

Chapter 26

CONTRACT CLAUSES MANAGING, ALLOCATING, AND TRANSFERRING CONSTRUCTION PROJECT RISKS

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SYNOPSIS

§ 26.1 INTRODUCTION

§ 26.1.1—Overview

§ 26.1.2—Types Of Risks To Which Parties To A Construction Contract Can Be
Exposed, And Which Risks Can Be Managed, Allocated, And Transferred

§ 26.1.3—The “Means” Of Parties Managing, Allocating, And Transferring
Construction Project Risks

§ 26.1.4—Methods Of Management, Allocation, And Transfer Of Construction Project
Risks By Contract

§ 26.1.5—The Meaningful Considerations About Risk Transfer Clauses

§ 26.2 PROCEDURAL CLAUSES FOR MANAGEMENT, ALLOCATION, AND TRANSFER OF RISKS

§ 26.2.1—Overview

§ 26.2.2—Choice Of Law Clauses

§ 26.2.3—Forum Selection Clauses

§ 26.2.4—Notice Of Claim Clauses

§ 26.2.5—Contractual Statutes Of Limitation

§ 26.2.6—Clauses Defining Commencement Of Statute Of Limitations

§ 26.2.7—Mediation Clauses

§ 26.2.8—Arbitration Clauses

- § 26.2.9—Waiver Of Trial By Jury
- § 26.2.10—No Discovery Clauses
- § 26.2.11—Change Order Requirements
- § 26.2.12—Warranties
- § 26.2.13—Summary Of Procedural Clauses

§ 26.3 DAMAGE LIMITATION CLAUSES

- § 26.3.1—Overview
- § 26.3.2—Limitations On Types Of Damages For Which A Party Can Be Liable
- § 26.3.3—Limitations On Recovery Of Incidental And Consequential Damages
- § 26.3.4—Liquidated Damages Clause
- § 26.3.5—No Liability For Punitive Damages
- § 26.3.6—No Damages Recoverable For Delay
- § 26.3.7—Release Of Claims
- § 26.3.8—Limitations On Total Amount Of Damages For Which A Party Can Be Held Liable
- § 26.3.9—Liability For Attorney Fees And Costs
- § 26.3.10—Exculpatory Clauses: No Liability For Negligence
- § 26.3.11—Indemnity Clauses — Generally
- § 26.3.12—Indemnification For Losses From One's Own Negligence And Acts
- § 26.3.13—Waiver Of Mechanics' Lien Rights
- § 26.3.14—Pro Rata Liability Clause
- § 26.3.15—Disclaimer Of Remedies And Warranties
- § 26.3.16—Damages Limited To Insurance
- § 26.3.17—Damages And Delays Due To Weather

§ 26.4 CLAUSES ALLOCATING THE COST OF COVERING RISKS

- § 26.4.1—Insurance Coverage
- § 26.4.2—Site Investigation
- § 26.4.3—Performance Bonds
- § 26.4.4—Bid Bonds

§ 26.5 SHOULD YOU INCLUDE RISK MANAGEMENT, ALLOCATION, AND TRANSFER CLAUSES IN THE CONTRACT?

- § 26.5.1—Overview
- § 26.5.2—Are The Clauses Generally Valid And Enforceable?
- § 26.5.3—Even If The Clauses Are Valid And Enforceable, Do You Want To Use The Clauses?

§ 26.6 CONCLUSION

§ 26.7 BIBLIOGRAPHY

§ 26.1 • INTRODUCTION

§ 26.1.1—Overview

Every construction project carries with it numerous risks to the parties involved. This chapter deals with the types of contract clauses that might be used by the parties to manage, allocate, and transfer the risks among the parties to the contract.

Most people's initial reaction to management, allocation, and transfer of risks is, "let's transfer every risk I have." However, upon more considered deliberation, most people in the construction industry recognize that the proper allocation of risk defines the role of each party to the construction project and determines the ability of each party to bear these risks. Equally important, in particular circumstances such clauses may not be enforceable. Hence, the most important section of this Chapter may be § 26.5.

Throughout this Chapter, the authors provide examples of types of common risk allocation and transfer clauses found in construction contracts. Please note, however, that these sample clauses are not drafted for insertion into specific contracts. Rather, they are drafted to provide basic ideas as to the types of clauses that can be considered. These types of clauses must be drafted to meet the facts and circumstances of the particular project and contract, and only after fully considering the validity and desirability of the clauses. Note should also be made that the UCC generally applies to only construction contracts that involve the sale of goods, not all construction contracts.¹

This chapter attempts to provide an overview only of Colorado law, although foreign jurisdiction cases are sometimes cited as examples. No attempt has been made to cover all Colorado case law, and clauses should be carefully researched before used. It should be noted that the attitude of the courts toward the validity/enforceability of risk management clauses varies dramatically from state to state.

§ 26.1.2—Types Of Risks To Which Parties To A Construction Contract Can Be Exposed, And Which Risks Can Be Managed, Allocated, And Transferred

As indicated above, there are numerous risks inherent in a construction project. However, these risks are not shared equally by all parties involved in the project. Thus, the question becomes what risks *should be* the risks of which parties. For example, being unable to obtain financing for a project normally is a risk for the owner/developer. Should financing ever be a risk of the subcontractor, and if so, under what circumstances?

This chapter is about the management, allocation, and transfer of construction project risks through contract clauses. Of course, many risks have been managed and allocated by the legislature. For example, the contractor, subcontractor, supplier, and laborer have always had a risk of not being paid, but the legislature has minimized and shifted much of that risk to the owner, by providing for mechanics' liens.² However, can the owner limit his or her liability to the contractor for not paying its subcontractors and override the legislative grant of mechanics' liens?³

Examples of Risks on a Construction Project

The following is a partial list of the common risks incurred by the primary parties to a construction project. Please note that this list is only partial and some of the risks may be common to multiple parties.

• Owner risks

- 1) Inability to obtain financing;
- 2) Default of the financier;
- 3) Unforeseen conditions;
- 4) Defective design;
- 5) Defective construction;
- 6) Delayed construction;
- 7) Cost overrun;
- 8) Destruction of project by the elements (fire, wind, flood, etc.);
- 9) Construction site injuries to construction personnel and third parties;
- 10) Nonpayment of subcontractors and suppliers resulting in mechanics' liens;
- 11) Misappropriation of contract funds by contractor or subcontractors;
- 12) Insolvency of contractor's surety.

• Architect risks

- 1) Misunderstanding owner's intent for the project;
- 2) Defective design;
- 3) Underestimating cost;
- 4) Negligent inspection/observation;
- 5) Unforeseen conditions;
- 6) Nonpayment.

• Prime contractor risks

- 1) Underestimating costs (fixed price contract);
- 2) Defective construction;
- 3) Nonperformance by its subcontractors and suppliers;
- 4) Unforeseen conditions;
- 5) Destruction of project during construction;
- 6) Insufficient/defective plans and specifications;
- 7) Performance being delayed: by owner's notice to proceed, by architect's plans, by material from suppliers, and by owner deficiencies, obstacles, and problems;
- 8) Nonpayment;
- 9) Strikes or labor shortages;
- 10) Injuries to construction personnel and to third parties;
- 11) Materials shortages;
- 12) Unusually adverse weather;
- 13) Performance specifications.

- **Subcontractor risks**

- 1) Defective plans and specifications;
- 2) Late receipt of plans and specifications, materials, equipment;
- 3) Interference;
- 4) Lack of access;
- 5) Defective performance;
- 6) Nonpayment;
- 7) Strikes.

- **Supplier risks**

- 1) Incorrect specifications;
- 2) Nonpayment;
- 3) Late delivery;
- 4) Defective goods.

§ 26.1.3—The “Means” Of Parties Managing, Allocating, And Transferring Construction Project Risks

Most construction project risks can be managed by contractual provisions. The risks can be imposed upon one party, or distributed among all parties. Certain allocations of risk may not be desirable, however, because the burden of a risk may be placed upon a party that may not have the ability to control or manage the risk. Furthermore, some parties may not have the financial capability to cover certain risks if the risk is realized. The rights and obligations of parties to a construction contract include the assumption and acceptance of risks. Generally, the rights and obligations (including risk assumption and transfer) between the parties to a construction contract are defined and governed by three sources: (1) the contract; (2) the law; and (3) the custom of the industry.

Risk Management, Allocation, and Transfer Under the Contract

The agreement of the parties, written or oral (unless the statute of frauds applies), express or implied, often defines a significant amount, if not all, of the risks and obligations of the two contracting parties. Furthermore, the rights and obligations of the parties may be affected by provisions in a contract between one of the parties and a third party. For example, a subcontract may incorporate the contract between the owner and the prime contractor, or even the contract between the owner and the architect.⁴ Thus, the terms of the owner/prime contract may become terms of the subcontract and create additional rights and obligations between the prime contractor and the subcontractor. Alternatively, the contract between the owner and prime contractor, even if not incorporated into the subcontract, may contain provisions that define the prime contractor’s duties in ways that inure to the benefit (or detriment) of the subcontractor. Examples of these provisions include the duties to coordinate subcontractors, establish schedules, and maintain safe working conditions.

Because all these sources potentially impose contract obligations, and because liability may attach to breaches of these obligations, parties may wish to use the one source over which they have full control — their contracts — to manage, allocate, and transfer the kinds and degrees of risk that they undertake in entering into an agreement. Therefore, this chapter mainly explores

the use of contract clauses to both manage the risk assumed by a party as well as to exculpate — to free a party from liability or responsibility or to transfer liability or responsibility.

Risk Management, Allocation, and Transfer Under the Law

Of course, the law is incorporated into every contract, and, indeed, into every relationship. In the absence of agreement, and sometimes in spite of agreement, the law governs. The law includes applicable federal, state, and local statutes, ordinances and regulations, as well as the common law.

For example, suppose the architect under the contract with the owner provides drawings that have defects. The owner provides these defective drawings to its contractor. The contract between the owner and the contractor is silent on the issue of defective drawings. The contractor suffers the risk of defective drawings and incurs the increased costs due to the defects. The law shifts that loss from the contractor to the owner by means of the “owner’s implied warranty of the accuracy of the plans and specifications.”⁵ The law in turn allows the owner to shift the risk to the architect: recovery of damages for breach of contract. But, this shifting does not enable the owner to escape liability to the contractor; it only enables the owner to have its loss reimbursed.

Furthermore, even if the contract expressly allocates a certain risk, no party should rely totally upon any contract clause to avoid liability for every situation, because that clause might be perceived by the law as unfair or unreasonable. Then again, in some instances, a contract clause may validly supersede the law in defining the rights and responsibilities of parties, and may serve as an effective tool to consciously manage risk.

Thus, the issues involved in drafting construction contracts are numerous. Should those risk transfers imposed by law be altered? Should the contractor’s risk not be transferred to the owner? Should the contractor’s risk be shifted directly to the architect? Should the owner not have a right to transfer the loss from the architect’s negligence to the architect? Usually, the law reflects what most people believe is the proper allocation and transfer of risks, but in other circumstances the law does not reflect the needs and abilities of specific parties. The means then becomes contractual management, allocation, and transfer of risk clauses.

This Chapter explains how and why such clauses are useful in managing risk through examples of these clauses followed by a discussion of their enforceability. In regard to enforceability, the discussion focuses upon enforceability issues endemic to each specific type of clause. Although generic contract defenses are only briefly mentioned at the end of this Chapter, it should be noted that risk management clauses, like any other contract clause, can be invalidated if they are the product of mistake or of prohibited behavior such as fraud, duress, undue influence, adhesion, and similar doctrines.

