



2022 Construction Conference  
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San Diego, CA

## **Stick to Your Guns: How Changes to Design, Materials and Methods Can Come Back to Bite You**

### **Session Description:**

Contractors and design professionals face increased liability as project delivery methods evolve; supply chain shortages force material replacement and/or substitution; and design changes result from cutting corners to control costs and to meet unreasonable schedules. Construction management and the increased use of technology between contractors and design professionals blur the lines of responsibility which results in contractors' potential design liability and design professionals' potential liability for performing tasks outside the professional scope. Further, design/build project delivery, desired for quicker and cheaper project completion, may result in a contractor being contractually responsible for design and/or result in shared design responsibility (between contractor and design professional). Even if a contractor is not hired as a design builder, the contractor may be managing design risk as a construction manager, by working in a design-assist role, or by hiring subcontractors that have design as part of their scope of work (e.g., MEP). The session will be an interactive discussion about current risks arising from contractors involved in pre-construction phase tasks; contractors and design professionals engaging in construction management services; and the pitfalls of changes in design, materials, and methods under the pressure to deliver on time and under cost.

### **I. The Current State of Construction Litigation**

#### **Economic Recovery and Resulting Changes to Design, Materials and Methods**

Conditions in the construction industry are constantly changing and, most significantly, about labor and supply chain shortages leading to construction inflation. The Associated General Contractors of America (AGC) publishes periodic construction inflation alerts. <https://www.agc.org/learn/construction-data/agc-construction-inflation-alert>. According to AGC's June 2021 Alert and data from the Bureau of Labor Statistics:

- (1)** input costs for construction soared 24.3% from May 2020 to May 2021.
- (2)** The price index for lumber and plywood jumped 111% from May 2020 to May 2021.

(3) “Extended and uncertain delivery times for construction items have been an even bigger problem for many contractors than the extreme prices increase. Currently, there are delays at every stage of the supply chain”; and

(4) Increases in material costs have outpaced bid prices for as long as 28 months.

Now more so than ever, contractors and design professionals want to be competitive to land the projects they need to sustain financial stability and keep pace with an unfavorable construction environment which also includes several projects being abandoned due to financing problems and projects that have restarted after a long period of inactivity which creates several unforeseen conditions upon re-entry.

Competition in the marketplace may give incentives for contractors to submit unrealistic bids to get business. The problem is that when a contractor has bid too low for a project and is awarded a contract, the contractor is now expected to fulfill the terms and conditions of the applicable contract. A low bid may leave the contractor little or no room for unexpected developments and place pressure to cut corners.

The conditions on a construction site may be different from expected which could result in an adverse impact, delays and the need for more corner cutting and/or “work arounds.” These may include challenges with obtaining permits; delays caused by others involved with the project (or replacement of contractors and/or the design professionals; unexpected environmental issues and/or site conditions; adverse weather; and external forces beyond the control of the contractor. “An event or effect that can be neither anticipated nor controlled,” like a pandemic, has proven to be a force majeure with long-lasting detrimental effects on the construction industry – both commercial and residential. (e.g., Toll Brothers pricing from 2019 to 2020 – home base price jumped \$120, 000 in one year).

#### **Causes of Action related to change in design/materials/methods**

There are several causes of action that result from a redesign gone bad and/or a shortage in supply and/or labor which leads to increased cost, schedule delays and inadequate materials and/or code violations. The claims being alleged because of these issues do not appear to be new or novel but are being asserted more frequently as the frustration level to complete projects on schedule within budget is increasing. These may include breach of contract (e.g. you agreed to poor language with little flexibility related to cost or scheduling estimates); breach of warranty (e.g. what promises were made; superlative statements on website or marketing materials); tort – professional negligence (not for the design professional alone - contractor professional liability is on the rise); negligent and/or fraudulent misrepresentation – promises made that cannot be kept due to unforeseen circumstances from which you are not protected under the contract (e.g. pandemic fallout); interference with contractual relationship (e.g. Owner pitting contractor and design team against one another and/or dispute between owner and designer or contractor pulls the other into the dispute based on tasks performed on job; contract or construction administration); and counterclaim for Negligence brought by Owner in response to a claim for fees owed to design professional or contractor (e.g. boomerang claim); claims to recoup or recover unanticipated costs related to materials, delay, labor shortage etc.

