



DESIGN-BUILD TEAMING AGREEMENTS:

This, the last of a three-part article, discusses business opportunities, and risks of participation in the teaming structure, and makes recommendations for resolving disputes.

FOSTERING THE RELATIONSHIP

MARK C. FRIEDLANDER, ESQ.

One of the major reasons that relationships between design professionals and contractors have tended to be adversarial is that they often are involved in only a single project together rather than a series of projects. The absence of a regular working relationship creates an incentive for each company to maximize its profits on each individual project because there is no reason to expect that a compromise on any particular project will be of any benefit in future projects. Consequently, each party tends to "make hay while the sun shines."

These incentives do not automatically change simply because a design-build method of project delivery is employed. It is not uncommon for an owner or developer to "marry together" a design professional and a contractor who have had no prior business relationship and who may have no business

relationship with each other after completion of the project. This is the construction industry's equivalent of the "shotgun marriage." Although it may succeed, its single-project nature renders it more likely than other design-build teams to fail.

A design-build team whose members intend to continue doing business as a team together on future projects has much greater incentive to cooperate and to eliminate adversarial roles than does a design-build team that is put together for a single project. The design-build team with long-term business plans is more likely to realize that compromise and cooperative behavior on the first project are likely to be paid back or rewarded by similar compromises and cooperative behavior by the other member of the team on future projects. Similarly, to the extent that the design-build team desires to use the first project as a

MARK C. FRIEDLANDER, ESQ. is co-Chair of the Construction Law Group of Schiff Hardin, LLP in Chicago and an adjunct professor at the Architecture School of the University of Illinois at Chicago. He has served as the Chairman of the Professional Practice and Contracts Committee of the Design Build Institute of America and of the Project Delivery Systems Committee of the American College of Construction Lawyers. Mr. Friedlander is a frequent speaker and writer on project delivery methods and other issues of construction law and is credited with having developed a successful and increasingly popular approach to Designer-Led Design-Build. He can be reached at (312) 258-5546 or mfriedla@schiffhardin.com and keeps one of the internet's most useful and acclaimed websites on Design-Build at <http://www.schiffhardin.com/design-build/>

prototype or basis for future marketing, it has extra incentive not to blemish its reputation by making inappropriate claims or otherwise engaging in counterproductive behavior.

Protective business provisions

If the design professional and contractor intend to continue to market their services as a design-build team in the future, then the teaming agreement should address the issues involved in such future marketing. In particular, it is important for the parties to spell out in detail any assumptions that they may have regarding future marketing efforts so that there is no misunderstanding that might infect future business relations. Depending on the nature of the project and the market niche, the categories listed below are the issues which most frequently merit discussion.

Confidentiality. Confidentiality provisions are not uncommon in teaming agreements, but their substance may vary greatly depending on what kind of information is deemed to be confidential and to whom it belongs. For example, if the confidential information in question belongs to the client, then both design-build team members have identical interests in preventing the other from improperly disclosing the information. In such a case, the confidentiality provision is simple and short.

However, the confidential information may belong exclusively to the design professional or to the contractor. In that case, the confidentiality provision should clearly identify what is confidential and what is not, and under what circumstances the confidential information may be disclosed. For example, if the design professional owns a patented process, it may nevertheless be in the design professional's interest to allow the contractor to disclose certain aspects or elements of the process if the contractor is attempting to secure additional work for the design-build team. Or if the confidential information is the contractor's pricing data, it may be in the contrac-

tor's interest to allow the A/E to disclose certain aspects of it in order to secure additional projects for the design-build team.

A good confidentiality clause also considers related issues. For example, how should the parties react if the confidential information is requested in a subpoena? For what length of time will disclosure be barred? What remedies will the owner of the confidential information have in the event that disclosure of the information is imminent (or has already occurred)?