§ 26.1.4—Methods Of Management, Allocation, And Transfer Of Construction Project Risks By Contract

The most common, and usually most effective, method of management, allocation, and transfer of construction risks is by the contract terms between the parties. For example:

- There is a risk that the building being built will fall down during construction, whether by reason of unusual wind, fire, sabotage, or negligent construction.
- The risk of the building collapsing during construction, for whatever reason, is placed on the contractor.
- To provide financial strength to the contractor's undertaking of this risk, the contractor must (a) provide a performance bond or (b) obtain insurance that covers the risk.

Theoretically, this transfer of the risk to the contractor (which, for the most part, already resides with the contractor under law) costs nothing: the contractor includes in its bid the cost of insurance or a bond, and the owner omits from its budget those costs.

Thus, early questions in managing project risks include:

- Who ought to bear the risk, and why?
- Who can most economically bear the risk, and how?
- What impacts, if any, does transfer of risks have? Does it affect control?

§ 26.1.5—The Meaningful Considerations About Risk Transfer Clauses

It is easy to draft risk management allocation and transfer clauses; the real questions are:

(1) Are they valid? (2) Will they be enforced? and, if so, (3) Do you in fact want to use them?⁶

§ 26.2 • PROCEDURAL CLAUSES FOR MANAGEMENT, ALLOCATION, AND TRANSFER OF RISKS

§ 26.2.1—Overview

The first category of contract provisions that can be used to manage, allocate, and transfer risks of one party to the construction process is procedural clauses. Procedural clauses are those contract provisions that define the methods and procedures that must be followed should particular situations or problems arise. Although these clauses may seem innocuous, they can dramatically affect the management, allocation, and transfer of risks among the parties on a construction project.

Again the reader must be cautioned: some of these clauses may not be enforced by the court in particular circumstances.

§ 26.2.2—Choice Of Law Clauses

Example: This Agreement shall be governed, interpreted and enforced in accordance with the laws of the State of Colorado.

Obviously, the laws of the several states differ. Thus, the laws of one state may be more favorable to one party regarding the distribution of risks. Hence, in a multi-state transaction, the rights and responsibilities of the parties may differ depending upon which state's law is applied to the transaction.

A simple example is the states' differing attitudes towards contractual risk management, allocation, and transfer clauses. Some states are very liberal in enforcing them, while others are very conservative and construe them narrowly. Of course, some states even refuse to enforce certain clauses that other states honor. Thus, the choice of law clause may be the most important risk management and allocation clause in the construction contract.

In general, if the parties make no provision, the applicable law will be chosen for them by the court in accordance with the forum state's often subjective choice-of-law rules.⁷ Instead of letting the court decide which state's law will apply, the parties can enhance the predictability of their relationship by choosing which state's substantive law will govern their relationship and define their risks.

For example, if a contractor and subcontractor are both located in Colorado, but the project is located in Wyoming, they may prefer to have their rights and duties defined by more familiar Colorado law. As an alternative, the parties could also choose to have different issues in their contract governed by different laws.⁸

Enforceability

Generally, choice of law provisions are held binding and enforceable.⁹ The key limitation is that the chosen state must bear a reasonably close relationship to either the parties or the transaction.¹⁰ Courts consider a number of factors in discerning whether the requisite relationship exists, including the parties' principal place of business, place of incorporation, location of the contracted property, place of execution, place of performance, place of payment, and purpose of the contract.¹¹

However, choice of law clauses cannot be utilized to frustrate the forum's public policy as to remedies.¹² Under Colorado law, the forum state should apply the law chosen by the parties unless (a) there is no reasonable basis for the parties' choice, or (b) the application of the law chosen would be contrary to a fundamental policy of a state that has a materially greater interest in the issue.¹³

Similarly, choice of law clauses may be deemed to apply only to substantive law and not to procedural law. In some circumstances, it is an ambiguous line. Consider, for example, notice requirements and statutes of limitation.

§ 26.2.3—Forum Selection Clauses

Example: The parties hereby agree that any dispute between them will be resolved, if legally possible, in a state court located within the City and County of Denver, State of Colorado.

Example: In the event that any dispute shall arise with regard to any provision or provisions of this Agreement, jurisdiction shall be solely in the State of Colorado, and venue shall lie solely in the County of El Paso, Colorado.

One of the risks of a construction project is the high cost of litigating a dispute because of the inconveniences of the forum. In addition to choosing the applicable substantive law, parties may select the particular forum for litigating or arbitrating disputes. For example, a project may be located in Arapahoe County, but if the parties are based in Denver County, they might prefer that all disputes be decided by a court located in Denver. Assuming federal jurisdictional requirements are met, parties may even select between a federal or state court located in Denver.¹⁴

More commonly, a forum selection clause is used when a party who is participating in an out-of-state project desires that any controversy that arises be litigated in its home state. Similarly, an owner who is subject to jurisdiction of various states might want all controversies regarding the project to be resolved in the state where the project is located.

Enforceability

Colorado courts have generally found reasonable forum selection clauses binding and enforceable.¹⁵

§ 26.2.4—Notice Of Claim Clauses

Example: The Owner shall not be liable to the Contractor for damages caused by delay for any reason whatsoever, unless the Contractor gives notice of the delay to the Owner within five business days after the cause of the delay occurs.

Example: The Contractor shall not be entitled to an extension of time or to additional compensation or damages, unless the Contractor submits a written request to the Owner within seventy-two (72) hours after the event giving rise to the request. The request shall set forth all facts upon which the request is based, together with all supporting documents.

Example: Any claim by the parties that arises out of or in connection with this Agreement shall be barred, unless a notice thereof is given to the other party within thirty days after the date of the act or omission that gave rise to such claim.

The essence of a notice clause is that notice of some act or intended action is a condition precedent to enforcing a right under the contract. A common use of such provision is in insurance policies that require timely notice to the insurer of claims by or against the insured. If timely notice is not given, courts have held that coverage may be lost.¹⁶

There are multiple potential benefits and reasons for notice clauses. First of all, they provide the party who will be liable an opportunity to investigate the facts while the facts are fresh. Prompt investigation of the facts surrounding a potential claim often gives the parties a clearer

understanding of their respective position and can aid settlement. Notice clauses also require the claimant to promptly decide whether to assert or not assert a claim. Thus, since the progress of a job largely depends upon everyone knowing where everyone else stands, notice of claims requirements provides the parties with a realistic assessment of the status of a project at any given point in time. In other words, the parties know right away if there are problems on a project and what those problems are.

Note that many Colorado construction statutes contain specific notice provisions. See Chapter 24, “Procedural Aspects of Construction Litigation,” for details.

Enforceability

Generally, most notice provisions are valid, so long as the time frame for timely notice is reasonable.¹⁷

§ 26.2.5—Contractual Statutes Of Limitation

Example: Any claim arising out of or in connection with this Agreement shall be asserted by a complaint in a civil action commenced within eight months after the claim arose, and, if not, shall thereafter be barred.

All states have statutory time limits within which a party may be sued by another party. The statute of limitations in Colorado for most construction claims is two years, with the statute of repose usually six years.¹⁸ Sometimes, however, the parties desire to shorten that period of time in order to insure that they are safe from the threat of litigation sooner than provided by state law. A construction project, and the claims that arise therein, must eventually come to an end. Thus, unless the party does not know of the claim, there is little benefit to permitting a party to delay asserting a claim.¹⁹

Enforceability

The courts generally enforce such contractual statutes of limitation even though the statutory period of limitation or period of repose may be substantially longer — so long as reasonable.²⁰

§ 26.2.6—Clauses Defining Commencement Of Statute Of Limitations

Example: The applicable statute of limitations shall commence to run upon issuance of a certificate of occupancy and shall not be tolled by any ongoing activities or assurances by the Contractor with respect to the punch list or warranty work.

C.R.S. § 13-80-108 defines the commencement date for most statutes of limitation to begin running. Stated very generally, the applicable statutes of limitation begin to run after the injury is known or reasonably ought to be known. However, the “construction” statute of limitations begins to run when the claimant or its predecessor discovers or in the exercise of reasonable diligence should have discovered the physical manifestation of a defect in the improvement which

ultimately causes the injury.²¹ However, there appears to be no prohibition upon a contractual provision making the statute begin to run either earlier or later than the statute provides. In *Regents of the University of Colorado v. Harbert Construction Co.*,²² the warranty section stated:

The warranty period provided in Section 18.2 shall begin upon Acceptance or the date that care, custody and control of a portion of the WORK is transferred to the OWNER . . . and shall end twelve (12) months later ²³

The court enforced the clause, rejecting that the warranty, as written, deprived the plaintiffs of the substantial value of the contract in violation of the essential purpose doctrine under C.R.S. § 4-2-719(2) (UCC). The court held that “the warranty provision did not provide an adequate remedy to plaintiffs during the warranty period; it merely limited the duration of the contractor’s liability.”²⁴

§ 26.2.7—Mediation Clauses

Example: If a dispute arises out of or relates to this contract, or the breach thereof, and if the dispute cannot be settled through negotiation, the parties agree first to try in good faith to settle the dispute by mediation administered by the American Arbitration Association under its commercial mediation rules before resorting to arbitration, litigation, or other dispute resolution procedures.

Mediation is a process whereby the parties, with the assistance of a neutral third party, negotiate a resolution to their differences. In many instances, mediation can be extremely effective in resolving contract disputes, thus avoiding the time, energy, and cost of arbitration or litigation. However, a mediation clause may also pressure one party to compromise and ultimately accept less than litigation would have awarded.

Enforceability

Even when parties assert that they refuse to settle, courts have recognized that, in fact, settlements and compromises are often obtained through mediation, notwithstanding the parties’ predisposition. Thus, although mediation, unlike arbitration, concludes a dispute only through agreement of the parties, courts generally enforce a mandatory mediation clause.

The issue of a contractual obligation to mediate as a condition precedent to arbitration or a civil action does not appear to have been considered in Colorado. However, the concept is recognized by the legislature in a different context.²⁵

§ 26.2.8—Arbitration Clauses

Example: Any controversy or claim arising out of or relating to this contract, or the breach thereof, shall be settled by arbitration administered by the American Arbitration Association under its construction arbitration rules, and judgment on the award rendered by the arbitrator may be entered in any court having jurisdiction thereof.

Like mediation, arbitration is a process where the parties to a dispute refer the dispute to an impartial third party. Unlike mediation, however, arbitration usually encompasses limited discovery and a hearing. The parties usually agree to abide by the arbitrator's decision. Accordingly, an arbitration clause may manage risks and substantially affect the allocation and transfer/elimination of risks.

A related consideration is whether parties desire arbitration in lieu of litigation to resolve disputes. See Chapter 21, "Arbitration and Mediation of Construction Disputes," for a discussion of the pros and cons of arbitration. For example, under Colorado law an arbitrator cannot award punitive damages.²⁶ This may eliminate the risk to the parties of suffering punitive damage awards. On the other hand, this may simply mean a separate judicial proceeding must be held as to punitive damages.²⁷ In *Mastrobuono v. Shearson Lehman Hutton Inc.*,²⁸ the U.S. Supreme Court held that punitive damages in arbitration are not precluded by a general choice of law clause, at least when the Federal Arbitration Act applies.

Does arbitration change the ultimate bearer of the risk? Is the amount of liability of a defendant less in arbitration than in a court or jury trial? Is the likelihood of a defendant even being found liable greater or lesser in an arbitration proceeding than in court trials? Many believe the answer to these questions is yes. If so, an arbitration clause is a substantial tool in the management, allocation, and transfer of risks.

Enforceability

Enforceability of an arbitration clause is determined under C.R.S. §§ 13-22-201, *et seq.* (Colorado Uniform Arbitration Act) or 9 U.S.C. §§ 1, *et seq.* (Federal Arbitration Act). Generally, all arbitration agreements are valid, but *see, e.g.*, arbitration of statutorily created rights, particularly employment rights.²⁹

§ 26.2.9—Waiver Of Trial By Jury

Example: Each of the parties hereto waives any right to a jury trial with respect to any controversy between the parties.