## **II. Design and Construction Claims Trends**

Design Build project delivery and contracts, contractors assuming professional liability or design risk and design professionals performing tasks that are not traditionally professional in nature has resulted in a significant increase in liability exposure generally.

Construction project delivery methods continue to evolve, and owners / architects are increasingly delegating construction phase services to contractors. Coupled with the growth in construction management services and increased use of technologies for early collaboration, contractor design liability has fundamentally shifted. From pre-construction services, where a project's strategic direction is created to design/build where a contractor is contractually responsible for design to integrated project delivery where the owner, contractor, architect/engineer along with key trades share all the project risk, design responsibility for construction companies continues to increase.

Even if a contractor is not hired as a design builder, they are managing design risk as a construction manager, by working in a design-assist role, or by hiring subcontractors that have design as part of their scope. Many trade contractors, including but not limited to mechanical, electrical, and plumbing, routinely have design in their scope of work.

Being involved in the pre-construction phase of a project also increases professional liability risk. This risk is even greater if the contractor is not awarded the construction phase of the project. During the pre-construction phase, the project strategy is set, and this plan is an ongoing reference point for other project participants. During pre-construction, design begins. Schedule and budget are determined. Permits, entitlements, labor and resources are procured, some involving long lead time. Value engineering for certain project components may also be performed at this point to meet client budgetary constraints.

It is relatively easy to identify professional liability risk if an entity is stamping design drawings. It becomes much more difficult to identify when there is a lot of knowledge applied to complex pre-construction and/or construction processes but there are no drawings to stamp. Design risk starts in setting the project scope and ends with the client's expectations as to what they are getting. Claims and disputes arise when there is a disconnect between the two. There must be a clear understanding of client expectations on design and getting that documented in the contract.

Complicating this issue is the escalating costs related to the continuing labor and supply chain shortage along with projects abandoned due to financing problems and suspended projects being restarted after long periods of little to no activity.

Additionally, claims related to code changes have resulted in an exterior finishing system construction defect epidemic. Specifically, frequent changes in and variations of local codes contributed to significant litigation surrounding the design, means and methods related to exterior finishing systems (e.g., stucco).

Scope creep or "added value" claims are more frequent during periods of financial challenges because contractors want to win bids and cultivate relationships with developers/owners who will use them on multiple projects. Scope Creep entails contractors assuming design tasks and design professionals engaging in tasks that are outside the professional services scope. In both scenarios, the design

professional and the contractor are exposing themselves to increased liability because of stepping outside the outlined scope of work or services and doing so to give their respective clients “added value” for the fee the client is paying. The scope of work outlined in the contract documents should match what is being done and all necessary coverages should be procured.

Claims related to new and novel project types are cropping up when contractors and/or design professionals get involved in projects for which they do not have the requisite knowledge or expertise because of the specialized design, materials, methods, etc. that are necessary. This is common in green building, cannabis growth and manufacturing facilities and, most recently, modular construction.

Lastly, claims related to “Warranty” statements involve superlative statements made about the quality of work or services and, to a creative attorney, may formulate the basis for a breach of warranty claim. Determining what statements rise to the level of a “warranty” statement is very jurisdiction specific and may result from content on a construction professional’s website or in marketing materials.

