Construction Law 2023

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USA: Law & Practice
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USA

Law and Practice

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Jones Walker LLP has more than 30 construction attorneys who deliver comprehensive legal services to clients throughout the construction industry. The firm’s national footprint, the depth and breadth of the team and the scale of the projects on which it works enable it to provide effective counsel on virtually every issue its clients may face. Members of the construction team regularly represent clients across the USA and abroad, and excel at handling large-scale construction and infrastructure projects across industries such as aviation, energy, natural resources, healthcare, retail and education. The firm is familiar with the full scope of US and international procurement and government contracting regulations, and the lawyers regularly help negotiate and close agreements involving economic development funding, tax incentives and P3s. They also advise on environmental regulation and permitting, real estate, finance, government relations, labour and employment, and other areas involved in planning and executing projects.

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1. General

1.1 Governing Law
Under the US federal system, there is federal or national law and the laws of the 50 individual states. Commercial relations are principally governed by state law. Other than federal laws addressing specific federal policies, discussed below, there is no “national construction law” in the USA.

The Associated General Contractors of America (AGC) and the American Bar Association Forum on Construction Law (ABA), two large and respected national organisations, create and annually update the online Construction State Law Matrix. This practice guide references the AGC/ABA Construction State Law Matrix throughout.

The matrix can be found here: www.agc.org/industry-priorities/contracts-law/state-law-matrix.

This matrix is a starting point for identifying and researching state construction laws; it is not a definitive statement of the law on any topic in any state.

There is substantial similarity across state laws, but each state has its own constitution and statutes, and common law governs both. Model uniform laws enacted by many or most states reinforce similarities across state laws. When federal law applies and it conflicts with the otherwise applicable state law, federal law controls.

1.2 Standard Contracts
Standard contract forms are frequently used in the construction industry in the USA. The use of standard forms on private projects is voluntary and not mandatory. Parties are free to draft their own contracts, with limited exceptions that the contract terms cannot violate the public policy of a particular state.

On contracts with federal, state or local governments or involving public funding, the contract form or specific terms may be required by statute or regulation. The federal government, in particular, has extremely specific and detailed mandatory contract clauses that must be employed. Part 36 of the Federal Acquisition Regulation (FAR) regulates federal projects and prescribes policies and procedures unique to contracting for construction and architect-engineer services, and includes requirements for using certain clauses and standard forms that apply also to contracts for dismantling, demolition, or removal of improvements. These can be found at www.acquisition.gov/far/part-36.

FIDIC standard contracts are generally not used on projects in the USA, but there is nothing prohibiting the use of FIDIC standard contracts by private parties. The American Institute of Architects (AIA) publishes the most commonly used standard construction and design form contracts at www.aiacontracts.org/. The AIA has a large variety of standard forms depending on the project delivery system, the relationship between the parties, including Owner-Contractor, Owner-Design-Build, Contractor-Subcontractor, Owner-Architect, type of contract pricing, etc.

In the USA, the term “employer” is not used. Instead, the term most widely used in the USA, including in standard construction contracts is “owner”, “project owner”, or if the owner is a public entity, the “government”. For consistency, the term “owner” rather than “employer” will be used throughout this practice guide.
The standard construction contract forms published by ConsensusDocs at www.consensus-docs.org/contracts/ are the next most frequently used set of forms after those published by the AIA. ConsensusDocs was founded under the leadership of the AGC, the largest national construction trade organisation, along with 19 other construction organisations. ConsensusDocs also offers a complete library of forms to cover a wide range of construction transactions, similar to the AIA’s offerings.

Other standard forms are published by the Engineers Joint Contract Documents Committee (EJCDC) at www.ejcdc.org, and the Design-Build Institute of America (DBIA), dbia.org/contracts/. EJCDC documents tend to focus on heavy civil and industrial construction, rather than building construction. The family of standard forms published by the DBIA obviously focuses on construction under a design-build delivery system.

2. Parties

2.1 The Employer
In the USA, project owners are typically federal and state governments (public contracts), or private developers and builders (private contracts).

Owner’s Responsibilities on Federal Projects
As noted in 1.2 Standard Contracts, public contracts are subject to complex regulations established by federal and state governments including FAR Part 36. The government agency (such as the Army Corps of Engineers, the Department of Defense, or the Department of Agriculture) procures pre-qualified private contractors or design professionals to competitively bid on public contracts. The government agency may award the project based on a traditional sealed bid process or through a competitive negotiation process. Public owners have rights and obligations to disclose information, pay contractors, direct changes to the work and enforce the contract in the event of a contractor default or if the work is defective or incomplete.

Owner’s Responsibilities on Private Projects
On private contracts, project owners such as private developers, owner-builders and private investors may contract with multiple parties to assist with construction activities, including lenders (financing the project), design professionals and general contractors. A private owner’s typical duties include managing financing, land acquisition, providing accurate site data (geotechnical data, utilities, surveying), paying design professionals and contractors and interacting with local government agencies. Once construction is completed, a private owner may operate and maintain the project/facility, or sell the project/facility to a new owner.

The standard industry contract forms set forth specific owner responsibilities including providing information to the contractor and the design professional, describing the work site (surveys, drawings, subsurface conditions); securing permits; and reserving the right to stop, suspend, or carry out the work (AIA Document A201 – 2017 § 2; ConsensusDocs 200 § 4 (2011, Revised 2019)).

2.2 The Contractor
The traditional method of contracting in the USA is a design-bid-build process in which the owner contracts separately for design and construction services. Under this method, a “general” contractor is hired by the project owner to build, manage and oversee all aspects of construction from the start of construction through to completion, including providing the materials,
labour, equipment and services necessary for construction.

General contractors are usually larger contractors with ample resources and manpower to oversee larger construction projects. During construction, general contractors work directly with the owner and the design professional and its subcontractors to schedule, plan and execute construction activities. On a day-to-day basis, general contractors are responsible for project safety, co-ordinating site access, monitoring schedules and managing subcontractors.

On public projects, a contractor is subject to more complex rights and obligations in performing its work. FAR Subpart 36.2, “Special Aspects of Contracting for Construction”, sets out detailed regulations relating to labour, liquidated damages and bonding requirements applicable to federal construction projects, which would not be applicable on private projects.

2.3 The Subcontractors

Subcontractors, including speciality trade contractors, suppliers and service providers, contract with the general contractor or other subcontractors to perform a specific scope of work. Subcontract agreements set forth the subcontractor’s rights, obligations, scope of work, conditions of payment and dispute resolution process. The industry standard contracts, including those supplied by ConsensusDocs and the AIA, have established a subcontractor series specific to subcontractors (ConsensusDocs 700 Series; AIA A401 (2017 ed)), which incorporate and consider important rights and terms unique to a subcontractor, including conditions of payment and “flow-down” clauses.

Flow-Down Clauses

“Flow-down” clauses require the subcontractor to agree to have the same rights and privileges in relation to the general contractor as the general contractor has to the owner. Such clauses are common in subcontract agreements as they ensure consistency between the owner/contractor and contractor/subcontractor agreements. See, for example, AIA Document A201 – 2017 § 5.3 and ConsensusDocs 200 § 5.2 (2011, Revised 2019). More information on subcontracting is addressed in 8.2 Subcontracting.

2.4 The Financiers

Lenders, banks, government agencies, real estate investment trusts, or other special purpose investment vehicles (“lenders”) regularly provide the financing to support construction projects. Owners enter into financing arrangements and contracts with lenders to receive financial support for the major components of construction such as land acquisition, design planning services (architect, engineer) and paying contractors.

A construction financing agreement sets forth the rights and terms between a lender and owner, including the lender’s financing obligations, the terms of the loan, the collateral or guarantee obligations of the owner, schedule requirements and conditions precedent to loan distributions. Although lenders are not involved with day-to-day construction activities, lenders may contract to have certain rights to approve qualified contractors, take over construction activities if the owner defaults, declare owner default, pay contractors and subcontractors, and accept project completion.
3. Works

3.1 Scope

Private and Public Contracts

On private contracts, the owner is responsible for determining the scope of the work for the construction contract. Owners typically engage a design professional and possibly other consultants to assist the owner and handle much of the detailed development of the scope of the work and to ensure that the scope of the work is complete and accurate to meet the needs of the project. On public contracts, heavy civil and infrastructure projects, larger government agencies, especially the federal government and state departments of transportation, are more likely to develop the scope of the work in-house. Governments, regardless of size and sophistication, will almost always engage an outside design professional for building construction scopes of work. Smaller government entities are more likely to engage outside resources to develop the scope of the work, regardless of the type of construction.

