Article originally appeared in the Summer 2009 issue of *The Professional Engineer*

Study Those Contracts

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Engineers are sometimes presented with a contract drafted by their client, or are presented with one of the form contracts such as AIA or EJCDC, which often have been modified. Most engineering firms have their own custom made contracts. No matter what type of contract the engineer is dealing with, he/she will want to pay particular attention to the following contract provisions during a contract negotiation. This article is not meant to provide an exhaustive account of all of the material terms that should be reviewed in a contract negotiation, and it is recommended that you consult you attorney with any questions about contract drafting or negotiation.

When engineers have not been paid for services provided under a contract and need to involve an attorney in the collection on the past due account, the engineer may wonder if he/she can collect the attorney's fees incurred in the collection? The answer is maybe. North Carolina does have a statute that allows for the awarding of attorney's fees for debts owing under a contract, but the contract must specify that the engineer has this right if collection procedures become necessary. The statute limits the amount of attorney's fees collectible to 15% of the amount owing, and the debtor must be provided with five days written notice within which to pay the debt before becoming responsible for the engineer's attorney's fees.

The engineer will also want to collect interest on any past due accounts. Interest may be collected in two portions: pre-judgment and post-judgment interest. The judgment refers to an entry of judgment made by a judge. The statutory rate for interest in North Carolina is 8% per annum. However, the interest rate may be increased by contract, up to a maximum of 1.5% per month (18% per annum). Therefore, the engineer should specify in the contract that the client will be responsible for interest on any past due accounts accruing in the amount of 1.5% per month for both pre- and post-judgment interest if the engineers wants to collect the maximum amount of interest allowed by law in North Carolina. When dealing with a non-paying client, the engineer may be satisfied to finally receive payment of the principal amount due (or a portion) and move on to a better client. On the other hand, if the engineer needs to pursue payment through litigation, the right to collect interest is available. The engineer is well-advised to make sure assessment of interest is covered in his/her contract.

With the *Blaylock* decision handed down by the North Carolina Court of Appeals in 2008 (see article in the Spring 2008 edition of *The Professional Engineer*), engineers will want to consider the use of limitations of liability clauses in their contracts. Limitation of liability clauses can be used by engineers to limit their contractual liability on a project to an agreed upon amount with the client. Typically, the limitation on liability is capped at either the (1) amount paid by the client to the engineer under the contract, (2) amount of insurance coverage obtained by the engineer, or (3) a stipulated amount, such as $50,000.

The limitation of liability clause should not be contained in small-font boilerplate language or hidden on the back page of a proposal. The language of the clause should be clear and unambiguous. The better practice is for the engineer to raise the issue of limitation of liability with the client along with their agreement on a scope of work and contract price. The client, however, may not be willing to agree to the limitation of liability clause. By agreeing to the limitation, the client is foregoing the right to pursue certain claims against the engineer above the limitation amount. This could be a large release of liability by the client, potentially hundreds of thousands or even millions of dollars. The engineer will need to consider the relationship with the client along with the current work environment in determining whether to modify or remove the limitation of liability provision if the client requests it.

Engineers should consider inclusion of an alternative dispute resolution clause ("ADR") in their contracts. In an ADR clause, the parties typically agree to resolve all of their potential disputes arising under the contract through mediation, arbitration, or a combination of the two. Resolving a dispute through ADR is typically thought to be less expensive and faster than litigation and provides the parties with some control over the process.

In mediation, the parties attempt to settle their dispute with the help of a neutral third party, the mediator. Mediation is non-binding, meaning the dispute is only settled if both parties agree. The mediator cannot force a settlement nor does the mediator decide the case as would an arbitrator or judge. The location for the mediation should be specified in the mediation clause. The engineer can choose the location of his/her home office or another location convenient to the engineer such as the project location. If the location is not specified, and the client and/or project are in another state, then a dispute can arise over the location of the mediation. While contractual mediations can typically be held without specifying any procedures or rules in the contract, the parties can agree to conduct the mediation under a set of rules such as the American Arbitration Association's ("AAA") Construction Industry Mediation Procedures.

Arbitration is more similar to litigation than mediation. Instead of a judge, the parties select an arbitrator or a panel of arbitrators to hear the dispute and render a binding decision. The parties will present evidence through exhibits and testimony before the arbitrator in a hearing, similar to the trial. Arbitrators can be someone with significant experience in the construction industry such as a construction attorney, an architect, or an engineer. The engineer can specify in the arbitration clause that the arbitrator have certain experience or qualifications. Thus, the parties to the dispute may feel that the arbitrator is better suited than a random judge to consider the complex issues that arise in a construction project. Arbitration can result in a faster resolution of the dispute and lower costs than litigation because the parties are not at the mercy of the trial court's schedule and the North Carolina Rules of Civil Procedure. In arbitration the parties can agree to limit the amount of discovery. The parties can agree to set a ceiling on the amount of interrogatories, depositions, and exhibits. The parties can also agree to limit the length of the arbitration hearing.

Arbitration clauses in North Carolina do not have to specify the procedures and rules to be used in the arbitration in order for the clause to be enforceable. The North Carolina Revised Uniform Arbitration Act ("RUAA") statute provides a minimum level of procedures and rules and sets forth the arbitrator's authority. The AAA Construction Industry Arbitration Rules are commonly included in design and construction contracts and provides more extensive procedures and rules than the RUAA. Some parties, however, prefer to draft their own procedures. Parties must be careful in designing their own procedures, however, because if the procedures are left to be developed after the dispute arises, the parties can spend many months negotiating with each other over the procedures. If the parties are unable to reach an agreement on the procedures and arbitration schedule, they may need to involve the arbitrator. The arbitration provision in the contract should set forth the location for the arbitration hearing, or else that may be subject to negotiation as well.

The ADR clause may provide for mediation, arbitration, or a combination of the two. If mediation is selected in the ADR clause without arbitration, then the clause should specify that the dispute will be subject to litigation in the event that mediation is unsuccessful. Typically if mediation and arbitration are included in the ADR clause then arbitration is held in the event that mediation is unsuccessful. Once the dispute arises, the parties can agree to waive the requirement for mediation if they feel arbitration is a better way to resolve the dispute.

There are many other contractual provisions that engineers should pay careful consideration to when drafting or negotiating a contract. At a minimum, engineers should make sure they address collection, limitation of liability, and ADR provisions in their next contract.

Bio

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