

How Do the New National Subcontract Forms Compare?

By Tom Barfield

As one who participated actively throughout development of the updated American Institute of Architects (AIA) A401-2007 subcontract document and also served as a member of the drafting group for the newly minted ConsensusDOCS 750 subcontract, I am glad to say that both documents provide solid, level playing field subcontract forms that are far better for subcontractors than the one-sided ones ordinarily offered by general contractors. The A401 still represents subcontractors' top choice, but the Consensus 750 is a good alternative, especially if the general contractor is looking for a subcontract form that is endorsed by the Associated General Contractors of America (AGC).

AIA's A401 has been published for more than 90 years, and it is revised about once a decade. Before the 1970's, AGC offered suggested A401 changes to AIA on behalf of both general contractors and subcontractors. However, for the past 35 years, AIA has instead relied on subcontractor organizations for proposed A401 revisions, and AGC has elected not to participate in the periodic updating process. As a result, the A401 has become a highly subcontractor-friendly document. Thirty years ago, it passed through the general contractor's prime contract obligations to subcontractors, but not the rights and remedies. Now the A401 is chockfull of subcontractor protections. The 2007 edition adds more such beneficial terms in the sections on payment, contractor jobsite services and subcontract assignment to owners. While the new A401 does contain a limited additional insured requirement, just a few computer keystrokes are needed to download an A401 having a reduced additional insured obligation or else specifying Owners and Contractors (OCP) coverage instead. The heavily used AIA A201 general conditions are still made a part of the A401 except when in conflict with a specific subcontract term.

Development of the ConsensusDOCS family of documents, including its 750 subcontract form, involved a new concept built on the principle of direct collaborative drafting of document terms by representatives from a wide cross section of construction owners, engineers, contractors, subcontractors, insurers and sureties. The DOCS denotes Designers, Owners, Contractors and Sureties, although AIA elected not to participate in the project. The Consensus 750 is largely an enhanced version of the former AGC 650 document which was already a well balanced agreement form. The AGC 650 was developed jointly about ten years ago by AGC and Associated Specialty Contractors (ASC) representatives. The Consensus 750 has the virtue of more favorable additional insured terms for subcontractors than the A401 and entitlement to added compensation for contractor directed timing and sequence changes. However, the 750 form suffers in comparison with A401's broad array of helpful payment terms and ease of use with private general contractors' prime contract documents. Many subcontractor benefits are available only when the 750 subcontract form is used in tandem with Consensus 200 since the 750 lacks adaptability when used with other general contractor forms. This is because, unlike the merging of A401 and A201 general condition terms in AIA's subcontract, Consensus 200 is not made a part of the 750 by reference or otherwise. Thus, many important Consensus 200 terms are lost when the 750 subcontract is used with some other prime contract form. Since Consensus 200 is a project specific general contract form, its terms are not well suited for inclusion by reference in a subcontract.

Comparison of Key Issues

Payment

The all important payment terms represent a big plus for subcontractors in the A401. Advantages for subs include helpful stand-alone terms in the A401 and also by flow through of beneficial A201 general conditions terms. The 2007 edition of A201 added options for the owner to contact subcontractors directly and to issue joint checks, if necessary, to assure prompt pass through of payments to subcontractors. Consensus 750, by contrast, does not offer similar protection to subcontractors, but it does include contractor options for protecting sub-subcontractors and suppliers if subcontractors fail to pay them promptly. The Consensus 200 prime contract form has subcontractor-helpful language allowing retainage release for a subcontractor's work accepted by the owner and for no further retainage once a project is 50% complete. However, these terms are not repeated in Consensus 750 and would flow through to the 750 subcontract agreement only if Consensus 200 is used as the prime contract.