Building Construction

In building construction, the process will typically start with the development of the owner’s programme of requirements, but ultimately result in detailed plans and specifications, unless design-build is used. For infrastructure projects, the process will typically start with the conceptual design, but also result in detailed plans and specifications, unless design-build is used. Even on design-bid-build projects, contract specifications often include at least some element of performance specifications, which require the contractor to “design-build”. Performance specifications generally provide less specific information but give the desired result of the construction, and require the contractor to design that element of the work, subject to review and approval by the owner through its design professional.

3.2 Variations

Changes or variations, whether initiated by the owner or the contractor, are typically addressed through the changes clause of a contract. A changes clause typically defines what constitutes a change, which party is entitled to request the change, notice requirements once a change is identified, practical steps involved in requesting and implementing a change, and procedures to determine adjustment of the contract price and performance time. A changes clause is commonly utilised to address issues such as differing site conditions, design conflicts, scope changes and force majeure events. For changes or variations that extend the time for performance, delays that are considered non-compensable delays (eg, bad weather) entitle the contractor to a time extension but do not entitle the contractor to any additional cost that may be incurred as a result of a non-compensable delay. However, delays that are unforeseeable and beyond the contractor’s control may be compensable, entitling the contractor to not only a time extension by also additional compensation.

Industry Standard Construction Contracts

The industry standard construction contracts specifically address how such changes will be managed by the parties during construction, whether requested by the owner or contractor (A201 – 2017, Article 7; ConsensusDocs 200; Article 8 (2011, Revised 2019)). Owners have the right to change the contractor’s work, but the problem often arises when the parties cannot agree on a price for the changed work. If the parties cannot agree on the adjustment of the time or contract sum, the contractor can submit a claim in accordance with the contract; however, the contractor will be required to perform the
work to avoid delays (A201 – 2017, Article 7.3; ConsensusDocs 200; Article 8.2 (2011, Revised 2019)).

Federal Government Construction Contracts

On federal government construction projects, the changes clause gives the government the right to make changes to the contract scope of the work, including changes to the specifications, method or manner of performance of the work, and to direct acceleration of the work. Along with that authority, the government also has an obligation to issue an equitable adjustment and modify the contract if the directed changes cause an increase or decrease in the contractor’s costs or the time of performance (FAR Part 52.243-4). Like the industry forms, if the parties cannot agree to any adjustment of the contract cost or time of performance, the contractor is required to submit a claim in accordance with the disputes clause of the contract (FAR Part 52.243-5).

3.4 Construction

General Contractor

The general contractor is typically responsible for all major construction activities, including planning and scheduling, and providing all the labour, materials, equipment and services necessary to complete the work. Relying upon the project design documents to perform construction, the general contractor is responsible for its own construction means, methods, techniques, sequences and procedures utilized (ConsensusDocs 200 § 3.1.3 (2011, Revised 2019)). Subcontractors are also responsible to the general contractor to perform their respective scope of work in accordance with the subcontract and project requirements.

Design Professional

Design professionals may have certain construction administration tasks requested by the owner in the design professional’s contract with the owner. For example, a design professional may be responsible for reviewing the contractor’s proposals, approving shop drawings, reviewing a contractor’s applications for payment, issuing changes and certifying completion of the project. Unless contractually agreed to, a design professional is not responsible for the contractor’s means and methods of performing its construction work.
Owner
Owners may also elect to perform construction activities themselves and to award separate contracts to contractors other than the general contractor. The AIA A201 form expressly reserves this right for the owner (see AIA Document A201 – 2017 § 6.1.1).

3.5 Site Access
Through the parties’ contracts, owners typically assume the risk of the project site and conditions, such as underground obstacles, geotechnical conditions and any archaeological findings. Such issues are not typically governed by mandatory or regulatory law, although the FAR clauses do specifically govern differing site conditions on public projects and provide that the government assumes the risk of differing site conditions (FAR Part 52.236-2).

Typically, a contractor will be required to provide the owner with prompt notice of a concealed or unknown condition when the conditions are encountered. The AIA General Conditions form provides that if the contractor encounters site conditions that differ from those expected, the contractor may be entitled to an equitable adjustment in the Contract Sum or Contract Time, or both (AIA Document A201 – 2017 § 3.7.4). A similar clause and relief are set forth in ConsensusDocs 200 Standard Agreement and General Conditions between Owner and Constructor (ConsensusDocs 200 § 9.6.2 (2011, Revised 2019); AIA Document A201 – 2017 § 9.8.4).

3.6 Permits
Different forms of permits may be required to access, construct and operate a building or facility (ie, building, safety and occupancy permits). Typically, owners place the burden on the general contractor or design-build contractor to obtain building and construction permits, and the contractor will be responsible for the fees, licences and inspections by government agencies necessary for proper execution and completion of the work. If the permit relates to land acquisition (easements or surveys) or use modifications (residential, commercial, mixed use), the owner is generally responsible for obtaining the permit and the associated fees (AIA Document A201 – 2017 §§ 2.3.1 and 3.7.1; ConsensusDocs 200 § 4.3 (2011, Revised 2019)).

3.7 Maintenance
During construction, the contractor is typically responsible for maintenance of the works. Maintenance can include a broad range of activities such as storage, signage, waste disposal, debris removal, clearing roads and pavements, and providing electricity to the project. Once a project reaches final completion, the owner will typically assume maintenance responsibilities. The division of maintenance responsibilities is addressed in the industry form contracts (ConsensusDocs 200 § 9.6.2 (2011, Revised 2019); AIA Document A201 – 2017 § 9.8.4).

3.8 Other Functions
Other functions of the construction process, such as operation, finance and transfer of ownership are generally addressed between the owner and third parties, not the owner and contractor.

3.9 Tests
The contractor typically assumes responsibility for the costs of tests, inspections and approvals, including co-ordinating with third parties or public authorities (AIA Document A201 – 2017 § 13.4.1; ConsensusDocs 200 § 3.7.1 (2011, Revised 2019)). However, an owner may be responsible for inspections deemed necessary after contract execution, as the contractor was unable to account for such costs in its pre-contract bid (AIA Document A201 – 2017 § 13.4.1;
ConsensusDocs 200 § 3.7.2 (2011, Revised 2019)). If procedures for testing, inspection or approval reveal portions of the work that fail to comply with the requirements established by the contract, the contractor will bear responsibility for the costs to meet the standards necessary to pass the tests, inspections or approvals (AIA Document A201 – 2017 § 13.4.3; Consensus-Docs 200 § 3.7.3 (2011, Revised 2019)).

3.10 Completion, Takeover, Delivery
Achieving substantial or final completion, takeover and delivery of the project generally occurs when the work has been performed in accordance with the contract documents such that the owner can occupy or utilise the work for its intended use. After inspections are complete and the work is designated as substantially complete, the design professional will prepare a certificate of substantial completion that will establish the date of substantial completion, at which time the warranties required by the contract documents will commence and the owner will take over the project (AIA Document A201 – 2017 § 9.8).

The owner may occupy or use any completed or partially completed portion of the work at any stage when such portion is designated by separate agreement with the contractor, provided such occupancy or use is consented to by the insurer and public authorities (AIA Document A201 – 2017 § 9.9; ConsensusDocs 200 § 9.6 (2011, Revised 2019)).

3.11 Defects and Defects Liability Period
In the United States it is standard for the contractor to cure defective work for a period of one year after substantial completion of the work (AIA Document A201 – 2017 § 12.2.2; ConsensusDocs 200 § 3.9 (2011, Revised 2019)). Owners are required to provide the contractor with prompt notice of defective work discovered after substantial completion, otherwise the owner may risk waiving its rights for the contractor to correct the defect (AIA Document A201 – 2017 § 12.2.2.1; ConsensusDocs 200 § 3.9 (2011, Revised 2019)). If after receiving prompt notice the contractor fails to correct the work in a reasonable time period, the owner may correct the work under its contractual right to carry out the work and issue a deductive change order for the cost of correcting the defective work, or recover the costs from the contractor (AIA Document A201 – 2017 § 12.2.4; ConsensusDocs 200 § 3.9.3 (2011, Revised 2019)). The one-year warranty period will not release the owner’s right to breach of contract claims alleging defects in the work (AIA Document A201 – 2017 § 12.2.5; ConsensusDocs 200 § 3.9.6 (2011, Revised 2019)). The breach of contract claim remains available to the owner for the applicable law and statute of limitations. The time period to assert a claim for a construction defect is set by state statutory law and varies from state to state. A general survey of state statutes of limitation and repose can be found here: www.agc.org/industry-priorities/contracts-law/state-law-matrix.

