

Common waiver an all-too-common problem

A frequently used contract clause shifts too much risk to developers

Historically, project owners could count on their architects, engineers and contractors to take responsibility for damages if a project were delayed or defective through no fault of the owner. Occasionally, a contract would include a limit on damages the owner could recover, such as a liquidated damages clause governing delay damages. But generally, an owner could seek contractually unfettered redress if the other party failed to get the job done and done right.

Today, however, both standard industry contracts and non-standard contracts prepared by designers, contractors and design-builders almost always contain provisions that substantially limit an owner's remedies for damages resulting from the other party's wrongdoing.

The most common type of such contract limitation is the waiver of consequential damages. The 2007 versions of the American Institute of Architects' standard contracts, released in October, continue to contain a waiver of consequential damages. The new ConsensusDocs standard contracts, issued in September and spearheaded by Associated General Contractors, also contain a waiver of consequential damages. So, too, do the standard form contracts of the Engineers Joint Contract Documents Committee and the Design-Build Institute of America.

Indeed, the ubiquity of the waiver poses a substantial and usually unjustified transfer of risk to owners – a risk owners commonly don't realize they're assuming or don't take as seriously as they should.

The waiver, in essence, bounds the owner to relinquish its right to assert claims for damages that are "consequential." The term "consequential" is understood by virtually everyone in the industry to cover damages resulting from delay, loss of use and loss of income. However, what additional kinds of "indirect" damages ultimately fall within the definition is a question that has defied resolution by courts and legal scholars alike.

As a result, an owner that agrees to waive consequential damages can count on two things happening. First, the owner will have no remedy against the other party for lost profits resulting from delayed completion (except through liquidated damages), from the shutdown of the project after completion to correct defects, or from damages caused to third parties. Second, the other party will assert that any other damages were arguably "indirect" in nature and ask that they be waived.

The waiver of consequential damages contained in most contracts technically is mutual in nature. In reality, however,



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the owner is much more likely to have its damages limited by the waiver, because the designer, contractor or design-builder is far more likely than the owner to cause damages of a "consequential" nature. Moreover, most "mutual" waivers aren't truly mutual – they don't constrain the other party from recovering damages resulting from delay.

So why do contracts today commonly contain a waiver of consequential damages? One reason is an infamous 1992 New Jersey case, *Perini Corp. v. Great Bay Hotel & Casino*. In the Perini case, a construction manager entitled to \$600,000 under its contract was held liable to the owner for \$14.5 million in delay damages. In response to the seeming inequity, the AIA in 1997 for the first time inserted a waiver of consequential damages into its standard contracts. Once the AIA took this step, the floodgates opened, and the provision was included in other contracts throughout the industry.

A second reason the waiver of consequential damages appears in contracts is that owners as a rule don't push back and just say no – or, alternatively, either insist on making the waiver truly mutual or demand the Perini problem be avoided by including in the contract a dollar limit on consequential damages rather than a waiver.

The fundamental problem with the waiver of consequential damages is that it shifts to the owner all of the risk of damages that frequently go to the heart of the owner's business exposure: damages resulting from delay, loss of use, and loss of income. All this even though the designer, contractor or design-builder caused the problem.

Savvy owners understand the significance of a waiver of consequential damages. They also make its inclusion in a contract a deal-breaker in the same way their designers, contractors and design-builders contend the provision's removal will cause them to walk. Savvy owners also push to make the waiver truly mutual, and seek as an alternative to the waiver a dollar limit as a way of balancing the legitimate interests of both parties under the contract.

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