Example: In the event a dispute arises out of or in connection with this Agreement, the parties agree that it shall be tried to a judge without a jury, and expressly waive any right to a trial by jury.

Example: Each party to this Agreement hereby expressly waives any right to trial by jury of any claim, demand, action, or cause of action (1) arising under this Agreement or any other instrument, document, or agreement executed or delivered in connection herewith, or (2) in any way connected with or incidental to the dealings of the parties hereto or any of them with respect to this Agreement or any other instrument, document, or agreement executed or delivered in connection herewith, or the transaction related hereto or thereto, in each case whether now existing or hereafter arising or whether sounding in contract or tort or otherwise; then each

party hereby agrees and consents that any such claim, demand, action, or cause of action shall be decided by court trial without a jury, and that any party to this Agreement may file an original counterpart or copy of this section with any court as written evidence of the consent of the parties hereto to the waiver of their right to trial by jury.

Are liabilities and damages affected by whether a judge or a jury determines them? Many would say yes.

Enforceability

Most jurisdictions uphold the validity of a jury waiver clause as to most claims, as long as the waiver is done knowingly and intentionally.³⁰

§ 26.2.10—No Discovery Clauses

Example: In the event of litigation between the parties, the parties agree that there shall be no discovery of any nature, whether written or oral.

One party can usually benefit by the other party's not having a right of discovery. Many believe that discovery, or the lack thereof, can substantially affect the outcome of litigation. On the other hand, eliminating discovery can also substantially reduce the cost of litigation.

Enforceability

Enforceability of no discovery clauses was discussed in *Developments in the Law—Discovery*:³¹

A court may refuse to enforce a contract limiting discovery if it is unconscionable. This would depend on the inequality of the parties' bargaining power, the scope of the restriction imposed, and the stage in the parties' relationship in which the agreement is made. Thus if it is made after the cause of action accrues, both parties will presumably be aware of the issues to be proved and the facts that must be uncovered. Such an agreement is therefore more likely to be upheld than one made, for example, at the beginning of a course of business dealings, before the parties have any idea of their respective obligations of proof in a lawsuit not yet materialized. . . . For the same reasons, a limitation of discovery in a contract for a single business transaction is much more likely to deal with foreseeable and specific problems of disclosure than is a contract made with a view to a long period of business dealings.³²

§ 26.2.11—Change Order Requirements

Example: No alteration, change, addition, or deviation shall be made from that shown or described in the contract documents, except upon the execution by both parties of a written change order.

Many states have adopted statutes requiring that contracts involving certain subjects, *e.g.*, sale of real estate,³³ must be in writing and signed to be enforceable. They are generally referred to as statutes of fraud, being perceived as avoiding the potential for fraud considered to be inherent in oral contracts. However, no such statutes exist for most aspects of construction agreements.

Enforceability

Contract provisions that require a change order to be in writing are generally enforceable.³⁴ Courts will, however, consider whether there has been an express or implied waiver of the contract provision.³⁵

The enforceability in Colorado generally of oral amendments to contracts is defined by CJI-Civ. 30:6 (CLE ed. 2005): “(An oral) (or) (A written) contract may be (changed) (or) (amended) (or) (canceled) by (oral) (or) (written) agreement with the consent of all parties to the contract.” Of course, consent need not be explicit, but rather inferred from the conduct of the parties.

§ 26.2.12—Warranties

Example: All materials and equipment furnished under the contract will be of good quality and new unless otherwise required or permitted by the Contract Documents. All work will be performed in accordance with the Contract Documents and in accordance with generally accepted engineering and construction principles and practices.

Normally, warranties are thought of as something extra given or received. The owner views the contractor's warranty as something the Owner would not otherwise have.

Usually, this is not the case. Usually, the warranty claims take away rights and remedies by a provision to the effect that “This warranty is in lieu of all other claims, rights, and remedies provided by law.” Thus, when properly drafted and enforced, the receiver of the warranty loses all breach of contract, breach of implied warranties, and negligence claims. In addition, sometimes a contractual statute of limitations clause is inserted that is shorter than the statutory period, and commences to run earlier than do statutory statutes of limitation.³⁶

Enforceability

Warranty clauses are particularly disfavored when inserted into contracts for new residential construction.³⁷ When a homebuilder attempts to limit its implied warranty of habitability, Colorado courts require that the clause be unambiguous, and any ambiguity is strictly construed against the homebuilder.³⁸ In commercial construction contracts, a limiting warranty is enforceable if it clearly expresses the intent of the parties.³⁹

§ 26.2.13—Summary Of Procedural Clauses

Procedural clauses, when properly drafted for the particular circumstances, can have a substantial impact upon the management, allocation, and transfer of risks for the parties to an agreement. However, whether such clauses will be enforced, and whether such clauses should be

used in a construction contract are questions that require more careful consideration, and case law must be considered in terms of the specific fact circumstances.⁴⁰

§ 26.3 • DAMAGE LIMITATION CLAUSES

§ 26.3.1—Overview

Each party is interested in limiting the liability that it might have to another party. However, damage limitation clauses can also serve the useful function of circumscribing the scope of a party's liability and of providing more certainty regarding the outer boundaries of a party's potential monetary risk.

Agreements exculpating a liable party in whole or in part are generally disfavored by the courts and closely scrutinized.⁴¹ They are strictly construed against the drafter because of their one-sidedness.⁴² In *Lahey v. Covington*,⁴³ the court reaffirmed the elements to be considered in determining whether an exculpatory agreement is valid:

- existence of a duty to the public;
- nature of the services performed;
- whether the contract was fairly entered into; and
- whether the intention of the parties is expressed in clear and unambiguous language.⁴⁴

In *Lahey*, the court noted that the agreement does not need to describe in detail each risk to which the clause might apply.⁴⁵ Similarly, an exculpatory clause need not define the legal theories such as negligence or breach of warranty.⁴⁶ However, the more specific the terminology, the more likely a wording will be interpreted as the drafter intended.⁴⁷

§ 26.3.2—Limitations On Types Of Damages For Which A Party Can Be Liable

One effective method of limiting liability exposure of a party is to place restrictions on the kinds of damages for which the party can be held liable. There are several categories of damages, having varying probabilities of enforceability, which are possible candidates for limitation.

§ 26.3.3—Limitations On Recovery Of Incidental And Consequential Damages

Example: The parties agree that neither party shall be liable to the other for any incidental or consequential damages of whatsoever nature, however caused, whether by the negligence of the party or otherwise.

This type of clause limits liability for incidental or consequential damages. The Uniform Commercial Code (applicable generally to goods) defines incidental damages of an aggrieved seller as “including any commercially reasonable charges, expenses or commissions incurred in stopping delivery, in the transportation, care and custody of goods after the buyer's breach in connection with the return or resale of the goods, or otherwise resulting from the breach.”⁴⁸

The Uniform Commercial Code also defines consequential damages of a buyer as “losses resulting from particular requirements and needs of a buyer, which at the time of contracting the seller had reason to know and could not have been reasonably prevented, and injury proximately caused by breach of warranty.”⁴⁹

An example of incidental or consequential damages is where an owner contracts to have a motel built, but the motel is not finished on time. Incidental/consequential damages could be the money the motel owner loses by his or her inability to rent rooms due to late completion.

Another example of limitation of liability for consequential damages might read:

Example: Neither party to this Agreement shall be liable for any special, indirect, incidental or consequential damages of any nature, including, without limitation, loss of profits, loss by reason of shutdown, and loss of use or interest.

The Engineers Joint Contract Document Committee (EJCDC) consequential damage limitation clause provides:

Owner hereby agrees that to the fullest extent permitted by law, Design Professional shall not be liable to the owner for any special, indirect or consequential damages whatsoever, whether caused by the Design Professional's negligence, errors, omissions, strict liability, breach of contract, breach of warranty or other cause or causes whatsoever, including but not limited to (list here particular types of consequential damages that Design Professional may be concerned about by reason of the nature of the project, e.g., costs of replacement power, loss of use of equipment or facility, loss of profits or revenue, etc.).⁵⁰

Enforceability

Generally, a no consequential damages clause is valid and enforceable in Colorado.⁵¹ However, in *Lutz Farms v. Asgrow Seed Co.*,⁵² the court held an exclusion of consequential damages in a contract selling onion seed to be unconscionable under C.R.S. § 4-2-719(3), and therefore void.⁵³

§ 26.3.4—Liquidated Damages Clause

Example: If either of the parties to this Agreement fails to comply with the terms and conditions of this Agreement or to carry out any provisions of this Agreement by such party to be performed, such party shall pay to the other the sum of \$10,000 as liquidated and agreed damages.

Enforceability

In Colorado, a liquidated damages clause generally is valid and enforceable, if:

- 1) at the time the contract was entered into, the anticipated damages in case of breach were difficult to ascertain;

- 2) the parties mutually intended to liquidate the damages in advance; and
 - 3) the amount of liquidated damages, when viewed as of the time the contract was made, was a reasonable estimate of the potential actual damages the breach would cause.⁵⁴
- The drafter of a liquidated damages clause should take care not to characterize the liquidated damages as a penalty for untimely performance of the contractor, lest the owner run the risk of the clause being deemed void and unenforceable.⁵⁵

§ 26.3.5—No Liability For Punitive Damages

Example: Neither party shall be liable to the other for punitive (exemplary) damages. or The arbitrator shall not have jurisdiction or authority to award punitive (exemplary) damages.

The parties may wish to consider agreeing to limit their respective liabilities for punitive damages. Generally, most states allow punitive damage awards only when the injuries complained of are attended by circumstances of malicious intent or flagrant disregard for the rights of the plaintiff.⁵⁶ In Colorado, punitive damages may only be awarded pursuant to C.R.S. § 13-21-102, which “contemplates tortious conduct,” and thus precludes an award of punitive damages in breach of contract actions.⁵⁷ Punitive conduct includes fraud, malice, or “willful and wanton conduct,” *i.e.*, “purposefully committed which the actor must have realized as dangerous, done heedlessly and recklessly, without regard to consequences, or of the rights and safety of others”⁵⁸

Enforceability

The trial court in *G.E.C. Minerals, Inc. v. Harrison Western Corp.*⁵⁹ enforced a punitive damage exclusion similar to the one above, although in that case the validity of the clause was apparently not challenged.⁶⁰ Colorado’s appellate courts have not specifically defined circumstances under which agreements exempting liability for punitive damages may be valid.⁶¹ The Colorado Supreme Court has opined that, “in no event will [an exculpatory] agreement provide a shield against a claim for willful and wanton negligence.”⁶² However, the court may have been referring to liability, and not to the type of damage. Similarly, “[t]he public policy of Colorado prohibits an insurance carrier from providing insurance coverage for punitive damages.”⁶³

“Unless otherwise provided by law, exemplary damages shall not be awarded in . . . arbitration proceedings, even if the award or decision is enforced or approved in . . . court.”⁶⁴ If the statutory right to avoid such an award is not asserted however, it may be waived.⁶⁵ In addition, if the parties’ choice-of-law provision identifies the law of a state that prohibits arbitral punitive awards, but the parties’ intent regarding punitive damage awards by an arbitrator is not expressly set forth in the contract, the contract may implicitly allow an arbitral award of punitive damages, if the Federal Arbitration Act governs the arbitration.⁶⁶

§ 26.3.6—No Damages Recoverable For Delay

Example: Contractor shall not be liable to Subcontractor for any delay to Subcontractor's performance of its work caused by the act or omission of the Owner or Architect, or by any act beyond the Contractor's control. or If Contractor's performance is delayed by [non-negligent] acts of the Owner or by events beyond the Contractor's control, the Contractor shall be entitled, upon request, to a reasonable extension of time for performance, but shall not be entitled to an increase in compensation or to damages by reason of the delay.

