The New AIA Documents: Selected Issues on Finance, Insurance, Dispute Resolution, BIM and Collaborative Agreement

ABA RPTE Section Spring Symposium
May 2, 2008
Washington, D.C.

by Martin A. Onorato, Esq.
Thelen Reid Brown Raysman & Steiner, LLP

Selected Issues on Finance

Table of Contents

I. Introduction

In the latest of its decennial revisions to its contract document forms, on November 5, 2007 the American Institute of Architects published updates to many of its documents, including its A201 General Conditions and all of its B-Series agreements between owner and architect. These 2007 documents replace the 1997 versions, which in turn supplanted the 1987 versions. As set forth in the AIA Commentary,[1] the AIA's "goal in revising documents every ten years is to maintain state-of-the-art legal documents that reflect industry trends and practices and balance the interests of the parties on the construction project."

As part of the revision process, the AIA solicited industry comments, many of which, according to the AIA Commentary, concerned financial matters such as the owner's and contractor's respective rights to obtain information and the owner's right to remedy non-payment to

[1] Suzanne H Harness, et al. 2007 Revisions to AIA Contract Documents ("AIA Commentary").

subcontractors. The AIA did implement changes in these and other areas of the contracts, although these changes were not without controversy. For the past 50 years, the Associated General Contractors has endorsed the A201 General Conditions, to wit: "This document has been approved and endorsed by the Associated General Contractors of America." After reviewing the 2007 version of the document, however, the AGC withheld endorsement of the revised document. In fact, while the AIA was busy updating its documents, the AGC was spearheading a parallel initiative with other major construction industry groups to create a new set of contract forms under the name ConsensusDOCS. The first set of ConsensusDOCS contract forms were published on September 28, 2007 – just over a month before the AIA published its 2007 updates. While a complete comparison of the AIA forms and the ConsensusDOCS forms is beyond the scope of this paper, it will suffice to note that ConsensusDOCS departed from AIA in a number of significant areas.

Given the large market share that AIA commands over construction industry forms, it is vitally important that attorneys become familiar with the new documents. The AIA publishes its documents through on-line software, and electronic reproduction of the documents is prohibited and constitutes a violation of the AIA's copyright. To encourage use of the new documents, the AIA has provided users with an 18-month transition period during which they can either use the retired documents or the 2007 documents. Retired documents (including the superseded 1997 versions) will remain available in software through the May 31, 2009. "After the transition period concludes, software users will not be able to generate new drafts or finalize existing drafts based on the retired documents."[2]

The purpose of this seminar is to point out many of the issues arising from the changes appearing in the 2007 version of the document. It is not intended to identify all of the provisions that you may wish to modify. Indeed, the AGC's Preliminary Commentary to the 2007 documents contain a host of suggested revisions that you may wish to make to the document that have nothing to do with the changed provisions. Accordingly, it is strongly recommended that you retain counsel to develop standardized supplemental general conditions for contracts governed by the A201 and that these be reviewed for applicability to each project.

Disclaimer. While we believe the materials accurately state the law as it is in effect as of the date of this seminar for the jurisdictions referenced, no implied or express warranties accompany the materials, and reading the manual is no substitute for reading the relevant cases and statutes themselves. Moreover, to the extent that any specific legal issue is covered in the course of the seminar, no substitute exists for the advice of a competent lawyer licensed in the appropriate jurisdiction who can devote the time necessary to fully explore the particular issues that may affect a transaction or case. The speakers and the authors expressly disclaim any liability for opinions expressed in the seminar.

II. Overview of the New Documents

While many of the changes found in the 2007 versions clearly affect the risk allocation between Architects, Owners and Contractors, the AIA also made a large number of changes to simplify and unite the families of documents and to eliminate inconsistencies within and among the

[2] http://www.aia.org/docs_updates.

documents themselves. While these housekeeping changes may not have much substantive significance, they have significance in that they reveal the AIA's perspective on the evolution of the construction industry, its norms and processes, and the roles of the professionals that comprise it.

