

**CONSTRUCTION LAW BASICS
AND TIPS FOR CONTRACTS**

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TOPICS TO BE DISCUSSED

- Types of Contracts
- Important Contract Clauses
- Insurance
- Bonds
- Special Subcontractor Issues
- Damages



TYPES OF CONTRACTS

- Firm Fixed Price
- Fixed Unit Price
- Cost Reimbursement With Fixed Fee
- Cost Reimbursement With Fixed Fee Up to Guaranteed Maximum Price.
- Time and Materials



IMPORTANT CONTRACT CLAUSES

- Scope of Work
- Coordination
- Change Orders
- Responsibility for Site Conditions
- Termination
- Notice of Claims
- Dispute Resolution
- Attorney's Fees



SCOPE OF WORK

- To the greatest extent possible, a contract should spell out the exact nature of the work to be performed.
- Most projects will change to some extent from the time the contract is written to the time of performance.
- Change provisions in contracts allow for routine changes.
- A “Cardinal Change” constitutes a breach of the contract by the owner.



COORDINATION

- For a project to proceed in an efficient manner, the general contractor and the subcontractors work must be coordinated.
- Therefore, the general contractor should will normally bind subcontractors to coordinate with the general contractor and all others involved with the project.



CHANGE ORDERS

- Many contracts contain provisions requiring that change orders be done in writing.
- However, changes are often made without a writing.
- Sometimes a waiver of the written requirement is valid.



RESPONSIBILITY FOR SITE CONDITIONS

- There is always a risk that the site conditions will vary from those anticipated when the contract was formed
- Contractors should include a contractual provision requiring subcontractors to:
 - Inspect conditions at project site; and
 - Based upon that inspection, accept responsibility to satisfactorily perform work without additional expense to contractor.
 - A “Differing Site Conditions” provision can be used to share the risk of changing conditions.



TERMINATION

- Most construction contracts allow the contractor or owner to terminate the contract if certain criteria are met.
- Convenience or Cause
- In order to validly terminate a contract in Minnesota, the terminating party must pay close attention to the termination clause and follow it to a “T.”



NOTICE OF CLAIMS

- Contractors should make note of any “notice provisions” included in a contract.
- Unless there is a finding of no prejudice against the non-claiming party, or a waiver of notice by the non-claiming party, notice provisions will likely be enforced by Minnesota Courts.
- Notice provisions can be implicitly waived if there is actual knowledge and acquiescence. *New Ulm Bldg. Center, Inc. v. Studtmann*, 225 N.W.2d 4 (Minn. 1974).



DISPUTE RESOLUTION

- Arbitration – usually using the AAA Arbitration rules and systems
 - Require monetary deposit (\$6-\$10k) – non-refundable
 - No cheaper than litigation but faster
 - Selection of Arbitrator important
- Check the “Flow Down” provisions – You may be bound to Arbitration from General Contract and not know it.



ATTORNEY'S FEES

- “The general rule is that attorneys’ fees are allowable if authorized by contract or statute, or if a party acts in bad faith.” *Material Movers, Inc. v. Hill*, 316 N.W.2d 13, 18 (Minn. 1982).
- Additionally, in certain cases, if you can show Fraud



TYPES OF INSURANCE

- Liability
- Auto
- Workers Comp
- Builder's Risk



Other Insurance Issues

➤ Waiver of Subrogation

- As a general matter, after payment of a loss to an insured, the insurer is entitled to sue a third party whose act caused the loss. The insurer is able to do this through subrogation.
- In other words, the insurer “steps into the shoes” of its insured in seeking recovery of its loss. Therefore, any defenses available against the insured would also apply to the insurer in the subrogation action.
- The purpose behind waivers of this type is to avoid the hassle of litigation and allocate the risk of loss related to the contract to the insurance carrier.

➤ Additional Insurance Requirements after Buldoc



The Buldoc Case and Minnesota's Anti Indemnification Law

- In January of 2013 in *L. H. Buldoc v ECI* the Minnesota Supreme Court stated that a General could not be indemnified all losses but was limited to losses caused by the subcontractor.
- The Minnesota Legislature stepped in by amending the anti-indemnification statute to prohibit agreements in which one contracting party requires the other to purchase insurance covering the other party's fault. This eliminates a common practice in construction contracting. Owners, for example, will no longer be able to require contractors to cover owners as additional insureds for the owner's own fault. Any offending insurance requirements are not enforceable and will be written out of the contract by operation of law.
- With Some Important Exceptions



The Buldoc Case and Minnesota's Anti Indemnification Law - Exceptions

- First, A contractor, can require a subcontractor to name the contractor as an additional insured on the subcontractor's policy, but only to the extent that the subcontractor is at fault.
- The second exception to the prohibition is project-specific insurance, The statute does not define the term "project-specific." Some argue that project-specific means any coverage that a person is required to purchase for a specific project. More likely the courts will interpret the term to include only those types of policies that cover the fault of everyone working on the project and not just the named insured.