Like the statutory time periods mentioned above, the remedies for construction defects vary from state to state. Generally though, remedies for construction defects include recovery for diminished value of the project or building, loss of income (ie, loss of rent) and costs of repairs.

4. Price
4.1 Contract Price
In the USA, the owner generally determines the method of establishing the contract price through
the owner’s selection of its preferred contract structure and means of procuring price bids or proposals from contractors. In design-bid-build construction, the owner typically solicits lump-sum price bids through a competitive bidding process. The contract price may also be established through competitive negotiations with competing contractors, or by directly selecting the contractor and negotiating the price.

Selecting a Contractor by Competitive Bid
The contract award from a bidding process may be based solely on the lowest price, or on the best value, experience of the contractor, proposed work plan, schedule and other factors. The bidding process and manner of award is determined by the owner and whether the project is funded or owned by public or private entities. Public entities are subject to specific laws that determine the manner in which the procurement is conducted and how the contract is awarded. A private owner can select whatever contractor it prefers and the owner is not required to engage in any competitive process.

Determining the Type of Contract Price Structure
The project delivery structure selected by the owner will affect the contract price structure, the status of the project design when the construction contract price is determined and the various project components that will be included in or excluded from the contract price. The contract price can be structured as a fixed, lump-sum price; unit price; cost reimbursement with a fixed fee or a percentage fee; or a guaranteed maximum price.

4.2 Payment
In the USA, construction contracts generally provide certain remedies for late payment and non-payment. The construction contract may provide a rate of interest for late payments or provide the contractor with the right to stop work (after providing proper notice concerning the non-payment) without the contractor breaching the contract. Non-payment or late payment can also be a breach of the construction contract that results in the contractor being entitled to damages or, if on a prolonged basis, the right to stop work and/or terminate the contract (AIA Document A201 – 2017 §§ 9.7, 14.1; ConsensusDocs 200 §§ 9.5, 11.5 (2011, Revised 2019)).

In addition to contract remedies, there are specific federal statutes that address prompt payment of subcontractors and suppliers on federal construction projects (31 U.S.C. §§ 3901-3905). Numerous states have also enacted specific statutes similarly addressing prompt payment of contractors and/or subcontractors and suppliers. A survey of such prompt payment statutes can be found here: www.agc.org/prompt-payment-state-state-map.

State mechanic’s and materialmen’s lien laws provide extra-contractual remedies to contractors for non-payment. The lien laws allow an unpaid contractor, including subcontractors and often sub-subcontractors and suppliers, to place a lien on the property improved by the contractor’s labour, services, and/or materials. State lien laws also frequently authorise the lien claimant to recover its attorney’s fees in a court foreclosure action.

A lien claimant may bring a lawsuit against the property owner to foreclose the lien and sell the property to pay the amounts owed to the contractor. Lien rights and requirements are a matter of state law. There is no federal or national lien law. The substantive rights and required procedures vary significantly from state to state. A general survey of state lien laws can be found
Federal, state and local public construction projects are generally not subject to liens; payment protection for subcontractors and suppliers, but not contractors, comes through statutorily required payment bonds.

Payment bonds, whether required by state and federal law or at the direction of the owner, provide protection to subcontractors for non-payment. A payment bond is an agreement between a contractor and a surety where the surety guarantees payment for the labour and materials to be employed on a project. Claimants may be subcontractors, suppliers or labourers who perform work for a contractor on the bonded project.

To protect subcontractors and suppliers, the Federal Miller Act requires that federal government construction contractors on projects over USD100,000 provide a payment bond, typically with the required value or “penal sum” equal to the value of the construction contract (40 U.S.C. §§ 3131-3134). The Miller Act also requires the contractor to provide a separate performance bond equal in value to the contract price. The performance bond is generally for the protection of the federal government as project owner.

Many states have enacted laws similar to the Federal Miller Act that require payment and performance bonds from contractors on state and local construction projects. The state statutes are generally referred to as “Little Miller Acts”. A general survey of state laws addressing payment and performance bonds can be found at the state law matrix site listed in 1.1 Governing Law.

Private owners may also require payment bonds from the contractor. Such bonds are not required by statute and are generally governed by traditional state commercial or contract law, or state statutes separate from Little Miller Acts.

A construction contract is typically invoiced:

- on a monthly basis for the percentage of work completed during the invoiced period, based on a schedule of values;
- as equal monthly payments over the construction period; or
- based on the contractor achieving certain project milestones.

Monthly payments based on percentage completed against an agreed-upon schedule of values is the most widely used method. Milestone payments are usually restricted to large industrial projects. Advance payments are not typical in construction contracts; however, contractors are generally paid an upfront amount for mobilisation.

4.3 Invoicing

As discussed in 4.2 Payment, monthly payments based on percentage completed against an agreed-upon schedule of values is the most widely used method. Most construction contracts and many state and federal laws stipulate the time by which payment must be made after invoices are submitted. This is usually as soon as 15 days after receiving the contractor’s invoice. Otherwise, late payments will incur interest and entitle a late-paid contractor to other remedies (AIA Document A201 – 2017 § 13.5; Consensus-Docs 200 § 9.9 (2011, Revised 2019)).
5. Time

5.1 Planning Programme
The project owner generally dictates the planning of projects in the USA. The project delivery method selected by the owner will largely dictate how project planning is organised, especially the choice between design-bid-build, design-build or engineering, procurement and construction (EPC), and construction manager at risk.

The transition from project planning to project execution is generally tied to development of the design. In the USA, the progress of the design is typically measured against the following milestones:

- programming phase of design;
- schematic design;
- design development;
- construction documents; and
- bidding phase.

These phases or milestones are tied to the design-bid-build project delivery system. In design-build or EPC contracting, drawing up a contract with the designer-builder or EPC contractor will take place long before final construction documents are completed. In design-build, EPC contracting and construction management at risk, parts of the design can be fast-tracked, meaning that parts of the design are finalised early to release fabrication and installation and construction before the entire design is complete.

5.2 Delays
Most construction contracts and all standard construction contracts include detailed requirements for the contractor to provide notice, explanation and documentation of delays anticipated or experienced.

Generally, contracts oblige the contractor to provide written notice to the owner in the event of delay. Such initial notice and documentation may be the first step in the contract change order-claim-disputes procedures if the parties disagree over entitlement to relief. See, for example, ConsensusDocs 200 § 6.3.3 (2011, Revised 2019).

Under the FAR, a contractor’s claim for government-caused delay may not be allowed “[u]nless the claim, in an amount stated, is asserted in writing as soon as practicable after the termination of the delay or interruption, but not later than the day of final payment under the contract” (FAR 52.242-17).

In addition to initial notice, the process to determine the cause and responsibility for delay also generally requires the contractor to document the events giving rise to the delay, related communications, the effects of the delay and efforts to mitigate the delay. If the contractor fails to provide timely notice and otherwise fails to comply with contract procedures to seek a time extension, the contractor may lose the right to an otherwise valid request for a time extension.

Delays are either compensable or non-compensable, as defined by the contract. Delays that are considered non-compensable delays (eg, bad weather or concurrent delay caused by the owner and contractor) entitle the contractor to a time extension but do not entitle the contractor to any additional cost that may be incurred as a result of a non-compensable delay. However, delays that are unforeseeable and beyond the contractor’s control may be compensable, entitling the contractor to not only a time extension by also additional compensation.
5.3 Remedies in the Event of Delays
Owners have several remedies against the contractor for delays that do not merit a time extension (inexcusable delays), including:

• demanding acceleration to meet the schedule;
• actual costs of the delay or liquidated damages (discussed in 9.3 Sole Remedy Clauses); and
• in certain cases, the right to terminate the contract for default.

Under FAR 52.249-10, for example, the government may “terminate the right to proceed with [a contract] that has been delayed” (FAR 52.242-17).

A contractor may be able to defeat or reduce an owner’s claim for liquidated or actual delay damages if there is a separate, excusable delay that is concurrent with all or part of the contractor’s delay. In the event of concurrent delays, the owner and contractor typically each bear their own costs for the delay and the contractor is entitled to a time extension for the duration of the concurrent delays.