The re-orientation of the owner-architect agreements is a good example of this adjustment in perspective. The former flagship architectural agreement, the B141-1997, was a two part document, with Part 1 relating to design services and Part 2 relating to contract administration services. This proved clumsy and, according to the AIA Commentary, most architects chose to use the B151-1997 instead, which was a single-part agreement and retained the traditional concepts of Basic and Additional Services that had been abandoned in the B141-1997. By introducing a new document in 2007, the B101-2007, as its flagship architectural agreement, the AIA signaled a rejection of the B141-1997 experiment and a return to a single document suitable for architects providing traditional design and contract administration services.

III. Changes to the A201 General Conditions

A. Owner's Tempered Obligation to Provide Financial Assurances

A201-1997, § 2.2.1 included a provision that required the Owner to provide, at the Contractor's request, "reasonable evidence" that the Owner had procured financing for the Work. The Contractor was expressly entitled to make such request both prior to commencement of the Work "and thereafter." This provision frequently was opposed by owners, and the 2007 documents have restricted the Contractor's right to request this information.

In the 2007 version, the Contractor still has an unfettered right to such information prior to the commencement of the Work, just as before, and receipt of such evidence remains a condition precedent to the Contractor's obligation to commence or to continue the Work. See A201-2007, § 2.2.1 and § 14.1.1.4. After the Work has begun, however, the Contractor is entitled to further financial assurances only if one of three conditions have occurred:

- The Owner fails to make a payment as required by the Contract Documents;
- A change in the Work materially changes the Contract Sum; or
- The Contractor identifies in writing a reasonable concern regarding the Owner's ability to make payment when due.[3]

By comparison, the ConsensusDOCS counterpart retains the former approach of the AIA, providing that the Owner must provide the Contractor with such information at the Contractor's request both prior to commencement of the Work and thereafter. ConsensusDOCS 200, ¶ 4.2. It also requires the owner to notify the contractor of any material change in the Project Financing. Id.

[3] The modification of § 2.2.1 was one of the specific changes that the AGC cited in refusing to endorse the new documents.

B. Subcontract Assignments in Event of Default.

The AIA's General Conditions have long provided the Owner with a right to take an assignment of the subcontracts after terminating the Contractor. E.g. A201-1997, § 5.4.1. Under the common law "an assignment of a contract does not operate to cast upon the assignee the duties and obligations or liabilities imposed by the contract on the assignee, in the absence of the assignee's assumption of such liabilities." 2A Michie's Jur. Assignments § 27 (2004). The AIA's previous assignment clause was silent as to the Owner's assumption of the Contractor's liabilities under assigned subcontracts.

Now, however, the A201-2007 adds a sentence stating that the Owner "assumes the Contractor's rights and obligations under the subcontract." As stated in the A201 Commentary, this "obligation includes paying the assigned subcontractor all amounts that are past due at the time of the contractor's termination." A201 Commentary at 25. This is very problematic for an Owner, who may not be aware of, or may have been mislead as to, amounts owed to or claimed by Subcontractors at the time it is considering terminating the Contractor. Where the Owner had no obligation to accept the Contractor's pre-assignment liabilities in the absence of such an obligation in the A201-1997, the Owner is now exposed to double liability under the 2007 version if the Owner has already paid the Contractor for amounts due to the Subcontractor, but the Contractor nonetheless failed to pay the Subcontractor.

Of course, the Owner could expressly reject the assignment under the 2007 version, but that would defeat one of the primary purposes of the assignment clause. By providing for an assignment of the trade contracts, the Owner can mitigate the negative effects of a termination by retaining experienced companies to complete the Work under the balance of their pre-existing fixed price contracts. If the General Conditions require the Owner to remain obligated for contract arrearages as a condition to accepting the assignment, the Owner's opportunity to mitigate its losses drop substantially.