A party may also attempt to avoid liability for specific types of acts, occurrences, or omissions. Perhaps the most common limitation of damage clause in the construction industry is the no damage for delay clause.

Enforceability

In general, the courts are reluctant to automatically enforce no damage for delay clauses although they are generally valid.⁶⁷ C.R.S. § 24-91-103.5(1)(a), relating to public works contracts, provides that a provision releasing or extinguishing the right of a contractor to recover for a delay from a public entity is void as against public policy.⁶⁸ The most successful arguments to avoid the application of the clause appear to be (1) the delay was caused by the active interference (omission) of the owner; (2) the delay was from a cause not contemplated by the parties when entering into the agreement; and (3) the delay is not within the specific wording of the clause.⁶⁹

§ 26.3.7—Release Of Claims

See § 26.3.10, "Exculpatory Clauses."

In *Regents of the University of Colorado v. Harbert Construction Co.*,⁷⁰ the following clause was contained in a construction contract for a project at the University of Colorado.

"Acceptance of the work . . . shall constitute a release by the Owner of all claims against Contractor."⁷¹

The *Regents* contract, which provided for construction of a power cogeneration facility, contained an enforceable release that included the above language. Although warranty claims were specifically exempted from the release, the court of appeals upheld the trial court's conclusion that the provision "released the contractor from liability for claims related to negligence, breach of contract, and strict liability."⁷² In doing so, the court stated that, "[h]ad the parties wished to exclude negligence, breach of contract, and strict liability claims from the scope of the release, they could have easily done so. If a contract clearly expresses the intent of the parties, it must be enforced as written."⁷³ Additionally, claims of latent defects were apparently subsumed within the scope of the release.⁷⁴

In release cases, the relevant inquiry is "whether the intent of the parties was to extinguish liability and whether this intent was clearly and unambiguously expressed."⁷⁵

Although the word “negligence” is not “invariably required” to extinguish liability for negligent acts,⁷⁶ if the release language is too broad, a court may refuse to enforce the clause if the court determines the plaintiff did not understand the risks.⁷⁷

§ 26.3.8—Limitations On Total Amount Of Damages For Which A Party Can Be Held Liable

Example: The parties stipulate and agree that the liability of each party to the other as to claims arising out of or in connection with the subject matter of this contract shall be limited to \$50,000.

The parties may agree to simply place a limitation on the amount of damages for which each can be held liable for the other. For example, if a party enters into a \$100,000 contract, perhaps neither side is willing to be exposed to more than \$50,000 in liability. Such a clause might read:

Example: Except to the extent finally determined to have resulted from Company’s fraudulent behavior or willful misconduct, Company’s maximum liability for any reason, including Company’s own negligence, relating to its services shall be limited to the fees paid to Company for the services or work product giving rise to liability.

An architect may also wish to protect himself or herself from claims from the owner by inserting a clause that places a cap on damages. Such a clause might read:

Example: 12.2.1 Compensation. Neither the architect, the architect’s consultants, nor their agents or employees shall be jointly, severally, or individually liable to the owner in excess of the compensation to be paid pursuant to this agreement or of _____ Dollars (\$_____), whichever is greater; by reason of any act or omission, including breach of contract or negligence not amounting to a willful or intentional wrong.⁷⁸

These clauses are not uniformly upheld, however. For example, in *Lutz Farms v. Asgrow Seed Co.*,⁷⁹ a contract for the sale of onion seed contained the following clause:

LIMITATION OF LIABILITY: The exclusive remedy for loss or damages due to breach of the foregoing warranty or contract or for negligence or other cause shall be limited to return of purchase price of . . . [Seller’s] products and shall not include consequential damages. Claims for defects in . . . [Seller’s] products must be presented to . . . [Seller] as soon as practical and in any event within 30 days after discovery.

The trial court, applying the UCC, held that Asgrow’s attempted limitation of remedies failed of its “essential purpose,” in violation of C.R.S. § 4-2-719(2), and that Asgrow’s attempted exclusion

of consequential damages was “unconscionable,” in violation of C.R.S. § 4-2-719(3). The Tenth Circuit affirmed.⁸⁰ See also § 26.5.2. Note that the UCC is probably not applicable to contracts between owners and design professionals. The UCC applies only to goods, not services.⁸¹

In some situations, a party may desire to make the damage limitation inapplicable if the claim is for indemnity. Thus, if the prime contractor is sued by a third party for acts in fact committed by the subcontractor for which the prime contractor is responsible, the prime contractor may not wish any limitation on the amount it can recover for wrongs in which its liability is premised solely on *respondeat superior*.

Enforceability

In general, a reasonable limitation on the amount of damage recoverable probably will be upheld by the Colorado courts.⁸² However, public policy grounds may invalidate such clauses if the restriction is too severe.⁸³ Colorado courts may invalidate severe clauses because they are either (1) unconscionable or (2) fail of their essential purpose.⁸⁴

§ 26.3.9—Liability For Attorney Fees And Costs

Example: In the event of litigation arising out of or in connection with this Agreement between the parties hereto, the prevailing party shall be entitled to recover reasonable attorney fees and expenses incurred in the prosecution or defense thereof.

Attorney fees clauses that award fees to the prevailing party are universally upheld. What constitutes “prevailing party,” however, is a frequently litigated issue.⁸⁵

§ 26.3.10—Exculpatory Clauses: No Liability For Negligence

Example: The Parties agree that neither party shall be liable to the other in negligence, or in any other legal theory (except for breach of contract and willful, wanton or intentional conduct) for acts or omissions arising out of the subject matter of this contract.

Example: The parties stipulate and agree that each shall be liable to the other by reason of acts or omissions arising out of or in connection with this Agreement solely if the conduct of the party asserted to be liable is willful, wanton or intentional. Neither party shall be liable to the other for its own negligence, breach of contract, or other claim that does not constitute a willful, wanton, or intentional act.

The parties may consider whether the exclusion of simple negligence liability should become a part of their bargained-for exchange.⁸⁶

Enforceability

Exculpatory agreements are disfavored in Colorado. They “stand at the crossroads of two competing principles: freedom of contract and responsibility for damages caused by one’s own negligent acts.”⁸⁷ “An exculpatory agreement, which attempts to insulate a party from liability from his own negligence, must be closely scrutinized, and in no event will such an agreement provide a shield against a claim for willful and wanton negligence.”⁸⁸

Generally, Colorado courts decide the validity of exculpatory agreements based upon the following: (1) whether a duty to the public precludes the release of liability; (2) what the nature of the services performed was; (3) whether the contract was fairly entered into; and (4) whether the language of the contract clearly and unambiguously expresses the intent of the parties.⁸⁹ Unambiguous expression may be evidenced by the following factors: (1) “simple and clear terms free from legal jargon”; (2) the agreement “was not inordinately long and complicated”; (3) the plaintiff’s deposition statement that he or she “understood the release”; and (4) the language “specifically addressed a risk that described the circumstances” of the subject injury.⁹⁰

Generally, disparity in bargaining power will invalidate “exculpatory agreements between employer and employee, and between common carriers or public utilities and members of the public.”⁹¹ Agreements to exculpate public entities from their own negligence in public contracts for “construction, alteration, repair, or maintenance of any building, structure, highway bridge, viaduct, water, sewer, or gas distribution system” are void and unenforceable on public policy grounds.⁹²

In *G.E.C. Minerals, Inc. v. Harrison Western Corp.*,⁹³ defendant Harrison had contracted with the plaintiff G.E.C. to deposit fill into G.E.C.’s open-pit coal mine as part of a reclamation project. An exculpatory clause in the parties’ contract provided that the “defendant would be liable only for compensatory damages in negligence arising from its ‘gross negligence or willful misconduct.’” The plaintiff brought an action for negligence and breach of contract after the fill deposited allegedly caused an underground fire. The jury was instructed it could find defendant liable only if defendant’s actions constituted “willful and reckless negligence.” The jury found the defendant liable, but it reduced plaintiff’s award by finding the plaintiff was also negligent and then applying the comparative negligence statute as instructed by the trial court.

On appeal, the plaintiff argued the comparative negligence statute should not apply when the conduct of the plaintiff constitutes simple negligence and the defendant’s negligence is willful and reckless. The court of appeals upheld the trial court’s application of the comparative negligence statute to compensatory damages. The appellate panel reasoned, “[t]he intent of the parties as expressed by their contract exempts the defendant from liability for compensatory damages for acts of simple negligence; however, defendant is liable for acts of willful or gross negligence. The contract is silent as to the effect of plaintiff’s negligence, if any.”⁹⁴ The panel held that the comparative negligence statute required comparing the fault of each party “irrespective of whether such fault is attributable to simple negligence, gross negligence, or willful and reckless negligence.”⁹⁵

Therefore, parties should keep in mind that the comparative negligence statute could be applied, regardless of the existence of an exculpatory clause, if the negligence of each party is not addressed in the contract.

§ 26.3.11—Indemnity Clauses — Generally

Example: Subcontractor agrees to indemnify and hold Contractor harmless from any loss, damage, or expense arising out of or in connection with [to the extent resulting from] any act or omission of Subcontractor. **or** To the extent permitted by law, Contractor shall indemnify and hold the Owner harmless from and against all losses, claims, and expenses of any nature arising from or in connection with Contractor's performance herein.

Technically, an indemnity clause should relate to the acts of a third party. The law and the contract define the liability of a party, and it serves little purpose for the first party to agree to indemnify the other for that which the first party is already liable.

Enforceability

See § 26.3.10, *supra*.

§ 26.3.12—Indemnification For Losses From One's Own Negligence And Acts

Example: Contractor agrees to indemnify and hold Owner harmless from and against any loss, damage, or injury, including by reason of Owner's own negligent acts and omissions (excluding willful and wanton misconduct) with respect to the Project which is the subject of this Agreement.

The principal issue with an indemnity clause is when a party to the contract seeks to be indemnified for losses suffered by reason of its own acts or negligence, or the acts of or negligence of a third party. Most states have some form of anti-indemnity statutes that void clauses that call for the indemnification of one who causes a loss by his or her own actions, negligent or otherwise. Colorado recently joined the ranks of these states as of July 1, 2007, enacting such a provision specifically for construction agreements. Previously, such clauses were only void in public works contracts under C.R.S. § 13-50.5-102(8).

Under C.R.S. § 13-21-111.5, provisions in construction agreements that require one party to indemnify another for its own negligent acts are rendered void. There are, however, limited exceptions. First, one party may agree to indemnify another for its proportionate share of such damages caused through its conduct. Also, the statute specifically excludes builder's risk insurance and workers' compensation from its reach. Last, the statute permits clauses in construction agreements that require an indemnitor to purchase insurance covering its own actions and naming the indemnitee as an additional insured on the indemnitor's policy, but only to the extent that it provides coverage to the indemnitee for liability due to the acts or omissions of the indemnitor.

Indemnity provisions are extensively discussed in §§ 6.4.3, 8.4.7, 10.2.5, and 11.10.

§ 26.3.13—Waiver Of Mechanics’ Lien Rights

Example: Contractor hereby waives and relinquishes all rights to any mechanics’ lien it may hereafter have.

C.R.S. § 38-22-119 provides that no agreement to waive or not enforce a mechanic’s lien shall be binding except as between the parties to the contract. This impliedly recognizes the right of parties to agree that mechanics’ liens will not be asserted, and the courts have so acknowledged.

Enforceability

The Colorado Supreme Court held that a lien waiver is valid if consideration exists for the release.⁹⁶ If, however, the language of the purported waiver is not clear, all doubt will be resolved against a waiver.

By its terms, C.R.S. § 38-22-119 applies only to the party who signs the waiver. Thus, a general contractor cannot waive the lien rights of a subcontractor. But subcontractors should use caution if the prime contract contains a “flow down” provision, because the subcontractor may unintentionally agree to waive its lien rights.⁹⁷

§ 26.3.14—Pro Rata Liability Clause

Example: In the event a dispute arises out of or in connection with the subject matter of this Agreement, it is agreed that neither party shall be liable for an amount greater than that represented by the degree or percentage of fault or responsibility attributed to such party that produced the claimed injury, death, damage, or loss.

