

5 KEY TAKEAWAYS

Construction Contracts, Lease Agreements, and Other Real Estate Contracts

Kilpatrick partners **Brian Gaudet** and **John Livingston** recently presented on construction contracts, lease agreements, and other real estate contracts at the University of Texas School of Law 48th Annual Corporate Counsel Institute. Their presentation addressed critical contract considerations for developers, owners, tenants, and contractors across commercial leasing projects.

Key takeaways from their presentation include:

1

Lease construction provisions require careful structuring to properly account for delivery methods and allocation of risk.

Parties must clearly define whether the landlord or tenant is responsible for construction and how costs and risks will be allocated. The three primary delivery methods (landlord builds turnkey, landlord builds with an allowance, and tenant builds with an allowance) each carry different risk profiles for cost and construction management. Work letters should establish the structure of the construction process, including strict procedures and deadlines for design plan approval, change orders, substantial completion, and the disbursement of allowances, and the work letter should align with the underlying construction contracts.

Lease negotiations should address important issues such as insurance, building standards, and ownership of improvements from the outset.

Insurance requirements must specify coverage and limits for both landlord and tenant, as well as for the contractor, including additional insured designations and waiver of subrogation provisions. Parties should also clearly define building standards, including design specifications and signage, and address who owns the improvements at the end of the lease term, including whether the tenant must remove improvements or fixtures.

2

Force majeure clauses deserve close scrutiny and precise drafting.

Many force majeure clauses are poorly written and fail to clearly define triggering events, notice requirements, or the start and end of a force majeure period. Many clauses require notice from the start of a force majeure event, which produced some odd results during the covid pandemic. Notice should be tethered to expected/actual impacts to the project. For those projects susceptible to the impacts of hurricanes and tropical storms, Parties should consider proactively addressing practical issues such as evacuation and return time.

3

Price escalation clauses require a clear measurement framework to be effective.

While these clauses gained popularity during the COVID-19 era, their continued use should be carefully evaluated. Owners should consider negotiating price fluctuation clauses that capture both increases and decreases in costs. The two biggest challenges are how to measure escalation (whether through indexes or invoices) and how to verify that claimed escalation charges are legitimate and not masking contractor errors. Contracts should clearly define the baseline price, purchased price, and qualifying escalation amounts.

4

Supply chain risks demand proactive contractual protections, particularly for tariffs and advance material purchases.

Contracts should clearly address responsibility for tariff establishment or increases and whether tariff changes constitute a ‘change in law’ warranting a price adjustment. When materials are purchased in advance to mitigate delays and price increases, parties must address storage location, insurance coverage, risk of loss, bonding, warranty implications (since many manufacturer warranties begin upon delivery, not installation), and restrictions on the contractor returning stored materials for credit.

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