5.4 Extension of Time
Typically, when requesting a time extension, a contractor must provide formal notice to the contract administrator in the manner and within the timeframes specified in the contract, as well as all documentation supporting the claim. After the request has been sent, the owner’s designated representative will determine if the evidence is sufficient to justify a time extension. The representative’s determination will turn on the grounds provided in the contract that may entitle the contractor to a time extension.

If the owner’s designated representative agrees and grants an extension, a change order is issued to the contractor. If the request is denied, the contractor may escalate or appeal in accordance with the dispute resolution provisions in the contract. These procedures are generally set forth in the standard industry contracts. See, for example, ConsensusDocs 200 §§ 6.4, 8.4 (2011, Revised 2019).

5.5 Force Majeure
Under US law, “force majeure” commonly refers to natural and unavoidable catastrophes that affect contract performance. If a force majeure event occurs, force majeure clauses in construction contracts are written to make sure that the parties are protected from interruption of the work by events that are outside of their control.

Most standard form construction contracts do not specifically use the term “force majeure”. Instead, relief for force majeure events is addressed in delay and time-extension remedial clauses. See, for example, AIA Document A201 – 2017 § 14.1.1.2.

For public projects, the relevant FAR provision (Excusable Delays) includes examples of force majeure events, such as, “(1) acts of God or of the public enemy, (2) acts of the Government in either its sovereign or contractual capacity, (3) fires, (4) floods, (5) epidemics, (6) quarantine restrictions, (7) strikes, (8) freight embargoes, and (9) unusually severe weather” (FAR 52.249-14 May 2007).

It is also possible to contractually limit or exclude certain circumstances from being qualified as force majeure or what the AIA describes as “unavoidable casualties” and “other cause beyond the Contractor’s control” (AIA Document A201 – 2017 § 14.1.1). One way to do so is for the con-
tract to contain a very specific list of qualifying events (e.g., epidemic, earthquake, or hurricane) or other certain terms. In that case, the precise language of a force majeure clause may be interpreted to exclude events that are not specifically identified.

5.6 Unforeseen Circumstances
Standard form construction contracts, such as AIA and ConsensusDocs, do not have specific clauses to address “unforeseen circumstances.” These contracts do, however, contain excusable delay clauses that may cover unforeseen circumstances. The relief offered in these contracts could be a time extension, and for either party, the opportunity to terminate the contract.

Even if a contract does not contain an express clause addressing “unforeseen circumstances”, “force majeure” events, or other similar language addressing “acts of God” or unanticipated delays beyond the contractor’s control, a contractor may still have a legal right to relief against the owner under the common law doctrines of frustration of purpose or impracticability.

5.7 Disruption
In the US, disruption is acknowledged as a legal and/or contractual ground for additional compensation and/or a time extension. Contractors generally have two basic means of recovery for a disruption claim: (i) specific provisions of the contract, and (ii) general principles of contract law. Different from a claim for delay, disruption is usually a loss of efficiency during the contractual performance period, but the performance period itself is not necessarily extended. Damages associated with disruption are likely to be in the form of increased labour costs, for example, due to inefficiency, whereas damages for a pure delay claim result from an extended performance period.

Types of Disruption
The mere occurrence of a disruption does not entitle the contractor to additional compensation. Types of non-compensable disruption include events that should have been anticipated by the contractor, or disruption caused by the contractor’s own conduct. Another type of non-compensable disruption is events specifically excluded in the contract, such as acts of God, labour strikes and inability to procure materials. Also, while the disruption may be non-compensable, the disruption may entitle the contractor to additional time for performance, if the event extended the time necessary to perform a particular portion of the work.

Disruption can also be compensable pursuant to the contract or general principles of contract law. The FAR contains three clauses that often serve as the basis to recover costs arising from disruption on government projects: (i) the “Changes” clause (§ 52.243-4), (ii) the “Differing Site Conditions” clause (§ 52.236.2), and (iii) the “Suspension of Work” clause (§ 52.242.14). Similar provisions can be found in standard industry forms.

Proving Disruption
To establish disruption, claimants have the burden to identify events for which the owner was responsible, that caused disruption, and led to the contractor incurring additional costs for which he is entitled to recover from the owner. Contemporaneous project documents are often the best evidence to substantiate the events that may give rise to a claim for disruption. Causation and quantification of disruption and loss of productivity can be shown through a variety of productivity-based methods and cost-based methods – each with their own strengths, weaknesses and tailored applicability to the particular facts and circumstances in each case.
6. Liability

6.1 Exclusion of Liability
Contract clauses that limit or relieve parties from liability are generally referred to as “exculpatory clauses”. In the USA, exculpatory clauses are not favoured and will generally be narrowly construed. At a minimum, for exculpatory clauses limiting liability to be enforceable, they must be clear, unambiguous, unmistakable and conspicuous. Even when these criteria are met, state law, whether by statute or court precedent, may prohibit or limit certain exculpatory clauses as against public policy. Examples of impermissible exclusions of liability include indemnity of a party against a claim caused by the sole negligence, gross negligence or intentional misconduct of the party claiming the indemnity. Many states have enacted specific statutes that limit such indemnities in construction contracts. A general survey of state anti-indemnity clauses can be found here: www.agc.org/industry-priorities/contracts-law/state-law-matrix.

6.2 Wilful Misconduct and Gross Negligence
The concepts of “wilful misconduct” and “gross negligence” exist under US law. The definitions of gross negligence and wilful misconduct also vary from state to state and the conduct that the courts consider as falling under those definitions depends on the facts of each case. Typically, states prohibit limiting liability in construction cases if the conduct giving rise to the claim constitutes wilful misconduct or gross negligence. A general survey of state laws prohibiting limiting liability if the conduct involves wilful misconduct or gross negligence can be found here: www.agc.org/industry-priorities/contracts-law/state-law-matrix.

6.3 Limitation of Liability
Limitations of liability are considered exculpatory clauses that are disfavoured and narrowly construed under US law. Nonetheless, limitations of liability are enforceable if they are clear and unambiguous and do not violate an applicable law or public policy.

Construction contracts in the USA limit liability by waiving liability consequential damages. By establishing a ceiling for damages for delay, liquidated damages provisions can also serve as limitations of liability. Other limitations often found in construction contracts include limiting liquidated damages to a specific cap and limiting all damages to another specific cap, whether expressed as a specific dollar value or percentage of the contract price. If clear and unambiguous, such limitations of liability in construction contracts are regularly enforced.

Many states have anti-indemnity statutes, which limit and make void certain liability-shifting agreements as against public policy, to the extent that the provision requires an indemnitor to indemnify a party against a claim caused by negligence or intentional misconduct, a violation of statute, or breach of the contract by the indemnitee.

7. Risk, Insurance and Securities

7.1 Indemnities
Indemnity clauses – sometimes referred to as “hold harmless” clauses – are key components of a construction contract to help manage and mitigate liability and risks. Indemnity clauses can address a broad range of risks on a construction project, including but not limited to breach of contract, negligence, personal injury, property damage, third-party claims and loss of profits. A
general survey of state anti-indemnity clauses can be found here: [www.agc.org/industry-priorities/contracts-law/state-law-matrix](http://www.agc.org/industry-priorities/contracts-law/state-law-matrix).

### 7.2 Guarantees

Parties on a construction project are sometimes required to obtain guarantees of performance from other parties that may take the form of a personal guarantee by a corporate shareholder or a guarantee by a parent of a subsidiary company. However, on US construction projects, surety bonds are the most common form of guarantees used to limit risk for parties.

A surety bond, which is not insurance, is a guarantee in which a third party – often an insurance company – agrees to assume a defaulting contractor’s performance or financial obligations under the construction contract. The key difference between sureties and insurance is that sureties can seek reimbursement from the defaulting contractor if the surety is forced to take over and fulfill the defaulting contractor’s obligations under the contract.

An owner can require the contractor to guarantee its bid commitments, payments to subcontractors, and performance of the work by requiring the contractor to obtain a (i) bid bond, (ii) payment bond, and (iii) performance bond, respectively, from a licensed and financially responsible surety experienced in the needs of the construction business. Whether a public or private project, these three bonds generally protect the owner against the following risks.