In jurisdictions that do not have a pro rata liability statute, or if the pro rata liability statute might not apply to certain claims, the parties may want to ensure that they will be responsible only for the degree or percentage of fault or responsibility that produced the claimed damage or loss. In such a case, a pro rata liability clause might be utilized.

The above-quoted example is the beginning point only. For the Colorado Pro Rata Liability Statute, see C.R.S. § 13-21-111.5. An alternate provision might read:

Example: The Colorado Pro Rata Liability Statute, C.R.S. § 13-21-111.5, shall be applicable to all claims between the parties hereto (or claims by one of the parties hereto against the other party hereto), regardless of the legal theory of the claim asserted. If literal application of the statute is not functional, the fundamental principles of the statute shall be applied and govern the decision.

Enforceability

Such a clause has not been judicially tested in Colorado. However, because the Colorado pro rata liability concept was adopted by the state legislature, it does not seem that its expansion by contractual agreement presents problems. Most certainly it is “fair” and does not run the risks of traditional defenses.

§ 26.3.15—Disclaimer Of Remedies And Warranties

Example: SELLER/CONTRACTOR MAKES NO EXPRESS OR IMPLIED WARRANTY OF MERCHANTABILITY, FITNESS FOR A PARTICULAR PURPOSE OR OTHERWISE. or ALL OTHER WARRANTIES EXPRESSED OR IMPLIED INCLUDING THE WARRANTY OF MERCHANTABILITY AND THE WARRANTY OF FITNESS FOR A PARTICULAR PURPOSE ARE EXPRESSLY DISCLAIMED.

Usually, such language is in bold face and/or capitalized to comply with requirements for conspicuousness and validity. Sometimes, the parties may attempt to eliminate any common law or statutory remedies, and limit remedies to those defined in the contract:

*Example: The parties' rights, liabilities, responsibilities and remedies with respect to this Agreement, whether in contract, tort, negligence, or otherwise, shall be exclusively those set forth in the Agreement.*⁹⁸

Enforceability

If the UCC (sales) is applicable to the contract, C.R.S. § 4-2-316(2) applies. Thus, Colorado law requires that language purporting to exclude or modify the implied warranty of merchantability must include the word merchantability and, in the case of a writing, be conspicuous.⁹⁹

Colorado also recognizes the strong public policy in favor of the implied warranty of habitability in the sale of a new residence.¹⁰⁰ Thus, purported disclaimers of the implied warranty of habitability are disfavored and will be construed against the builder-vendor.¹⁰¹

§ 26.3.16—Damages Limited To Insurance

*Example: 12.2.1 Insurance. Neither the Architect, the Architect's consultants, nor their agents or employees shall be jointly or individually liable to the Owner in any amount in excess of the currently maintained professional liability insurance coverage carried by the Architect.*¹⁰²

The parties to a construction contract often limit their liability to the maximum amount of their respective insurance coverage.

The parties may also wish to provide for the option to purchase additional amounts of liability insurance prior to the commencement of the work. Such a clause might read:

Example: The liability of Contractor to Owner is limited by the terms hereafter. These limits, however, may be increased by Owner, by payment prior to commencement of work, the sum of \$_____ per \$1000 of increased liability.

Enforceability

Barring clauses that are unenforceable on “fairness” or public policy grounds (*see* §§ 26.5.2, *et seq.*, *infra*), these clauses appear to be readily enforceable.¹⁰³

§ 26.3.17—Damages And Delays Due To Weather

Some construction contracts specifically discuss whether adverse weather conditions will be a basis for a contractor to claim entitlement for additional time and money, and if so, what conditions must be satisfied.¹⁰⁴ Other contracts place all risk of extreme weather conditions on the contractor.¹⁰⁵ Still others specify that a given number of days where adverse weather conditions will affect that contractor’s performance have already been assumed in the contractor’s schedule.

§ 26.4 • CLAUSES ALLOCATING THE COST OF COVERING RISKS

Any party involved in construction projects has the risk of potential loss. The most obvious risk is the fixed price of the contract. Many risks that a party might have under law can potentially be reallocated by the contract. For example, a cost-plus contract, depending on how “cost-plus” is defined in the contract, reallocates many risks.

§ 26.4.1—Insurance Coverage

Example: Contractor’s aggregate liability arising out of or in connection with this Agreement, regardless of the theory of recovery, shall not exceed the amounts of insurance required by this Agreement to be maintained, except as to claims arising from damages caused by Contractor’s willful, wanton, or intentional misconduct.

One of the most common means of risk allocation is to provide that the owner will carry certain kinds and types of insurance coverage and that all contractors and subcontractors, etc., shall be named as additional insureds thereof. This affords a substantial benefit. Most owners want to have basic coverage regardless of what the contract has defined as its responsibility. In a situation where the owner, the prime contractor, and the subcontractor all buy essentially the same insurance coverage, it can result in an increase in the total cost of the project. Thus, it is often desirable to have one party carry the insurance coverage that covers all parties on the project. Such insurance coverage could potentially include builder’s risk, comprehensive general liability, and professional errors and omissions.

Enforceability

The following clause was upheld in *Florida Power & Light Co. v. Mid-Valley, Inc.*:¹⁰⁶

Upon written request of Owner received within five days of the acceptance hereof, Engineer will provide additional insurance, if available . . . and the Owner will pay Engineer an agreed amount for the increased coverage. Engineer’s liability to

Owner for any indemnity commitments or for any damages arising in any way out of the performance of this contract is limited to such insurance coverages and amounts. *In no event shall Engineer be liable for any indirect, special or consequential loss or damage arising out of the performance of services hereunder including, but not limited to, loss of use, loss of profit, or business interruption whether caused by negligence of Engineer, or otherwise, and Owner shall indemnify and hold Engineer harmless from any such damage or liability.*¹⁰⁷

Requirements for a valid limitation of liability clause may include proof that it was in fact negotiated, was a definite limitation amount, and had an unambiguous description of precisely the risk that it covers.¹⁰⁸

§ 26.4.2—Site Investigation

Example: Bidders are required to satisfy themselves by personal examination and investigation at the site of the work as to the conditions existing and the difficulties likely to be encountered in the construction of the work.

No plea of ignorance of conditions that exist or that may hereafter exist, or of conditions or difficulties that may be encountered in the execution of the work as a result of failure to make such personal examination and investigation will be accepted as an excuse for any failure or omission on the part of the contractor to fulfill in every respect all the requirements of the contract, nor will such plea be accepted as a basis for any claim whatsoever for extra compensation or for an extension of time.

Each party's responsibility can be specifically defined by the contract. Owners are generally responsible for soils tests, but the contract can shift the risk of the accuracy of the test. For example, if a contractor elects to rely upon the soils investigation performed by the soils engineer hired by the owner, the contractor will assume responsibility for the soils test.¹⁰⁹

Enforceability

Site investigation clauses are generally enforceable.¹¹⁰ When a contract contains both a site investigation exculpatory clause and a changed conditions clause, courts generally find that the changed conditions clause trumps the site investigation exculpatory clause.¹¹¹

§ 26.4.3—Performance Bonds

Performance bonds are required by statute, code, or ordinance by many governmental entities. In general, to the extent the contractor (or its subcontractors) fails to perform the contract, the surety is monetarily liable for performance. In short, it is analogous to insurance. However, whereas an insured does not have to reimburse the insurer for losses sustained, the principal does have to reimburse the surety. Thus, in fact, the performance bond does not shift risk away from the contractor.¹¹² However, it does protect an owner from some of the dangers associated with a contractor abandoning a project, becoming insolvent during construction and unable to continue

to perform, or otherwise failing in its performance, as the performance bond surety must provide a replacement contractor to complete the project, as well as compensating the owner for certain damages associated with its principal's failure of performance.

§ 26.4.4—Bid Bonds

Bid bonds are similar to the function of performance bonds, but their scope and obligation are more defined. Bid bonds are typically required on public construction projects and some private projects where competitive bidding is utilized. The bid bond is posted by prospective bidders on a project and warrants that if the contractor is awarded the work, yet refuses to begin performance, the owner is entitled to a liquidated sum. The bid bond amount, then, is simply a liquidated damages clause similar to those discussed in § 26.3.4, but for the narrowed scope of damages that an owner may suffer due to delays and costs incurred in awarding the work to another contractor.

§ 26.5 • SHOULD YOU INCLUDE RISK MANAGEMENT, ALLOCATION, AND TRANSFER CLAUSES IN THE CONTRACT?

§ 26.5.1—Overview

So, you have reviewed and considered the risk allocation and transfer clauses outlined above, and a lot of others. And you or your client like some of them, and maybe most of them. Should you incorporate them into your next construction contract? If you do, will a court enforce them?

§ 26.5.2—Are The Clauses Generally Valid And Enforceable?

As discussed above, most of the clauses in particular circumstances probably are valid and enforceable. However, in specific circumstances, any of the clauses may be void/voidable or unenforceable. The following is a brief discussion of some of the basic theories under which risk management and transfer clauses may be held invalid in any particular circumstance.

It is important to note, however, that you should not simply consider each clause separately. The court probably will look at the entire package of risk management, allocation, and transfer clauses contained in the contract to determine their validity. Nonetheless, the following sections discuss general principles of Colorado law with respect to the validity and enforceability of risk allocation clauses.

Duress

Duress is usually easy to understand but difficult to define. Generally, duress is compulsion (such as to execute a contract) caused by threats that destroy freedom of will. One court has described duress as the result of unlawful threats resulting in a contract essentially unjust toward the party seeking relief.¹¹³ The elements of a contract entered into under duress are: (1) one side involved unfairly accepted the terms of another; (2) the circumstances permitted no other alternative; and (3) the circumstances were the result of coercive acts of the opposite party.¹¹⁴

Unconscionability

C.R.S. § 4-2-301 covers unconscionable contracts or clauses in sales contracts. Unconscionability has been defined under this section as when the provision defeats the reasonable expectation of the parties.¹¹⁵

Regardless of whether the UCC governs the contract, Colorado courts consider four factors in determining whether a contract provision is unconscionable. The court will ask whether: (1) the contract is a standardized agreement executed by parties of unequal bargaining strength; (2) one party lacked the opportunity to read and become familiar with the document before signing it; (3) the contract used fine print in the portion of the contract containing the provision; and (4) there is an absence of evidence that the provision was commercially reasonable or should reasonably be anticipated to appear in the contract.¹¹⁶

Impossibility and Impracticability

When unanticipated circumstances have rendered contract performance impossible, the parties are excused from their contractual obligations.¹¹⁷ Similarly, when such anticipated circumstances render contract performance impracticable, the parties are also released from the contract.¹¹⁸ The significant element for impossibility and impracticability is that the arising circumstance was reasonably unanticipated by the parties. Indeed, as Williston said, “a [person] may contract to do what is impossible.”¹¹⁹ However, market changes, government actions, mere difficulty, expense, or hardship are not sufficient grounds for a successful impracticability defense.¹²⁰

Mistake of Fact

The Colorado Supreme Court recognizes that a bidder may rescind its bid because of a mistake of fact under certain circumstances.¹²¹ Generally, public contract law supports a contractor's bid rescission for several reasons, most notably because a bid based on mistake does not reflect a meeting of the minds.¹²² The Court concluded that a bidder may rescind its bid when (1) the mistake is due to clerical or mathematical error, (2) the mistake was made in good faith, (3) the mistake relates to a material aspect of the bid, *and* (4) the public entity did not rely on the mistaken bid to its detriment.¹²³

Though most of the courts' attention in this area is focused on public contracts, it may be a good idea for private parties to include a clause indicating that a mistake of fact is indeed contemplated by the parties. Generally, haphazard or mistaken bids indicate impending doom for both parties. A contractor that expects to lose money with a bad bid may attempt to compensate through the change order process. A bad bid may force an owner, on the other hand, into a situation where it either has to deal with additional change orders, a contractor who chooses to walk off, or litigation after the job is complete. Under even the best of circumstances, a bid based on a clerical or mathematical error has the potential to ruin a construction project.

