

Between the two

Straining contractor/subcontractor relationship



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When prime contractors and subcontractors enter into written agreements, a potential exists for conflict between what the prime contractor is required to deliver to the project owner and what the subcontractor has agreed to deliver to the prime contractor.

Partial

In *Encon Utah, L.L.C. v. Flour Ames Kraemer, L.L.C.* 2009 WL 172438 (*Utah*), a

contractor, Flour Ames Kraemer LLC, entered into a design-build contract with the Utah Department of Transportation (UDOT) for construction of the Legacy Parkway. Flour Ames Kraemer, in turn, entered into a subcontract with Encon Utah LLC to manufacture, deliver and install bridge girders.

The UDOT contract contained a typical Termination for Convenience clause that allowed the department to terminate the contract for any reason. It also limited the contractor's recovery upon termination to "out-of-pocket costs" for work performed, including reasonable overhead and profit on those costs, and reasonable costs occasioned by the termination. However, in no event could the contractor's compensation for termination exceed "the value of the Work performed" as established in the contract.

The subcontract between Flour Ames Kraemer and Encon also included a Termination for Convenience clause quite similar to the one in the prime contract. However, that clause contained no "value of the work" cap on the subcontractor's recovery in the event of termination. The subcontract also included provisions incorporating the prime contract stating that in the event of conflict between subcontract and prime contract terms, the latter governed. When environmentalists obtained an injunction against UDOT enjoining construction of the project, UDOT issued a partial termination of the contract for convenience and Flour Ames Kraemer, in turn, partially terminated Encon's subcontract for convenience. A dispute between Flour Ames Kraemer and Encon ensued when Encon's costs, including allowances for overhead and profit, exceeded the subcontract value of the work it had completed and Flour

Ames Kraemer was faced with the prospect of paying Encon in excess of \$1 million more than it was entitled to receive from UDOT for Encon's work. After the trial court sided with Encon and refused to limit Encon's recovery to the value of the work, Flour Ames Kraemer appealed.

Flour Ames Kraemer believed it had adequately covered the gap between prime contract and subcontract requirements.

Different reads

The Supreme Court of Utah agreed with Flour Ames Kraemer that the subcontract Incorporation by Reference provision—when read alone—incorporated the entire prime contract. However, it pointed

to another provision in the subcontract that must be read along with the Incorporation by Reference provision, and held that the prime contract Termination for Convenience Clause was not incorporated into the subcontract. Accordingly, the subcontract Termination for Convenience clause governed and Encon's recovery was not limited to the value of the work.

The Court cited the Description of Work provision of the subcontract, which stated, in pertinent part, that Encon "understands and agrees to comply with the [prime] Contract, as applicable to the Scope-of-Work of this [sub]Contract."

The court ruled that the underlined language in the Description of Work provision substantially limited the otherwise broad language of the Incorporation by Reference provision to cover only those prime contract provisions that directly addressed manufacturing, delivering and installing the bridge girders. The incorporation language did not include more general "commercial terms" including the Termination for Convenience clause. 📄

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