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UNDER CONSTRUCTION

Risk Allocation Between Design-Builders and Their Lead Designers in Design-Build Delivery

Henry Bangert and Michael Cowan

The challenge of proper risk allocation in design and construction contracts is nothing new. The challenges of risk allocation in modern design-build delivery, however, present construction attorneys with an ever-changing test, which belies a rote, one-size-fits all approach. As the popularity of design-build projects has increased in recent years, so too have related legal issues, in particular between design-builders and their lead designers. There has been much written about the increasing transfer of risk from project owners to design-builders,[1] including the transfer of risks which have traditionally been borne by the owner/developer (e.g., permitting, utilities, site conditions, etc.). This increasing allocation of risk onto the design-build team, combined with the increasing size of many design-build projects, especially in the public infrastructure space, has inevitably led to additional pressure on the relationship between design-builders and their lead designers, which manifests in larger and more frequent issues and disputes between the parties. Attorneys representing design-builders and lead designers must understand this unique landscape in order to best serve their clients' interests from negotiating contract terms to resolving these disputes.

The Design-Build Model's Reliance on Preliminary Designs

The primary source of many of the issues between design-builders and designers arises from the fact that design-build projects are frequently bid based on preliminary designs prepared by a lead designer.[2] Contrast traditional design-bid-build delivery, in which the cost and schedule are fixed later based on the final or near-final design. In traditional delivery, the risk of cost and schedule increases between preliminary design and final design is typically borne by the owner. Not so on a design-build project. In design-build, cost and schedule are often established based on the preliminary design, and the design-build team often bears the risk of increases in the cost and time of performance of the work resulting from design development between preliminary and final design.

Such increases in cost and time derive from several reasons, including changes in the quantity of work, the quality of work, the complexity of the work, site conditions, and in the design schedule. This raises the question: who, if not the owner, should bear these risks? The answer, in most cases is either (a) the design-builder, (b) the lead designer, (c) insurance, or (d) a combination of the three.

From the design-builder's perspective, the lead designer is obligated to develop the final design consistent with the preliminary design. Any increase in time or costs arising from a deviation from the preliminary design should be borne by the designer. The designer, however, will often take the position it should be liable only if the preliminary design fails to meet the applicable standard of care. Such debates frequently lead to challenging disputes because while the standard of care does not differ between

IN THIS ISSUE

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preliminary design and final design services, the circumstances under which the preliminary design is prepared differ significantly.

Designers will argue the preliminary design is inherently incomplete and is often developed under time and financial constraints, and with significant input and direction from the design-builder. However, while all of these things may be true, they are inherent to the design-build process. Such circumstances are not created by the design-builder or the designer. Accordingly, the design-builder often relies on the adage that the risk should be borne by the party in the best position to manage the risk. After all, it is the designer who is in the best position to manage design development consistent with the design-builder's price and schedule established at bid time. Therefore, the designer should bear the risk. Given these fundamental challenges, it is not surprising that negotiations of contractual risk allocation between designers and design-builders are becoming more complex.

Allocating the Risk of Design Delays

Design development risk does not end with increases to direct costs. In a traditional design-bid-build delivery method, if the design is delivered late to the owner/developer, there may be a risk of delay damages assessed by the owner. However, such delays are frequently concurrent with the owner's own development delays (e.g., permitting and approval delays). In addition, the owner's damages do not typically include the prime contractor's delay damages because, again, the contractor has not yet started construction until the final design is complete and the bid package issued. In design-build delivery, by contrast, the schedule for both design and construction is typically fixed on bid day. Thus, any delay in delivery of the design to the design-builder carries significant added risk to the designer of not only the owner's delay damages (e.g., liquidated damages), but also the design-builder's extended general conditions costs and possibly the cost of accelerating the construction schedule.[3]