Economic Loss Rule

The Colorado Supreme Court's decision in *BRW v. Dufficy*¹²⁴ is likely to impact contract enforceability of the duty of care. In *BRW*, a subcontractor, Dufficy, sought to recover tort damages from the engineer, BRW, based on defective plans. BRW and Dufficy were not bound under

contract; like most conventional construction projects, BRW and Dufficy were obligated only by interrelated contracts.¹²⁵ As established in *Town of Alma*,¹²⁶ the economic loss rule restricts parties under contract to recovery only under contract theory when suffering economic loss. *BRW* expanded *Town of Alma* to include parties connected by “interrelated contracts,” or in other words, parties in a construction project who are not in direct privity. This expansion will affect subcontractors, especially when the contract between the general contractor and subcontractor, for example, includes a flow-down clause.

The other important consideration that practitioners should extract from *BRW* is its suggestion that in order for the economic loss rule to apply and preclude recovery in tort, parties should clearly state the duty of care in the contract.¹²⁷ Stating the duty of care ensures that the parties will be held to that specific duty.¹²⁸

Against Public Policy

In *Stanley v. Creighton Co.*,¹²⁹ the court declared void as against public policy an exculpatory clause in a residential rental agreement that relieved the landlord of liability except for gross negligence. The decision was based in part upon the Premise Liability Act, C.R.S. § 13-21-115.¹³⁰ Generally, public policy dictates that parties cannot contract away their potential liability for their own negligence. Only where parties of equal bargaining power enter into such agreement, and where the agreement is express and unequivocal, have such clauses been held enforceable.¹³¹

Contract of Adhesion

In *Bauer v. Aspen Highland Skiing Corp.*,¹³² a skier sued the equipment manufacturer, rental shop, and ski school for injuries suffered while skiing. A part of the ski rental agreement contained language that pointed out, among other things, that skiing is a hazardous activity, that injuries are common, and that the ski boot binding system cannot release to prevent injuries at all times and under all circumstances. Its rental agreement then concluded:

I hereby RELEASE the ski shop and its owner, agents and employees, Marker [manufacturer] and its owners, agents and employees from any and all liability for injuries or damage to the user of equipment listed on this form or to any other person, resulting from NEGLIGENCE, the selection, installation, maintenance, adjustment, and use of this equipment. In addition, they shall not be held liable for any consequential damages. I agree NOT to make a claim against or sue this ski shop or Marker for injuries or damages relating to skiing and/or the use of this equipment.

The court applied the four factors defined in *Jones v. Dressel*¹³³ to determine if the exculpatory clause was valid. With respect to the assertion that the contract was a contract of adhesion, and therefore failed the third factor that it was entered into fairly, the *Bauer* court stated:

Colorado defines an adhesion contract as ‘generally not bargained for, but imposed on the public for a necessary service on a take it or leave it basis.’ However, printed form contracts offered on a take it or leave it basis, alone, do not render the agreement an adhesion contract. Rather, ‘[t]here must be showing that the parties

were greatly disparate in bargaining power, that there was no opportunity for negotiation, or that [the] services could not be obtained elsewhere.’ In *Jones*, the court held that the agreement was not an adhesion contract and the party seeking exculpation did not possess a decisive bargaining advantage ‘because the service provided by Free Flight was not an essential service.’¹³⁴

The court granted defendant’s motion for summary judgment.¹³⁵

Thus, the general rule in Colorado is that printed form contracts offered on a “take it or leave it” basis do not alone render an agreement one of adhesion. Factors also to be considered include greatly disparate bargaining power, no opportunity for negotiations, and no alternative to the services.¹³⁶

Contract Construed Against the Drafter

The general rule is that ambiguities in a contract are construed against the drafter.¹³⁷ Perhaps the parties can negate this common law rule by an express provision in the contract. Such a clause might read:

Example: The parties have jointly participated in the drafting of this Agreement; no one party or group of parties shall be deemed to be the draftsman of the Agreement. Neither this Agreement as a whole nor any provision herein shall be construed against either of the parties hereto.

Failure of Essential Purpose

Will the clause in question cause the contract to fail in its essential purpose? If so, it will not be enforced — at least under the UCC.

For example, in *Cooley v. Big Horn Harvestore Systems*,¹³⁸ the Colorado Supreme Court said, with respect to contracts subject to the UCC, that:

while contracting parties may generally limit the remedies available in the event of foreseeable and bargained-for contingencies, when a limited remedy fails of its essential purpose any contractual limitation directly related to the assumption that the limited remedy constituted a sufficient remedy must also fail.¹³⁹

Cooley stated the basic principle that “[A] remedy fails of its essential purpose if it operates to deprive a party of the substantial value of the contract.”¹⁴⁰

In *Lutz Farms v. Asgrow Seed Co.*,¹⁴¹ a seller appealed a judgment in favor of a buyer who had purchased defective onion seed. The district court in the original action held that a clause in the contract limiting the seller’s liability to a recovery of the buyer’s purchase price failed of its “essential purpose” under C.R.S. § 4-2-719(2), and the seller’s attempted exclusion of consequential damages was “unconscionable” under C.R.S. § 4-2-719(3). The 10th Circuit, relying on *Leprino v. Intermountain Brick Co.*,¹⁴² declined to reverse the district court’s holding.¹⁴³

The court in *Cooley* seemed to leave open the validity of a clear and unambiguous exclusion of consequential damages, even if the remedy provided fails of its essential purpose.¹⁴⁴ However, parties should be aware that the *Leprino* court found that a contract contained a valid exclusion of consequential damages clause but the remedy's failure of its essential purpose was enough to allow consequential damages because of latent defects and the inaction of the seller.¹⁴⁵

Clauses Negating in Whole or in Part Statutory Rights and Remedies

If the risk management, allocation, and transfer clause has the effect of eliminating or substantially impacting rights and remedies created by the legislature, it is doubtful that such clauses will be enforced as a matter of public policy.¹⁴⁶

The Facts and Circumstances

Notwithstanding the law generally upholding a clause, the factual circumstances can make a substantial difference in the interpretation and application by the court or a jury. Such circumstances include:

- the relative sophistication of the parties;
- whether the clause is fair and reasonable;
- whether the clause was in fact a bargained term; and
- the equality of bargaining power of the parties.

For example, if one party is at an obvious disadvantage in bargaining power such that the effect of the contract is to put him or her at the mercy of the other's negligence, the agreement may be void.¹⁴⁷ Additionally, the specific terms "negligence" and "breach of warranty" need not be referenced to preclude such claims.¹⁴⁸ However, such specificity assists in defeating other attacks.

§ 26.5.3—Even If The Clauses Are Valid And Enforceable, Do You Want To Use The Clauses?

The law is reluctant to interfere with the bargaining process and power of the parties to contract, and does so only in extreme circumstances. However, the fact that you may be able to transfer and allocate risks to the other party to the contract does not mean that you should do it. One should consider that those who impose an "unfair" contract upon another party often get what they deserve. For example, suppose there is a breach of contract. Most jurors and judges can quickly spot an unfair or lopsided contract.

Also, when one party to a contract has been "taken advantage of," that fact is often reflected in the performance of the disadvantaged party. Again, judges and jurors may take it upon themselves to level the playing field and compensate the party who has suffered under an enforceable, but unfair, contract.

In sum, there is no free ride. Risk management, allocation, and transfer clauses should be used to achieve bargained-for conclusions, and to achieve fair results reflecting terms both parties desire, not terms forced on one party just short of duress or unconscionability. One who uses the clauses to achieve an unfair or unreasonable allocation of risks most often will ultimately receive his or her just desserts.

§ 26.6 • CONCLUSION

The types of risk management allocation and transfer clauses discussed above are only a few of the many such types of clauses that might be considered. Indeed, for every risk and every problem in a construction project, there is a contract clause to eliminate or alleviate the concern.

However, as old-fashioned as it may seem, justice usually will ultimately prevail to place risks where they properly belong — within a broad range. Thus, more important than drafting the clause is the determination of whether it will be enforced by the courts, and whether it should be used at all.

§ 26.7 • BIBLIOGRAPHY

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NOTES

1. See generally §§ 11.2.1 and 23.2.2 (of this book).
2. See Chapter 19, “Mechanics’ Liens.”
3. See C.R.S. § 38-22-119.
4. See §§ 11.9, 17.3, 17.4.3 (of this book).
5. See § 7.4.2 (of this book).
6. See § 26.5, *infra*.
7. E.g., *Restatement (Second) of Conflict of Laws* § 6 (1971) (apply the law of state having most significant relationship); *Hawks v. Agri Sales, Inc.*, 60 P.3d 714, 715 (Colo. App. 2001); *ITT Specialty Risk Serv. v. Avis Rent A Car Sys., Inc.*, 985 P.2d 43, 47 (Colo. App. 1998).
8. See generally *Restatement (Second) of Conflict of Laws* § 187, comment i (1971).
9. *Wright v. Martek Power, Inc.*, 314 F. Supp.2d 1065, 1068 (D. Colo. 2004); *Am. Express Fin. Advisors, Inc. v. Topel*, 38 F. Supp.2d 1233 (D. Colo. 1999); *Hansen v. GAB Bus. Serv., Inc.*, 876 P.2d 112, 113 (Colo. App. 1994); *Lauritzen v. Larsen*, 345 U.S. 571, 588-89 (1953).
10. *Restatement (Second) Conflict of Laws* § 187 (1971); UCC § 1-105(1) (1989).
11. *Power Motive Corp. v. Mannesmann Demag Corp.*, 617 F. Supp. 1048, 1050 (D. Colo. 1985). See also, A. Covey & M. Morris, “The Enforceability of Agreements Providing for Forum and Choice of Law Selection,” 61 *Den. L. J.* 837, 854-55 (1984).
12. *Am. Express Fin. Advisors, Inc.*, 38 F. Supp.2d at 1238 .
13. *Id.*
14. See *Excell, Inc. v. Sterling Boiler & Mech., Inc.*, 106 F.3d 318, 321 (10th Cir. 1997) (holding mandatory jurisdiction in the El Paso County District Court, and not a Colorado Federal District Court).
15. See *Milk ‘N’ More, Inc. v. Beavert*, 963 F.2d 1342, 1346 (10th Cir. 1992) (forum selection clauses are *prima facie* valid and should be enforced unless enforcement is shown by the resisting party to be unreasonable under the circumstances); *Riley v. Kingsley Underwriting Agencies, Ltd.*, 969 F.2d 953, 956-57 (10th Cir. 1992); *Excell, Inc. v. Sterling Boiler & Mech. Inc.*, 106 F.3d 318, 321 (10th Cir. 1997); *REO Sales, Inc. v. Prudential Ins. Co. of America*, 925 F. Supp. 1491, 1492 (D. Colo. 1996); *Zimmerman Metals, Inc. v. United Eng. & Constructors, Inc.*, 720 F. Supp. 859, 861 (D. Colo. 1989); *Edge Telecom, Inc. v. Sterling Bank*, 143 P.3d 1155, 1162 (Colo. App. 2006); *Vessels Oil & Gas Co. v. Coastal Ref. & Mktg.*, 764 P.2d 391, 393 (Colo. App. 1988); cf. *Vanderbeek v. Vernon Corp.*, 25 P.3d 1242, 1247 (Colo. App. 2000); cf. *Union Pac. R. Co. v. Equitas Ltd.*, 987 P.2d 954, 956 (Colo. App. 1999).
16. *Clementi v. Nationwide Mut. Fire Ins. Co.*, 16 P.3d 223, 226 (Colo. 2001) (timely notice by insured required; however, if the claim involves a non-liability issue, the insurer must prove it was prejudiced by the delay); *Freidland v. Travelers Indem. Co.*, 105 P.3d 639, 643 (Colo. 2005).
17. *Clementi*, 16 P.3d at 226 (a policy’s requirement of notice “as soon as practicable” meant that notice must be given within a reasonable length of time). See also C.R.S. § 24-10-109 (requiring that a person having claim under Colorado Governmental Immunity Act must file written notice with public entity within 180 days after date of discovery of injury).
18. See C.R.S. § 13-80-104; C.R.S. §§ 13-20-801 through -807.
19. See also § 26.2.6, “Clauses Defining Commencement of Statute of Limitations” and § 26.3.7, “Release of Claims.”
20. See *Regents of the Univ. of Colo. v. Harbert Constr. Co.*, 51 P.3d 1037, 1041 (Colo. App. 2001) (upholding a 12-month statute of limitations on warranty claims).
21. C.R.S. § 13-80-104(b); see also *Hersh Cos. v. Highline Village Assocs.*, 30 P.3d 221 (Colo. 2001).
22. *Regents of the Univ. of Colo. v. Harbert Constr. Co.*, 51 P.3d 1037 (Colo. App. 2001).
23. *Id.* at 1041.
24. *Id.*
25. C.R.S. § 38-1-102 provides that a reasonable good faith effort to negotiate and failure to agree upon compensation is a prerequisite to the commencement of the condemnation proceedings. See *Minto v.*

