

Contract Negotiating **Tips**

By David B. Ratterman

Good negotiators do their homework. Here are some tips for making your next negotiation session productive for both you and your potential project partner.

One of the great benefits as an attorney representing clients in the construction industry is the opportunity to interact with a variety of dynamic and interesting people. Sometimes, however, that interaction comes during extremely trying times, such as during contract negotiations.

Over the past 30 years, I have been privileged to observe a wide variety of negotiating techniques in those situations—some good, some bad. The tips that follow here are based on my reflections of those experiences and provide comment on what I have observed¹. I do not claim to be an expert on the subject of contract negotiations—be wary of anyone who claims to be an expert on this subject. Hopefully, however, these suggestions will be of benefit to the fabricated structural steel industry as a whole.

Preparation: Sizing Things Up

Good negotiators don't just walk into a room and start talking. They spend a lot of time doing their homework and preparing for the negotiations. They size up the project, they size up their potential project partners, and they size up themselves.

Sizing up the Project

Recognize that there are important factors that will be fleshed out in every negotiation. These factors will predict the potential for project disputes and the potential to avoid project disputes².

The leading factors to predict disputes include:

1. The contract documents are unclear in their definition of scope, responsibility, and contract requirements.
2. Poor communication in administration of the project or poor project management.
3. Lack of experience or capabilities on the part of one or more major participants in the project.
4. The risk and reward are out of balance: this includes situations where the project is under-funded.

The leading factors to avoid disputes include:

1. The ability to recognize and walk away from a contract that contains unreasonable and uncompensated risks.
2. Clear, complete contract documents with well-defined scope, responsibility, and requirements at all levels.
3. Involvement of experienced management and stable companies.
4. Project administration that includes thorough planning and systematic review, as well as evaluation of project conditions and prompt reaction as those conditions change during the course of the project.

Sizing Yourself Up

Determine the objective you want to achieve from the negotiation. Your approach to the negotiation could vary dramatically depending on your objective. Is your objective to:

- Maximize profit on a particular project?
- Cover overhead costs created by short-term holes in your shop or office schedule?
- Stay alive for another day?
- Establish an entrée for your firm in a new market?

Where are You on the Construction Matrix?

Once you've determined your objective, imagine a two-dimensional matrix. One axis defines the uniqueness of the project; the other axis defines the uniqueness of the product or service that you may be providing the project.

At the low end of the project scale are temporary structures or non-descript, minimalist shell buildings. At the high end are structures designed to house and protect those persons or objects that society values, or those structures that strive to achieve a status of great artistic merit and vie for public recognition, approval, and envy.

At the low end of the product/service scale is delivery of a commodity that is readily available and can be provided with comparatively small effort or risk. At the high end of the product/service scale is the rendering of a construction service or the providing of a unique product—either of which requires a great deal of skill and experience and involves a certain amount of risk.

Beware of Overly-Aggressive Lawyering

An initial, important disclaimer to set the tone for productive construction contract negotiations: don't turn your future over to a lawyer who doesn't understand your business. You must remain in control and understand what is absolutely required by law and what is not. You also must understand the potential consequences of following or not following your lawyer's recommendations in areas that do not involve strict compliance with legal requirements.

Those attorneys who draft contracts that place all the risk on other parties are not doing their clients or the construction project a favor—mostly they're just making a lot of future work for other lawyers.³ Clients, especially owners, who think they have "won" the negotiations often end up losing in the long run. To provide maximum, long-term value to most owners, construction contracts have to be fair to all concerned.

The more unique the project and the more unique the product or service you are providing to the project, the more risk you will have to assume, the more leverage you may have in negotiations, and the greater the potential reward you will receive if the project is a success.

Sizing up Your Project Partners

After you know your objective and have defined the relative point on the matrix at which you will be operating, you must recognize that you are entering into a partnership for the duration of the project—a marriage of sorts. You don't want it to end in divorce. Recognize that you will need to rely upon your project partners living up to their obligations. The other parties to your contract are going to be your partners, and you are going to be bound by your agreement. You may not have a voice in the selection of all the entities and individuals who will be your partners on the project. All partners present potential risks, and they must be evaluated like all other risks.

Formulating Your Negotiating Position

After you have sized things up, it's time to establish your negotiating position.

Society values people who provide value. Society also consistently rewards people who take reasonable risks and manage those risks wisely. Society seldom rewards richly those who shy away from any risk at all.

To optimize profits, you need to combine creativity and risk taking in a manner that adds value and places you in control of your own work product. In most instances you must assume that your competitors, who are willing to compete for the same work, will be able to match your price. You must formulate a strategy that will allow you to add value to the project other than price, even if low price is the primary selection criterion.