- **Bid bond** – this guarantees that the contractor with the winning bid meets the requirements to enter into the construction contract, and in the event that the contractor fails to meet the requirements, the surety agrees to pay the owner the difference between the winning contractor’s bid and the next lowest bidder up to the amount of the bond.
- **Performance bond** – this guarantees that the contractor will perform in accordance with contract conditions and state regulations, and in the event of default by the contractor, the surety agrees to step in, investigate and, if necessary, ensure completion of the project and payment of the associated costs up to the amount of the bond.
- **Payment bond** – this works in conjunction with a performance bond to guarantee that labourers and suppliers are paid by the contractor, and if the contractor fails to pay its labourers and suppliers, to pay amounts owing up to the penal sum of the bond; on private projects, a payment bond also prevents liens on a project, which can impact the owner and the success of the project.

Contractors may also require subcontractor payment and performance bonds to obtain the security of the same type of financial guarantees.

Lastly, letters of credit may also be used as financial guarantees on construction projects in the USA; however, their use tends to be fairly rare as compared to surety bonds. In fact, most statutes requiring payment and performance bonds on public construction contracts require surety bonds rather than letters of credit.

### 7.3 Insurance

There are many different types of insurance tailored to protect owners, contractors and other project participants through all phases of a construction project. The insurance coverage typically required under US construction contracts is reflected in standard contracts (eg, Section 10.2 of ConsensusDocs) and includes:
• builder’s risk insurance for coverage of damage to buildings and other construction during the course of construction;
• commercial general liability insurance to provide liability protection to the insured in case of bodily harm or property damage;
• automobile and truck insurance for business vehicles; and
• worker’s compensation insurance to protect businesses and contractors if employees are injured on the job.

7.4 Insolvency
Insolvency of any important player on a construction project can have significant consequences for the project and all the participants.

Standard industry contracts such as the AIA and ConsensusDocs do not provide generally for any consequences if a party ceases to pay its debts in the ordinary course of business, cannot pay its debts as they become due, or seeks bankruptcy protection under federal bankruptcy laws.

Furthermore, US bankruptcy law restricts enforceability of “termination-on-bankruptcy” provisions if conditioned on the insolvency of the debtor or its financial condition, or the commencement of a bankruptcy case. Importantly, when an owner, contractor or other project participant in the USA seeks bankruptcy protection, federal law and other applicable laws will affect, and in many cases dictate, the parties’ remaining obligations under the construction contracts at issue, including obligations related to surety bonds.

7.5 Risk Sharing
Reasonable and equitable risk-sharing is common practice and a core principle for modern-day construction projects in the USA.

Standard form contracts such as those offered by ConsensusDocs and the AIA, as well as government contracts, seek to equitably allocate project risks to the party in the best position to control the risk and also to permit the parties to concentrate on key variables when negotiating the construction contract.

Provisions of critical importance to risk-sharing include: time extensions and time for completion, differing site conditions, damages for delay, change orders, excusable delays, defects in design, notice requirements, dispute resolution procedures and terms of payments.

8. Contract Administration and Claims

8.1 Personnel
Construction contracts in the USA typically include contractual provisions regarding the contractor’s personnel. These provisions typically address project oversight and supervision, safety, quality control, removal of personnel and the supply of adequate labour forces. Much less frequently, construction contracts may also limit the contractor’s ability to remove or replace the contractor’s own key personnel.

Project Oversight and Supervision
Parties will typically be required to designate a single project supervisor, such as a project manager or superintendent, who is regularly present at the project work site with full responsibility for the oversight, supervision and management of the contractor’s workforce. This designated supervisor will often have authority to make decisions for the contractor and bind the company to change orders and other contractual matters (AIA Document A201 – 2017 §§ 3.1, 3.9). Other key personnel are safety and quality
control managers, who can be required under the contract.

**Labour Force**

Contractors and subcontractors are generally required to provide adequate labour forces to carry out their work as necessary to achieve substantial completion within the time allowed by the contract (AIA Document A201 – 2017 § 8.2.3). Schedules incorporated into construction contracts typically do not establish a specific head count for the contractor’s labour force, unless the schedule is resource-loaded.

**Right to Require Removal of Personnel from the Project**

The employer/owner regularly retains the right to require removal from the project of any employee of the contractor or subcontractor who does not follow safety procedures, or is unfit or unskilled for the assigned work (ConsensusDocs 200 § 3.4.3 (2011, Revised 2019)). Contractors typically maintain in their subcontracts the same right to remove subcontractor personnel.

**8.2 Subcontracting**

Contractors in the USA are generally free to employ subcontractors to execute the work, provided the subcontractor has a licence to perform its scope of work and is authorised to do business in the location of the project. Employers/owners are generally given the right to reasonably and timely object to selected subcontractors (AIA Document A401 – 2017 § 5.2.3; ConsensusDocs 200 § 5.1 (2011, Revised 2019)).

Some limitations on the contractor’s ability to subcontract may come in the form of the requirement that all subcontractors be pre-approved by the owner or that the contractor utilises subcontractors from an owner pre-approved list or uses a subcontractor or supplier specifically designated by the owner. In state and local public contracting, the contractor may be required to list their subcontractors in their bid proposal.

**8.3 Intellectual Property**

In the USA, intellectual property that may be at issue in a construction contract includes patents, copyrights, trade marks and trade secrets. Federal law alone governs patents and copyrights. What constitutes trade secrets or proprietary information is generally a matter of contract or state law. Construction contracts typically address intellectual property issues on two fronts:

- ownership of the intellectual property associated with the design, and construction or fabrication techniques; and
- liability for violating the intellectual property rights of third parties who are not involved in the design and construction of the project.

Federal copyright law typically governs ownership of intellectual property in design documents. Copyright in a work vests initially in the author or authors of the work. Authored works include the engineering and architectural drawings and specifications that are typically the basis of all construction contracts. Federal law provides the owner of a copyrighted work the exclusive right to reproduce, adapt, publish, use or display the copyrighted work (17 U.S.C.S. § 106).

Ownership of intellectual property can be modified by contract. As a result, a designer can grant the owner a perpetual licence to use the design for the intended project while simultaneously retaining the copyright or the rights to any patents or trade secrets developed during the project.
Ownership of the Design on Design–Bid–Build Projects
On design-bid-build projects in which the owner provides a complete design for the contractor to construct, the contractor is typically authorised to use and reproduce the drawings and specifications for the execution of the construction (AIA Document A201 – 2017 § 1.5.2). The rights to the ownership of the design are determined by the contract between the owner and the designer.

On design-build projects, the design–build contract typically addresses the disposition of intellectual property rights over the design. For example, the design-build contract will outline the ownership of the electronic design documents (ie, the drawings and specifications); the copyright over the designs; and whether the parties can reuse the designs for other projects (ConsensusDocs 400 §§ 3.1-3.4 (2007, Revised 2011)).

9. Remedies and Damages

9.1 Remedies
Breach of contract is a cause of action available to two contracting parties in direct privity with one another. Contract damages available to parties for breach of contract include direct, indirect and consequential damages. The aggrieved party has an obligation to mitigate damages and typically cannot recover damages that could have been avoided through reasonable diligence and ordinary care.

Owner’s Remedies Against the Contractor or Design Professional
Contractor’s breach
In the event of a contractor’s breach, an owner typically has the right to carry out the work, terminate for cause, the right to withhold payment (set-off), and the right to recover direct, indirect, and/or consequential damages, subject to any remedy waiver or limitation of liability language expressly agreed to in the contract. See, for example, ConsensusDocs 200 § 11 8 (2011, Revised 2019); AIA Document A201 – 2017 § 14.

Design professional’s breach
If the design professional is in breach, the owner may seek similar remedies as against the contractor, as well as seek economic loss if the construction is unusable or defective. The design professional owes a duty of care generally defined as the professional skill and care that other professionals in the profession would use under similar circumstances in that area or jurisdiction. The design professional can be held liable to the owner if the design professional fails to meet the requisite standard of care.