A common issue related to confidentiality is the information generated by the project itself. The design may be reusable at other locations, or cost or other construction data derived from the project may provide a competitive advantage in bidding on similar projects in the future. The teaming agreement should identify whether there are any restrictions on the use of such information, which party has the right to control the use, and what the procedure is for obtaining permission, if any, to use the information.

Exclusive relationships. In deciding whether to continue to try to work together in the future, it is natural for both design-build team members to seek some kind of assurance that the other team member will choose to team with them again. Mutual assurances of this type provide a strong incentive for continued teamwork rather than adversarial relations. The relationship does not have to be exclusive; it may be enough for one team member to indicate that the other would be its "preferred teammate" in future projects of a particular type.

True exclusive relationships between otherwise unaffiliated design-build teammates are quite rare. Most companies would deem it an unsound practice to link their fortunes inextricably to those of another company. But it is not uncommon for a teaming agreement to describe certain circumstances under which each teammate would agree not to form a team with anyone else.

Several different factors are commonly identified as conditions to an exclusive or "preferred teammate" relationship. One such factor is geography; a con-

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tractor may agree to team exclusively with a particular design professional in that design professional's local market. Another factor is expertise or market niche; an architect may agree to enter into a teaming agreement for high-end single-family houses exclusively with a contractor who has an excellent reputation and experience in such projects. A third factor is size of project; one team member may agree to team exclusively with the other for all projects below (or above) a certain size. Obviously, different kinds of agreements involving various permutations of these factors are possible.

Exclusive or preferred relationships are valuable because of their long-term incentives, but they may be extremely restrictive on the parties' business plans. To increase the palatability of such relationships to the business leaders of both team members, it is usually wise to include limitations on the relationship, particularly as to length of time. There may also be a provision permitting termination of the relationship by advance written notice.

One particular form of exclusive relationship is an agreement not to compete. This is an agreement or provision by which one team member agrees not to solicit or accept certain kinds of business. An agreement not to compete is usually appropriate only when one team member obtains access during the course of the project to business opportunities or similar information that were previously in the exclusive possession of the other team member. This usually occurs when one of the team members possesses certain intellectual property rights, like a patent or copyright, or when it possesses certain unique expertise or highly developed marketing information like customer lists.

There is a great deal of legal precedent regarding agreements not to compete, which, in general, are not favored by the courts. Courts only enforce agreements not to compete if they are appropriately limited in duration and geography and not otherwise overly restrictive. If the design-build team members agree to enter into an agreement not to compete,

it is wise to consult a lawyer with regard to its language and terms.

Future marketing and sales efforts. Even without an exclusive or preferred relationship, design-build teammates may create procedures that provide a strong incentive for them to continue to work together. These procedures usually involve joint marketing or sales efforts that attempt to develop business for the design-build team. There are several ways that such provisions can be included in a teaming agreement.

One way to provide for future marketing and sales efforts is for the teaming agreement to spell out in detail precisely what efforts will be undertaken by each party. There may be provisions for marketing staffs to work together and for the creation of published materials promoting the design-build team. The teaming agreement may establish territories or even quotas for both parties.

It is rare, however, for design-build teammates to devote much detail to the specifics of future marketing and sales efforts unless they have some unique "wrinkle" to the services they will be providing together. It is more common for the teaming agreement to include relatively vague promissory language regarding future marketing and sales efforts but without the kind of detail necessary to bind each party to performing specific tasks. In such a situation, the reference to future marketing and sales efforts may or may not be worth the paper on which it is written; it will be up to senior management and the marketing staffs of each team member to convert those vague representations into real joint marketing and sales. The incentives that the team members may perceive regarding future work would then be a function of the degree to which they actually undertake to work together.

A third possibility is for the teaming agreement to build in financial incentives for each team member to market actively on behalf of the team. The teaming agreement may establish a procedure by which credit for business generation in the form of tangible financial reward is attributed to the team member whose mar-

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keting and sales efforts are primarily responsible for the business opportunity. Care should be taken, however, to ensure that any competition between the team members' marketing staffs does not rise to unhealthy levels which may result in disputes between the team members.