To address these risks, designers in subcontract negotiations with design-builders are more commonly seeking to limit their exposure to damages. By far the most common mechanism designers are employing to control their risk is a limitation of liability. While it is nothing new to have an overall limitation of liability in a design contract, designers and design-builders are increasingly relying on tailored limitations of liability, which may include separate sub-limits for delay and/or quantities risks, and may be further tailored around the insurance programs of the project. Design-builders, however, may push back on these provisions because such limitations shift the risk of a late design or design errors and omissions to the design-builder. That is, project owners are often not willing to provide the design-builder similar limitations of liability, leaving the design-builder exposed to additional unreimbursed cost caused by its designers. While negotiating a limitation of liability may seem simple on its face, smart risk allocation balances (i) incentivizing the designer to manage the risk, (ii) incentivizing the design-builder to assist the design team, (iii) transferring the risk to insurance where possible, and (iv) avoiding excessive pricing/contingencies.

For example, design-builders frequently push back on limitations of liability where the potential damages are covered by insurance. Such as in the situation where a delay is caused by errors or omissions in the designer's construction documents. Because the risk of such delays is equally present in design-bid-build (i.e., is nothing new) and is likely covered by insurance, many design-builders argue such risk should not be limited. On the other hand, a design-builder may agree to a limitation of liability for delays that are not caused by errors or omissions in the final design but are instead caused by design development. Design-builders may be more open to such limitations because design-builders are frequently involved in determining the level of preliminary design required for bidding purposes and thus have a hand in helping to manage this risk pre-bid.

The Right to Withhold Payments

In addition to limitations of liability, another frequent area of contract negotiation is the design-builder's right to withhold payment from the designer on account of damages caused by the designer. While payment withholding is a common issue in contractor-subcontractor negotiations, historically, in traditional design-bid-build delivery, the designer was not exposed to payment withholding because the designer is frequently fully paid at the time the design is completed, i.e., before construction. In design-build, however, the contractor may recognize damages resulting from a breach by the designer during or even prior to the start of construction.

Withholding payment is, of course, not without its problems. From the design-builder's perspective, withholding payment only offers incomplete relief. The construction costs and potential damages often will far exceed the designer's entire fee on the project, meaning the design-builder cannot withhold enough payments to be made whole. From the designer's perspective, if payment is withheld during design development, this may create cash flow problems and could exacerbate the impacts to the project. Also, because construction costs far exceed design fees, designers are concerned their entire fee will be too quickly eroded by the design-builder's withholding.[4] Designers also believe that when a design-builder withholds payment, it unfairly shifts the burden of proof to the designer. Finally, designers often argue that when a project becomes financially stressed, the design-builders look for others to blame and may abuse withholding provisions.

All of these issues can lead to significant disputes, and the designer likely has an obligation to continue its

services while the dispute is resolved, meaning the designer ends up financing project cost overruns before its fault has been proven. Further, designers often argue payment withholding is unnecessary because the design-builder is adequately protected by the designer's professional liability insurance. However, from the design-builder's perspective, someone is inherently required to finance the cost overruns because the costs are incurred well before any professional liability insurer is likely to pay the claim. As a result, design-builders justifiably ask why they should finance such costs which are ultimately due to an error or omission in the design. Moreover, the designer should be incentivized to resolve the dispute quickly so that its professional liability carrier timely pays the design-builder's claim.[5] Considering the competing positions, designers and design-builders are forced to get creative in negotiating payment withholding rights, often by negotiating limits on withholding or through expedited dispute resolution procedures.

These are just a small sample of the issues attorneys representing design-builders and designers are forced to wrestle every day. As design-build delivery continues to grow in popularity, new ideas and approaches to allocating these increasingly large and complex risks will be needed. In addition, given the significant increase in project costs and claims, project owners are also beginning to realize once again that some risks are best retained by the owner. ■


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Endnotes

1. *See, e.g.,* Jamie Peterson, What is Wrong with Design-Build Contracting, American Bar Association (December 9, 2019), https://www.americanbar.org/groups/construction_industry/publications/under_construction/2019/Summer2019/design-build-contracting/

2. Progressive design-build is, of course, an exception.

3. Delays caused by the design are often attributed to (i) late delivery of design, (ii) design development (e.g., quantities of work increase, which now take the design-builder longer to complete) and (iii) errors and omissions in the final design that are first discovered during construction. Of these design delays which result in increased costs of construction, the first two are largely unique to design-build delivery and only the last is shared with traditional design-bid-build delivery.

