I. NEGOTIATIONS IN GENERAL

Negotiating a contract with a general contractor, for the improvement of retail space is not unlike any other type of negotiation: One must first identify one's own goals, identify the goals of the contractor, and then move toward maximizing the overlapping of those goals. Once the owner and the contractor identify mutual goals, negotiation really begins. In this context, negotiation is the process of compromising disparate goals, in an effort to achieve a fair result.

Winning in negotiating a construction contract does not mean getting your way on every point. Rather, winning means achieving an agreement that will get your project built, with a minimum of conflict, in the face of the inevitability of unanticipated circumstances.

In construction, only uncertainty is certain. Thus, a well negotiated construction contract will anticipate and resolve, in advance, as many circumstances as possible and, more importantly, set in place a fair and equitable process for resolving conflicts that occur from the unanticipated.
Fairness should be the hallmark of negotiation. Indeed, every contract contains implied covenants of good faith and fair dealing. Further, a one-sided agreement, far from being an accomplishment, may result in the project being abandoned at a critical time or force litigation to avoid an unconscionable result. A well negotiated agreement will help you avoid ending up in court, as well as enhance your chances of success, should court prove unavoidable.

Negotiation, before construction begins, usually occurs in the most cooperative atmosphere to be encountered throughout the project. Everyone likes each other, everyone shares a vision of a successful, profitable project and no concrete actual conflict yet exists to require the staking out of adversarial territory. Once construction begins, and actual conflicts that must be addressed arise, the parties naturally become less cooperative. Their interests diverge and the disparity in positions becomes clearer. Compromise becomes proportionately more difficult.

The purpose of this presentation, is to raise and discuss various areas of potential conflict, so that they can be aired and addressed during negotiation. Through give and take during negotiation, a fair compromise may be accomplished. There will be few "right" answers. This is simply because "right" on these issues depends on one's subjective perspective, rather than an absolute, objective measure. The right answer is only determined in hindsight. Did the answer avoid dispute or protect the right party in the event of a dispute? Did the answer provided by the contractual agreement result in a fair resolution of the disagreement?

This paper will explore the various considerations behind each side on an issue. More questions than answers will be presented. That is because, while there are an infinite number of questions to be addressed, there are few "right" answers. At the end of the day, it will always be up to the parties to determine areas where compromise would be acceptable and those areas where any compromise would be a "deal breaker." Where cooperation is born and nurtured, the paper agreement becomes merely a fail safe, hopefully to be set in a drawer, never to be needed to resolve a problem.

II. INTERESTS OF OWNER vs. INTERESTS OF TENANT

In general terms, the interests of the Owner and the Tenant are aligned with respect to the contractor hired to improve leasehold. Both the Owner and the Tenant want the improvement built on time, on budget, in accordance with the plans and specifications. However, the interest do diverge in important respects. First, who will control the design of the project. Who will control the actual construction and the myriad of decisions inherent in any project? Who is funding the construction? Who owns the improvement? These questions are properly the subject of the lease negotiation, which will determine whether the improvement is landlord funded but tenant controlled, landlord funded and controlled or tenant funded and controlled. These important questions are the subject of another presentation at this program and are not discussed in this paper.

Once the Owner and Tenant are aligned with respect to control and responsibility, design and funding of the project, they can act in unison, in negotiating the
construction contract.

**III. FORM OF THE CONTRACT TO NEGOTIATE**

It is always easier to edit a document than it is to write it from scratch. However, while editing the contractor's proposed form of agreement may be easier than writing a new document, it is preferable to have the contractor work from your document of choice. If your negotiation starts with the form of the document that is your "home run," you likely will end up with a more favorable agreement than if the negotiation starts from the contractor's preferred form or a totally neutral form.

Where both sides want to start from their own document, and neither wants to work with the other's, a reasonable compromise would be to start from a recognized industry standard document. However, think about just whose industry the "standard form" is geared to protect. Many contractors will try to work from the series of agreements endorsed by the American Institute of Architects ("AIA"). In many instances, these agreements present an excellent starting point for negotiating a fair final document. However, it is important to keep in mind that input for the forms came from the construction industry, not any organized group with Owner's interests at heart.