Risk-shifting devices

The use of risk-shifting devices is routine in virtually all construction projects. The most common risk-shifting devices are insurance and contractual loss allocation provisions, such as indemnity and contribution. These devices are used in design-build projects very similarly to how they are used in traditional construction projects.

The major difference in the use of risk-shifting devices in design-build projects derives from the fact that the designer and constructor are members of the same team and share each other's interests and risks to a greater extent. In particular, depending on the structure of the design-build team, the contractor or design professional may be vicariously liable for risks and other problems caused by the other. Similarly, they are more likely to have a mutual interest in how risks are borne by or allocated to other people or entities involved in the project, particularly the owner and subcontractors.

As with most of the other issues discussed in this article, there is no particular right or wrong way to use risk-shifting devices. The members of the design-build team should, however, discuss and reach agreement regarding these issues. Then the agreements reached should be recorded in the teaming agreement.

Insurance. Construction projects inevitably require several different kinds of insurance. The most common types of insurance are general liability, professional liability, property/builder's risk and worker compensation/employer's liability. There are numerous other kinds of insurance that may be appropriate depending on the nature of the project, including boiler, marine, efficacy, etc.

The first step is for the design-build team to identify what kinds of insurance are likely to be necessary or advis-

able for the project. This determination is likely to be made in concert with the client. It may also involve use of an insurance broker, risk manager, or similar consultant.

The next step is to determine which party will be responsible for procuring and maintaining each type of insurance. It is common for each party to provide its own worker's compensation/employer's liability insurance. General liability insurance is usually provided by the contractor, and professional liability is usually provided by the design professional. Property or builder's risk insurance may be provided by the owner, contractor or the design-build team—usually whoever can purchase it least expensively. Construction subcontractors usually purchase and maintain their own general liability and worker's compensation/employer's liability insurance, while design subconsultants often are required to carry their own professional liability coverage and worker's compensation/employer liability insurance.

One option is for the owner to purchase or to reimburse the design-build team for purchasing a project or wrap-around policy that insures all of the companies involved in the project. This option is usually more efficient and cost-effective in relatively large projects. It is particularly useful in design-build projects because of the closer involvement of and overlap between the design and construction functions.

In addition to determining what kinds of coverage to require, the design-build team members must agree on the coverage limits, deductibles, procedures for demonstrating proof of insurance coverage and other terms. Usually, these issues require consultation with the client, both for input as to the client's requirements and to impose requirements on the client. For example, the design-build team has a significant interest in determining the size of the deductible in any builder's risk insurance to be purchased by the owner.

An insurance concern relatively unique to design-build, particularly where the contractor is prime and the design professional sub, involves the contractor's potential liability for professional errors

or omissions on the plans. It may not be possible for the A/E to name the contractor as an additional insured party on its professional liability policy. Recently, other alternatives have become possible, such as a contractor's professional liability policy.

Surety bonds. The role of performance, payment and bid bonds are essentially the same in design-build as in traditional projects. In a design-build project, they may be provided by the design-builder rather than the contractor alone, but they are usually secured by the contractor's financial capitalization, rather than by the design professional's, because of the disparity between them. The design professional and contractor need to discuss and incorporate into the teaming agreement whatever bonding arrangements, if any, they agree to for the project. The teaming agreement should include an explanation of how the bond

premium, which is usually reimbursed directly by the owner, will be treated, as well as any other risk, notice or proof issues

pertaining to the bond. Input from the client may be required to determine these agreements.

The major issue of concern for bonding companies with regard to design-build projects is the extent to which the bond will be responsible for the A/E's professional errors and omissions. Although traditional construction bonds did not include coverage for such issues, it is now relatively easy to find sureties who are willing to bond the entire project, including professional liability. Such coverage is usually contingent on the maintenance of appropriate professional liability insurance coverage. It may be necessary for the design-build team to consult with the surety before reaching final agreement on these issues.

Contractual indemnity and contribution.