4. Design fees are commonly in the range of 6-8% of the design-builder's total bid.

5. Care must be taken, however, to ensure that the payment withholding is not offset against the damages ultimately paid by the professional liability insurer.

MESSAGE FROM THE CHAIR-ELECT

The Forum Has Great Programming in Store For 2022-2023!

Wm. Cary Wright

The Forum will start the 2022-2023 ABA Bar year in Memphis – Home of the Blues and Birthplace of Rock 'n' Roll. There, the topic will be *Building the Next Generation – Learning from the Past*. Memphis has so much to offer – the Mississippi River, museums, Beale Street and, of course, Graceland. The meeting will be held on September 28-30 at the historic Peabody Hotel – ducks and all!

The topic of the Regional Meetings this year will be *Construction Contracts* – a must know for every construction lawyer. The meetings will be held on December 2nd in four locations - D.C., Dallas, Indianapolis and San Francisco. As always, the faculty will be top notch!

The first week of February 2023 will find us in the warm weather of Puerto Rico at the MidWinter meeting. There, the program *Old World Meets New World: New Solutions to Timeless Problems* will examine "Old World" problems and consider how "New World" solutions and innovations can help the modern construction lawyer deliver efficient and impactful results for their clients.

The ever popular Trial Academy will be back next spring in either D.C. or Dallas. There, the attendees will have a 3-day intensive course in trial practice, led by some of the leading construction lawyers and industry experts in the nation. Keep a look out for the brochure as there is limited seating, and it always sells out fast!

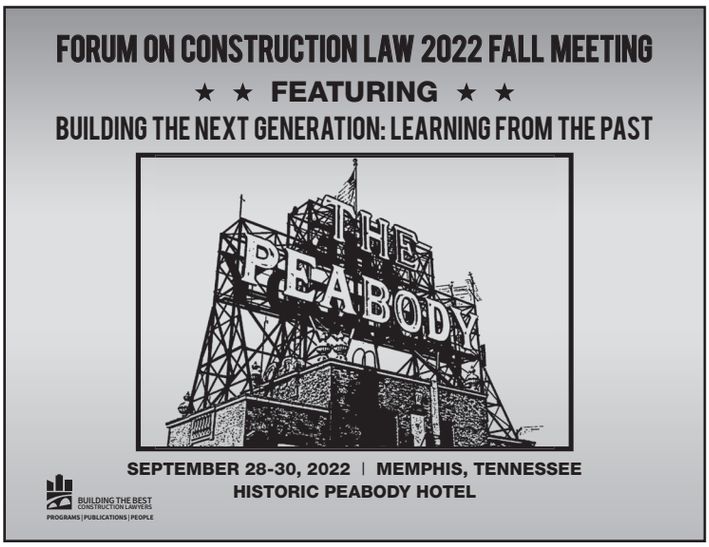
We will end the in-person national meetings with the Annual Meeting in beautiful Vancouver, British Columbia on April 12-15, 2023, learning about *The Future of Construction Law*. We will learn about the "transformational events" in the history of the construction industry and construction law; emerging trends in ADR; the implications of big data on construction claims; the intersection of blockchain and construction, and much more.

In between the in-person meetings there will be many distance learning opportunities from the SPEC Committee.

As you can see, much is planned for the 2022-2023 ABA Bar year. I want to thank all those who are contributing their valuable time to make these programs happen, and encourage those who want to get involved to please do so. The Forum needs and welcomes you! ■

Wm. Cary Wright, Carlton Fields, Tampa, FL

Save the Date



Forum on Construction Law Fall Meeting

September 28-30, 2022 | Memphis, TN

Join us on the banks of the Mighty Mississippi River in the Birthplace of Rock and Roll and Home of the Blues. We'll gather at the historic Peabody Hotel, the South's Grand Hotel, steps from Beale Street in the vibrant downtown of Memphis, Tennessee.