If this first change was not enough of a burden on the Owner, the A201-2007 also introduces a new provision by which the Owner may reassign a subcontract to a successor Contractor. Often, such reassignment is a necessary consequence after terminating a general contractor, and the ability to assign the unperformed subcontracts to the successor Contractor is an important tool for controlling the Owner's termination damages. However, this new clause in the A201 provides that the Owner "shall nevertheless remain legally responsible for all of the successor contractor's obligations under the subcontract." A201-2007, § 5.4.3. Thus, the Owner becomes a guarantor of the successor contractor's obligations to the Subcontractor. Therefore, the changes to § 5.4.1 and § 5.4.3 in the new AIA General Conditions, if unchanged, will place owners in a significant quandary when facing non-performing general contractors.

C. Disputed Change Order Pricing.

Under the 1997 documents, the Contractor was permitted to bill only for the undisputed portion of a Construction Change Directive, and then to bill the remainder when the dispute was resolved. A201-1997, § 7.3.9. Partial billing for disputed extras has always been problematic, as contractors are reluctant to bill for a partial amount out of concern that they could be waiving claims for the disputed amount. Similarly, owners tend to avoid paying toward a matter in

dispute. This clause was changed in the 2007 documents to ease the Contractor's reluctance, though it does not eliminate the Owner's concern.

The Contractor is now invited to bill for the full amount set forth in a Construction Change Directive, and the Architect is to certify only that portion that it determines to be justified. A201-2007, § 7.3.9. Amounts not certified by the Architect are to be handled through the dispute resolution process. Id. This should have the beneficial effect of better defining amounts in dispute during the course of the Project, given that the Contractor is required to put its entire claim on the table for consideration and resolution. The Owner remains obligated to pay amounts not in dispute, but the Owner presumably does so knowing the full extent of the amount in dispute. Moreover, this new procedure will mean that the Owner's lender and others reviewing the Contractor's invoices will be on notice of disputed extras.

Practitioners should keep in mind, however, the limitations of this clause, even after the 2007 amendments. A Contractor is permitted to bill only for those changes included in a Construction Change Directive, which signifies that the Owner and Contractor agree as to the Contractor's entitlement to a change, while disagreeing as to the cost or time impact of such change. If entitlement is disputed, no Construction Change Directive will be issued and the Contractor will not be able to include it in its applications for payment, but will instead need to proceed directly to the claims process.

By interesting contrast, the ConsensusDOCS provides that in similar circumstances, the Contractor may include its extra costs in each invoice as it performs the work, and the Owner must pay the Contractor 50% "of its estimated cost to perform the work," while both parties reserve their rights as to the disputed amount. ConsensusDOCS 200, § 8.2.2.

D. Subcontractor Payments

The A201-2007 significantly diminishes the Contractor's control over payments to Subcontractors. First, § 9.6.2 no longer requires the Contractor to pay Subcontractors "promptly," but instead requires payment to Subcontractors within seven days of receiving payment from the Owner. There is no carve-out to allow for separately negotiated timing terms between the Contractor and the Subcontractor, so if a subcontract permits later payment, the Contractor will be in breach for observing the longer payment terms.

The new General Conditions also open up communication between the Owner and the Subcontractor, at § 9.6.4, by adding a provision entitling the Owner to request written evidence from the Contractor that its Subcontractors have been paid. If the Contractor fails to provide the evidence within seven days, the Owner may contact the Subcontractors directly "to ascertain whether they have been properly paid." This provision opens the door to communications regarding the reason for non-payment and provides the Owner with a means of verifying the information that would ordinarily be reflected in monthly lien waivers and certifications of payment by the Contractor.

In the even that payment irregularities are discovered, there have been changes that empower the Owner with options for direct payment. Under § 9.5.1.3 of both the 1997 and the 2007 versions, the Architect may withhold certifying payment for "failure of the Contractor to make payments

properly to Subcontractors or for labor, materials or equipment." New to the 2007 documents, however, is a provision allowing the Owner, at its sole option, to make payment by joint check to the Contractor and any Subcontractor, or material or equipment supplier to whom the Contractor failed to make payment.