Both subcontract documents require that the contractor make progress and final payments to its subcontractors for properly performed work and suitably delivered material even if the owner has not paid the contractor for any cause that is not the fault of the subcontractor. However, there is a huge difference in the timing. The A401 calls for such payments to be made upon the subcontractor's demand whereas the 750 terms require only that contractors pay their subcontractors after an undefined "reasonable time" has elapsed. This could be a very long time. With the A401, interest would start to accrue when payment is demanded by the subcontractor if payment is not made promptly. By contrast, Consensus 750 terms limit interest to the proportionate share, if any, of owner interest payments to the contractor, although the contractor would owe interest to its subcontractors if late owner payments were the contractor's fault.

Subcontractors are entitled by A401 to progress payments for material delivered and stored either on site or at an off site location, whereas Consensus 750 requires payment approval in advance by the owner, even for material stored at the jobsite. A401 does call for contractor approval for storage of the subcontractor's material off site.

Both the A401 and Consensus 750 forms prohibit contractors from withholding a higher percentage of retainage from a subcontractor than the owner withheld in its payments to the contractor for the subcontractor's work and material. The two forms also call for payments to subcontractors within 7 days after receipt by the contractor of owner's payment for such subcontracted work. Each further provides for reduction in retainage to the extent allowed in the prime contract upon substantial completion of a subcontractor's portion of the project work, as well as prompt notification to the subcontractor of any payment application amounts that are disapproved. The A401 adds a significant benefit to subcontractors by allowing them to contact the architect directly to learn the amount of their progress payment applications that was approved for payment.

Additional Insured

The additional insured issue is one where Consensus 750 terms are more favorable to subcontractors than those in A401. Unlike A401's requirement that additional insured coverage must be provided by subcontractors, Consensus 750 allows the contractor to choose whether or not the subcontractor will be required to purchase and maintain primary additional liability insured insurance at the contractor's expense. If the contractor decides to require the additional liability coverage, it may then choose between an Owners and Contractors Protective (OCP) policy for the subcontractor's operations and/or additional insured coverage for operations and completed operations.

While A201's additional insurance requirement is specifically limited to losses caused in whole or in part by the subcontractor's negligent acts or omissions, the subcontractor's insurer could become liable for 100% of a loss for just a scintilla of fault. The subcontractor would then have to pay an often costly deductible amount, and its experience rating would suffer. Unfavorable ratings may result in more costly future insurance premium rates, inability to bid work requiring a superior safety record and possible loss of insurability. The A201, unlike Consensus 750 terms, does not require that the additional insured coverage be primary to the contractor's or owner's own insurance.

Under the circumstances, subcontractors may wish to revise the additional insured section when bidding subject to the use of A401 terms and when substituting these AIA subcontract terms for one-sided subcontractor terms being offered by a general contractor. CAUTION: No matter which subcontract form is used, subcontractors need to be sure that their insurance brokers not provide additional insured endorsements in excess of contract requirements since such volunteered added coverage may allow claims for losses caused by an additional insured party despite relatively benign contract terms.

Indemnity

The Consensus 750 no longer contains a prior AGC 650 duty for the subcontractor to defend claims filed against others, and it clarifies that the hold harmless terms apply only to the extent of losses *caused by* the subcontractor's negligent acts or omissions. This brings the Consensus 750 indemnity language into general agreement with existing A401 terms. Hence, both of the documents are highly protective of subcontractors when claims arise. New language was also added in Consensus 750 that entitles the either party to reimbursement of legal defense costs paid above its percentage of liability for an underlying claim. Now that the duty to defend claims against others has been eliminated, the courts may be reluctant to reimburse a subcontractor for volunteered legal expense, and it is ordinarily tough to reach agreement as to the percentage of each party's fault when cases are settled out of court. Under Consensus 750, the parties indemnify one another against fines caused by a failure to comply with applicable safety requirements, such as OSHA regulations, but not for added fines covering repeated or willful violations.

Consequential Damages

An example of consequential damages is the owner's loss of prospective revenue if a job is not completed by the agreed upon target completion date. Where a completion date is crucial, best industry practice calls for use of liquidated damages so that contractors and subcontractors know in advance the extent of their exposure for causing a delay. Consequential damages apply either if required by contract or if the contract is silent on the subject.

