









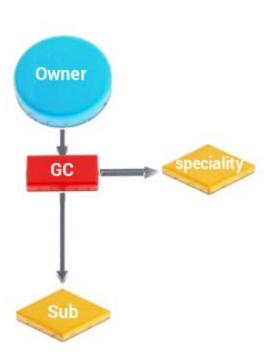
Risk Management

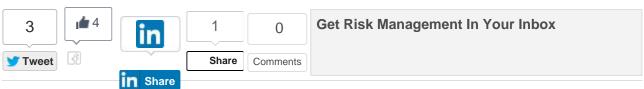
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Using Flowdown Clauses for Risk Allocation

By Christopher R. Opalinski & Timothy D. Berkebile Published On: Friday, February 20, 2015 12:45 PM







isk allocation should be at the center of every construction contract negotiation. Conscientious owners, contractors, subcontractors and design professionals should attempt to limit their own legal exposure by shifting duties, obligations and liabilities to

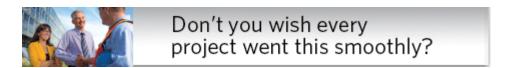


other parties in the contracting chain, as leverage allows.

The use of a flowdown clause is one important method of achieving this goal. On its face, a flowdown clause pushes risks and obligations, and shares rights and remedies, assumed under a separate contract down the contract chain to another contracting party. For instance, an owner may require a contractor to pass down certain obligations to its subcontractors. Section 5.3 of the AIA A201 does this by requiring the contractor to include language in its subcontracts by which subcontractors agree to assume toward the contractor all the obligations and responsibilities that the contractor assumes toward the owner with respect to the subcontractor's work. In addition it provides the subcontractor with the benefit of all rights, remedies and redress against the contractor that the contractor has against the owner. Similarly, Article 2 of the AIA A401 mutually binds the contractor and subcontractor to the terms of the contractor's agreement with the owner to the extent such terms apply to the subcontractor's work.

Strategic use of flowdown clauses can provide benefits to contracting parties in a number of ways. Owners obtain assurance that subcontractors are on the same page as the contractor, at least contractually. Contractors may use such a provision to limit the subcontractor's right to progress payments or delay damages or increase the subcontractor's financial obligations per the terms of the various rights and remedies in the prime contract.

Obtaining the intended benefits of a flow-down provision requires that the contracting parties fully appreciate the way in which all of the "flowed-down" language and the parties' contract are intended to interact. It is virtually certain that a lazily constructed flow-down provision will have unintended consequences for the parties. Therefore, it is vital that all contracting parties have a firm grasp of what is required by the terms that flow down and whether any potential conflicts or ambiguities are created between the two agreements. In that regard, it is crucial that the parties carefully define what terms are included or excluded from the scope of the flow-down clause. For example, payment terms are often the subject of such exclusions.



To the extent the contract may contradict with flowdown language, the contract should carefully set forth – either specifically with regard to certain provisions or more generally in an order of precedence clause – which language governs. This is particularly the case with damage limitations, "pay-when-paid" clauses and disputes provisions. It is important to understand that certain clauses that make sense between the owner and contractor may not make sense further down the contract chain depending on the circumstances. The party to whom the additional obligations and responsibilities flow down to should make every effort to further flow such obligations and responsibilities down to lower-tiered subcontractors or suppliers.

Flowdown clauses can be a valuable risk management tool, but they must be properly understood and carefully applied.

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Christopher R. Opalinski



Chris Opalinski's litigation practice at Eckert Seamans Cherin & Mellott, LLC involves a broad range of commercial disputes with a concentration in the area of construction law. Chris represents owners, developers, design professionals, prime contractors, subcontractors, material and equipment suppliers and sureties in both the public and private sectors, nationally and internationally, on all types of construction claims before various state and federal courts and arbitration panels. He has extensive experience drafting construction contracts, advising on contract administration and project management matters and handling cases involving all types of direct and

indirect cost claims, including claims for delay, acceleration, loss of productivity, default, termination, extra work, defective specifications, design errors and omissions, differing site conditions, defective construction, product failures, bid protests, mechanics lien and payment and performance bond claims. Chris serves on the Firm's Executive Committee and is a member of the Firm's Board of Directors. Chris also has a broad range of experience in a variety of commercial and business litigation, including misappropriation of trade secret, unfair competition, shareholder disputes, breach of contract and real estate disputes. Eckert Seamans Cherin & Mellott, LLC is a national law firm with over 375 attorneys located in offices throughout the eastern United States. The firm's clients represent nearly every facet of the economy, including multinational corporations, small businesses, nonprofit institutions, municipalities, government agencies and individuals. Contact Chris at copalinski@eckertseamans.com; 412.566.5963.

Contact: Email Website

Timothy D. Berkebile



Tim Berkebile's practice at Eckert Seamans Cherin & Mellott, LLC includes construction litigation and commercial litigation matters, with a focus on construction litigation and advising. His construction law practice has involved many types of claims on both public and private projects, including mechanics' liens, bond claims, nonpayment, delay, impact, loss of productivity, differing site condition, defective work, design defect, construction-related products liability, extra cost and default. Eckert Seamans Cherin & Mellott, LLC is a national law firm with over 375 attorneys located in offices throughout the eastern United States. The firm's clients represent nearly every facet of the

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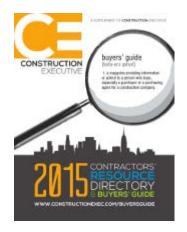
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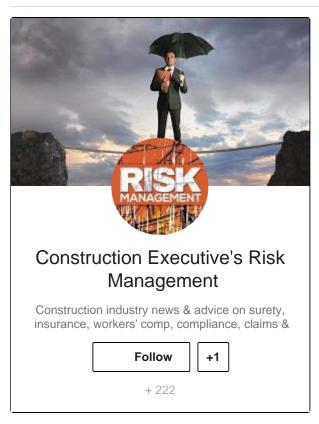


Marla McIntyre

For more than 25 years, Marla has educated contractors, subcontractors, bankers, public and private owners, legislators, educators, insurers, and attorneys on contract surety bonding and

construction issues. She's the author of more than 100 articles, including an award-winning series for the Risk Management Association, and has written books, directories, informational brochures, and reports. Her extensive construction and risk management background includes stints as executive director the American Subcontractors Association of Metro Washington and the Surety Information Office. She also worked for Associated General Contractors of America, National Conference of States on Building Codes & Standards, Association of Major City Building Officials, and National Concrete Masonry Association. She served on the boards of the Construction Writers Association, and American Council for Construction Education and was active in the Construction Owners Association of America.

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