**Construction and Design Law: Managing the Network of Interdependent Relationships**

Carl J. Circo

**Lesson 5: The Owner-Builder Relationship**

Rather than covering legal principles governing a single construction industry role, as was the case in Lesson 4 (The Design Professional), this lesson explores the legal relationship between two principal participants, the project owner and the primary builder. As a convenient methodology, this lesson looks at the relationship through the lenses of two of the most popular standard industry forms, along with reflections on a doctrine that has characterized that relationship for more than a century.

Standard Industry Forms

Projects commonly rely on standard industry form contracts to govern the relationships among project participants. Begin by reading Sections 5:1-5:10 in volume 2 of *Bruner & O’Connor on Construction Law* (Westlaw Aug. 2023), by Phillip L. Bruner & Patrick J. O’Connor, Jr. The first nine sections offer a general overview of several industry contract forms and the industry organizations that promulgate them. Section 5:10 introduces you to the American Institute of Architects’ “general conditions” document, AIA A201 (2017), “General Conditions of the Contract for Construction.” A201 establishes contract terms of general applicability to construction contracts between a project owner and the primary builder (a role A201 labels “contractor”). A201 probably remains the most popular of the industry forms used for design-bid-build projects in which the owner’s architect provides the full range of project design and construction administration services.

For efficiency’s sake, project participants often rely on standard industry contract forms rather than negotiating bespoke contracts. The most popular industry forms reflect lessons from years of collective experience in anticipating, allocating, and managing the complex risks inherent in most construction projects. Differences in project types (e.g., residential, commercial, industrial, infrastructure, government) and delivery systems have led to the development of many alternative standard forms. The wide acceptance of industry forms, however, coexists with an equally well-accepted penchant project participants and their lawyers have for negotiating modifications and supplements to adapt those forms to the specific circumstances of each project and the perspectives and objectives of that project’s participants. Moreover, participants and lawyers, especially when negotiating the largest and most complex projects, often jettison industry forms entirely and draft customized contracts, usually based on templates from previous large and complex projects in which they have been involved. Furthermore, public owners frequently insist on using their own contract forms or adaptations of standard forms.

In a single construction law course, examining multiple industry forms in common use, or even reviewing a complete set of alternative forms from any single industry organization, would prove utterly impractical. A selective review of key terms from illustrative forms provides a meaningful primer for those new to the construction law practice. This lesson uses two of the most popular AIA forms for that purpose.

Design-bid-build project using fixed pricing: the A101 approach

Read AIA A101 (2017), “Standard Form of Agreement between Owner and Contractor where the basis of payment is a Stipulated Sum.” As the title indicates, this form should only be used if the parties have elected to set a fixed price for the construction work. What is just as important, although not clarified by the title, is that the form contemplates a design-bid-build delivery system. As is true of other organizations that promulgate forms, the AIA offers alternative documents for projects using cost-based pricing or alternative delivery systems.

A notable characteristic of this relatively brief document is that it does not itself provide the complete terms establishing and governing the owner-contractor relationship. Rather, it identifies key information about the parties and the project, including the plans and specifications that define the scope of work, the schedule, the fixed price, and related compensation details. It also covers other basic terms that may be specific to the project or the parties or that may only be applicable to a fixed-price arrangement. Many of the provisions of A101 require the parties to fill in pertinent information or to select among listed options. For some of the most important contract terms, however, A101 incorporates by reference other documents, as enumerated in Article 9. In this way, A101 covers key terms that vary from one project to another while leaving to those forms incorporated by reference terms that, at least in theory, may apply without regard to the details specified in A101. Thus, an attorney for either the owner or the contractor merely takes an initial step in the process of negotiating and documenting the deal by carefully addressing the A101 details to assure that they reflect the client’s understandings and intentions for the project concerning those limited points. The process necessarily also involves, among other things, reviewing and advising the client about the other “Contract Documents,” as refenced in Articles 1 and 9, including the “General Conditions of the Contract for Construction.” The concluding part of this lesson discusses the AIA general conditions document.

Two topics that A101 covers by reference to a document other than the AIA form of general conditions deserve further discussion at this point for two distinct reasons. First, they involve important contractual devices—insurance and surety bonds—that owners and builders routinely use to manage special risks inherent in their relationship. Second, in contrast to many other contractual devices that allocate or shift risks between the contracting parties, through insurance and bonding requirements, industry participants transfer risks to external sources (insurers and sureties).

