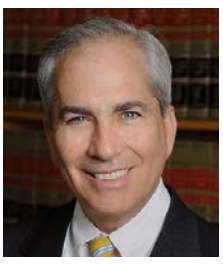
STA LEGAL LOG – DANGERS IN SUBCONTRACT FORMATION



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Your subcontract is your "bible." A subcontractor will "live or die" by what is contained, or perhaps not contained, within any particular subcontract or purchase order.

There are many pitfalls to which subcontractors must be aware during subcontract formation. While a subcontractor may just want to "get to work, " it is imperative that during subcontract formation that a subcontractor "step back" and take particular care to ensure that all of the terms and conditions upon which its bid was based are properly included. Unfortunately, if all of the requisite terms and conditions are not included in the subcontract during the critical formation stage, there are numerous legal principles, some of which are discussed below, which could ultimately bar you from later amending the terms of the subcontract, even if indisputably "agreed-upon" terms were omitted.

It is regrettable, but experience has taught us that too few subcontractors carefully review the subcontracts submitted to them for review after negotiations. No matter how laborious, it is imperative that a subcontractor carefully read through all of a general contractor's proposed subcontract prior to signing to ensure that all negotiated terms and conditions are included. Furthermore, upon receiving a fully-executed subcontract back from the general contractor, we recommend that subcontractors carefully read through the subcontract again to ensure that the fully-executed subcontract still fully embodies the actual agreement between the parties. If the counter-signed version does not, the subcontractor must immediately bring this fact to the attention of the general contractor.

For example, during the bidding and estimating process, scope sheets are often exchanged between the parties during the "bid leveling" process. A subcontractor may (and often should) seek to have specific exclusions included in its bid checklist as to work that it considers outside the scope of its work. There may be a great deal of back-and-forth negotiation between the estimators of the subcontractor and those of the general contractor and the chance of an error is significant. Diligence at this stage will pay dividends in preserving your as bid profit.

However, during the subcontract formation process, there may also be other "cooks in the kitchen. " A project manager may become involved in the subcontract negotiation, and/or an in-house counsel. It is imperative that during the subcontract formation process that all of the individuals involved remain on the same page as to what items should be, and, sometimes more importantly, should not be, included in the subcontract. A subcontract often has several exhibits attached, including the aforementioned bid checklist, which will ultimately dictate what will be considered base subcontract work.

Moreover, while an estimator, project manager, and/or in-house counsel may be involved in the subcontract negotiation, the proposed subcontract will then very likely go to yet another individual with ultimate authority, be it the president, CEO, owner, etc., who will then finally execute the subcontract. However, this individual may know little about the details of what should, or should not, be included in the subcontract. As such, it must be standard operating procedure that the individuals with the requisite knowledge thoroughly "cross-check. "

There are at least two legal theories under which a subcontractor may later find itself bound to terms to which it did not agree if such discrepancies are not caught, and promptly addressed, during subcontract formation.

The first is based upon a contract's "merger" clause. Merger clauses are found in almost all contracts, and provide that the contract embodies the "final and complete" understanding and agreement between the parties and supersedes all prior understandings or agreements between the parties relating to the subject matter of the contract. In other words, the subcontractor would not be able to vary the terms of the written and signed subcontract with, for example, a prior exchange of emails between the parties in which the contractor agreed that certain exclusions would be carved out from the scope of work, if said exclusions did not make it into the bid checklist that ultimately became part of the subcontract.

The second is based upon the "parol evidence" rule, pursuant to which a subcontractor would be barred from presenting evidence in a later litigation of any "oral" or "implied" agreement that contradicts the actual written subcontract between the parties.

G&C Commentary

"The devil is in the details"... and, so is the profit. By taking extra caution during subcontract formation to ensure that the final, executed subcontract embodies all of the terms and conditions, and exclusions, to which the parties agreed during their negotiations, subcontractors can seek to avoid costly conflicts during the course of, or upon completion of, their project. In order to "get what you bargained for, " a subcontractor must be proactive and vigilant during subcontract formation, or pay the consequences later.

Tara D. McDevitt, an associate with Goldberg & Connolly, assisted with the preparation of this article.