Lambert, 870 P.2d 572, 576 (Colo. App. 1993) (mediation is not a restriction on the court's subject matter jurisdiction, but rather a condition precedent as an element of the claim for relief).

26. C.R.S. § 13-21-102(5); *but see Pyle v. Sec. U.S.A., Inc.*, 758 F. Supp. 638, 639 (D. Colo. 1991) (state arbitration laws restricting arbitrator's power to award punitive damages do not apply to actions under Federal Arbitration Act absent agreement by parties that state arbitration law will govern).

27. *See Quist v. Specialties Supply Co.*, 12 P.3d 863, 867 (Colo. App. 2000) (arbitration clause does not preclude party from pursuing punitive damages under the Colorado Consumer Protection Act); *see generally Mulder v. Donaldson, Lufkin & Jenrette*, 648 N.Y.S.2d 535 (App. Div. 1996).

28. *Mastrobuono v. Shearson Lehman Hutton Inc.*, 514 U.S. 52, (1995).

29. *See Gourley v. Yellow Transp., LLC*, 178 F. Supp.2d 1196 (D. Colo. 2001) (court denied motion by employer to compel arbitration for employees' Title VII claims under arbitration agreement citing, among other reasons, that employer could unilaterally modify the agreement terms, and it required the employee to share the costs of arbitration).

30. *Dreiling v. Peugeot Motors of Am., Inc.*, 539 F. Supp. 402, 403 (D. Colo. 1982) (however, courts will indulge every reasonable presumption against waiver); *aff'd in part and rev'd in part*, 850 F.2d 1373 (10th Cir. 1988); *see generally Jay M. Zitter, Anno.*, *Contractual Jury Waivers in State Civil Cases*, 42 A.L.R. 5th 53 (1996); *Debra T. Landis, Anno.*, *Contractual Jury Trial Waivers in Federal Civil Cases*, 92 A.L.R. Fed. 688 (1989); 47 Am. Jur. 2d *Jury* §§ 72-78 (1995).

31. *Developments in the Law — Discovery*, 74 Harv. L. Rev. 940, 942 (1991).

32. *Id.* at 979, n. 301; *see also C.R.S. § 4-2-302* (unconscionable contract or clause in sales contract). *But see Rains v. Found. Health Sys. Life & Health*, 23 P.3d 1249, 1254 (Colo. App. 2001).

33. C.R.S. § 38-10-108.

34. *See Hahl v. Langfur Constr. Corp.*, 529 P.2d 1369, 1370 (Colo. App. 1974) (not selected for official publication); *High-Valley Constructors, Inc. v. Heyser*, 428 P.2d 354, 357 (Colo. 1967).

35. *See Hahl*, 529 P.2d at 1370-71. *See generally Anno.*, *Effect of Stipulation in Private Building or Construction Contract That Alterations or Extras Must Be Ordered In Writing*, 2 A.L.R. 3d 620 (1965).

36. *See* §§ 26.2.5 and 26.2.6, *supra*.

37. *See Erickson v. Oberlohr*, 749 P.2d 996, 999 (Colo. App. 1987) (applying warranties only to first buyer of new home).

38. *See Sloat v. C.E. Matheny*, 625 P.2d 1031, 1034 (Colo. 1981); *see also Roper v. Spring Lake Development Co.*, 789 P.2d 483, 485 (Colo. App. 1990).

39. *See Regents of the Univ. of Colo. v. Harbert Const. Co.*, 51 P.3d 1037, 1040 (Colo. App. 2001) (noting that if the parties wanted to exclude negligence, breach of contract, or strict liability claims, they could have easily done so).

40. *See* § 26.5, *infra*.

41. *Rowan v. Vail Holdings, Inc.*, 31 F. Supp.2d 889, 896 (D. Colo. 1998); *Jones v. Dressel*, 623 P.2d 370, 376 (Colo. 1981).

42. *Rosen v. LTV Recreational Dev., Inc.*, 569 F.2d 1117, 1122 (10th Cir. 1978).

43. *Lahey v. Covington*, 964 F. Supp. 1440 (D. Colo. 1996).

44. *Lahey*, 964 F. Supp. at 1445. *See also B & B Livery, Inc. v. Riehl*, 960 P.2d 134 (Colo. 1998); *Potter v. National Handicapped Sports*, 849 F. Supp. 1407, 1409 (D. Colo. 1994).

45. *Lahey*, 964 F. Supp. at 1445.

46. *Heil Valley Ranch, Inc. v. Simkin*, 784 P.2d 781, 785 (Colo. 1989) (use of the specific terms "negligence" and "breach of warranty" is not required in exculpatory agreements; inquiry should be whether intent of parties was to extinguish liability and whether such intent was clearly and unambiguously expressed).

47. *See Ricciardi v. Frank*, 620 N.Y.S.2d 918, 922 (N.Y. City Ct. 1994). *See generally* 57 Am. Jur. 2d *Negligence* §§ 49-64.

48. C.R.S. § 4-2-710.

49. C.R.S. § 4-2-715. *See Vanderbeek*, 25 P.3d at 1245 (in a contract action, an injured party is entitled to recover only those damages in contemplation at the time of formation of the contract). *Olson Plumbing & Heating, Inc. v. Douglas Jardine, Inc.*, 626 P.2d 750, 752 (Colo. App. 1981) (construction con-

tractor is responsible for natural, probable, and reasonably foreseeable consequences of failure to perform his or her contract).

50. See EJCDC Doc. No. 1910-1 (1996).

51. C.R.S. § 4-2-719(3) (under the UCC, consequential damages may be limited or excluded, unless the limitation or exclusion is unconscionable); *Leprino v. Intermountain Brick Co.*, 759 P.2d 835, 836 (Colo. App. 1988).

52. *Lutz Farms v. Asgrow Seed Co.*, 948 F.2d 638, 646 (10th Cir. 1991).

53. See also *J.A. Balistreri Greenhouses v. Roper Corp.*, 767 P.2d 736, 739 (Colo. App. 1988) (contractual exclusion of consequential damages was unconscionable and contract failed for its essential purpose by leaving plaintiffs without a remedy), *cert. granted* (Jan 23, 1989), *appeal dismissed*, 773 P.2d 1074 (Colo. 1989).

54. *Perino v. Jarvis*, 312 P.2d 108, 109 (Colo. 1957).

55. *Klinger v. Adams County School Dist. No. 50*, 130 P.3d 1027, 1034 (Colo. 2006).

56. Model Punitive Damages Act § 5 & Comment (1996); see also *Smith v. Wade*, 461 U.S. 30, 46 (1983) (discussing majority common law standards for punitive damage awards).

57. *Mortgage Finance, Inc. v. Podleski*, 742 P.2d 900, 902 (Colo. 1987).

58. C.R.S. §§ 13-21-102(1)(a) and (b).

59. *G.E.C. Minerals, Inc. v. Harrison Western Corp.*, 781 P.2d 115 (Colo. App. 1989).

60. See § 26.3.10, *infra* (for discussion).

61. See generally § 26.3.10, *infra* (requirements for valid exculpatory clauses).

62. *Jones v. Dressel*, 623 P.2d 370, 376 (Colo. 1981).

63. *Lira v. Shelter Ins. Co.*, 913 P.2d 514, 517 (Colo. 1996); see also *Bohrer v. Church Mut. Ins. Co.*, 12 P.3d 854, 856 (Colo. App. 2000) (citing *American Family Mut. Ins. Co. v. Johnson*, 816 P.2d 952 (Colo. 1991) (the “purpose of excluding intentional injuries from coverage is to prevent extending . . . a license to commit harmful, wanton, or malicious acts”)).

64. C.R.S. § 13-21-102(5).

65. *Padilla v. D. E. Frey & Co.*, 939 P.2d 475, 477-78 (Colo. App. 1997).

66. 9 U.S.C. §§ 1, *et seq.* (FAA) See *Mastrobuono*, 514 U.S. at 63 (reasoning drafter of ambiguous agreement cannot claim benefit of doubt after combining choice-of-law clause with FAA, which allows punitive awards).

67. See generally 13 Am. Jur. 2d *Building and Construction Contracts*, §§ 58-68 (2000).

68. See Anno., *No Damages for Delay Clauses*, 74 A.L.R. 3d 187 (1976).

69. See *City of Westminster v. Centric-Jones Const.*, 100 P.3d 472, 481 (Colo. App. 2003); (*cert. granted* 2004). See generally *W.C. James, Inc. v. Phillips Petroleum Co.*, 347 F. Supp. 381 (D. Colo. 1972); *Indiana Dept. of Transp. v. Shelly & Sands, Inc.*, 756 N.E.2d 1063 (Ind. App. 2001).

70. *Regents*, 51 P.3d 1037.

71. *Id.*

72. *Id.*

73. *Id.*

74. *Id.*

75. *Heil Valley Ranch, Inc.*, 784 P.2d at 785; see also *Forman v. Brown*, 944 P.2d 559, 563-64 (Colo. App. 1997) (enforcing river-rafting release in negligence case based on unambiguous language); *Brooks*, 941 F. Supp. at 963 (holding under Colorado law in diversity action that valid release of snowmobile tour company encompassed negligence and “any claim based on breach of contract theory”).

76. *Heil Valley Ranch, Inc.*, 784 P.2d at 785.

77. See *Day v. Snowmass Stables, Inc.*, 810 F. Supp. 289, 294-95 (D. Colo. 1993) (denying summary judgment in diversity action despite release from “any liability,” where plaintiff was inexperienced and contract language anticipating horse-drawn wagon ride did not enumerate risks).

78. AIA Doc. B511, Guide for Amendments to AIA Owner-Architect Agreements (2001 Ed.).

79. *Lutz Farms v. Asgrow Seed Co.*, 948 F.2d 638 (U.S. App. 1991).

80. *Id.* at 646.

81. See *Powder Horn Constructors, Inc. v. City of Florence*, 754 P.2d 356, 372 n.1 (1988) (UCC governs Colorado construction contracts only when the “primary purpose” of the contract includes a sale of goods. To determine “primary purpose,” the court looks at (1) the contract language, (2) whether the contract involves one price that includes both goods and labor, or, instead, calls for separate billings for goods and services, (3) the cost ratio of goods to services, and (4) the nature and reasonableness of the purchaser’s contractual expectations of acquiring a property interest in goods).