Subsection 8.5.1 requires both the owner and the contractor to purchase and maintain insurance. Subsection 8.5.2 provides for the contractor to provide surety bonds. A101, however, does not specify details concerning insurance or bonds. Rather, subsection 9.1.2 incorporates a separate document, Exhibit A, designed specifically to address these requirements for a project using A101.

Lesson 2 generally introduced the roles that insurance and surety bonds play in the construction industry, but it did not delve into these topics. This lesson still is not the place for a full exploration of insurance and surety bond issues, but it does present an opportunity for a selective summary of Exhibit A, which will at least serve to alert you to some of the complexities involved, especially with reference to insurance. In practice, insurance and bonding matters often require industry participants and construction lawyers to seek input from lawyers and consultants who specialize in these two areas.

Article A.2 of Exhibit A provides for the owner to maintain “the owner’s usual liability insurance,” and it also requires the owner to carry a builder’s risk policy of property insurance meeting the requirements the parties specify in section A.2.3, unless the parties agree to shift this obligation to the contractor. These provisions address many details, such as coverage limits and sub-limits, deductibles and self-insured retention, and special requirements if the project involves remodeling or an addition to an existing structure. Section A.2.4 allows the parties to select options for additional property insurance the owner could secure, including loss of use, business interruption, and delay in completion insurance, as well as several other specialized coverages. Section A.2.5 contemplates that the owner may opt to purchase cyber security insurance or any other insurance the parties elect to list at the end of that section.

Article A.3 addresses the contractor’s insurance obligations. Subsection A.3.1.1 requires the contractor to provide to the owner evidence of insurance prior to starting the work and at other specified later times. Subsection A.3.1.3 requires the contractor to designate the owner, the architect, and the architect’s consultants as additional insureds on the contractor’s commercial general liability policy for purposes of certain claims. Section A.3.2 itemizes the required coverage and dollar limits for the following categories: commercial general liability; automobile liability, workers’ compensation; and employers’ liability. It also provides for other specialized coverage as applicable to the specific project for such circumstances as work on or near navigable waterways, any professional services the contractor may provide, pollution risks, and special risks associated with the operation of a maritime vessel or aircraft. If the parties mark any options for other insurance under section A.3.3, the contractor may also be required to provide these additional coverages: property insurance under a builders’ risk policy (insurance the owner would otherwise be required to provide); railroad protective liability insurance, asbestos abatement liability insurance; insurance for property in storage or transit, insurance covering the contractor’s own property used on the project; any other insurance the parties list. Given the obviously complex nature of establishing specifications for insurance a contractor might carry, you should see why even sophisticated clients and their experienced construction lawyers often refer these matters to insurance specialists.

Section A.3.4 specifies the amount of any payment and performance bonds. While this section reads as if these surety bonds will necessarily be secured, unless other contract documents require them, the parties will simply leave blank the areas in the section designated for specifying the amount of each bond. When a contract requires surety bonds, it may be important to consider applicable statutory provisions, regulations, and surety industry customs and procedures. Those matters, however, are beyond the scope of this lesson.

Purely as a practical matter, the next logical step in exploring the AIA approach to the conventional relationship between an owner and builder would be to turn to the AIA general conditions. For reasons that will soon be apparent, however, a doctrinal detour is in order.

Spearin Doctrine revisited

 Why interrupt this discussion of the AIA approach to the owner-builder relationship in a design-bid-build project with a flashback to the Spearin Doctrine already mentioned in earlier lessons? First, A101 manifests the contractual elements that gave birth to the doctrine—the owner furnishes detailed plans and specifications for work the builder agrees to complete for a fixed price. Second, the treatment the Spearin Doctrine has received so far falls short of what every construction law student needs to know. Thus, this lesson presents a convenient time to delve more deeply into this golden nugget of construction law that characterizes the owner-builder relationship in a design-bid-build project.

Deepen your understanding of the Spearin Doctrine by reading *United States v. Spearin*, 248 U.S. 132 (1918). The Court’s original statement of the doctrine, commonly characterized as the owner’s implied warranty of design, is that “if the contractor is bound to build according to plans and specifications prepared by the owner, the contractor will not be responsible for the consequences of defects in the plans and specifications.” *Id*. at 136. Even after over 100 years, *Spearin* remains one of the most cited and discussed construction law cases, and courts and commentators continue to debate its implications and limitations. See Phillip L. Bruner & Patrick J. O’Connor, Jr., 3 *Bruner & O’Connor on Construction Law*, §§ 9:90-9:104 (Westlaw Aug. 2023).