Indemnity and contribution are two different but related risk-shifting devices. They are ordinarily explicit provisions in the applicable contract which require

one party to reimburse the other party for part or all of a loss that is incurred to third parties. The difference between contribution and indemnity is how completely the risk is shifted to the other party. Contribution shifts a portion of the risk or loss to the other party, usually proportional to the relative culpability or fault of the two parties. Indemnity is an "all or nothing" concept. The indemnitor defends and/or reimburses the indemnitee for 100% of the indemnitor's risk or loss. Thus, at least in theory, indemnity is a fair and equitable risk-shifting device only when the indemnitor is 100% responsible for the risk or problems and the indemnitee bears no responsibility or risk at all.

Indemnity and contribution clauses can be and frequently are written into the contracts at each level of the construction project. There ordinarily are contribution or indemnity clauses in the design-build team's agreement with the client. Similarly, there will probably be indemnity or contribution clauses in each subcontract between the design-build team and subcontractors or subconsultants of every tier. Most design-build teaming agreements also include indemnity and contribution clauses to allocate risk and loss between the design-build team members. The teaming agreement may also describe the kinds or features of the contribution or indemnity clauses to be negotiated into the design-build team's various contracts with third parties.

Contribution and indemnity clauses may be quite legally complex. Many states have anti-indemnity acts which would render certain kinds of indemnity provisions void and unenforceable. In particular, the courts of some states refuse to enforce certain clauses whereby one party agrees to indemnify the other against the consequences of the indemnified party's own negligence. This is an area where there is no substitute for consultation by the design-build team members with legal counsel regarding the language and requirements of specific clauses.

With regard to allocation of risk and loss between the design-build team members, the simplest way of agreeing on appropriate indemnity and contribu-

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tion clauses is first to attempt to reach philosophical agreement in the abstract regarding how specific losses and risks should be shared. A common and workable agreement that most industry members recognize as fair involves identifying the various risks that may occur on a construction project. Then, for each risk, the design-build teammates agree on whether it falls into one of the following three categories: one for which the contractor has sole and complete responsibility; one for which the design professional has sole and complete responsibility; or one for which both parties share responsibilities in some unspecified ratio. An example of the first category would likely be construction worker safety. An example of the second category would likely be design calculations. Most risks fall into the third category of shared responsibility. The parties then agree that the contractor will defend and indemnify the design professional against those risks in category number one, and the design professional will defend and indemnify the contractor against those risks or losses which fall into category number two. The risks or losses which fall into category number three are subject to the contribution provisions, with the parties sharing any losses or expenses in accordance with their relative culpability or responsibility.

There are other collateral issues that should also be resolved. For example, which of the design-build team members will control the decision-making process in defense of a claim, including such key decisions as whether to settle, for how much, whether to enlarge the dispute by bringing in other third parties, etc.? Of course, the most critical question is how to divide the risk or loss when the contractor and design professional disagree as to their relative percentages of culpability. Procedures for resolving these and other disagreements are considered next.

Dispute resolution

Entire books have been devoted to dispute resolution in the construction indus-

try. Lawyers and other proponents of particular dispute resolution processes have different points of view. Some favor arbitration over litigation while others have the opposite opinion. Many advocate non-binding dispute resolution processes like mediation as a precursor to a binding approach.

Of course, these recommendations are made in the abstract. They are attempts to determine the best dispute resolution system in a vacuum without regard to the parties' specific situations or objectives. In design-build projects, the objectives of the design-build team include quick and fair resolution of any claims between them as well as maintaining a close business relationship for future projects. These objectives are different from those that a design professional or contractor is likely to have in a traditional project.

What dispute resolution processes are best suited for disputes between the members of a design-build team? If the design professional and the contractor are unwilling or unable to agree on their ratio of culpability for a particular incident of damage or loss, is there a "best" way of resolving this dispute? What dispute resolution provisions should be written into the teaming agreement? Some answers follow.