### **III. How to Mitigate Risk and Avoid Future Claims Related to Changes in Design, Materials and Methods**

#### **Contract Language is Always Key**

Reviewing and restructuring contract documents is Key. Despite the need to be ultra-competitive, construction professionals now more than ever need to pay attention to contract language and their right to negotiate better language and greater flexibility in contract documents –developers and builders need our clients and taking the time and effort to get a good contract in place should be a top priority especially post-pandemic. (e.g., force majeure language; owner as ultimate decisionmaker; what constitutes the trigger for mandatory review of cost estimates/project schedule due to “unexpected” or “unanticipated events, conditions). Contracts should be reviewed regularly for consistency, emerging risks (Force Majeure, alternative delivery methods, unique construction projects (i.e., Cannabis, Modular, Greenbuild) and to ensure that applicable insurance policies respond to the promises made in the contract documents. It is always recommended that contractor and design professional clients review the contacts of others (on a project) to see what rights you are afforded under those contracts(third party beneficiary) and to confirm that the contract documents for a project, when read in their entirety do not attempt to bind a client to a clause in a contract to which it is not a party (arguably unenforceable but if it is a legitimate flow through clause and the client simply failed to read the documents the client was entitled to review, it may very well be binding). As the enforcement is very state specific and Anti-indemnity statutes vary from state to state, it is strongly suggested to have project contracts reviewed for each project and regularly, especially if the design professional or contractor is involved in multi-jurisdictional projects.

Considering supply chain and labor issues that continue to plague projects across the country, it is necessary to take steps to avoid unreasonable cost and/or schedule estimates, with contract language which addresses the uncertainty if getting the proper materials timely and having the manpower to stay on schedule, which may be similar to the following:

## **Avoiding the Pitfalls of the Revival of a Suspended Project**

When managing risk related to resumption of old and/or lingering projects, contractors and design professionals must ensure that the resumption of design services and work on the Project be accompanied by appropriate contractual protections that reflect new conditions, costs, man power in today's industry. Best practices to engage in when getting involved in a project that is resuming (whether you were involved before the project shut down or not) would include ensuring accounts to all parties involved on the project prior to suspension are brought current prior to commencing work on a resumed project (especially if your role or scope involves review of payment applications and/or progress of the work as related to payments to others); **resolve** issues that arose prior to project being halted (if you were not involved, ask to review meeting minutes, schedules, contract documents, outstanding payment applications, RFIs and COs); re-establish new budgets, schedules, etc. with new owner; Visit the project site to review and document visible changes from project prior to suspension (request photos, plans etc.); your contract should state that you have the right to a copy of and/or review any contract documents that may affect you and you should review them to confirm that the contracts address changes in project after resumption. If there are significant changes to the parties involved in the project upon resumption, the ownership of intellectual property rights and the right to rely on work and information provided by others should be addressed along with a limitation of liability and indemnification if it is feasible –especially if you are a successor to another design professional or contractor who was terminated or did not return to the project for whatever reason.

## **Old, New and Changing Code Requirements and Performance Criteria**

In most jurisdictions, compliance with a code or standard is at best a partial defense, so if a design professional or contractor has not complied with the law initially, there is certain liability exposure. Most laws are not retrospective so it is difficult to see how delay could change the potential liability.

The harder claim to defend is one where codes/performance criteria change several times over the course of a project. In circumstances where the construction professional knows that the project is being constructed to obsolete codes or the design and/or construction is not compliant with current codes/industry standards, because of changes to the standards, it may cause a breach of the new statute. Generally, claims resulting from failure to meet applicable codes will include both design and construction entities but (e.g. Superstorms (negligent design for failure to design consistent with flood protection); exterior envelope litigation (adequacy of material and requisite thickness of materials used); material changes due to unavailability as related to code requirements.

## **Combatting Supply Chain Interruption and Inadequate Cost and Schedule Estimates**

Design professionals should make no guarantee or warranty that a project can be built within the estimate. In fact, the project owner should be made to identify a project budget in writing once it is agreed upon to the extent that no absolute assurances can be made and there is an “escape” clause so that reassessing the project budget is a necessary and regular exercise. Accordingly, if a project does not move forward within a specified time period, contract documents can be negotiated to allow the cost and schedule estimate to be revised

Design professionals should limit responsibility for redesign due to reduced scope or budget constraints. The scenario is one where the owner is looking to cut cost from the original design based on financing constraints, costs related to delay and materials. This is never recommended in that the original design is one that the professional stood behind and for the reasons provided to “rework” the design or use cheaper materials, if there is an issue with code violations, structural integrity of the project and/or materials (quantity or quality) it may fall squarely on the design professional (e.g. collapsed bridge due to redesign 3 times; no evidence that it was ultimately owner who insisted on doing so; nothing in contract to protect design professional)