The U.S. Supreme Court developed the Spearin Doctrine in the context of a fixed-price contract for construction work thoroughly defined via detailed plans and specifications for a design-bid-build project. In other words, the Spearin Doctrine derives from the context for which A101 is designed. Moreover, as you will see when this lesson considers Article 3 of the AIA general conditions, the Spearin Doctrine remains largely intact in the AIA approach to a design-bid-build project.

With limited exceptions, state courts have widely embraced the Spearin Doctrine in that same context. Less clear, however, are Spearin’s implications in other situations. The design-build system represents a clear case for rejecting or severely limiting the owner’s implied warranty of plans and specifications. Similarly, the Spearin Doctrine should not apply to the extent an owner furnishes “performance specifications,” which do not direct the builder to follow detailed or complete plans and specifications for some aspect of the work but, instead, explicitly leave to the builder the responsibility to prepare the detailed design. More complicated issues arise in other situations, such as when the builder participates in the design phase in some limited way or when evidence suggests that the builder did not sufficiently rely on or adhere to the plans and specifications the owner furnished.

One authority lists several circumstances in which Spearin may not protect a contractor even when the project uses the design-bid-build delivery system:

Under the modern rule, the *Spearin* doctrine cannot be invoked when (1) the contract contains a specific exculpatory clause or other express disclaimer of design liability; (2) the contractor had a duty to inquire as to patent or obvious defects but failed to do so; (3) the specifications provided are classified as performance specifications only, and not design specifications; (4) the defects in the plans and specifications are minor and do not result in substantial design changes; and (5) in some jurisdictions, delay damages are sought flowing from design defects.

Lauren P. McLaughlin, Shoshana E. Rothman, *When Spearin Won't Work: How Contractual Risk Allocation Often Undermines This Landmark Ruling*, Constr. Law., Summer 2015, at 39, 40.

Having completed this brief theoretical diversion, we turn now to the AIA general conditions document to see how it fleshes out the AIA’s approach to the owner-builder relationship in a design-bid-build project.

General conditions of the contract for construction: the A201 approach

To a novice, a reference to the general conditions of a contract might suggest the kind of tedium sometimes associated with “miscellaneous” and “boilerplate” clauses. In the AIA lexicon, however, a contract’s general conditions include some of the most important terms that define the legal relationship between the contracting parties (typically the owner and the primary builder or the primary builder and subcontractors). In the A201 approach, general conditions reside in a lengthy form document that parties can easily incorporate into their contracts without change to fill in many details of the relationship. Sophisticated industry participants and their lawyers, however, review the general conditions carefully in the context of each project, and they frequently negotiate changes to the general conditions or replace some of the provisions with alternative terms more suitable to the circumstances of the project and the parties. (As an unfortunate aside, you should know that the construction industry also sometimes uses the term “general conditions” to refer to certain general or administrative costs involved in performing construction work, but we can safely ignore this alternative usage for now.)

AIA’s A201 represents the most familiar “standard” set of construction contract conditions, especially for traditional commercial projects. Under the AIA approach, A201 furnishes the general conditions for design-bid-build projects whether they use fixed pricing, as A101 contemplates, or a cost-based pricing system. If you ask ten experienced construction lawyers for their opinions on A201 and how they typically approach a project for which A201 is proposed as the general conditions, you might well receive ten different and somewhat conflicting responses. In this lesson, the objective is not to endorse or reject A201 as the preferred approach, but merely to appreciate the scope and significance of A201 as an example of some of the most important issues construction contracts should often address. Indeed, even construction lawyers who firmly object to using A201 will generally recognize that it provides a good template or checklist of the common issues an owner-builder agreement should cover. For these purposes, these concluding paragraphs invite you first to consider A201’s overall scope, then to reflect on how three of its specific articles function to define the basic relationship more fully, and finally to review one practical commentary on some of its most important provisions.

To begin, carefully think through page 1 of A201 (the Table of Articles), which lists each of the main topics this standard form covers. In one way or another, you should expect most owner-contractor agreements to address each of these topics because each one allocates and manages distinct risks common to construction projects, especially in design-bid-build projects. While all these broad areas deserve attention, for this lesson, focus primarily on the basic relationship between the owner and the contractor and on how A201 anticipates the inevitability of changes in the work. Read Articles 2, 3 and 7, which concern these matters.