Registration Opening Soon!

IN MEMORIAM

Frank Elmore

On December 28, 2021, the Forum, and this world, lost one of its most generous spirits when Frank Elmore lost his courageous battle with lung cancer.

To describe Frank as a generous spirit is an understatement. He was always there to help, whether it was to listen to a creative legal argument, or to help you with your golf swing. Frank made it a point to make everyone feel welcome in the Forum, especially newcomers. He went out of his way to greet folks and help them become engaged. In doing so, he made many friends and was greatly admired. Frank volunteered to organize our Forum meeting golf outings, which he did superbly, as he did everything. For that reason, many believed that golf was Frank's passion. For those of us who were very close to him and his family, we know that his real passion was his wife, Lee, who he fell in love with when they were both law students at the University of South Carolina, and his wonderful daughters, Marguerite and Sarah Lawton. Frank bragged about their accomplishments all the time. We will miss Frank's smile and his hearty laugh. But we will, and cannot, miss him as much as his "girls," as he affectionately called them. He has left a hole in their hearts and in their lives. Please keep them in your prayers.

Hugh Reynolds, Jr.

On December 22, 2021, Hugh Reynolds, Jr., passed away at the age of 92. Hugh was an extraordinary person, brilliant lawyer, a great leader, a Napoleonic and Civil War historian, a Veteran, a mentor, a devout Catholic, and a family man.

While his innumerable awards, appointments, and honors are too many to mention, Hugh served as chair of both the ABA's Forum on Construction Law (1987 – 1988) and ABA Fidelity and Surety Law Committee; and was a recipient of the Cornerstone Award for Lifetime Achievement from the ABA's Forum on Construction Law (1989).

Hugh spoke and wrote with eloquence and authority not only on subjects in his fields of practice, but also on many other topics, among which were Civil War battles, Napoleonic Wars, religion, wine and high cuisine. It was a privilege to enjoy dinner with Hugh where many, if not all, of these topics were discussed.

Hugh was a mentor to young lawyers and was very instrumental in the development and advancement of female lawyers through his firm and national organizations. Upon hearing of Hugh's passing, many have said that he made this world and legal profession better. This truly describes the impact Hugh Reynolds made upon the legal profession and upon others.

While Hugh is gone, he will never be forgotten.

~~Good~~ Any Help is Hard to Find: A Crisis in the Construction and Design Labor Markets

John Frehse, David Ponte, Lawrence A. Dany, and Jocelyn M. Weinstein

Sansdemic" is a term coined by EMSI, a leading provider of labor market data. The term means "without people" or "without enough people." The sansdemic is a growing demographic drought, projected to continue worsening throughout this century. To put it simply, there are more open jobs than there are people to fill them—or people who are willing to fill them. And that impacts all sorts of industries, including construction and engineering. This Article highlights some of the most common complaints seen in the construction and design labor markets to date and potential ways employers can address this growing crisis, based on a recent Ankura survey.

The Importance of Labor

Labor is typically the largest controllable cost in a business, and its optimization pushes performance, reduces waste, and maximizes margins and profits. In construction, once a project has been "bought out", except for unanticipated escalation costs, labor remains the key variable impacting a project's bottom line. Too much or too little labor affects crew efficiency and a firm's ability to complete the work on time. In a world where the labor participation shortage is real and not going away, companies are looking for measurable ways to drive productivity, performance, and retention of talent. Just paying employees more is not driving major improvements and may not be sustainable over time. What can be done?

The first step is to understand what modern employees view as currencies. This is not just cash and time off, but a range of other categories where they identify value. A partial list includes:

- The ability to make a difference every day
- Feeling valued
- Structured mentoring
- Fringe benefits
- Being on a winning team
- Supporting the production of socially responsible brands
- Being a part of a diverse team
- Earned wage access
- Flexible shift schedules
- Alternative shifts from classic 8s
- Being told "Thank You" when earned
- The right amount of overtime

The list goes on. Everyone is different and people value compensation categories differently, which can require a wide range of compensation categories to be satisfied. Companies focused singularly on cash will find that there is not an amount of money that they can rationally pay employees to create satisfaction. Frankly, high paying companies often have poor cultures where employees are treated terribly because they cannot measure up to the performance expectations matching the pay. This creates a severe culture crisis.

