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Tailoring Construction Contracts to Avoid Costly Repercussions

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A contract tailored to your unique construction project is essential in avoiding potential misunderstandings, disagreements and costly litigation. Not only can a well-drafted contract limit exposure to liability, it can also strengthen your reputation in the industry. Cooperating with the other side and trying to resolve any foreseeable issues at the commencement of the relationship fosters trust between the parties and lessens the likelihood of litigation.

Form contracts, such as those available from The American Institute of Architects (AIA) or the newer ConsensusDocs, are relatively comprehensive and provide a good starting point. However, these contracts may

require further customization for governing your specific construction project. A well-drafted contract may require more effort on the front end but taking time to consider the needs of all parties involved before a project begins is a best practice.

Contracts can cover topics such as the relationship between the parties, expectations for completing the work and who bears the risk of the entire project. However, the single most important aspect of the contracting process is confirming that the language is fully understood and agreed upon by all parties involved. Ambiguity in contracts can lead to misunderstandings, disagreements and, eventually, costly litigation.

Ensuring the contract language is fully understood and agreed upon by all parties involved requires an open dialogue. Making assumptions can lead to unnecessary misunderstandings and sour the relationship. Prior to drafting or redlining the contract, it is important to discuss what concerns each party has about the project. In many cases, disputes over items such as price or payment terms can be resolved if the parties simply discuss those issues during the contract drafting stage.

Risk Mitigation and Indemnification Clauses

One of the more contentious clauses of a construction contract involves risk mitigation. Not surprisingly, each party wants to lower their risk; however, that risk must ultimately be allocated in some fashion. Indemnification clauses are standard in form contracts and are commonly used to allocate risk. The principle of indemnification permits one party to pass their risk onto another party. A poorly drafted indemnification clause — or a lack of understanding about the consequences of indemnification — can leave one operating under the faulty assumption that they have allocated their risk elsewhere, when that party actually bears the entire risk of the project.

Under Pennsylvania law, the right of indemnity is created either by an express contract, through equitable principles of implied contract or operation of law. An indemnification clause must:

- Not contradict public policy
- Relate only to the contracting parties
- Result from the equal bargaining power of both parties
- Clearly state the beneficiary is relieved of liability only for his or her own negligence

Alternative Dispute Resolutions

Arbitration and mediation clauses are also effective tools in mitigating risk. Engaging in litigation can be a long and expensive process; therefore, it may be beneficial to include such a clause in your contract.

Arbitration is typically less expensive and quicker than traditional litigation. This can be appealing when a dispute arises in the middle of a project and time is of the essence. Parties can choose an arbitrator who is an industry insider, technical professional or legal professional who is familiar with the construction industry. During an arbitration hearing, the parties present their respective cases and the arbitrator makes a legally binding decision.

Mediation, on the other hand, is more like a settlement conference. After choosing an agreed upon mediator, the parties sit down and discuss the disagreement. The mediator suggests various resolutions to the issue. Their suggestions are not binding, and either party is free to leave the table at any time.

Saxton & Stump attorney [Ron Pollock](#) is available to discuss how to properly draft contracts to prevent costly repercussions and how our [Construction Law Group](#) can provide advice on mitigating risk during a construction project.

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