82. See *Connell v. Sun Oil Co.*, 596 P.2d 1215, 1217 (Colo. App. 1979).

83. See *Amer. Gen. Fin., Inc. v. Branch*, 793 So.2d 738, 748-50 (Ala. 2000) (limitation on damages to five times amount of economic damages among factors resulting in arbitration agreement being held unconscionable).

84. See generally *Leprino v. Intermountain Brick Co.*, 759 P.2d 835, 836-37 (Colo. App. 1988) (limiting remedy from brick wall defect to cost of bricks fails to provide injured party benefit of its bargain).

85. E.g., *Mackall v. Jalisco Intern. Inc.*, 28 P.3d 975, 977 (Colo. App. 2001) (holding that the prevailing party is the one who has succeeded on a significant issue and has achieved some of the benefits sought in the lawsuit); *Travers v. Rainey*, 888 P.2d 372, 374 (Colo. App. 1994).

86. See *Restatement (Second) Contracts* § 195 Comment a (1981) (discussing caveats or proscriptions generally applicable to exculpatory clauses in various jurisdictions).

87. *Heil Valley Ranch, Inc.*, 784 P.2d at 783.

88. *Jones*, 623 P.2d at 376 (upholding clause exempting corporation from negligence in parachute-jumping contract).

89. *Id.* See also *1745 Wazee LLC v. Castle Builders, Inc.*, 89 P.3d 422, 426 (Colo. App. 2003) (applying the *Jones v. Dressel* factors to a construction contract and holding that the exculpatory clause did not violate public policy).

90. *Id.* at 138 (citing *Heil Valley Ranch*, 784 P.2d at 785).

91. *Heil Valley Ranch, Inc.*, 784 P.2d at 784; see also *Stanley v. Creighton Co.*, 911 P.2d 705, 706 (Colo. App. 1996) (invalidating clause exempting landlord from negligence liability on public policy grounds).

92. C.R.S. § 13-50.5-102(8). See generally “The Validity of Exculpatory Clauses in Architectural Services Contracts,” 25 *Colo. Law.* 3 (March 1996).

93. *G.E.C. Minerals, Inc.*, 781 P.2d at 116.

94. *Id.*

95. *Id.*

96. *W. Fed. Sav. and Loan Assoc. v. Nat’l Homes Corp.*, 445 P.2d 892, 893 (Colo. 1968) and *In re Woodcrest Homes, Inc.*, 11 B.R. 342, 344 (Bankr. D. Colo. 1981), *aff’d in part and rev’d in part* 15 B.R. 886 (D. Colo. 1981); see also *Bishop v. Moore*, 323 P.2d 897, 898 (Colo. 1958) (a mechanic’s lien may be waived by express agreement of the party in whose favor the lien exists).

97. See Blieszner, *et al.*, *Mechanic’s Lien Law and Strategies in Colorado*, 18 (NBI, Inc. 1999).

98. Section 14.7, AGC Docu. No. 410, Standard Form of Design-Build Agreement.

99. See *Cherokee Inv. Co. v. Voiles*, 443 P.2d 727, 729 (Colo. 1968); *Richard O’Brien Companies v. Challenge-Cook Bros., Inc.*, 672 F. Supp. 466, 469-70 (D. Colo. 1987). See also *Lutz Farms*, 948 F.2d at 646 (discussing C.R.S. § 4-2-316, Exclusion and Modification of Warranties).

100. *Cosmopolitan Homes, Inc. v. Weller*, 663 P.2d 1041, 1045 (Colo. 1983).

101. *Sloat v. Matheny*, 625 P.2d 1031, 1034 (Colo. 1981). See also § 14.4.3 of this book.

102. See AIA Doc. B511, Guide for Amendments to AIA Owner-Architect Agreements (2001 Ed.).

103. See, e.g., *Jefferson County Bank v. Armored Motor*, 366 P.2d 134, 136 (Colo. 1961).

104. American Institute of Architects Document A201-1997, ¶ 4.3.7.2.

105. *Associated Eng’rs & Contractors, Inc. v. State*, 567 P.2d 397 (Haw. 1972).

106. *Fla. Power & Light Co. v. Mid-Valley, Inc.*, 763 F.2d 1316 (11th Cir. 1985).

107. *Id.* at 1318. See also *Markborough Cal., Inc. v. Superior Court*, 227 Cal. App.3d 705, 714-15 (1991).

108. See also Anderson, “Contractual Limitations on Remedies,” 67 *Neb. Law Rev.* 548 (1988).

109. See Beh, Hazel G., *Allocating the Risk of the Unforeseen, Subsurface and Latent Conditions in Construction Contracts: Is There Room for the Common Law?*, 46 U. Kan. L. Rev. 115 (1997).
110. See generally *Green Const. Co. v. Kan. Power & Light Co.*, 717 F.Supp 738, 742 (D. Kan. 1989), *aff'd* 1 F.3d 1005 (10th Cir. 1993). See also *Saddlewood Downs, L.L.C. v. Holland Corp.*, 99 P.3d 640, 645 (Kan. App. 2004) (noting that when the parties do not include a changed conditions clause, the risk of unknown site conditions shifts to the contractor).
111. See generally 56 A.L.R. 4th 1042, § 4(a) (2005).
112. See generally §§ 12.5.1 through 12.5.5.
113. *McClair v. Wilson*, 31 P. 502, 503 (Colo. 1892).
114. See 25 Am. Jur. 2d, *Duress and Undue Influence*, §§ 3-6 (1996); CJI-Civ. 30:16 (CLE ed. 2005); 11 Am. Jur. Proof of Facts 2d, *Promissory Note Executed Under Economic Duress or Business Compulsion* § 23.
115. *Lepirino v. Intermountain Brick Co.*, 759 P.2d 835, 836 (Colo. App. 1988); see also *Lutz Farms*, 948 F.2d at 646 (holding exclusion of consequential damages was unconscionable under C.R.S. § 4-2-719(3), and therefore void).
116. *Indus. Products Int'l, Inc. v. Emo Trans, Inc.*, 962 P.2d 983, 988 (Colo. App. 1997). See also Milton Roberts, Annotation, *Unconscionability Under UCC § 2-302 or § 2-719(3), of Disclaimer of Warranties or Limitation or Exclusion of Damages in Contract Subject to UCC Article 2 (Sales)*, 38 A.L.R. 4th 25 (1985); *Davis v. M.L.G. Corp.*, 712 P.2d 985, 991 (Colo. 1986); *Mullan v. Quickie Aircraft Corp.*, 797 F.2d 845, 850 (10th Cir. 1986).
117. See *City of Littleton v. Employers Fire Ins. Co.*, 453 P.2d 810, 812 (Colo. 1969).
118. *Id.* (adopting Restatement rule on impracticability).
119. *Id.* (citing 6 Williston, Contracts § 1931 (Rev. ed.)).
120. See *Beals v. Tri-B Assocs.*, 644 P.2d 78, 81 (Colo. App. 1982), see also *Great Am. Ins. Co. of N.Y. v. City of Boulder*, 476 P.2d 586, 587 (Colo. App. 1970) (not selected for official publication).
121. See *Powder Horn Const., Inc. v. City of Florence*, 754 P.2d 356, 358 (Colo. 1988), *cf. In re Marriage of Manzo*, 659 P.2d 669 (Colo. 1983) (holding that a contract cannot be avoided due to error of judgment by one party unless the other party also knew of the error).
122. *Id.* at 360. It is important to note that the court actually decided the case for Powderhorn because the city had not yet accepted or relied upon the bid before Powderhorn rescinded its bid. The court went on, however, to discuss whether it should adopt a form of relief for mistaken bidders. For a discussion of the importance of the city's lack of acceptance prior to rescission in *Powder Horn*, see *Shoels v. Klebold*, 375 F.3d 1054, 1068 (10th Cir. 2004).
123. *Id.* at 363 (noting also that the contractor must prove all elements beyond a preponderance of the evidence).
124. *BRW, Inc. v. Dufficy & Sons, Inc.*, 99 P.3d 66 (Colo. 2004).
125. See *id.* at 69 (chart explaining the contractual relationship between the various parties).
126. *Town of Alma v. AZCO Const., Inc.*, 10 P.3d 1256 (Colo. 2000).
127. *BRW*, 99 P.3d at 74 ("The BRW contract provides that the drawings and specifications prepared by BRW 'must represent a thorough study and competent solution for the Project as per usual and customary professional standards and shall reflect all architectural and engineering skills applicable to that phase of the Project.' The contract also states that the plans and specifications 'shall be adequate and sufficient for the proper construction of the Project.'").
128. *Id.*
129. *Stanley v. Creighton Co.*, 911 P.2d 705 (Colo. App. 1996); but see *Mincin v. Vail Holdings, Inc.*, 308 F.3d 1105, 1110 (10th Cir. 2002).
130. See also *Otis Elevator Co. v. Md. Cas. Co.*, 33 P.2d 974, 977 (Colo. 1934).
131. *Threadgill v. Peabody Coal Co.*, 526 P.2d 676, 679 (Colo. App. 1974).
132. *Bauer v. Aspen Highland Skiing Corp.*, 788 F. Supp. 472 (D. Colo. 1992).
133. *Jones*, 623 P.2d at 374.
134. *Bauer*, 788 F. Supp. at 474-75 [citations omitted].

135. See also *Batterman v. Wells Fargo Ag. Credit Corp.*, 802 P.2d 1112, 1116 (Colo. App. 1990), *cert. denied* (no adhesion contract where lender's only wrong was to use superior bargaining position to protect its investment); *Clinic Masters v. Dist. Court*, 556 P.2d 473, 475-76 (Colo. 1976) (printed form contract on "take-it-or-leave-it" basis alone does not make contract one of adhesion).

136. *Rowan*, 31 F. Supp.2d at 897; *Ad Two Inc. v. City and County of Denver*, 983 P.2d 128, 132 (Colo. App. 1999).

137. See CJI-Civ. 30:13 (CLE ed. 2005) and cases cited thereat. See generally *Stegall v. Little Johnson Assocs., Ltd.*, 996 F.2d 1043, 1049 (10th Cir. 1993); *Cheyenne Mountain Sch. Dist. No. 12 v. Thompson*, 861 P.2d 711, 716 (Colo. 1993).

138. *Cooley v. Big Horn Harvestore Sys.*, 813 P.2d 736 (Colo. 1991).

139. *Id.* at 747.

140. *Id.*

141. *Lutz Farms v. Asgrow Seed Co.*, 948 F.2d 638, 646 (10th Cir. 1991).

142. *Leprino*, 759 P.2d at 837 (holding that one situation in which a limitation of remedy to return of purchase price has been held to fail of its essential purpose is when goods have latent defects which are not discoverable upon receipt and reasonable inspection); see also *Wenner Petroleum v. Mitsui & Co.*, 748 P.2d 356, 357 (Colo. App. 1987) (failure of the essential purpose is measured by whether the buyer is deprived of the substantial value of his or her bargain).

143. *Lutz Farms*, 948 F.2d at 646.

144. *Id.* at 748. Cf. *Fiberglass Component Prod., Inc. v. Reichold Chemicals, Inc.*, 983 F. Supp. 948, 960 (D. Colo. 1997) (the failure of essential purpose exception generally applies only to those situations in which buyer is left without a remedy).

145. *Leprino*, 759 P.2d at 837.

146. See § 26.5.2.3, *supra*.

147. *Lahey*, 964 F. Supp. at 1444-45 (also defining the elements to consider); *B & B Livery, Inc.*, 960 P.2d at 136.

148. *Del Bosco v. U.S. Ski Ass'n*, 839 F. Supp. 1470, 1473 (D. Colo. 1993).