So, what can we do? If we dig into the list above and work on a few of the alternative forms of compensation, employees get a broader range of "thank yous" from their employer. Not having a singular focus on cash creates a more complete level of satisfaction. Management teams know their employees better than anyone (although there are always some blind spots). Starting with an anonymous survey is always a good idea, especially if you plan to take action. Top "currencies" from the Ankura survey in the last 24 months have been shift schedule improvements, better communication, and increased overtime levels.

Shift Schedule Improvements

The shift schedule improvement is often the largest challenge of all the categories, but may drive the biggest positive results. The right shift schedules can significantly improve morale while also driving performance by having the right people in the right place at the right time. They often do not cost more when implemented properly, but can be very costly when the right work and pay policies are overlooked. However, they directly impact days off and work hours and so are an emotional topic. We know from experience that employees working a schedule they love will not leave for an additional dollar an hour of pay. Their lifestyles would be too disrupted, and they would not receive the same compensation based on the quality of life they would need to forfeit.

If an operation is currently running five days a week with two eight-hour shifts each day, it is running for a total of 80 hours, or utilizing approximately 48% of the 168 hours available in a week. One way an operation with this schedule could expand is to add a third shift at night. This would give a 50% increase in capital utilization without adding equipment for a total of 120 hours of operation each week. However, this assumes that the additional labor to sufficiently staff the third shift can be found.

If the eight-hour shift is so terrible, what is a better solution? Twelve-hour shifts, as an example, provide a dramatic increase in days off and increase weekend time off by 50%. Figure 2 provides an example of a 12-hour shift with the same exact staffing and coverage as the eight-hour shift in Figure 1, but the distribution of hours provides a different experience for the employees. In this option, employees get every other weekend off instead of every fourth weekend off. All of their weekends off are three- day weekends. They get 87

more days off than the eight- hour shifts and work 182 days a year and get 182 days off. Also, they never work more than three days in a row in their base schedule. Other iterations of 12-hour shifts can provide up to 17 additional weeks off each year without any loss of pay. Why must management teams continue to assume that everyone wants to work the same five-day schedule? Although it is right for some people, it certainly is not uniformly right for everyone. To attract and keep the best talent, companies must work to offer better options to shift workers. This not only helps attract the best talent but helps to keep them once they have arrived.

FIGURE 1: THE SOUTHERN WING

WEEK/CREW	M	T	W	TH	F	SA	SU	HOURS
1	•	8	8	8	8	8	8	48
2	8	•	•	8	8	8	8	40
3	8	8	8	•	•	8	8	40
4	8	8	8	8	8	•	•	40
							AVG.	42
Total Coverage								168 Hours
Shift Length								8 Hours
Rotation Length								4 Weeks
Work Days								273 Days
Days Off								91 Days
Weekends Off (Full)								13 Weekends
Longest Break								3 Days (13x)
Max. No. Of Shifts in a Row								7 Days

FIGURE 2: MORE WEEKENDS FREE

WEEK/CREW	M	T	W	TH	F	SA	SU	HOURS
1	•	12	12	•	•	12	12	48
2	12	•	•	12	12	•	•	36
							AVG.	42
Total Coverage								168 Hours
Shift Length								12 Hours
Rotation Length								2 Weeks
Work Days								182 Days
Days Off								182 Days
Weekends Off (Full)								26 Weekends
Longest Break								3 Days (13x)
Max. No. Of Shifts in a Row								3 Days

In construction, particularly on projects, shift scheduling improvements can be tricky in that there will be salaried project management staff working in conjunction with hourly craft trades, and if the trades are union members, then any shift schedule modifications will have to be in alignment with the union agreements, which is not necessarily impossible, just difficult. With the growing demand for alternatives, unions are beginning to more actively listen to their workforces' preferences to remain relevant.