Claims involving third parties. Most disputes between the design professional and contractor on a design-build team involve third parties. The third party may make a claim against the design-build team, or the team may have a claim against one or more third parties. It is quite likely that the ratio of culpability between the A/E and contractor cannot be determined until after the claims involving the third party are resolved.

In situations in which a third party is adverse to a team of two or more allied parties, it is almost always in the third party's interest to drive a wedge between the allied parties so as to bring any disputes between them into the open. Conversely, it is virtually always in the interest of the allied parties to avoid or postpone any disputes between them and to present a unified front against the third party. As most lawyers, particularly litigators, instinctively know, the value of the third party's claim

or position may increase dramatically if the alliance between the other parties is fractured by infighting.

These considerations are particularly true of claims involving design-build teams. The natural animosity in a traditional construction project is between the design professional and the contractor. Their alliance in a design-build project makes it considerably more difficult for a third party to prevail in a dispute against them.

There are several reasons for this. First, the design professional and contractor between them have greater access to information regarding the project; there is virtually no information concerning the project that is not available to one of them. Second and similarly, the design-build team has greater resources—financial, personnel, knowledge—than either team member possesses alone. Third and probably most important, the design-build team's ability to take and advocate a single position creates extra likelihood that it will prevail in the dispute resolution process. For example, in a design-build project, a subcontractor who is seeking additional compensation or a change order for work that it claims was not described clearly in the plans will find the design professional and contractor united in asserting that the plans are perfectly clear and that the subcontractor was made aware at the onset of the project of the scope and nature of its work. In a traditional project, the subcontractor may have an ally at trial in the general contractor who agrees that the plans were vague, with the design professional denying any ambiguity and claiming instead that the subcontractor's misunderstanding of design intent was due to the general contractor's failure to discuss the issue at the pre-construction meeting. When the design professional and the contractor are pointing fingers at each other, the subcontractor is much more likely to prevail.

Accordingly, the teaming agreement should contain a clause specifically applicable to claims involving third parties. The design professional and contractor should agree that they will adopt a sin-

gle, mutually agreeable position, and that they will postpone any disagreements between them until after all claims involving third parties have been finally resolved. Only after resolution of the third-party claim should the team members begin a dispute resolution process between themselves to allocate any losses or costs.

There is one danger in such an agreement: It may take a long time to resolve the dispute with the third party. By the time that dispute is resolved, it is possible that the applicable statute of limitations may have passed. In that event, the design-build teammates would be barred from bringing actions against each other to allocate between them the loss to the third party.

This problem can be avoided simply by including a "tolling agreement" in the teaming agreement. A tolling agreement is an agreement by both parties that the statute of limitations will not bar any claims between them arising out of third-party claims. A simple version of such a provision would be the following: "With regard to any claims by one team member against the other arising out of or pertaining to the design-build team's dispute with any third party or parties, the applicable statute of limitations shall not commence to run until the claim involving the third party has been finally resolved."

Sequence of dispute resolution actions.

It is more likely that the project representatives of design-build team members would be able to resolve a dispute between them than could representatives of a design professional and contractor in a typical project. In traditional projects, the design professional and contractor typically occupy adversarial roles and have no particular expectation of continuing to work together on other projects. Design-build teammates, hopefully, build a certain level of trust between them and know that each of their companies wants to maintain good relations with the other for future projects. Nevertheless, even in design-build projects, there are some disputes that simply cannot be resolved by negotiation between each team member's project representatives.



THE NATURAL ANIMOSITY IN A TRADITIONAL CONSTRUCTION PROJECT IS BETWEEN THE DESIGN PROFESSIONAL AND THE CONTRACTORS.

For disputes that project representatives cannot resolve, I recommend that the teaming agreement explicitly require each party's senior management, preferably the president or CEO, to meet in good faith to attempt to resolve it. Senior management may be more likely to resolve the dispute than project representatives. Each company's president is more likely to be focusing on the "forest" than the "trees" with regard to their mutual business relationship. The project representatives' egos, stature and possibly compensation may be a function of the outcome of the project, creating a counter-incentive to settlement.