If you cut your price below the level at which you will make a reasonable, or any, profit, and you wish to remain in business, then you must receive proportionate value in some other area (to cover overhead, to develop a presence in a new market, etc.). The risk of further revenue loss on this particular project must be understood and must be capable of being controlled.

To minimize the potential for loss on all projects, you must minimize the potential for surprises and, in many regards, you must anticipate the future. You must anticipate that there will be change, and assure yourself that there is enough flexibility in the contract to allow change to be managed effectively.

Good negotiators take all of this into consideration when formulating their negotiating positions. After they formulate a risk/reward matrix for each contract issue that they anticipate could arise in the negotiating process, and develop something of an overall project matrix that correlates all of these potential issues together, they establish a "bail out" point on each matrix in advance of the face-to-face negotiations. The bail out point is the point below which they will have determined, in advance of the heat of the negotiation process itself, that they must walk away from the project. But they do not enter the negotiations with only one mandated outcome. They enter face-to-face negotiations prepared to be flexible.

Before they negotiate, they also size up the proposed contract language. When reviewing language in your own contracts, keep these things in mind:

→ Read difficult language out loud. It sounds stupid, but it isn't. Try it.

Recommended Reading

Robert C. Bordone, Deputy Director of Harvard Law School's Negotiation Research Project, suggests the following titles for further reading on contract negotiation. While most of the titles were not written with the construction industry specifically in mind, Bordone says their principles are applicable to anyone entering into contract negotiation.

"The general way you think about contract negotiation cuts across all industries," he says. "The issues are different, but the basic preparation framework is the same."

Architect's Essentials of Contract Negotiation, Ava J. Abramowitz, 2002

Getting to Yes: Negotiating Agreement Without Giving In, 2nd Edition, Roger Fisher, William Ury, and Bruce Patton, 1991

Getting Past No: Negotiating Your Way from Confrontation to Cooperation, William Ury, 1993

Bargaining for Advantage: Negotiation Strategies for Reasonable People, G. Richard Shell, 1999

The Handbook of Dispute Resolution, Edited by Michael L. Moffit and Robert C. Bordone, 2005

- If you don't understand the language, ask someone whose opinion you respect to read it and explain it to you. If you still don't understand it, then don't agree to it.
- Don't agree to performance requirements that cannot be quantified. Don't agree to do something foolish that can't be measured objectively, like providing "first class work." (I have actually seen such a provision in an engineer's contract with an owner.)
- Seek input from others in areas where you don't personally have the necessary expertise to evaluate the language and any risk involved (insurance, engineering, operations, scheduling, legal, etc.).
- Determine the actual risk presented by each instance of objectionable language. Plug this into your negotiating matrix. Develop a hierarchy of objectionable terms and determine the cost of dealing with the risk involved with each of these terms.

Face-to-Face Negotiating Sessions

Good negotiators are flexible and solve problems. When problems arise in the course of negotiations, good negotiators don't clam up or immediately bow their necks, they come back with multiple, alternative solutions. They place the burden back on the other side to choose one of the available alternatives.

Good negotiators discern: they know that the risk will change during the course of the negotiations as the form and substance of the deal changes. As it does change, good negotiators continue to re-evaluate and size up the risk. They place a price on the risk, and then they try to make the price match the risk or lower the risk to meet the price.

→ If a good negotiator can't control the risk, avoid the risk, al-

locate/transfer the risk, or insure against the risk, then he or she will walk away from the deal.

- Good negotiators are not bashful to talk price.
- Good negotiators are hard on problems but soft on people. They separate the people from the problem.
- Good negotiators are very careful about the use of words like “unreasonable,” “over-reaching,” “bad faith,” and the like, and they don’t over-react when these words are used by the other side.
- Good negotiators recognize that almost everything is subject to negotiation and that almost all negotiations are capable of being re-opened. Time and reflection heal a lot of bruised feelings and change a lot of positions.
- Good negotiators present themselves and their companies as competent, candid, and concerned. They act and look like professionals, and they make the other party want to be their partner.

Regardless of whether they represent owners, design professionals, or contractors, effective negotiators enter into potentially difficult negotiations in essentially the same manner. They solve problems. They add value. And they present themselves and their organizations as people with whom other professionals will be able to work with cooperatively to achieve common goals and mutual success.

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Notes

¹I have drawn extensively for this article from a book I reviewed not long ago for my friend and colleague Ava J. Abramowitz, J.D., FAIA. I recommend the book, *Architect's Essentials of Contract Negotiation*, John Wiley & Sons, Inc., New York, 2002, to anyone involved in the construction industry.

²These factors were derived from a comprehensive study undertaken by Victor O. Schinnerer & Co. See Abramowitz, *supra*, note 1 at 17.

³The general corporate attorney for an occasional construction owner, and other attorneys inexperienced in construction law, are the worst offenders. Their documents can do almost as much damage to a project as a category four Hurricane can do to a coastline.