



SUBCONTRACTOR'S RIGHT TO NEGOTIATE SUBCONTRACT TERMS

by *Thomas R. Olson*

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Our experience is that standard subcontracts do not fairly allocate rights and obligations. Rather, the subcontract is one-sided in favor of the general contractor. The subcontract typically provides the general contractor with maximum freedom and leverage, and the least amount of financial risk. It does not fairly allocate rights and obligations. And if a subcontractor will sign the subcontract as written, for the general contractor, this is good business: minimize risk, maximize reward.

This article is about why subcontractors have the right to negotiate the subcontract terms, to request that the proposed standard subcontract be re-written to fairly allocate both rights and obligations.

Subcontractors are Not Legally Required to Sign a Proposed Subcontract

It is often assumed by both general contractors and subcontractors that if a general contractor relies upon the subcontractor's bid in successfully submitting the low responsive bid, the subcontractor is required to sign the general contractor's standard form subcontract. This assumption is incorrect.

When a general contractor solicits a subcontractor bid, the subcontractor's bid is an 'offer' to perform a specified scope of work at a specified price (and often also subject to specified conditions). If the general contractor relies upon that bid, and is awarded the general contract, the general contractor has 'accepted' the subcontractor's 'offer.' As a matter of black letter law, the general contractor has the legal right to require that the subcontractor honor its 'bid,' its 'offer.' This enforceable legal right is referred to as 'promissory estoppel.' Insofar as the general contractor 'relied' upon the subcontractor's 'promise' (i.e. its bid, its offer), the subcontractor is 'estopped' (i.e. prevented) from not honoring its bid notwithstanding that a formal subcontractor has not been executed.

What is critical to understand is that the general contractor's right to enforce the subcontractor's bid is expressly limited to the terms of the subcontractor's bid. When the general contractor sends its standard form subcontract for the subcontractor to sign, since the general contractor's 'solicitation' of a bid was not then predicated on the requirement that the subcontractor sign the standard form subcontract, the general contractor cannot compel the subcontractor to sign the subcontract. Under these factual circumstances, the general contractor's standard form subcontract is a 'counteroffer' which the subcontractor can agree to or refuse to 'accept.'

How Should Subcontractor Exercise its Right to Negotiate Subcontract Terms

Since the proposed standard for a subcontract is a 'counteroffer,' the subcontractor has the legal right to negotiate terms which extend beyond the scope of the subcontractor's original bid. Subcontractors should exercise this right. It matters not that the general contractor responds that "this is the standard subcontract we use with all our subcontractors." As a matter of law, regardless of how the proposed subcontract is written, and how 'standard' it is, the subcontractor can and should negotiate this.

'How' to do this and 'what' to request can be rightfully overwhelming. The subcontractor is in the business of evaluating plans and specifications, not standard form subcontracts. Part of that is admittedly due to the fact that standard subcontracts are typically prepared by attorneys for the general contractor. While the general contractor's attorneys understand 'what' terms were used and 'why' they were written the way they were, it is understandable that the typical subcontractor who does not have a legal education will not fully understand what risks it is assuming with the proposed subcontract. Similarly, it is difficult for a subcontractor to know 'what' changes it can and should request be made to the subcontract. As a consequence, we are often retained to assist the subcontractor to review the standard form subcontract and recommend appropriate changes.

With rare exceptions, we are generally successful in negotiating proposed changes. This is because our approach is to propose changes which do nothing more than fairly allocate rights and obligations. Regardless of which attorney you use to assist you in doing this, or if you attempt doing this yourself, we recommend you follow this approach.

Surprisingly, what changes a subcontractor should request is not dependent on the work at issue. That is because all subcontracts should include a fair allocation of specific rights and obligations. While exactly what changes should

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be requested and how they should be written will vary according to the proposed standard form subcontract used, I can offer you some specific examples of subcontract language which should be changed and how to do it.

Specific Examples of Appropriate Subcontract Changes

A subcontractor sometimes wrongfully assumes that if the general contractor decides to use the subcontractor, the subcontractor's bid necessarily becomes part of the subcontract. That is not correct.

As a matter of black letter contract law, unless the bid is expressly incorporated into the subcontract, it is not part of the subcontract. So, if the subcontractor maintains that all or portions of its bid should be incorporated into the subcontract, the bid (or any portions thereof) should be made an exhibit to the subcontract. It should be expressly stated in the subcontract that it is part of the subcontract.

A critical example of a utility subcontractor's terms which should be made part of the subcontract include the assumed subgrade conditions on which the bid is based, and the right to additional compensation if actual subgrade conditions are different.

Some other examples of standard changes which should be made include the following:

- Standard subcontracts often provide that if the subcontractor delays the general contractor, the subcontractor owes the general contractor payment for the related extra costs, but if the general contractor delays the subcontractor, the general only owes the subcontractor a time extension. This should be changed so both parties have the same payment obligation if they delay the other.
- Standard subcontracts typically provide that the subcontractor shall perform its work as scheduled by the general contractor. This should be changed to provide subcontractor input on the durations of its work as well as the number of mobilizations required.
- Standard subcontracts often require the subcontractor to indemnify the general contractor for extra costs incurred even if it is caused in whole or part by the general contractor's negligence or breach of contract. This should be re-written to limit the subcontractor's indemnity to extend only to the extent of the subcontractor's negligence or breach of contract.
- Standard subcontracts typically provide that the general contractor is only required to pay the subcontractor 'when' or 'if' paid by the owner. The problem with that conditional payment obligation is that the general contractor may not be paid by the owner because the general contractor breached a substantive and/or procedural aspect of the contract.

For example, if the subcontractor was delayed by the general contractor's improper conduct, the owner is not going to pay the general contractor for that delay (and hence the subcontractor would not get paid). Similarly, if the general contractor failed to pass on a subcontractor's notice of a differing site conditions claim when contractually required, the subcontractor is not going to get paid. To protect against this, the pay when/if clause must be changed to provide that if the general contractor causes the owner's non-payment through its breach of contract, the general contractor remains contractually obligated to pay the subcontractor notwithstanding non-payment from the owner.

Conclusion

If given the opportunity, general contractors are going to continue insisting that subcontractors sign subcontracts that are unfairly written in favor of the general contractor.

The good news is that subcontractors can and should be able to successfully negotiate standard subcontracts to fairly allocate rights and obligations. Ideally, once the subcontractor has successfully negotiated changes to the standard subcontract, that can and should be the template for future projects. There should be no reason to re-negotiate the subcontract again.

This article is not intended to be legal advice and does not form an attorney-client relationship. Please consult with an attorney for applicability to your specific situation. ■



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