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Owner Friendly Documents Spell Trouble

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Recent industry publications bring the news that the Construction Owners Association of America has promulgated a new series of standard contract documents that purport to restore balance to the relationship between owner and designer. The documents derive from the proposition that architects and engineers have too successfully limited their legal exposure in the AIA and EJCDC standard documents. Not only is this proposition a dubious one, but the new documents, because they are founded on misunderstanding, are likely to cause much more trouble than they resolve.

One can perhaps appreciate that owners would tend to mistrust documents developed and proffered by one of the other parties to the typical triangular arrangement of Owner-Architect-Contractor, and when they see liability limitations protective of the designer imposed in the language, that mistrust is augmented. In assuming they are getting the short end of the stick, however, owners are missing several points that explain why the documents are drafted the way they are and why they have struck a fairly workable balance.

The most significant point is an economic one. The ultimate value of a project, of course, inures to the owner, not to the contractor or designer. It is the owner who will have a building, a structure, a system to use. This concept underlies, for example, the notion of betterment in the legal treatment of design defect claims. Even if the designer omits the sprinkler system required by Code, the building has to have it anyway; while it may be appropriate to charge the designer with the increased cost of adding the system later, it is unfair to make the designer pay the entire cost of a necessary system simply because the designer neglected to put it in the plans to start with. Because the owner acquires the asset created by the project, it is equitable to impose on the owner some of the costs of uncertainty, i.e. contingencies.

A broader economic point is also missed in the COAA approach. The cost of a designer's performance, and therefore his fee, is directly related to the amount of responsibility imposed on him. If he is made responsible, for example, for ensuring the contractor's conformance with the design documents, then he will have to undertake, and bill for, a much more extensive inspection and supervision program than is typical under the traditional arrangement. As Milton Lunch has recently pointed out, this harks back to the days of the master builder, and if owners want that level of involvement by the designer, they will have to pay for it. My guess is they won't want to.

Some of the people involved in the development of the new documents have commented that the impetus for some of the specific provisions was frustration at the lack of a specific performance standard for the design professional in the standard contracts and application of the "economic loss rule" to disputes between owner and designer. Courts do often become confused over the interaction of these two concepts; the courts of my own state of Virginia have generated a considerable haze in this area. Here is what I think the law purports to be in most jurisdictions (how's that for a caveat?):

A designer is not held to a standard of perfection in creating his design and the design documents, and he does not warrant the plans or guarantee the success of the ultimate structure. Instead, his performance is measured against that of a "reasonable" professional in the same or similar circumstances. To establish liability under this regime, the owner must prove that a reasonable architect would not have made this or that particular error. All too often this is easily done, because courts focus solely on aspects of the project that went wrong rather than evaluate the designer's performance as a whole. But this "reasonable care" standard is at least intended to recognize that perfection in an enterprise as complex as construction is, if not unattainable, at least economically infeasible. Again, owners simply would not pay for the level of effort necessary to insure that every detail has been accounted for.

The economic loss rule should have nothing to do with evaluation of liability under the standard of care. Properly applied, the economic loss rule merely says that damages for economic loss alone, as opposed to injury to person or property, cannot be recovered under a tort theory of liability, i.e. negligence. The rule recognizes that economic risks and expectations are, or should be, allocated by agreement of the parties and it encourages courts to give effect to that allocation. It therefore permits only those with whom one has a contract to sue for these losses. Tort law, on the other hand, is meant to govern conduct, and redress misconduct, that affects the health and safety of persons or the integrity of property, societal interests independent of what the contracting parties would consider. Thus, any victim of a tort can sue.

So, what of the owners' complaint? Aren't they right, that the traditional contract documents, to which the economic loss rule forces owners to rely on, omit any standard of performance? The answer should be "no." Reasonable care is the contractual measure of performance unless it is altered by contract. Confusion arises because this standard looks just like the "negligence" standard, but its use should not result in the designer being vulnerable in negligence for economic loss; the duty of reasonable care is imposed solely by the contract, not by law, and the economic loss rule should still limit actions to those by parties to the contract.

If the courts misapply the economic loss rule ó and there is a lot of that going around ó the contractual solution is not to assume there is no standard of care and, as COAA proposes, impose a more exacting standard. Instead, the contract should clarify that the usual professional conduct, i.e. ordinary care, is expected. If your owner wants more and tries to impose a COAA sort of contract on you, beware, and make sure you carefully assess and account in your fee for the costs of compliance with the higher standard.

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