E. Limitations Periods

Beginning in 1987, the A201 provided for a contractual mechanism to determine when a claim arose for purposes of applicable statutes of limitations. As explained in the AIA Commentary, this allowed architects and contractors to avoid the uncertainly surrounding the discovery rule, and had the security of knowing a date beyond which they would not be exposed to potential liability. These rules, however, were fairly complex, and disputes over when a claim arose could defeat the purpose of avoiding uncertainty. Moreover, there are many states that do not apply a discovery rule.

For wrongdoing before Substantial Completion, the limitations period would begin "not later than" at Substantial Completion. A201-1997, § 13.7.1. For wrongdoing occurring between Substantial Completion and the issuance of the Certificate of Final Payment (i.e., the punchlist period), the limitations period would commence "not later than" the date the Certificate of Final Payment was issued. Id. at § 13.7.2. And as for wrongdoing occurring thereafter, the period would run from the date of the actual act or omission. Id., § 13.7.3.

Owners in states using a discovery rule considered this mechanism unfair, and "urged that the AIA follow applicable state laws."[4] Accordingly, the 2007 documents provide simply that the parties shall commence actions "within the period specified by applicable law," but that no claim may be brought "whether in contract, tort, breach of warranty or otherwise" more than ten years after Substantial Completion. A201-2007, § 13.7; B102-2007, § 4.1.1. Clearly, therefore, the AIA continues to favor a clear sunset rule on liability arising out of a construction project.

Careful attention should be paid to this provision. Most states have a statute of repose that typically bars claims against contractors and architects for personal injury, property damage and/or professional negligence after a certain period of time from completion of the project. These statutes usually bar both indemnity claims by the owner and claims by the injured party. For example, the statue of repose in Virginia is 5 years, and bars any claim by an injured party against the Contractor or the Architect that arises 5 years after completion of the work. Va. Code § 8.01-250. Absent contractual provisions to the contrary, the statute of repose also bars any claims by the Owner for indemnity for such claims against the contractor and the architect.

If the statute of repose is longer than 10 years in the state where the project is located, the Owner will be limiting its right to make a claim for indemnity to a period less than that to which it would be entitled by state law. This could also work against the Contractor if the injured party chose to sue the Contractor, but not the Owner. If the claim accrued after 10 years, but within the statute of repose, then the Contractor could be barred from seeking indemnity against the Architect or the Owner.

[4] AIA Commentary at 7.

Also, there is the issue of whether this language could be construed to expand statutes of repose that are less than 10 years. As explained by one court, there are three distinct types of statutes that preclude litigation of stale claims.

> First, and most familiar, are procedural or "pure" statutes of limitation. These serve merely to time-restrict the assertion of a remedy. They furnish an affirmative defense and are waived if not pleaded. Second are substantive or "special" statutes of limitation. They are ordinarily contained in statutes which create a new right and become elements of that newly-created right, restricting its availability. Compliance with such a statute is a condition precedent to maintenance of a claim.[5] Third, [] are statutes of repose. The time limitations of such statutes begin to run from some legislatively selected point in time which is unrelated to the accrual of any cause of action or right of action, whether accrued or yet to accrue. Such statutes reflect a legislative policy determination that a time should come beyond which a potential defendant will be immune from liability for his past acts and omissions.
>
> Commonwealth v. Owens-Corning Fiberglas Corp., 385 S.E.2d 865, 867 (Va. 1989).

Thus, while a "pure" statute of limitation functions as a procedural bar to the filing of an action, a statute of repose creates a "substantive right of repose in the potential defendants." Id. at 868. Does the clause requiring parties to commence actions "within the period specified by applicable law" apply only to "pure" statutes of limitations? Alternatively, by agreeing to a 10-year limitation in the A201, have the parties agreed to waive their "substantive right of repose" reflecting the legislature's "policy determination," and substituted their own contractual right to repose after a longer period? The parties may wish to address those issues in supplemental general conditions.

These provisions also play into insurance coverage issues. Typically, an Owner will want the Contractor to maintain completed operations coverage until the expiration of the statute of repose. To the extent the repose period is effected, the insurance provisions will need to be adjusted.