"Boiler plate" is defined as inconsequential, formulaic or stereotypical language. As such, it has no place in a well drafted agreement. Any attempt to gloss over points in a form preferred "by the industry" or the contractor as "boilerplate" should be viewed skeptically and read carefully. Every provision in the agreement should have clear and reasonably precise meaning, or it should be stricken.

Before the parties can agree on the content of a document, they must first reach agreement on the fundamental terms of the understanding which is to be memorialized by that document. First, what exactly is the Owner buying? Is the Owner designing the Project, and hiring the Contractor to implement the design selected by the Owner? Or, perhaps, the Owner has only certain design criteria, without an actual set of plans. In such case, a "design-build" agreement may allow the contractor to partner with an architectural firm, to design and then construct the Project, incorporating the Owner's design parameters.

Next, how is the construction to be priced? Is there a fixed price, based upon an existing, reasonably complete, conflict free set of plans and specifications? Does the Owner prefer to pay the Contractor its costs of performance plus an agreed upon fee for the Contractor's overhead and profit? Does the Owner prefer to cap this cost plus arrangement with a "Guaranteed Maximum Price"? Does the ultimate agreement stand alone, complete, by itself, containing all the terms of the understanding? Or, does the contract incorporate other documents, such as standard or modified general conditions or a book of specifications? Perhaps the form of the agreement will be a standard form agreement, modified by reference to project specific supplemental conditions. The basic framework of the written agreement should be discussed, in light of the requirements and limitations of the particular project.
A renovation of an existing space may be subject to far more uncertainty in actual field conditions than ground up construction. What will be found when the demolition begins, especially of an older structure with non-existent or incomplete as-built reference drawings, is always difficult to predict. In such case, a fixed price contract, even one subject to a relatively complete set of plans, will be subject to substantial change orders, to reflect field conditions that were unexpected or different from what was reflected in the history of the project. There, frequently, contractors will seek to avoid a fight over change orders by negotiating a cost plus contract.  

The key to a cost plus contract is to appropriately define exactly which costs will be reimbursable and which will not. It will also be important to set a method by which the cost of the work performed by the Contractor’s own forces (as opposed to subcontracted out) can be priced. Unit prices can be used, where appropriate. Alternatively, the Contractor could be required to provide competitive bids for its own work, to demonstrate the correct price to be charged. Of course, competitive bidding may be desirable for subcontracted work, as well. It may be that the Owner wants the Contractor to solicit competitive bids, but may not bind the Contractor to use the lowest bid where there are reasons beyond price alone that a particular subcontractor should be selected (high end finish work is not something an Owner would necessarily want the cheapest sub on).

When using the AIA A111 as the basis of an agreement, the Owner should be aware of paragraph 7.7.3, which provides that the cost of correcting defective or damaged work is reimbursable. A further curiosity in AIA A111 is paragraph 7.6.8 which allows the Contractor to charge, as a reimbursable cost of the work, the legal fees incurred by the Contractor in addressing subcontractor disputes, regardless of whether the Owner caused or contributed to the dispute or is right or wrong.

A further refinement to a cost plus contract is to impose a guaranteed maximum price ("GMP") upon the Contractor. When the reimbursable costs exceed the GMP, the Contractor must bear the burden of the overrun. In a normal Cost Plus, GMP contract, a Contractor may be over his reimbursable budget as to a particular line item, but not on the contract as a whole. An Owner may wish to impose a "line item GMP" limitation on the Contractor so that any overrun on one entry in the schedule of values cannot be compensated for by an underrun on another line item. In this way, the Owner preserves the benefits of any savings, without losing them to compensate for overruns. The countervailing view, of course, will be for the Contractor to negotiate a broad definition of what is reimbursable and a high GMP.

IV. ISSUES TO ADDRESS IN THE OWNER/CONTRACTOR AGREEMENT

Generally speaking, the Owner is concerned with getting the Project, as designed, built on time, on budget, without claims from the Contractor's subcontractors or suppliers. While the Owner’s goals are simply stated, they are rarely accomplished
without persistent attention to detail, documentation and follow-up. A well drafted agreement can go a long way toward providing the Owner powerful tools to insure that the Contractor acts properly. At the same time, however, one should be mindful that the contractual provisions are usually not self actuating; the Owner must timely document situations and solutions in order to insure that the contractual protections will be realized. The flip side is also true: the Owner must be prepared to respond to documentation received from the Contractor, to make sure that the situation is described fairly, and insure that a fact finder will have the benefit of all the facts.