Contractor’s remedies against the owner
A contractor’s breach of contract claims against the owner are typically based on contract changes from changed conditions or additional work, as well as requests for extensions of time for issues such as owner delays, change orders, design errors, or delays outside the contractor’s control (eg, weather and force majeure). If an owner refuses to acknowledge impacts to the contractor’s work caused by the owner or an owner’s representative, or the parties cannot agree on a price, the contractor may assert a breach of contract claim in accordance with the dispute resolution provisions of the contract. Common contractor claims for breach of contract against the owner include wrongful termination, delay and disruption, defective drawings and loss of productivity. Subcontractors have similar breach of contract remedies against the general contractor that the general contractor has against the owner as part of the flow-down rights and obligations in the subcontract.
9.2 Restricting Remedies
Remedies may be limited by contract or statutory law. For example, both the AIA A201 – 2017 and the ConsensusDocs 200 form agreements mutually waive consequential damages against the other party (AIA Document A201 – 2017 § 15.1.7; ConsensusDocs 200 § 6.6 (2011, Revised 2019)). Consequential damages do not flow directly from a breach of contract, but may indirectly relate to the breach; eg, loss of profits and loss of bonding capacity. It is inherently difficult to prove consequential damages, which is why it is common for the parties to agree to a mutual waiver.

9.3 Sole Remedy Clauses
Liquidated damages clauses are an example of sole remedy clauses common in construction contracts that define the owner or contractor’s damages if a project is delayed. Liquidated damages clauses provide for the recovery of a fixed sum specified by the contract (typically a certain sum applied on a daily basis) for the party injured by a delayed project. Liquidated damages clauses are generally enforceable but cannot be a penalty, and must be based on a reasonable estimate of a party’s anticipated damages at the time of contract execution if a project is delayed.

No damages for delay clauses are another example of sole remedy clauses. No damages for delay clauses provide that a contractor’s sole remedy in the event of owner-caused delay is an extension of time to complete the work. These clauses are upheld to varying degrees depending on the state. Some states limit the enforceability of no damages for delay clauses for public contracts or based on concepts of culpability (eg, bad faith or intentional delay by the owner). Even though the FAR, AIA, and ConsensusDocs do not include no damages for delay clauses, no damages for delay are sole remedy provisions that are used in the construction industry.

9.4 Excluded Damages
With some exceptions, punitive damages are typically excluded from liability in construction contracts. Punitive damages are not compensatory, but are rather intended to punish the wrongful actor. Punitive damages can be awarded in the context of intentional acts of fraud, malice, or wanton and wilful conduct. Punitive damages are rarely awarded in the construction industry and are typically specifically excluded from construction contracts.

9.5 Retention and Suspension Rights
Suspension rights are generally available in construction contracts. For example, an owner will generally have the right to suspend a project for convenience or for any reason the owner finds necessary (AIA Document A201 – 2017 § 14.3; ConsensusDocs 200 § 11.1 (2011, Revised 2019)).

Retention is typically withheld at a rate of 5% or 10% of monthly invoices or progress payments. Upon achievement of substantial completion or final completion, the owner is typically required to pay the withheld retention to the contractor; however, the owner will generally have the right to withhold retainage if the contractor is in breach of the agreement and the owner’s claim exceeds the value of retainage (AIA Document A201 – 2017 § 9.8.5; ConsensusDocs 200 § 9.2.4 (2011, Revised 2019)).

9.6 Termination
In the US, there are two basic types of termination of a construction contract:

- termination for convenience; and
- termination for default (or for cause).
Termination for Convenience
When a contract is terminated for convenience, the contract is being terminated unilaterally by one party to the contract without the need to prove default or breach of the other party. A termination for convenience is a contractually defined right and is not available simply by operation of US law – ie, the parties’ contract must provide the right to terminate the contract for convenience.

Termination for convenience clauses first appeared in US federal government contracts in the mid-19th century (currently FAR § 52.243-4 for fixed price construction contracts) and can now be found in industry form contracts (eg, AIA Document A201 – 2017 § 14.4.1). While the terms of a termination for convenience clause may vary, typical clauses grant broad authority to terminate the contract in consideration for a payment to the terminated party for the reasonable cost of the work, plus a reasonable profit, and demobilisation costs.

Termination for Default
A termination for default by either party may be justified based on contractually specified breaches of the construction contract and/or under common-law doctrines such as repudiation, frustration of purpose, or breach of an essential term. Regardless of whether the termination for default is based on the contract or common law, the differences between a termination for convenience and termination for default are significant. This is true under the FAR, industry form contracts and common law. Typically, if the owner terminates for default, the owner may recover damages for any increase in the cost to complete the project, plus other costs arising from the termination such as the cost to secure a replacement contractor to complete the work. Because it is difficult to determine what damages may be available to a non-breaching party following a termination for default, many contracts specify the remedies available to the non-breaching party in the event of a termination for default.

Wrongful Termination
Terminating a construction contract runs the considerable risk that the termination may be found “wrongful”. If a contractor wrongfully terminates the contract, the owner may typically recover the costs to repair defective work, actual or liquidated damages for delay, and costs to complete the scope of work of the terminated contract. When it is determined that an owner wrongfully terminates a contractor, a contractor who is not in default may recover damages in the form of the costs of the work completed, lost profits and restitution damages to the extent the owner was unjustly enriched by the contractor’s work. To limit liability for significant damages in the event a termination for default is deemed wrongful, the FAR (§ 52.249-10(c)) and many standard construction contracts include a provision that if a party is terminated for default, and the termination is later ruled (by a court or through arbitration) to be wrongful, the termination is automatically converted to a termination for convenience.

10. Dispute Resolution
10.1 Regular Dispute Resolution
In the USA, disputes concerning construction contracts may be adjudicated before federal courts or state courts. Parties also frequently agree to arbitration in lieu of courts. Disputes on construction contracts with the federal government and with some state and local governments must be adjudicated before specialised administrative boards.
Jurisdiction and Venue
Personal jurisdiction and subject matter jurisdiction are necessary predicates for determining which court, whether federal, state or either, is proper. Personal jurisdiction requires that the parties have certain geographic or transactional minimum contact with a court's geographic boundaries for the court to exercise jurisdiction over the parties.

Subject matter jurisdiction requires a court to have the legal authority to hear the claim brought before it. To be in federal court, the dispute must arise under federal law, or there must be diversity of citizenship jurisdiction, in that the parties are from different states. Diversity is usually the basis of construction disputes in federal courts with two major exceptions:

- the federal government is a party to the contract; or
- a subcontractor or supplier asserts claims pursuant to the Federal Miller Act.

Unlike federal courts, state courts are courts of general jurisdiction, meaning there are no requirements for special statutory or citizenship bases for subject matter jurisdiction.

Another issue that determines the appropriate court for a dispute is proper venue – whether the court is the proper court based on its physical location. In order to avoid venue issues, construction contracts frequently stipulate the venue and such stipulations are generally enforceable.

Controlling Law
The procedural rules of the court hearing a construction dispute generally control the litigation proceedings. The question of which state’s substantive law controls a dispute can be, and is often, stipulated in construction contracts. Many standard form contracts refer to the law of the state where the project is located as being the controlling law. Parties also frequently stipulate by name the laws of a particular state that may or may not also be the location of the project.

Right to a Trial by Jury and Waiver of That Right
Parties to construction disputes generally have a near absolute right to have their dispute heard by a jury, whether in federal or state court. The major exceptions to the right to a jury trial are an arbitration agreement and federal, state and local government construction disputes that must be heard by special courts that decide cases without juries or before specialised administrative boards.

Based on the concerns about a jury of lay people deciding large and complex construction disputes, parties often stipulate in construction contracts to the waiver of the right to jury trial.

Federal Boards of Contract Appeals
Construction disputes with the US federal government must be brought in one of two specialised forums: the United States Court of Federal Claims or in the corresponding administrative board. The two boards that handle the vast majority of construction disputes are the Civilian Board of Contract Appeals and the Armed Services Board of Contract Appeals.

10.2 Alternative Dispute Resolution
Arbitration and mediation are regularly used for construction disputes in the USA, as alternative means of dispute resolution. Arbitration is a matter of contract and requires the agreement of all parties to the dispute. Construction contracts frequently establish an agreement to arbitrate, but the parties can agree to arbitrate at any time. Mediation is also generally required by agree-
ment of the parties, but some court rules and state statutes may mandate mediation at some point in the proceeding.

**United States Law Favours Arbitration**

United States law enforces arbitration agreements under the Federal Arbitration Act (FAA). For the FAA to apply, the relevant contract must evidence a transaction of interstate commerce – meaning transactions across two or more states. Because of the extensive movement of construction services, and especially materials, across state lines, this is typically an easy hurdle to overcome on almost any construction contract.