IV. Changes to the B-Series Documents

A. Licenses for the Instruments of Service.

One of the most contentious issues with respect to Owner/Architect agreements involves the Owner's rights to the Architect's work product, which the AIA documents refer to as the Instruments of Service ("IOS"). Architectural plans have long been acknowledged to be eligible for federal copyright protection under the Copyright Act. The architectural work (i.e., the design embodied in the plans) is separate and distinct from the plans themselves, and has been protected as a separate copyright interest under the Copyright Act since 1990. As the author, the Architect is deemed to hold the copyrights interests in both. Historically, the AIA documents have

[5] In the construction context, such special statutes of limitation are often found in mechanic's lien statutes.

carefully preserved the Architect's exclusive ownership in the IOS, while extending limited licenses to others involved in the Project, including the Owner.

In response to criticism that the Owner's licenses under the 1997 agreements were too restrictive, the new agreements reflect some adjustment of these rights. Under the previous formulation, the Owner's rights to the IOS continued in force so long as the Owner continued to pay the Architect and the agreement was not terminated. If one of these conditions arose, however, the license was automatically terminated and the Owner could not use the IOS (to finish the Project or otherwise), until the Architect was "adjudged in default" of the Agreement. This placed owners, who may have paid for much of the architects' services and received IOS, in position where a dispute with the Architect could bring the entire Project to a halt.

The new copyright provisions (e.g., Article 7 of the B101-2007) contain several changes from predecessor clauses in the B141-1997. Now, the license is "solely and exclusively for the Project," and terminates if the Architect "rightfully terminates this Agreement for cause." E.g., B101-2007, § 7.3. So long as the Owner "substantially performs his obligation" and is not rightfully terminated by the architect, the license continues in force. Id. This seems to make the possibility of halting the project on a technicality more remote, as the license disappears only when the Architect, not the Owner, terminates the agreement. This creates a situation where the Owner can, to an extent, control its own destiny – but only if it terminates the Architect first.

If the Owner does terminate the Architect first and the Owner's license remains intact, the AIA has modified the agreement to protect the Architect from new liability following its termination. Specifically, the agreements now state that if the Owner uses IOS without retaining the author, then the Owner releases the Architect and its consultants from all claims and cause of action arising from such uses. The Owner also agrees to indemnify and hold harmless the Architect and its consultants from all costs and expenses related to claims and causes of actions asserted by any third person or entities arising from use of the IOS to the extent the costs and expenses arise from the Owner's use of the IOS. B101, § 7.3.1.

While such an waiver and indemnity provision may original in some rational basis because of the Architect's departure from the Project, the new term will be very problematic for an Owner seeking to terminate the Architect and complete the building in accordance with the IOS. Under this clause, if the Architect had committed an error or omission in the design, and if the Architect were terminated during construction, the Owner could find itself obliged to indemnify and defend the Architect from suits based entirely on the Architect's malfeasance.

B. Standard of Care

AIA documents have always been mindful that common law standards of care are applied to architects' services in virtually all jurisdictions, although AIA has not attempted to re-state that standard of care until the 2007 documents. Perhaps in awareness of a growing trend by owners and legislatures to alter the common law obligations of a professional architect, the AIA has now introduced into each of its Owner/Architect agreements a contractual standard of care.

The AIA utilizes a traditional description of the standard of care in its agreements, requiring that the Architect's performance be "consistent with the professional skill and care ordinarily

provided by architects practicing in the same or similar locality under the same or similar circumstances." B101, § 2.2. This likely does not stray too far from the common law of most jurisdictions, although it does commit the standard of care to the contractual intent of the parties for the first time, and as a consequence it runs the risk of being interpreted accordingly, rather than in accordance with the body of common law.

C. Architect's Duty to Indemnify Under the B103.

The B103-2007, intended for larger or more complex projects, contains an indemnity obligation running from the Architect to the Owner for damages, including reasonable attorney's fees, arising from claims by third parties. B103, § 8.1.3. The indemnity clause is not included in any of the other Owner/Architect agreements. The indemnity obligation only applies to the extent that the damages "are caused by the negligent acts or omissions of the Architect, its employees and its consultants in the performance of professional services" under the agreement. Id.

