BEST PRACTICES

What the Contract Doesn't Say

implied obligations in every contract

By Christopher S. Drewry

In reviewing contracts with our clients, we frequently advise on the various key risk management clauses in a construction contract. Terms governing payment, delays, claim notices, change orders, indemnity and insurance often dominate the discussion. We then have to advise that there are a number of *implied* obligations that, by law, are read into every contract. This can be a frustrating realization. Not only do you have key terms of which you must be aware, but you also have to worry about what your contract does not say?

Unfortunately, the answer is "yes" if you want to fully understand how your contract will be interpreted and applied to your company's performance on a project. A fundamental tenet of contract law is that certain "implied" terms and responsibilities exist between two contracting parties even if they are not expressly stated. Implied terms can help fill in the gaps or proverbial cracks in a contract.

Generally speaking, other than the express terms of the contract, there are other sources of the law forming the contractual relationship on a given job. ***First,*** there are statutes and laws that will be read into a contract and which will control over any conflicting contractual term. ***Second,*** there are the implied terms that a court (or arbitrator) will read into a contract. ***Third,*** there is the course of dealing between the parties during the life of the project. A court will look at how the parties treat the contract terms and conditions. While it will not imply terms that contradict express terms of a contract, a court will imply or "read in" such terms if necessary to give meaning to the intentions of the parties.

PREVAILING LAWS AND CODES

Laws and codes existing at the time and place of the making of the contract are considered implied terms of the contract documents. The parties are presumed to have understood the law at the time they entered into a contract. Generally, all laws in force on the date of the agreement form a part of the agreement without any express statement to that effect. A problem may arise when a law or code is enacted after the execution of a contract. Absent language demonstrating the parties clearly allocated for such a risk, the change in code will generally not be deemed to be included as a term of the contract. Obviously, this result under the law is not a free license to ignore changes in the law or technical codes. Another consideration is to provide for a change order and price increase if compliance with a change in the law or code increases the cost of performance.

Additionally, where there is a conflict between the terms of a contract document and the requirements of a statute, the requirements of the statute will always prevail. For example, if the state mechanic's lien statute prohibits no-lien contracts on commercial jobs, then a contractual attempt to create such a no-lien contract would conflict with the statute and the provision would not control. Another example lies in the payment or performance bond that contains terms that conflict with a public works statute, such as an attempt to shorten the time period for asserting a bond claim. In short, contracting parties must always comply with statutes.

CUSTOM AND USAGE

Standards of "custom and usage" are frequently applied by courts to resolve contract interpretation disputes. A court will consider standard practices in the industry in an effort to determine whether a party's particular course of conduct was accepted or anticipated by the parties to the agreement. The law generally holds that when considering the standard of "custom and usage," a party who is carrying on a known usage in a trade is deemed to have contracted with reference to the usage, unless the contrary clearly appears.

The impact of geography can be equally important. Although there are state and national standards common to all construction, what is standard practice or "custom" in one city, state or region of the country may be different than another city, state or region. In a dispute involving defective work, for example, a contractor may introduce evidence of its standard practice for its trade or in the region where the work was performed. More typically, "custom and usage" may be used to aid in the interpretation of contract documents and specifications to show that a particular word or phrase has a customary technical meaning in the trade. However, there are caveats to this standard. The custom and usage must be well-established, certain, uniform and reasonable. Such standards may not carry

the same persuasive weight as other forms of evidence, such as course of dealing.

STANDARD OF REASONABLENESS

Although it may seem as if logic and reason do not often carry the day in litigation, courts frequently use standards of reasonableness when resolving disputes. Courts will seek to find what is fair, just, and sensible. Implied terms must, by definition, be reasonable. For example, where parties have failed to agree on a price for the performance of work, a judge will likely find an implied agreement to pay the reasonable value of the work. Likewise, where contracting parties have failed to specify a time for performance, the court will likely find that performance was due within a reasonable time.

IMPLIED CONTRACTUAL DUTIES

While the above implied terms tend to impact the interpretation of a contract, there are two very important implied duties that can serve as the basis of a claim against another party: (1) the implied duty not to hinder performance; and (2) the implied duty of skill and fitness.

Duty Not to Hinder Performance: It is an implied condition of every contract that neither party will hinder the other in its discharge of the obligations imposed upon it nor increase its cost of performance. Where one party hinders or precludes completion of contractual duties, that party is liable for breach of the contract. This implied duty has particular application to issues of schedule delay. States typically recognize that delay damages can be awarded for breach of an implied or express contractual promise. As such, this implied warranty can be a valuable remedy in pursuing claims for increased costs in addition to a contract action.

Contractor Warranty of Skill and Fitness: An equally powerful remedy is the contractor warranty of skill and fitness. Although not expressly stated in the contract documents, a contractor impliedly warrants that it will perform its work in a workmanlike manner and that the resulting improvement will be reasonably fit for its intended purpose. This implied warranty is frequently utilized in asserting a claim for defective work, wherein a party argues that a contractor or subcontractor did not perform the work "skillfully" or in a "workmanlike" manner or otherwise failed to adhere to typical standards for construction of that type of work. However, be mindful of how this warranty will defer to the standards of workmanship established in the contract.

CLOSING THOUGHT

Always remember to read and understand your contract but also be aware what is not in your contract! ■

about the author

Christopher S. Drewry is a partner with the law firm of Drewry Simmons Vornehm, LLP, in Indiana (**www.dsvlaw.com**), where he focuses his practice on construction law and litigation, as well as labor and employment law and litigation. Chris is a current member and Past Chair of the Construction Law and Litigation Committee of the International Association of Defense Counsel, and he can be reached at cdrewry@dsvlaw.com.