PARTICULAR CONTRACTUAL ISSUES TO ADDRESS

TIMELY PERFORMANCE

The parties must discuss, ahead of time, the scheduling obligations and commitments to which each party will be bound. An as-planned schedule, at the time of contract, is a clear method by which misunderstanding can be minimized and the contractor forced to logically plan the Project. The logic of the Contractor's proposed sequencing and timing of activities will provide insight into critical issues such as man-power and equipment loading and windows of time for decision making. Through the scheduling process, the Contractor can also determine whether the Owner's time requirements are realistic.

The contract should also require, and the Owner should also monitor, period schedule updates. It has been suggested that an appropriate time for schedule up-dating is monthly, with each pay requisition. Slippage can be identified and addressed before it becomes critical, through acceleration, time extension, additional man-power or adjusting back-end commitments for store opening.

The schedule update process dovetails nicely into assessing responsibility, in incremental fashion, for slippage. Is the Contractor behind schedule due to unforeseen conditions or the Owner's failure to supply its own material or accomplish its own parallel scope of work? If so, and the delay is to the critical path, with no available float, a time extension may be warranted and the Contractor may seek additional general conditions, extended home office overhead or other indirect delay damages. It is preferable to know early, while alternatives are available.

Similarly, if the delay is due to the Contractor's failure to adequately plan or man the work, the delay may not be compensable to the Contractor, and may form the basis for holding back funds in a pay requisition or a later claim, by the Owner, for liquidated damages. The point here, as with most of the contractual provisions discussed in this presentation, is that early awareness and management promotes responsible decision making, throughout the process and maximizes the possibility that Owner and Contractor will work together throughout. Addressing these issues need not be confrontational, at a point where both Owner and Contractor have more to gain by continuing to work together than they might, later in the construction process.

Will either side be entitled to recover damages caused by the other's unexcused delay? What types of damages will be permitted and which precluded? Will there be
an attempt to liquidate, or fix the amount of these damages? Will either or both sides be required to waive the delay damages? Rarely, if ever, is a job completed exactly when predicted. If there is to be a reward or punishment for early or late completion, the parties must address and fully understand the issues raised by such realities.

Untimely performance, by either the Owner or the Contractor inevitably costs money. Besides direct damage, such as the additional general conditions a Contractor will incur, or the additional interest on a construction loan an Owner will incur, each side may indirectly be affected by delay. An Owner may be delayed in a store opening, incur rent payments (or loss rent that would otherwise begin) and not begin to realize an income stream from sales. A Contractor may be prevented from starting (or bidding) on other lucrative jobs or may have its bonding capacity tied up longer than desired. Either side can suffer these "consequential"

or indirect damages from delay. The contract must address how they are to be resolved when they occur.

In the 1997 version of the AIA General Conditions, A201, the parties each agree to waive their consequential damages from delay. However, since an Owner will likely suffer more certain and greater consequential damages, thought should be given to agreeing to such a provision.6

**WORKMANSHIP ISSUES**

How are disputes pertaining to workmanship to be resolved? Is the Project Architect available to act as a first level decision maker?7 Is the work up to the expected standard? What is the Owner's remedy where it is not? Will there be a provision that requires the Contractor to continue working, even where it is in disagreement with the Owner over a material issue? Generally, a fair compromise may be had where the Contractor must continue working, without prejudice to its rights, but the Owner may not withhold any undisputed portion of a construction draw that has come due. Where the Owner withholds the full amount of a draw, while only a portion is legitimately in dispute, a Contractor should retain the right to withdraw its forces from the job. It should also be mentioned that dispute resolution, discussed below, need not necessarily await project conclusion. The parties can invoke dispute resolution procedures while continuing to work.

