894 P.2d 657 (Alaska 1995).

Design-Build Risk Management Lesson 12

Ownership of Plans & Specs

Who Owns the Design-Builder's Design

- Contract should make clear who owns the design work product
  - After reaching a verbal agreement to design renovation of a large home, the architect (Johnson) and owner began negotiating a Design-Build contract and each began performance of their respective obligations
  - Architect obtained construction estimates, prepared general demolition and construction plans and completed several drafts of preliminary design drawings
  - Owner approved plans and paid for them

Johnson v. Jones, 885 F. (Supp 1008)

Who Owns the Design-Builder's Design (cont.)

- Owner terminated the relationship with the architect before executing a signed contract and then contracted with another architect. A CM firm who then used Johnson's work product to complete the project
- Johnson sued owner and successor architect for copyright infringement
- Court looked at documentation of contract negotiations and found that Johnson never intended to relinquish control of drawings
- Johnson had submitted several contract drafts based on AIA Document B141 language

Who Owns the Design-Builder's Design (cont.)

The intended contract language:

- "The drawings, specifications and other documents prepared by the Architect for this Project are instruments of the Architect's service for use solely with respect to this Project, and the Architect shall be deemed the author of these documents and shall retain a common law, statutory and other reserved rights, including the copyright….
- The Architect's Drawings, Specifications and other documents shall not be used by the Owner or others on other projects, for additions to this Project or for completion of this Project by others, unless the Architect is adjudged to be in default under this Agreement, except by agreement in writing and with appropriate compensation to the Architect."

Make Transfer of Ownership of Docs Contingent on Payment

- Be careful of wording stating that upon signing the contract the designer transfers all ownership and copyright interests

- Make this conditioned upon having been paid all undisputed amounts owed on invoices

Questions?

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