In addition to the FAA, each state maintains a separate set of laws regarding arbitration. The majority of states have adopted either the Uniform Arbitration Act or the later Revised Uniform Arbitration Act. The FAA and state law generally align. When in conflict, however, the FAA supersedes state law in both federal and state court. The standard form contracts most widely used in the construction industry routinely include arbitration clauses enforceable under these laws (AIA Document A201 – 2017 § 15.4.1; EJCDC C-700 ¶ 17.01B (2018 ed.); ConsensusDocs 200 § 12.5 (2011, Revised 2019)).

**Dispute Review Boards**

Dispute review boards or DRBs are sometimes used on major construction projects in the USA to offer non-binding assistance and “recommendations” for resolving disputes during the course of construction. Although the use of DRBs is growing, their use is still relatively limited, even on major projects. Large public infrastructure projects utilise DRBs more frequently, especially transportation projects. Use of DRBs is a matter of contract and is not required by statute or regulation, even on public construction projects. The AIA standard form construction contract incorporates procedures for the use of an “Initial Decision Maker”, who serves a similar function to a DRB (AIA Document A101 – 2017 § 6.1, AIA Document A201 – 2017 §§ 1.1.8, 15.2).
Jones Walker LLP has more than 30 construction attorneys who deliver comprehensive legal services to clients throughout the construction industry. The firm’s national footprint, the depth and breadth of the team and the scale of the projects on which it works enable it to provide effective counsel on virtually every issue its clients may face. Members of the construction team regularly represent clients across the USA and abroad, and excel at handling large-scale construction and infrastructure projects across industries such as aviation, energy, natural resources, healthcare, retail and education. The firm is familiar with the full scope of US and international procurement and government contracting regulations, and the lawyers regularly help negotiate and close agreements involving economic development funding, tax incentives and P3s. They also advise on environmental regulation and permitting, real estate, finance, government relations, labour and employment, and other areas involved in planning and executing projects.

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Introduction and Overview
Modular construction is not new. However, over the last several years, modular construction has seen significant growth with no signs of slowing down. In 2021, global modular construction represented a market of approximately USD130 billion and is projected to reach upwards of USD235 billion by 2031. Modular construction growth in the US is largely due to technological advances and globalisation.

In general, modular construction involves the manufacturing and fabrication of standardised components of a structure in an off-site, controlled environment. Once those components are fabricated, they are then transported to the project site and assembled by an installer or contractor. Moving these fabrication and construction activities off-site allows the fabricator to control the quality standards over the fabrication process and gain the economic advantage of an assembly line and manufacturing process. This leads to a reduction in cost. This cost savings is then passed on to the owner, thereby driving down the overall price of construction.

While modular (or off-site) construction has a broad reach, touching many different industries, this article will focus on modular fabrication in the industrial industry. So, whether it be in a Liquefied Natural Gas (LNG) facility or a petrochemical complex, modular construction has provided significant advantages in the planning and construction of these industrial facilities. This article describes and summarises some of the issues that are unique to modular construction that are different than the more traditional, on-site approach.

A Brief Overview of Modular Construction
The National Institute of Building Sciences Off-Site Construction Council defines modular construction as follows: “off-site construction is the planning, design, fabrication and assembly of building elements at a location other than their final point of assembly on site. An integrated planning and supply chain optimisation strategy, characterises off-site delivery”.

There are many examples of modular construction. For example, a single trade prefabrication approach could be the fabrication of a particular spool of piping that will then be incorporated into an industrial complex. Another example is pre-fabricated, multi-trade racks where piping, mechanical, and electrical work are all assembled off-site into a rack to create a complete sub-system that will then be incorporated into the on-site facility.

And yet another example is volumetric structures. Volumetric modular construction is a form of off-site construction in which industrial facilities (for example) are constructed by connecting a series of related, large, pre-built sections (modules). This includes modules where all the subsystems are incorporated into one structure completing the entire, main system. An example of a volumetric structure in the LNG industry would be a complete module that is part of a “train” of modules used to pre-treat natural gas. Prior to liquefaction of natural gas for transport/use, contaminants in the natural gas that freeze at low temperatures and that are destructive to the processing equipment must be removed from the natural gas. So, modules to remove contaminants would be fabricated off-site and later assembled at the project site and would include the entire steel structure containing all the piping, mechanical and electrical work and process equipment required to remove any desired contaminant in that natural gas (mercury, for example). This is a very common use of modular construction in the US energy industry.
The common thread among all these examples of modular construction is the off-site construction of components that are then later assembled at the project site. This process has a significant impact on schedule, increases efficiencies in the fabrication process, allows for greater quality control, improves safety (less personnel at site resulting in less congestion and job-site accidents), and less interferences with multiple subcontractors and trades working at the same project site.

Modular fabrication also allows owners of large industrial facilities to globally source the fabrication of these plug-and-play modules, thereby increasing competition and reducing costs while at the same time increasing quality. It is not uncommon, for example, to have specialised process equipment manufactured in Asia, then being shipped to North in Central America for off-site fabrication and incorporation into a module, that is then shipped to the US for a final assembly at an industrial complex. This ability to construct off-site and ship modules anywhere in the world allows many technology-based disruptors to now enter the once-localised construction marketplace and compete for construction mega-projects.

Challenges of Modular Construction
Modular construction does not come without its challenges. For example, the familiar Engineering, Procurement, Construction (EPC) contract relationship, where the owner engages one entity to build an entire industrial complex, can now be disrupted with modular construction.

Specifically, an owner who was previously beholden to a single EPC contractor can now, instead, contract directly with an engineering company to provide its process technology and equipment (the “E” and “P” in EPC) and then further reduce the cost of construction (the “C” in EPC) by directly contracting with an off-site fabricator in a different country who specialises in the fabrication of modules. In this scenario, the traditional EPC contractor now becomes the “installer” or “connector” of the components that arrive at the project site. Modular construction gives the owner more flexibility in its contractual relationships.

That is the good. But the bad in this scenario is the required co-ordination efforts. The owner now has much more co-ordination obligations that it did not have before. Even if the owner wishes to use a traditional EPC approach, it can still require that the EPC use modular, off-site construction, thereby reducing the overall construction costs and improving the overall quality of the new facility.

There’s also the added challenge of integrating the off-site fabricated components into the balance of project (BOP). Clear delineation of these all-important contractual responsibilities is paramount to ensure the modules meet the ultimate performance criteria. For example, and irrespective of whether the owner or EPC contractor is responsible for co-ordination, there need to be written assurances that the mechanical and substantial completion requirements are properly delegated to either the off-site fabricator or the on-site contractor. Otherwise, this can create problems for the owner if the fully assembled facility does not meet performance goals.

Finally, there’s also the challenge of transportation logistics. All of the off-site fabricated components (modules) need to be transported to the BOP site for assembly. While the risk of transportation is not new to construction projects, the heightened implications of risk allocation for transportation is obvious in a modular
construction contract when much of the new facility will be fabricated off-site and then transported to the BOP site. Therefore, it is critical that modular construction clients identify and reach clear terms on addressing and allocating that transportation risk. This can be handled by incorporating standard shipping terms, such as Incoterms FCA, DAP, FAS, etc.

But perhaps the more significant shipping risk particular to modular construction is the supply chain risk. As we have seen in the past few years, the supply chain can be subject to unexpected interferences that disturb the global supply chain. Accordingly, having a modular contract in place that now sources modules from around the world introduces more transportation risk to a construction project.

**Available Form Contracts for Modular Construction**

Given the recent growth of modular construction, there are not many standard, form contracts offered. For example, the American Institute of Architects currently has no form contract to address modular construction.

However, the ConcensusDocs – a diverse coalition of 40+ leading construction/engineering associations with members from all stakeholders in the design and construction industry – has created a form modular construction contract, which is its 753 ConcensusDocs form (“Prefabricated Construction Agreement Between Constructor and Prefabricator”) along with its form 253 (General Conditions Between Owner and Prefabricator (Lump Sum)). While these forms are certainly helpful and much needed, these still require significant modifications to address the nuances of a modular construction contract, particularly in the industrial setting. Accordingly, owners, contractors and process equipment providers will need to spend adequate time in the contract formation phase to ensure that all the new challenges associated with modular construction are properly addressed and risk is properly allocated.

**Does the UCC or Common Law Apply?**

Perhaps the most fundamental legal issue facing modular construction is this question: does the Uniform Commercial Code (UCC) apply, or does the common law apply? Or, is it some hybrid of the two?