At the end of a construction project, presuming it is substantially complete,8 the Contractor will be entitled to the *full* contract price, less the reasonable cost to correct defective construction and complete any incomplete, unexcused portion of the work. Holding back more than this amount may make it impossible for an Owner to "prevail" in litigation. Very often, in construction lien actions, the "prevailing party" recovers its attorneys fees from the non-prevailing party. Thus, it is important to determine the legitimate workmanship issues and assign a realistic price for correcting and
Almost always, it is cheaper to correct a problem during construction, at or near the time the defective construction occurred, than later. Thus, disputes arise where the Owner seeks to hold back an amount reasonable for correcting a problem later in the Project, where the Contractor agrees to a smaller hold back, arguing that had the condition been brought to its attention more promptly, correction would have been far less expensive. Thus, the contract should address the Owner's responsibility for discovering defective construction and the amount of permissible hold backs.

A significant workmanship issue is its obligation to coordinate contractors brought to the site by the Owner, not the Contractor. Generally, the Contractor should be contractually obligated to recognize the work of these "multiple prime" contractors, to coordinate the scheduling and sequencing of the work as to flow with Contractor's scope of work, and to call to the Owner's attention, deficiencies in the work of Owner's other contractors. The Owner has the reciprocal responsibility to require its other contractors to cooperate with the Contractor and to insure that Owner supplied materials are delivered to the site when appropriate. The issue of risk of loss for Owner supplied materials, once delivered to the site, as well as damage to the Project and injuries to other contractors or the public, and the role of insurance in this equation, is an area for substantial discussion in the contract negotiation phase. Care must be taken to insure that contractually required insurances are provided, with appropriate certificates naming the Owner as additional insured.

PRICE/CHANGES/CLAIMS ISSUES

Inevitably, as construction progresses, changes occur which give rise to additional costs. How they are to be addressed is one of the most important subjects to be negotiated during the contracting phase.

In a cost plus contract, the Owner naturally bears most all of the costs of changes or unexpected conditions. The reimbursable costs are defined at the time of contract negotiation. Changes which increase these costs, subject to a guaranteed maximum price (if applicable) are normally borne by the Owner.

In a fixed price contract, however, the parties interests are naturally divergent on this point. Neither party wishes to bear the cost of extra work. Therefore, it is important to incorporate a requirement of prompt written notice of changes which necessitate an adjustment to the contract, and a fair method of pricing and disputing such work, without interrupting the work itself.

Closely related is the need to document and price contract related "claims." Claims may not be changes in the work, but relate more to changed circumstances on the job giving rise to expense that the Contractor does not feel obligated to bear. For example, unforeseen site conditions, which make construction more difficult, time consuming or expensive, while not being a change in the work, will give rise to a "claim" for additional monies. Such claims, must, by contract, be required to be timely submitted, supported and priced.
The sanction for a Contractor's failure to provide timely notice of either an extra or a claim should also be clearly spelled out in the contract.

Under the 1997 version of the AIA General Conditions, as well as the 1997 version of the AIA Owner/Architect Agreement, an Owner that terminates a contract for convenience will still be responsible to the Contractor or Architect for the profits that would have been realized on the canceled portion of the project. It is suggested that a fee or some demobilization payment be substituted in place of the standard provision.

**SUBCONTRACTOR RELATIONS**

Subcontractors and suppliers do much of the actual construction work on most retail projects. As such, the negotiations between Owner and Contractor must account for the rights and obligations of these players. The Contractor is responsible for the work of its subs, but not necessarily their negligence. Insurance must address this gap. Subcontractor and supplier initiated warranties must be assigned to the Owner. Most importantly, payments to the Contractor must be made in a way where the Owner is assured that it will only pay once; that is, the subcontractors and suppliers must be protected, if only because they may have rights to lien the Owner's property.

The Owner should require, in the contract, that Contractor provide evidence of payment to all its subs and suppliers before receiving a payment from the Owner. This provision can be required on all pay requisitions, with the effect of having the Contractor front payment to its subs and suppliers for the first cycle, before being reimbursed by the Owner. Or, the Owner may take the risk for one cycle, only requiring proof that the Contractor has paid all its subs and suppliers from the last payment, before making the next payment. In this situation, the releases "trail" the payments. Pay requisitions should be required to be submitted on a form which contains the Contractor's certification that the work has been properly completed and that the Contractor has either paid all its subs and suppliers for the work reflected or has utilized the proceeds of the last payment to pay for work through the last requisition prior to the instant one.