The process of moving disputes up the corporate ladder to senior executives is called "step negotiations." It is a dispute resolution method commonly used in other organizational structures. In design-build construction projects, it serves the additional purpose of letting the president or CEO be the person to decide that it is worthwhile to escalate the dispute to the next stage.

If the CEOs cannot reach a compromise, the next stage should be non-binding mediation. Mediation has become an increasingly popular method of alternative dispute resolution. Even the standard form American Institute of Architects documents now require binding mediation as a precondition to arbitration or litigation. Mediation is essentially a structured negotiation assisted by a neutral, third-party facilitator. It is beyond the scope of this article to describe the details and procedures of mediation or to recommend strategies. However, the teaming agreement should require the parties to engage in good faith in non-binding mediation as a prerequisite to any further dispute resolution procedures for two reasons.

The first reason to use mediation is that it works. The overwhelming majority of disputes submitted to mediation, well more than 90%, ultimately settle prior to a trial or arbitration. This is particularly true when both parties approach the mediation in good faith and have a vested interest in continuing to work with each other. It is a dispute resolution procedure

well suited to disputes between design-build team members.

The second reason for design-build team members to employ mediation is that it is likely the last chance to preserve the relationship between them. It is very rare for a design professional and contractor who "go to war" (i.e., engage in a trial or arbitration against each other) to be able to continue working together afterwards. Mediation is an option short of all-out war. When it is successful, it results in a voluntary agreement by both parties to settle the dispute. Of course, there is an element of coercion involved, but the coercion derives from the business and legal pressures on the parties, not a jury or arbitrator imposing its will on two litigants. Furthermore, mediation can result in a creative resolution of the dispute, such as one which incentivizes the parties to continuing working together.

If the mediation is unsuccessful and at least one of the parties is determined to prosecute the claim, then there is little alternative but to submit it to some kind of binding dispute resolution process—either arbitration or litigation. There are advantages and drawbacks to each approach, and either may be included in the design-build teaming agreement. However, for several reasons, the use of binding arbitration when the dispute is between the design-build team members is probably the wiser course.

Both members of a design-build team are experienced construction industry professionals. They expect any dispute to be decided in accordance with proper and fair construction industry principles. These principles often follow the literal requirements of the law, but not always. Arbitrators in construction disputes have been known to fashion remedies that they believe to be proper and fair even if they are not the same resolution issues that a court of law would impose. Thus, an arbitrator's decision is more likely to conform to the parties' expectations and is less likely to be "random" than a jury's or even a judge's decision.

The key factor is the identity of the person or persons making the decisions and imposing the solutions. Arbitrators are also construction industry profession-

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als or construction lawyers with significant industry experience. In contrast, judges are legal professionals but usually without any understanding of the construction industry. Not only do juries rarely have any experience with typical construction industry disputes, but they are often composed of twelve (six) under-educated citizens who were unable to find an excuse to avoid jury duty. In my opinion, an arbitrator is more likely to "do construction justice" than a judge or a jury.

Many construction disputes involve two parties with different levels of knowledge and experience. For example, in an owner-contractor dispute, the contractor may want a construction industry professional to make the decision, but the owner may want a judge to apply the literal language of the contract regardless of its implications or consequences for the construction industry. In contrast, when there is a dispute

between design-build team members, the dispute is rarely over application of the literal language of the contract and more often concerns the fair resolution of a disagreement in light of typical industry practices applicable to the project. For such disputes, an arbitrator is more likely to impose a reasonable and satisfactory result.

Conclusion

Potential design-build team members should consider using this article, and the others in this series, as a checklist, not as a blueprint. It contains many of the author's personal recommendations which may not reflect the parties' preferences. But as long as the team members use the article to spot the potential issues, they should feel free to disregard those recommendations and to substitute different procedures or resolutions upon which all agree. ■