Both A401 and Consensus 750 contain waivers of consequential damages, but the impact on subcontractors varies greatly depending on which of these subcontract documents is used. A401 contains a stand-alone joint consequential damages waiver between the contractor and subcontractor plus the flow through of the comprehensive waiver provision in the A201 general conditions. By contrast, Consensus 750 has several potential holes in its safety net for subcontractors. The Consensus 200 provides space for the owner and contractor to insert exclusions to the consequential damages waiver in the prime contract. In turn, the 750 subcontract requires that the subcontractor accept these same exclusions so long as a copy of the prime contract is provided to the subcontractor prior to execution of the subcontract. Another potential pitfall comes when subcontractors use the Consensus 750 in conjunction with a prime contract that is silent on consequential damages. Since the 750 document specifically limits waiver of consequential damages to the extent contained in the general contract, the subcontractor may well be on the hook for a huge claim if it delays the job. Prudent subcontractors routinely condition their bids and subcontract terms on the understanding that, under no circumstances, shall either party be liable to the other for consequential damages. This becomes a necessary precaution when Consensus 750 is being used.

Warranty

The warranty terms for the two subcontract documents are comparable when the Consensus 750 is used in conjunction with the Consensus 200 prime contract document. Both call for a one-year warranty correction period beginning at substantial completion of the subcontractor's work unless otherwise agreed. However, when the 750 forms are used with most other general contract terms, an important protection is lost. A401 excludes from the subcontractor's warranty any damage or defect caused by abuse, alterations by others, inadequate maintenance, improper operation or normal wear and tear. A401 also exempts defects that are inherent in the quality of its contractually required work. Consensus 200 has warranty exemptions similar to those described in A401, but these are omitted in Consensus 750. Consensus 200 also provides that adjustments in price for defective work accepted by the owner in lieu of replacement are limited to any diminution in project value caused by the deficient work. There is no comparable language in either the Consensus 750 or A401 subcontracts.

Dispute Resolution

For the first time in its long documents history, AIA's A201 family of documents, including A401, does not mandate use of arbitration for binding resolution of disputes. Instead, the subcontract offers the parties a selection of arbitration, litigation or some other designated method. The contractor and subcontractor could later change the resolution method by mutual agreement in writing. Consensus 750 also provides space

for the parties to insert either arbitration or litigation. Previously, the AGC 650 subcontract called for disputes not resolved by mediation to be decided in the same manner selected by the owner and contractor in the prime contract. One Consensus 750 exception requires that disputes involving the owner, contractor and subcontractor to be resolved in the same forum as chosen in the prime contract.

Both of the subcontract forms require mediation as a precondition to binding dispute resolution. Consensus 750 goes a step further and also mandates good faith discussions between the parties' representatives and later, if necessary, by their senior executives prior to mediation. Both subcontracts also call for use of American Arbitration Association (AAA) mediation rules unless otherwise agreed. Consensus 750 further requires that the costs of any binding resolution procedure be borne by the loser.

A401 authorizes either party to join other persons or entities in an arbitration proceeding where there is a common question of law or fact, but only if the party that is being joined agrees in writing. Subject to some limitations, both subcontract forms permit consolidation with another arbitration involving common issues. Under limited conditions, Consensus 750 requires that resolution of contractor-subcontractor disputes be stayed pending adjudication of similar owner-contractor issues.

Temporary Services

New A401 language obligates the contractor to make available to subcontractors, at no cost, all temporary jobsite facilities, equipment and services except as otherwise specifically identified in the subcontract document. By contrast, Consensus 750 calls for the subcontractor's and contractor's responsibilities for temporary services to be shown on an attached exhibit. This approach presumes that the parties will prepare an exhibit that would include the dozens of temporary facilities that might create later back charge disputes. Hence, the definitive, best practice A401 terms are infinitely better for subcontractors than the Consensus 750 in an area that has long needed more specificity.