Owners may require that their Contractors prohibit subs or suppliers from claiming liens, require that the liens be bonded off within a particular time. In such event, the filing of a lien by a sub may constitute an event of default. Under any circumstance, the Owner may wish to obtain the right to make direct payments to subs or suppliers, or, at least, issue joint checks to the Contractor and a particular sub.

The Owner may reserve the right to retain a portion of any payment, normally 5% or 10%, as security to provide a fund from which corrective or completion work can be accomplished at the end of a project. Sometimes, the retention will be reduced, from 10% down to 5%, after an agreed upon portion of the project has been satisfactorily completed.

The Owner may require the Contractor to furnish a performance and payment bond, assuring
the Owner that the subs will be paid, provided the Owner properly pays the Contractor, and that the project will be completed, even where the Contractor or one of its subs defaults. Normally, the Owner pays for the bonds. It should be noted that where payment bonds exist and exempt the Owner's property from liens of subcontractors and suppliers, notice requirements may differ. For example, the existence of the bond must be noted on Notices of Commencement and physically attached, at the time of recording. The bond must also be posted with the permit at the site.

Where the project involves the improvement of a leasehold, Florida law permits an Owner of the fee interest to limit the attachment of liens arising out of the improvement of the leasehold to only the leasehold. The value of such a lien is obviously less than a lien on a fee, as the leasehold lien survives only so long as the lease survives. In order to enjoy this limitation, the lease must contain such a prohibition and a copy of the short form of the lease containing the prohibition must be recorded. A copy should also be furnished to the Contractor, upon its request.¹⁰

**DISPUTE RESOLUTION**

Disputes arise. It is a fact of life in construction. Those disputes that cannot be resolved without the intervention of an impartial factfinder must be resolved through a formal process of either arbitration or litigation. Arbitration cannot be compelled absent an agreement of the parties. Therefore, if the parties are inclined to arbitrate their disputes, that agreement must be set forth in the contract. It cannot be unilaterally imposed at the time the dispute arises.

Arbitration is generally regarded as less expensive and somewhat quicker than litigation. However, in return, the parties lose the right to a full legal review of an arbitral decision, have limitations on who may be brought before the arbitration panel and are limited on discovering the evidence marshaled by the other side.

Even if the determination is in favor of arbitration, there is no legal requirement that the arbitration be managed by the American Arbitration Association or even that the rules of the AAA apply. There is a statutory mechanism for convening and enforcing arbitration, independent of the AAA.¹¹ The parties are free to design their own arbitration process, including a method for selecting the arbitrator. However, that agreement must be set forth in the contract.

If the parties desire to litigate, generally disputes involving contracts are triable, at the request of either party, to a jury. Therefore, if the parties want to try their dispute to a judge rather than a jury, the contract must expressly waive the right to trial by jury.

Again, at the time the dispute arises, one party cannot unilaterally require the other party to waive a jury trial.
The construction contract should also designate the venue, or place, for dispute resolution. The parties may wish to require dispute resolution in a location other than where the project is located.

One no-lose precursor to litigation or arbitration should be mediation. The structured settlement conference may go a long way to minimizing areas of disagreement, so as to make resolution, without judicial or arbitral intervention, possible. Such a result always carries with it a substantial savings in time, money and relationships. Mediation may properly be made a condition precedent to formal dispute resolution processes. There is little downside to the mediation process. Even where the dispute is not resolved, one would still benefit from the opportunity to see and hear the story from the other side of the table, if only to assist in trial preparation.

V. ISSUES TO ADDRESS IN THE OWNER/ARCHITECT AGREEMENT

Even before negotiating with the Contractor, the Owner is likely to have contracted with an architect of its choosing, to design the Project and reduce the design to a set of buildable plans and specifications. It is important to note that the Owner generally warrants to the Contractor that the plans and specifications are "buildable." Therefore, problems in the construction drawings that cause the project to cost more or take longer, will result in recognizable claims by the Contractor against the Owner. The Owner needs to protect itself, through careful drafting of the Owner/Architect contract.

As with the Owner/Contractor documents, the American Institute of Architects has issued a recommended form of agreement. This form, AIA B141, if used, should be modified in certain important respects.

