

# Contract Risk Allocation

Together, We Build Saskatchewan



# Welcome and Introductions

- Session hosted by Construction Industry Advisory Council
- Introductions – share your:
  - Name
  - Title
  - Organization
  - Favourite Fall activity



# Presenters



**Troy Baril** - Partner, Miller Thomson



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Construction Management



# Industry Working Group

- Construction Advisory Council set up working group
- Group tasked with developing a series of info-sheets and holding education sessions on contract risk clauses that are perceived as challenging
- GOAL: To improve communication and understanding and achieve a more appropriate risk allocation



# What is “Risk”

- Risk exists as a consequence of uncertainty

Examples of Risk in Construction Projects	
Weather	Unexpected conditions
Errors in cost estimating and/or scheduling	Delays
Financial difficulties	Strikes
Faulty materials	Faulty workmanship
Operational problems	Inadequate plans and/or specifications
Natural disasters	



# Getting to Risk Allocation

- Construction contracts include a compact of rights and obligations between the parties, by which the parties allocate responsibilities between themselves in respect of the risks that may occur.



# Getting to Risk Allocation

- The impact of risk can be properly defined by three key elements:
  - The asset that is to be constructed by the contractor;
  - The time at which the asset must be completed by the contractor; and
  - The amount the owner is obligated to pay the contractor.



# How to Allocate Risk

- Proper risk identification and equitable distribution of risk is the essential ingredient to increasing the effective, timely, and efficient design and construction of projects.





# How to Allocate Risk

- Risk should be allocated to a party IF:
  - The risk is within **that** party's control;
  - The party can transfer the risk, for example, through insurance, and it is most economically beneficial to deal with the risk in this fashion;
  - The preponderant economic benefit of controlling the risk lies with the party in question;



# How to Allocate Risk

- Risk should be allocated to a party IF:
  - To place the risk upon the party in question is in the interests of efficiency, including planning, incentive and innovation; and/or
  - The risk eventuates, the loss falls on that party in the first instance and if it is not practicable, or there is no reason under the above principles, to cause expense and uncertainty by attempting to transfer the loss to another.



# Group Question

- Owners:
  - How do you make risk allocation decisions internally?
- Consultants/Contractors:
  - How often do you have concerns regarding risk allocation in contracts?
  - How often do you raise these concerns?
  - How receptive are other parties when you do?



# Risk Allocation Concerns

- Increasing incidents of downloading risks on to consultants or contractors that may be best retained by the owner
- Savvy contractors will price in risk or choose not to bid
- Less savvy contractors will miss this and expose project to risk



# Group Question

- Contractors/Consultants:
  - How does a difficult risk allocation change the way you bid?
- Owners:
  - In determining risk allocation, do you consider the increased cost or risk of losing bidders?



# Issues Identified by Industry

- Over the past year industry has identified several contract issues of concern. The first five we focused on were:
  - Award delays;
  - Holdbacks;
  - Indemnities;
  - Site Conditions; and
  - Unknown Conditions



# Info Sheets

- Introduce a single topic of concern
- Provide an example
- Address the typical original intent
- Identify why the clause is problematic
- Propose alternative options
- Suggest strategy for industry



# Award Delays

- Concerns with requiring contractors to hold price beyond 30 days
- Owners looking to provide time to evaluate
- Causes supply chain disruption
- Contractors will price this risk in
- Impact concurrent bidding and planning





# Award Delays

- Better options:
  - Don't require price holds beyond 30 days
  - If required, allow for price negotiations
  - Provide bid rankings during analysis or narrow list to top three to provide contractors with flexibility
  - Allow contractors to provide alternative price on bid forms for shorter awards



# Award Delays Discussion

- How often does this clause show up?
- What are some of the unintended consequences?
- What other options would allow the owner proper time to evaluate bids without shifting risk to the contractor?



# Holdbacks

- Concerns with any non-statutory holdback
- Owner attempting to ensure contractor performance or limit owner risk
- Holdbacks create cashflow issues and lead to contractor financing projects
- Cashflow restrictions limit ability of contractors to bid and pursue work
- Clauses are legally problematic



# Holdbacks

- Better options:
  - Rely on project team to assess progress billing and pay accordingly
  - Use performance bonds and labour bonds
  - Structure contracts to hold contractors accountable
  - Place a reasonable value on deficiencies and tasks



# Holdbacks Discussion

- How often are non-statutory holdbacks present in contracts?
- What kind of contract mechanisms might be more effective in ensuring performance and delivery?



# Indemnities

- Indemnification clauses have become very broad and sweeping, including parties not part of the contract
- Owners are looking to minimize their risk and assign all risk for all parties on the contractor
- Contractors cannot be responsible for things outside of their control



# Indemnities

- Better options:
  - Allocate risk to the party that is most in control of that risk
  - Discuss risk allocation with all parties
  - Consider limiting the contractor's indemnification in a reasonable way
  - Adopt CCDC indemnification wording



# Indemnities Discussion

- What has led to the increased scope of Indemnity clauses?
- How often are these clauses appearing in contracts?
- What other strategies might help owners accomplish their objectives with these clauses?





# Site Conditions

- Site condition clauses shift liability to the contractor for things like ground conditions regardless of whether accurate information was provided to them
- Contractors can't price this risk in which could led to catastrophic impact
- Contractors can't do site investigation work without guarantee of award



# Site Conditions

- Better options:
  - Provide as much site information as is possible
  - Revise the clause to note that unknown or changed conditions will be addressed when encountered



# Site Conditions Discussion

- How often do site conditions clauses appear in contracts?
- What other strategies might work to allocate this risk and manage it better?



# Unknown Conditions

- These clauses, common during COVID-19, put the entire risk of pandemic or unknown delays on the contractor
- Owners are attempting to limit their risk
- Contractors can't be held responsible for something beyond their control



# Unknown Conditions

- Better options:
  - Consider schedule and cost relief if unknown conditions are encountered
  - Allocate these risks to the party most in control of the risk



# Unknown Conditions Discussion

- Outside of the pandemic, was this type of clause common?
- How have contractors dealt with them?
- What other strategies might work better for owners?



# Small Group Discussion

- What other contract issues can create risk allocation imbalances?
- How can owners, consultants, and contractors collaborate on the issue of contract risk allocation?



# Next Steps

- Share your examples and feedback with us
  - [president@scaonline.ca](mailto:president@scaonline.ca)
- Review the info sheets and provide notes
- Working group to develop new info sheets
- If you're interested in engaging on this topic, let us know





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