Schedule Changes

An important plus for Consensus 750 is the subcontractor's right to an equitable adjustment in both contract time and amount due to contractor directed changes in the time, order or priority in which the subcontractor's work is to be performed. This hugely helpful provision was brought forward from the AGC 650-2006 draft subcontract form. There is no such specific authority found in A401 although it states that claims may be asserted for delays caused by contractor directed changes.

Design Delegation

A401, through inclusion of A201 terms, makes clear that reliance by recipients on the accuracy and completeness of delegated design certifications applies only if *all* performance and design criteria are furnished. While the Consensus 200 prime contract contains comparable language, Consensus 750 is lacking this important limitation.

Liens

A401 requires that the contractor promptly furnish its subcontractors, upon written request, with information necessary for evaluating and enforcing mechanics' lien rights, including identification of the owner's interest in the property. Although Consensus 200 provides similar authority, the requirement is not included in Consensus 750. Hence, the contractor's lien information obligation might well not apply unless Consensus 200 is used as the prime contract document. A401 does not require lien waivers as part of the progress payment process. Consensus 750 does mandate the furnishing of lien waivers, but it protects subcontractors by prohibiting requirements that subcontractors furnish unconditional lien waivers for any amount in excess of payments received by them.

Owner Financing Information

Consensus 750 allows subcontractors to request owner financing information received by the contractor. If the requested information is not received, the subcontractor is then authorized to request the financial evidence directly from the owner or its lender. There may well be a problem of enforceability since neither the owner or lender is a party to the Consensus 750 subcontract, and Consensus 200 does not obligate the owner to provide financing information to subcontractors either directly or through its lender. A401 requires only that the contractor promptly make available to the subcontractor information received from the owner that affects the subcontract.

Contractor Initiated Takeover of Subcontractor's Work or Termination

Consensus 750 allows the contractor to takeover performance of the subcontractors work if the subcontractor does not commence and continue satisfactory correction of a default with diligence and promptness following a single 3 business day notice. A401 has a similar provision, although it requires a 10 day notice to the subcontractor. Contractor termination of the subcontract is permitted by Consensus 750 following an original 3 day notice plus a subsequent 7 day notice. This provision is better than A401's requirement that calls for only a single 10 day notice prior to subcontract termination.

Ethics

Consensus 750 commits the parties to mutual trust, fair dealing and integrity during operations as well as their avoidance of conflicts of interest. A401 has no similar provisions, but courts generally hold that all contracts contain an implied duty of good faith and fair dealing.

Comparable Terms

It is important to bear in mind that there are far more comparable terms than differing ones in the A401 and Consensus 750 documents. The two forms have similar terms for such important issues as change orders, delays, digital documents, interest, property insurance, patents, safety, subcontract assignment and storage facilities.

Conclusion

Subcontractors are fortunate to have two level playing field national subcontract documents for their use in securing subcontract terms that are comparable to the obligations and rights found in equitable owner-contractor agreements. The enhanced former AGC 650 form, that has now become Consensus 750, is a good document that is beneficial for subcontractors, particularly when used in conjunction with the Consensus 200 general contract. The AGC endorsed 750 document offers subcontractors far greater protections than typical general contractors' private subcontract forms.

The A401 is a measurably better subcontract document for subcontractors. With its incomparably favorable payment terms and its ready adaptability for use in conjunction with practically any general contract document, the A401 is ideal for subcontractors to utilize in conditioning their bids on the use of its terms, except for possibly modifying the new additional insured requirement. Even if some A401 terms are not agreed to during subcontract negotiations, the remaining terms will almost certainly provide better subcontractor protections than the contractor's pet form.

ASC, an umbrella group composed of major construction specialty trade associations, has endorsed both the A401 and Consensus 750. The American Subcontractors Association (ASA) has endorsed the Consensus 750 but not the A401, presumably based on the latter document's additional insured requirement. ASA has also referred to A401 as containing "the worst practices of the construction industry". I urge that subcontractors take just a bit of time to read through the A401 and let the facts speak for themselves. The A401 is still a gem of a subcontract form and continues to far outshine its rivals from a subcontractor's perspective. It's easy to see why the A401 is AIA's best selling agreement document.