Improved Communication with Management

Only 33% of employees who took the Ankura survey felt that the management team communicated well. This is a huge blind spot for management teams, and it ties into other currencies. Employees need to understand how what their actions impact the organization and creates value. Communication is a currency that ties to many other topics like feeling valued and making a difference every day. Without communication, employees are often unaware of how the work they do translates into important outcomes. Leadership teams often respond when we share this information with comments like, "Will saying thank you really make a difference?" Employees are telling us that this is absolutely the case, and that leadership is largely missing from the day to day work, and rarely sharing information. Starving employees of this feedback will cause your best workers to leave and the company will be left with employees who do not care about making an impact – a terrifying thought.

Overtime

Overtime is also a major topic as it directly translates into pay. This topic will remain sensitive as a target of cost-cutting and waste. Unfortunately, for high-growth businesses, overtime is an incredibly effective tool. Employees get extra pay, and employers can satisfy customer demand. To overgeneralize, we are seeing two groups emerge in the workforce today. The older population is looking for a lot of overtime and the 20–40-year-old group is looking for something close to 40 hours. Companies that can create two different systems inside one organization are achieving a competitive advantage with the ability to please a broader range of workers. This is harder to manage, but when done right to leverage the right technologies for governance, performance and engagement improve dramatically.

In conclusion, companies need to look at a broad range of currencies when approaching the modern workforce. It is not acceptable to assume we know what all employees want or to use past practices to try and satisfy them. The key is to engage the workforce in a real and meaningful way, understand their wants and needs, and work hard to satisfy them where possible. This may mean increasing staffing to reduce overtime – or not increasing staffing to protect it. It may mean alternative shift schedules to give employees more days off or communicating in new and different ways to finally be effective. In the end, successful companies are the ones who are able to listen. Companies with employees who say that their management teams communicate effectively are great at listening. They know that talking less and listening more translates into great communication. The question is — are you listening to your people? ■

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Revisiting Force Majeure Provisions During a "Trifecta" of World Events

Wilson Pollan and Jack Robbins

The construction industry is in the midst of dealing with a "Trifecta" of unfortunate events – COVID-19, the Russia/Ukraine War, and a spike in cybercrime. This article looks at *force majeure* and how the current context of this Trifecta will shape the future of how construction lawyers approach the key elements in the interpretation and application of *force majeure* clauses identifying excusable events, foreseeability, the duty to mitigate, and establishing a causal link.

Electric Avenue: How Federal Policies and Automobile Construction Projects are Driving the Electric Vehicle Market Forward Together

Matt Arvin

A combination of federal policies supporting electric vehicles and consumer market forces are poised to create a tremendous increase in the use of electric vehicles preceded by a building boom of manufacturing facilities for EV's and the batteries on which they rely. This article looks at supportive federal policy and some specifics about this building boom

CONSTRUCTION 101

Statutory Remedies for Non-Payment on Public and Private Construction Projects

John J. Gazzola

This article summarizes statutory remedies available when upstream parties fail or refuse to release payments on public and private construction projects — mechanic's liens, payment bond claims, and/or claims for violation of state prompt payment laws. These potential remedies should be at the forefront of every practitioner's mind when faced with a dispute over payment.

DISPUTE RESOLVER

Using Time Impact Analyses in Projecting Delays and Resolving Claims

Brian Celeste

While a Time Impact Analysis ("TIA") is an effective (and often required) tool to resolve time-related disputes during a project, it can have significant limitations if solely advanced in an after-the-fact claim. This article shares the basics of TIA's as well as critical, practical considerations in the application of TIA's on the project and in resolving disputes.


Subcontractor Participation in Owner-Contractor Arbitration

Steve R. Lindemann and Jessica L. Knox

Whether a contractor prefers or the owner insists on arbitration of disputes, the contractor should be careful to not only require arbitration with its subcontractors, but also require the sub's agreement to join and be consolidated into the owner arbitration.

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