Article 2 (Owner) describes in general terms the owner’s role, and it lays out key responsibilities and rights the owner has. Subsection 2.1.2 allows the contractor to require certain information that may be necessary under state law to protect mechanic’s lien rights. These rights, which should be more accurately described as construction lien rights, provide payment security to those who perform construction work or provide construction services. Although construction lien laws vary significantly from one jurisdiction to another, information a primary builder may need to secure these rights for itself, subcontractors, and suppliers may include details about the project owner, a legally sufficient description of the land where the project is located, information about the ownership of that land, and whether mortgages and other liens affect title to the land. Section 2.2 allows the contractor to require evidence that the owner has sufficient funding to pay for the project before the contractor begins construction, and it also gives the contractor limited rights during the construction process to require supplemental information about the owner’s financial arrangements. Sections 2.4 and 2.5 authorize the owner to suspend the work or to take over construction in certain instances of contractor defaults. Another feature worth noting is that Article 2 reinforces the central role the owner’s architect plays in the AIA approach.

Article 3 (Contractor) completes the basic outline of the relationship. In contrast to Article 2’s concise description of the owner’s role, Article 3 delineates the contractor’s role more comprehensively. This difference makes sense because A201 contemplates a project for which a primary builder assumes the dominant responsibility. Note that Section 3.2 requires the contractor to review plans, specifications and other information the owner provides, become generally familiar with the project site, independently investigate other details relating to the work, and report any apparent discrepancies or other problems to the architect. Returning momentarily to an earlier theme, you should see that subsection 3.2.4 implicitly confirms that these duties do not override the owner’s Spearin warranty. From both parties’ perspectives, three other provisions of Article 3 are fundamental: section 3.5 (Warranty), subsection 3.7.4 (Concealed or Unknown Conditions), and section 3.18 (Indemnification). Note that Article 3, even more than Article 2, emphasizes the central role the owner’s architect plays under the AIA approach.

Article 7 (Changes in the Work) provides both procedural and substantive rules for managing a category of risks common to nearly every construction project—the potential that circumstances will arise making changes to the work either desirable or necessary. Section 7.2 provides for changes that the parties negotiate and that they document by contract amendments (change orders) specifying the change and any associated adjustments to the price and schedule. This provision is orderly, but hardly surprising because contracting parties are ordinarily free to modify their agreement. Section 7.3, however, supersedes the contract law principle that normally requires mutual consent to modifications. It allows the owner to require a change without securing the contractor’s agreement and without documenting in advance the impact the change will have on the price or schedule. Although most construction contracts give the owner such a right, applicable procedures and restrictions vary throughout the industry. The AIA approach, designated in section 7.3 as a “Construction Change Directive,” contemplates alternative methods for determining what impact such a unilateral change will have on the price and schedule, and it ultimately vests the owner’s architect with significant authority over the entire process. Section 7.4, which authorizes the owner’s architect to make “minor changes” that have no impact on price or schedule, goes beyond what many other industry forms contemplate.

With these brief introductory observations about just a few key aspects of A201 as background, now read *Anticipating and* *Allocating Risks in the 2017 AIA Owner-Contractor Agreement*, Constr. Law. Fall 2019, at 35, by Neale T. Johnson & Kristen Rectenwald Wang. This article illustrates how experienced construction lawyers, whether representing a project owner or the primary builder, may approach A101 and A201 based on their respective client’s perspectives and the specific circumstances of the project. Read the article primarily to develop a feel for the lawyering skills involved in reviewing and negotiating a complex construction contract. Later lessons will return to several of the most significant issues the authors discuss, many of which are important whether or not the parties use AIA documents and no matter which project delivery system they select.

For Review and Discussion

1. From what you have seen so far of AIA documents, does the AIA approach seem to favor one project participant or perspective over others? Identify two or three specific provisions relevant to your response to this question.
2. The discussion above of A201’s Article 3 concludes that subsection 3.2.4 aligns well with the Spearin Doctrine. Do you agree? Why or why not? What changes might an owner make to Article 3 to make the Spearin Doctrine inapplicable?
3. Identify one modification to A201 that Johnson & Wang propose that you might resist agreeing to when representing an owner and one modification they propose that you might resist when representing a builder. For each of the two proposed modifications you identify, explain why you might resist making the suggested changes.
4. Did you notice that the topic of Article 11 of A201 is “Insurance and Bonds?” Why do you think the AIA addresses these two important subjects in three separate forms used in connection with a design-bid-build project (A101, Exhibit A to A101, and A201)?