The UCC and common law provide different rules and requirements for contracts. The UCC is a set of laws that governs commercial transactions, while common law refers to a body of law that is derived from judicial decisions and precedents. The UCC traditionally applies to the sale of goods, and/or movables, while the common law applies to service contracts. Unless called out, most EPC contracts are governed by the common law.

What makes modular construction more complicated is that in a modular construction setting, the fabricator is completing the modular construction off-site using labour (services), but the end product it is providing its customer is clearly a good or movable (the module). So as a result of this hybrid construction process, the traditional form construction contracts simply do not fit well and require heavy modification. Many sophisticated clients in the industrial setting who use modular construction have found it better to draft the modular construction contracts from scratch because of the complex interplay between goods and services.

The answer to this fundamental question (UCC or common law) will have significant legal implications. For example, both legal regimes would...
yield different results with respect to acceptance of the modules, payment for the modules, revocation of acceptance of the modules, and warranty issues, to name just a few. Which legal regime is better for the project, and therefore the contract, is a case-by-case analysis, but it is certainly an unsettled issue within the industry, and can be easily overlooked during contract formation. It is always best to evaluate the project and end goal of the contractual relationship so that the appropriate legal regime can be invoked during contract formation.

UCC v Common Law: Applicable Terms
As discussed, the application of either the UCC or the common law will have significant implications for a modular construction contract. Perhaps the biggest difference between the UCC and the common law is the formation of the contract in the first instance. During contract formation, the parties typically negotiate the commercial and legal terms that will govern the contractual relationship. But even these terms can be influenced by the UCC and/or the common law. The importance of this threshold issue cannot be overstated as it will determine the commercial and legal terms governing the parties' agreement.

So, did the parties agree to certain commercial terms during contract formation? Maybe, maybe not. For example, the common law imposes a mirror image rule. That means under the common law, if a party offers/proposes a specific commercial term, for that term to govern and be part of the parties' final agreement, the party receiving those proposed terms must accept the same, specific commercial and/or legal term as was offered. If they do not and instead change the proposed term even slightly, then there will not be an agreement on that term. Therefore, it is important that the acceptance of proposed terms must match the offer in all its particulars, otherwise the offer is rejected (the mirror image rule).

However, the formation of a contract under the UCC occurs in a vastly different manner. Unlike the common-law rules, the UCC wants to find agreement on terms even if there are slight differences in what is proposed and what is "accepted". To be more precise, a contract for sale of goods will be formed under the UCC as long as there are sufficient facts to show an agreement was reached, even though at the moment of its making, the terms and understanding were still undetermined.

In fact, multiple terms of the contract can be left open, so long as the parties intended to make a contract. This would violate the "mirror image rule" under the common law and that specific term would not be binding on the parties. That is not so under the UCC. Interestingly, under the UCC, acceptance under these circumstances can even add additional terms. This crucial distinction between the UCC and common law can have a significant impact concerning the formation of a modular contract, and its ultimate performance.

UCC v Common Law: Inspection and Acceptance of the Modules
Acceptance of the completed module under the UCC is yet another key difference.

Under the common law – and therefore typically under an EPC contract, the parties define what constitutes final acceptance and completion of the contracted work. Final acceptance typically will be defined as the owner acknowledging the contracted scope of services is complete according to the specifications. While reach-
ing final acceptance is seen as the administrative close out of the services contract (EPC for example), the issuance of a final acceptance certificate, for example, implicates many rights, waivers of rights and warranty issues. Those are usually clearly defined in the EPC agreement and are triggered by completing all performance tests and achieving performance guarantees (ie, reaching substantial completion).

Under the common law of contracts, final acceptance means that the owner takes ownership of the project and the risk of loss passes from the contractor to the owner. At that point, the owner’s contract rights against the contractor become far more limited. Therefore, final acceptance of the work should be considered the most significant contractual event, except for contract award.

The UCC treats acceptance of completed modules differently. As noted, if the parties fail to identify any aspect of a commercial term (such as final acceptance), the UCC will “fill the gap” and impose general rules upon the parties, even if they did not negotiate or consider those terms. Again, this is a key difference between the UCC and the common law.

Under the UCC, when the modules are presented to the buyer as being complete, the buyer must either accept or reject the modules. Acceptance of the modules under the UCC is generally deemed to have occurred when the buyer does any act inconsistently with the seller’s ownership. Once acceptance occurs, the buyer cannot reject the modules. Perhaps most importantly, once acceptance of the modules occurs, the buyer must pay the seller for the complete value of the contracted modules.

UCC v Common Law: Acceptance of Defective Modules

Another key difference between the UCC and the common law concerns acceptance of modules that are known to have defects.

The UCC provides some protections for buyers who accept defective goods, but it is important for buyers to be aware of the defects and to take appropriate action to seek remedies. If a buyer accepts goods with knowledge of the defect, they very well may still be required to pay the full price of the contracted goods, but they may also be entitled to recover damages from the seller.

In a common law services contract, whether the buyer has to pay if they know the services were performed defectively will depend on the specific terms of the contract, as well as the applicable laws and regulations. Generally, in a services contract, the buyer is obligated to pay for the services rendered, as long as the services conform to the contract terms. However, if the services performed are defective, the buyer may have the right to withhold payment or seek damages from the service provider.

As noted, however, once the buyer accepts the modules under the UCC, it must pay the full contracted price for those modules. US courts have interpreted the UCC to further mean that the acceptance, continued retention and use of allegedly defective goods (industrial modules) for a substantial period of time constituted conduct inconsistent with the seller’s ownership, amounting to acceptance of the goods and therefore the obligation to pay the seller for its full contract price.

Accordingly, if a buyer of modules knows there are defects in the modules when presented for delivery, the buyer may still have an obligation...
to pay the full contract price to the seller even for defective modules. So, if the buyer knows there are uncompleted punch-list items, and it still nonetheless takes possession of and uses the modules, it may have been deemed to have accepted the modules.

This general rule is heightened when the goods at issue consist of sophisticated equipment such as found in many industrial modules which must be used, adjusted and tested after installation to determine conformity. US courts have held that a buyer’s extended usage may create an acceptance even if the buyer remains dissatisfied after the performance tests are completed. US courts have held in this situation that a buyer’s complaints while it continues to use the goods will not be sufficient to reject goods and avoid acceptance (or full payment for the known defective modules).

In sum, the fact that modules are allegedly non-conforming may very well not be a legitimate defence to payment. When modules are received, inspected and accepted by the buyer even if with known defects, the seller very likely will be entitled to recover the full contract price for the modules. Any claim for damages for defective items is separate and apart from the buyer’s obligation to pay the full purchase price for the modules.

The buyer does have one last remedy (outside of warranty claims). The buyer may revoke its prior acceptance of defective modules if done in a timely manner under the UCC. Revocation of acceptance must, however, occur within a reasonable time after the buyer discovers or should have discovered the grounds for its revocation (ie, defects). This revocation should occur before any substantial change in condition of the modules has taken place that is not caused by their own defects. So, assembling, connecting and testing modules at the BOP site could very well be seen as such substantial change in the condition of the goods. Moreover, a buyer’s continued use of modules could be seen as acts inconsistent with the seller’s ownership and the buyer may lose its ability to revoke its acceptance.

Given the complexities of required performance tests on modules at the BOP site and to achieve substantial completion, acceptance and revocation of that acceptance under the UCC could be very onerous on the buyer. Under the common law regime, the buyer of goods may have more latitude when dealing with acceptance of modules.

Conclusion

As the US construction market shifts more and more to off-site modular construction (particularly in the large, industrial context), it is critically important for US and international clients to fully understand the special legal and practical issues discussed in this article before they enter into a US modular construction contract. Key issues related to the traditional EPC (services) construction contract will typically be governed by the common law.

However, modular contracts will likely be governed by the UCC. As discussed, the UCC and its concepts are not commonly used in the EPC contract context and these concepts could have far-reaching implications that may take an unaware party by surprise. It is clearly the result of this move to off-site fabrication and modular construction that we are seeing these changes in the US. These changes mean unique challenges and involve more and more international parties up and down the supply chain.
This closely choreographed process requires careful consideration on the front end during contract formation. Despite these challenges, the US construction industry continues to take important steps toward the use of off-site modular fabrication because of the incredible benefits it offers owners and contractors. Having the correct contract form and applicable law in place is more important than ever.

(This article presumes the application of US laws.)
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