PARTICULAR CONTRACTUAL ISSUES TO ADDRESS

SCOPE OF SERVICES

The nature of the architect's undertaking must be clearly set forth. Is she being retained for drawings and specifications only? Will she play a part in administration of the construction contract? Will she supervise (or, as the AIA B141 Agreement, states, observe) the construction? Keep in mind that observation carries with it far less responsibility and accountability than does supervision. Will she review and approve the Contractor's pay requisitions?

Another critical issue in the Owner/Architect dynamic is ownership of the design drawings.

If the architect retains ownership and copyright over her instruments of service, she retains enormous leverage in a dispute with the Owner. The Owner would essentially have to start over with a new architect, if the Owner cannot make use of the drawings upon terminating the first architect. Retail tenants, with registered service marks must have the use of the drawings and control of the drawings is necessary before they can be assigned to a purchaser of the property.

A compromise may take the form of a license, which is granted by the architect to the
Owner, which survives termination of the architect's services, but is limited to the particular project. In this way, the Owner can complete the project, but cannot re-use the plans as a start on a different project of similar concept. Also, ownership of the plans is important to facilitate renovation in the future. The as-built drawings become the starting point for any such renovation.

The current AIA B141 prohibits the Owner from significantly modifying project scope or budget without architect consent. This provision causes the Owner to surrender an inordinate amount of control to the architect and should be modified.

**DISPUTE RESOLUTION**

The current version of the AIA Owner/Architect Agreement mandates arbitration and requires mediation as a condition precedent to formal dispute resolution. The same considerations addressed in the Owner/Contractor context, supra., apply here. Additionally, Article 1.3.5.4 prohibits the joinder of the architect in a owner/contractor arbitration, without the architect's consent. Thus, full resolution of a dispute, through mandated attendance of all responsible parties is precluded, absent modification of the provision.

**TERMINATION FOR CONVENIENCE AND SUSPENSION OF SERVICES**

Again, as with the Owner/Contractor agreement, the Owner may wish to negotiate a fee in lieu of the standardized entitlement to lost profit in a termination for convenience. Further, the AIA B141 provides that the Architect may suspend performance for non-payment and absolves Architects of responsibility for delay damages that may result.

**STATUTE OF LIMITATION and INSURANCE**

Article 1.3.7.3, unless modified, artificially commences a statute of limitation upon substantial completion, without regard to any discovery or tolling, necessary to achieve a fair result in latent defect claims.

Presently, no provision in B141 addresses or requires the Architect to maintain property damage and bodily injury liability insurance. It is respectfully suggested that such insurance may prove valuable during the course of a project.

**VI. CONCLUSION**

Keep in mind that the AIA documents were drafted primarily with architects in mind. Careful planning and scrutiny of any standard agreement will pay off through the negotiation of a proper balance of risk and reward. Although the planning and negotiation are not the most enjoyable or dynamic portions of a project, they may be the most important in assuring that, at the end of the day, the project is built on budget and on time.
VII. APPENDIX


2 See: AIA A111 form "Standard Form Agreement Between Owner and Contractor Where the Basis for Payment is the Cost of the Work Plus a Fee, with a negotiated Guaranteed Maximum Price" (1997).

3 Article 7 of AIA A111.

4 Article 10 of AIA A111.

5 This presumes that the contract does not prohibit delay damages.

6 In 1997, the AIA enacted a revised version of its General Conditions. The author of this paper has prepared a comparative analysis of the 1987 and 1997 versions of the AIA A201 General Conditions, which was presented at the 1998 ICSC Centerbuild Conference. A copy of the Comparative Analysis is attached as an appendix to this paper.

7 In a large enough project it may prove beneficial to designate a person who has been retained to render final and binding decisions. This person should be acceptable to both parties and should be named at the beginning of the Project.

8 Substantially complete has been defined as "so nearly complete as to allow the owner to use the project for its intended purpose.

9 See Article 14.4.3 of AIA A201 (1997) and Article 1.3.8.7 of AIA B141 (1997).


11 Chapter 682, Florida Statutes.

12 Article 1.2.2.1 and 1.2.2.2 of AIA B141.

13 Articles 1.3.8.6 and 1.3.8.7.

14 Article 1.3.8.1.