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BONDS

- Bid Bonds
- Performance Bonds
- Payment Bonds



SPECIAL SUBCONTRACTOR ISSUES

- Flow Down Clause
- Pay When Paid Clause
- Mechanics Liens



FLOW DOWN CLAUSE

- A Flow Down Clause is a must for General Contractors.
- A Flow Down Clause contractually binds the subcontractor to the general contractor in the same manner as the general contractor is bound to the owner (Lots of Litigation on this right now, especially Arbitration).



“PAY IF”/ “PAY WHEN” PAID

- Minn. Stat. § 337.10, subd.3, provides that a construction contract “shall be deemed to require the prime contractor and all subcontractors to promptly pay any subcontractor or material supplier contract within ten days of receipt by the party responsible for payment of undisputed services provided by the party requesting payment.”
- Some General Contractors include “pay-if-paid” clauses in their contracts with subcontractors.



MECHANICS LIEN

- *Serve pre-lien notices if required within 45 days of starting work.*
 - *You can hire a service locally to do this.*
- File a mechanic's lien statement within 120 days of the last date of work. Last day of visible improvement to property.
- Must commence foreclosure within one year of the last date of work.
- The above requirements must be followed exactly as required by Minnesota statute § 514, otherwise the mechanic's lien will be unenforceable.



Mechanics Lien Priority

- Big Lake Lumber v. Security Property Investments 836.NW2d.359 (Minn. 2013)
 - Changed the Landscape on issue of when does subsequent work relate back to first day of improvement
 - Old Test was Kahle v. McClary Test
 - Three Factors
 1. Intent of the subsequent work (good faith requirement)
 2. The timing of the subsequent work
 3. The scope of the contractual terms



Big Lake v. Security – Minnesota

Court of Appeals

- The court of appeals determined that two tests had been established to ascertain whether the later work bore directly on the prior work:
 - (1) Whether two projects of improvement to property are separate and therefore not continuous”; and
 - (2) Whether a project of improvement has been abandoned.
 - (3) Four Part continuity test consists of four factors:
 - (1) including “the parties’ intent,
 - (2) what the contracts covered,
 - (3) the time lapse between projects,
 - (4) and financing.



Big Lake v. Security – Minnesota Supreme Court

- Supreme Court said it is More Complicated (i.e. less predictable)
- Mechanic's lien priority inquiry is fact-specific and must be answered by reference to the statutory language, and not rote application of the continuity and abandonment tests.
- In particular, the court directed lower courts to consider “whether the pre-mortgage work on which the lien claimant relies ‘bears directly on’ the project of improvement and not merely on the ‘overall project involved,’” and whether the pre-mortgage work is “a part and parcel of the work” of improvement.
- While the court acknowledged that the four-factor continuity test and two-factor abandonment test will often be relevant, it stressed the importance of grounding analysis in the statutory language, rather than in “a multi-factor test that imposes additional requirements beyond the statutory language.”



CONSTITUTIONAL LIEN

- **Only Available in Minnesota at Texas**
- Subcontractors are not eligible to obtain constitutional liens. *Da-Col Paint Mfg. Co. v. American Indemnity Co.*, 517 S.W.2d 270, 273 (Tex.1974).
- Constitutional liens are self-executing between the original contractors and the owner. *First Nat'l Bank in Dallas v. Whirlpool Corp.*, 517 S.W.2d 262, 267 (Tex.1974).
- Constitutional liens are not enforceable against a third-party purchaser who lacks actual or constructive notice that the lien exists. *Apex Fin. Corp. v. Brown*, 7 S.W.3d 820, 830 (Tex. App. 1999).



DAMAGES

- **No Damage for Delays**
- Owners and general contractors may try to include a provision in the contract which eliminates their liability for any delay.
- The enforceability of such “no damage for delay” provisions in *private contracts* has not been ruled on by Minnesota courts.
- However, note that Minn. Stat. § 15.411 subd.2 prohibits “no damage for delay” clauses in *public works* contracts.



DAMAGES

❖ Liquidated Damages

- Contractual provisions providing for liquidated damages have been approved by Minnesota Courts.
- In *Gorco Construction Co. v. Stein*, 99 N.W.2d 69, 74 (Minn. 1959), the Minnesota Supreme Court stated: “The modern trend is to look with candor, if not with favor, upon a contract provision for liquidated damages when entered into deliberately between parties who have equality of opportunity for understanding and insisting upon their rights)



Damages

- **Waiver of Consequential Damages**
- Consequential Damages are damages that result from the damage to something else. (i.e. You didn't finish your contract so I lost the sale of my building to someone else.)



WRAP-UP

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