The mere fact of its presence in an agreement that is widely regarded as protective of architects makes this clause noteworthy, although there are other points of interest to note. For example, there is no limitation to claims arising from bodily injury or property damage (as with the Contractor's obligation under the AIA's General Conditions). Accordingly, the Architect's indemnity obligations may extend to claims by the Owner's tenants or separate contactors for economic losses in those states allowing such claims.

The breadth of this clause may be understandable in light of the fact that the Architect's indemnity duties are "limited to the available proceeds under insurance coverage." Id. This limitation on liability merits further scrutiny, not only because it threatens to leave the Architect partially unaccountable for its errors and omissions, but also because it raises questions regarding the available insurance proceeds. It is not uncommon for architectural firms to have errors and omissions policy limits of $1M, $2M and $5M, but these policies are universally written on a claims-made basis, and the policy limits are reduced by claims against any of the Architect's projects in a given claim year. In addition, the Architects consultants often have E&O policies of comparable size, but this indemnity clause does not indicate whether such limits are stacked.

D. Responsibility for Construction Cost

Architects' responsibility for construction cost was limited under the 1997 AIA documents and, although there were substantial changes to this area in 2007, their responsibility remains limited. Under the old regime, it began with a disclaimer that the Architect has no control over construction costs, methods or market conditions, and consequently "does not warrant or represent that bids or negotiated prices will not vary from the Owner's Project budget or from any estimate of Construction Cost or evaluation prepared or agreed to by the Architect." B151-1997, § 5.2.1. In fact, the only responsibility referenced in the document would not arise unless the parties took the additional step of identifying a "Fixed Limit of Construction Cost," Id., § 5.2.2, and only if such a limit were established in writing would the Architect be obligated, in the event of a bid bust, to modify the documents as required to reduce the construction cost. This free re-design was, however, to be "the limit of the Architect's responsibility" to the Owner. Id., § 5.2.5.

The 2007 versions have altogether abandoned the concept of establishing a "Fixed Limit of Construction Cost" as a trigger to the Architect's responsibility. Now, the default scenario under the B101-2007 agreement provides for a free re-design by the Architect in the ordinary course. It also continues to state that the free re-design is the extent of the Architect's obligation to the Owner. B101-2007, § 6.7.

Different treatment is applied in the B103-2007, which is applicable to very large and complex projects. The Architect's re-design obligations do appear in that document, but in a much different context because it is not based on bid numbers at all. Because the B103-2007 anticipates that the Owner will retain an independent cost estimator during the design phase, the Architect's re-design obligation is based on the estimate at the end of the Design Development Phase. If that estimate comes in over budget, then the Architect "shall incorporate the required modifications in the Construction Documents Phase" as the extent of its obligation to the Owner. B103-2007, § 6.6. Since the Architect has not yet officially begun the Construction Document Phase at that point, the Architect's obligation is more of a fine-tuning that a true re-design.

E. Limitations Period

Similar to the changes affecting the start of the Contractor's limitations period discussed above, the B-Series documents have been modified to provide a repose period for the Architect. Previously, the limitations period for bringing claims against the Architect began to run "not later than" the date of Substantial Completion for acts or omissions prior to Substantial Completion, and "not later than" the date the Architect issued the Certificate of Final Payment for Acts occurring after Substantial Completion. B141-1997, § 1.3.7.3; B151-1997, § 9.3.[6]

As with the A201-2007, these manipulations of the commencement of the limitations period have been eliminated in favor of a more concrete repose period of 10 years from the date of Substantial Completion. In addition, all the concerns mentioned in regard to interpretation of this provision in the context of local law remain.

[6] The AIA Commentary states that the AIA Owner/Architect agreements "contained provisions similar to the first two, but providing that the third triggering event was the date when the architect substantially completed its services." AIA Commentary at 7. This was correct only when issuance of the Certificate of Final Payment equated to substantial completion. If the Architect had duties that survived Certification, such as follow-up on warranty items or a post-completion review of project components, the AIA Commentary would be incorrect.