### **Scope of Work – Contractor’s Professional Liability and Design Professionals’ Scope Creep into Nonprofessional tasks**

In order to provide “added value” services, be competitive and to keep up with emerging project delivery methods (e.g. design build), contractors and design professionals are more and more blurring the lines of tasks that would normally fall into the categories of professional services or nonprofessional services. Construction Management or Contract Administration duties are riddled with overlap or perceived overlap of these tasks. The scope of work which is actually being conducted on the project should be detailed / job specific and clear as to what you are and are not responsible for doing on the Project (e.g. construction management continues to be problematic in litigation even if you are identified as a Construction Manager Not at Risk). Appropriate coverages should be sought, including general liability and errors and omissions for both contractors and design professionals.

### **Standard of Care - Design Professionals under Pressure from Owners; Redesign and Value Engineering**

Redesign and recovering unanticipated construction costs for the Owner has been discussed. It is a significant problem when there is pressure to do so and could ultimately jeopardize a design professional’s adherence to the professional standard of care which is expected and set forth in the contract documents. Generally, the design professional, along with other risk management guidance provided herein, should avoid assuming a heightened standard of care such as: accepting relationship of trust and confidence; assuming fiduciary duty; and covenant or promise to perform to one’s best skill and judgment.

The best language to use will compare a design professional to:<sup>1</sup>

- To a similarly situated design professional

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<sup>1</sup> We recommend language similar to this AIA-approved language:

“The Architect shall perform its services consistent with the professional skill and care ordinarily provided by members of the profession practicing in the same or similar locality under the same or similar circumstances. The Architect shall perform its services as expeditiously as is consistent with such professional skill and care and the orderly progress of the Project.”

(See AIA Document B101, Section 2.2)

- Reasonably prudent design professional

Regarding the issue of dealing with a client who is pressuring the design team and/or the general contractor to go the cheap route and, in essence, telling them to cut corners that may lead to increased liability exposure, we suggest **presenting options to client and document client's directives** /selections in design, materials; outline advantages and disadvantages; identify and obtain client agreement/approval on impact on cost, performance, schedule and aesthetic. Documenting contemporaneously to the discussions preserves the decision making time line for purposes of future settlement negotiations and, if necessary, litigation.

Specific to design professionals, it is important to review the requirements for redesign services. There is an increase in owner-drafted contracts requiring design firms to redesign projects for free, without any limitation on the number of redesigns. In many instances, the contractual redesign obligations are not the result of whether the design professional was negligent or at fault.

Since the design professional has no control over material escalation costs or the bids submitted by potential contractors, it is not possible to guarantee that the bids received will not exceed the budget. Also, as a result of normal change orders during construction, projects very often exceed budget.

Herein we provide two examples of Owner-drafted redesign clauses that are not tied to negligence and do not provide payment for the redesign. With these types of obligations, design professionals are forced to redesign for free, or **under-design it (value engineering)** to meet the owner's budget.

*Consultant will modify at its expense the drawing, specifications, and related bidding and contract documents to the extent necessary to reduce the anticipated construction costs so that the re-solicitation of bids or price proposal will realize bids or price proposals being received that are within the range of accuracy established for the project.*

*Consultant shall, at the Owner's direction, redesign each Project and/or work with the Owner to reduce the costs to within the Final Statement of Probable Construction Costs at no additional expense to the Owner.*

The problem with these examples is that the redesign obligation is not based on any negligence or fault of the design firm. The firm is required to work for no additional compensation due to construction cost and market conditions that are beyond their control. There also is no limit on the number of redesigns that the design firm must complete. With owner-drafted contracts, design professionals should negotiate adding language that allows for additional compensation if the redesign is not the result of negligence on the part of the design professional (e.g. "... and will do so without additional compensation when due to failure to perform services consistent with the Standard of Care.").