

# Top Ten Considerations for Municipal Construction Contracts

*A CLE Presentation for Texas City Attorneys Association*

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Top Ten Considerations for Municipal Construction Contracts

## Top Ten Considerations

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Top Ten Considerations for Municipal Construction Contracts

# 01

## Authority of Decision Makers



### 01 | Authority of Decision Makers — Legal Framework

#### Who can the City authorize to make decisions?

- Municipalities can only act through properly authorized officials
- Contracts (including amendments) executed beyond an official's authority may be void, not merely voidable

#### Key Threshold Questions

- Who has contracting authority?
- Has the governing body formally approved the contract or properly delegated that authority?
- Are there dollar thresholds requiring city council action?

#### Ratification

- Can the city ratify an unauthorized contract? Generally, yes — BUT cannot ratify a contract that violates state law
  - E.g., contract that violated procurement laws



## 01 | Authority of Decision Makers — Practical Guidance

### Before Executing a Contract

- Make sure proper procurement process followed
- Identify City's approval process for contract or changes
- Review contracts for Design Professionals or "Owner's Representative"
  - AIA and EJCDC forms often grant architect or engineer more authority than allowed - MODIFY

### During Contract Administration

- Change orders and amendments must go through the same approval process as the original contract
- Be wary of verbal authorizations – Proceed with work pending negotiation of CO
- Document all approvals in writing — email confirmations from staff may be insufficient



# 02

## Limits of Liability

*Tex. Gov't Code Chapter 271*



## 02 | Chapter 271 — Waiver of Governmental Immunity

### The Baseline Rule

- Governmental immunity bars breach of contract suits against municipalities absent a statutory waiver
- Tex. Gov't Code §271.152 provides the primary statutory waiver for public works contracts
- Waiver applies to written contracts for goods or services — construction contracts qualify

### Scope of Waiver — What Ch. 271 Allows

- Suits for breach of a written contract for goods or services (§271.152)
- Recovery of "Balance due and owed" under the contract (§271.153(a)(1))
- Recovery of amount owed for change orders or additional work contractor is "directed to perform" (§271.153(a)(2))
- Attorney's fees & Interest may be awarded in appropriate cases (§271.153(c), (d))

### Scope of Waiver — What Ch. 271 Does NOT Allow

- No recovery of exemplary or punitive damages (§271.153(b)(1))
- No recovery of damages for unperformed future obligations (§271.153(b)(2))
- Consequential damages (except — see Topic 3)



## 02 | Chapter 271 — Limitations and Strategic Considerations

### Key Procedural Requirements

- Written contract is mandatory — oral and implied contracts do not trigger the waiver
- Contract must be for 'goods or services' (construction qualifies; disputed land-use agreements may not)
- Contractual notice provisions may be enforced as conditions precedent

### The 'Balance of Payments' Cap

- Damages are limited to amounts due and owed under the contract for performed work
- Lost profits and expectancy damages above the contract price may be unrecoverable
- This cap interacts critically with consequential damages waivers — see Topic 3

### Drafting Strategy

- Include clear payment milestones
- Define change order process explicitly — owner's informal acceptance could trigger the contractor's recovery right
- City should avoid contractually allowing damages beyond those statutorily allowed



# 03

## Waiver of Consequential Damages



### 03 | Consequential Damages — Definitions and Scope

#### What Are Consequential Damages?

- Damages that flow from a breach but are not the direct, immediate result of it
- Examples: lost profits, lost productivity, home office overhead, extended general conditions, escalation costs
- Distinguishable from direct damages: cost to complete, cost to repair, unpaid contract amounts

#### Why They Matter in Municipal Construction

- Consequential damages can dwarf direct damages on complex public projects
- Common contractor claims: extended general conditions, loss of bonding capacity, business disruption
- Common owner claims: extended oversight costs, re-procurement costs, storage fees, lost tax revenue from delay

#### Texas Law Baseline

- Consequential damages are NOT recoverable damages for breach of contract under Ch. 271
  - Except for compensation for the increased cost to perform work as a direct result of owner-caused delays or acceleration
- AIA standard forms include mutual consequential damages waivers



## 03 | Consequential Damages — Waiver Enforceability and Drafting

### Chapter 271 Interaction

- Ch. 271 prohibits consequential damages against the City
- BUT allows compensation for the increased cost to perform work as a direct result of owner-caused delays or acceleration

### Types of Waivers

- Mutual waiver (both parties waive) — standard in AIA A201; most defensible in court & often negotiated
- One-sided waiver (contractor only) — in most governmental projects, consequential damages are the primary types of damages for the owner
- Partial waiver with carve-outs — e.g., delay damages, LDs, indemnity obligations

### Drafting Recommendations

- Define explicitly what 'consequential damages' includes in the waiver
- Carve out liquidated damages, indemnity obligations, and insurance proceeds from the waiver
- Ensure mutual waivers if you want them to be enforceable and balanced
- Include a delay damages or time compensation provision for owner-caused delay or acceleration as an alternative remedy



# 04

## Standard of Care

*Design Professionals & Contractors*



## 04 | Standard of Care — Design Professionals

### The Professional Standard

- A/E must exercise the degree of care and skill ordinarily used by professionals in good standing in similar localities under similar circumstances
- Not a perfection standard — errors and omissions are not automatically negligence
- Expert testimony is required in most cases to establish both the standard and the breach

### The Spearin Doctrine in Texas

- An owner who furnishes plans and specifications to a contractor impliedly warrants their adequacy
- If contractor follows the plans and the project fails, the owner — not the contractor — bears responsibility for design
- Texas statutorily implemented the Spearin Doctrine

### Contractual Modifications of the Standard

- Design-build delivery blurs the Spearin line — contractor assumes design risk & liability
- 'Best efforts' vs. 'reasonable efforts' — courts treat these differently; avoid 'best efforts' for A/E
- Limitation of liability clauses may cap A/E exposure — see Topic 5



## 04 | Standard of Care — Contractors

### Implied Warranty of Workmanlike Performance

- Every construction contract implies the contractor will perform in a good and workmanlike manner
- Applies even when the contract is silent on quality of work, but you should include still in the contract

### Express Warranties and Performance Guarantees

- Contractors may expressly warrant work against defects for a stated period
- Distinguish warranty obligations from defect correction under the contract's correction-of-work clause

### Statute of Repose and Limitations

- Tex. Civ. Prac. & Rem. Code §16.008-.009 — 8-year statute of repose for government projects
- Runs from substantial completion
- Exception for civil projects §16.008(a-1)(3)
- Tex. Civ. Prac. & Rem. Code §16.061 — No limitations for breach of contract claim



# 05

## Statutory Indemnity

*Design Professionals — Tex. Ins. Code §130.001*



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### 05 | Statutory Indemnity — The Anti-Indemnity Statute

#### **Tex. Civ. Prac. & Rem. Code §§130.001–.004**

- Voids indemnity provisions requiring design professionals to indemnify for claims arising from the indemnitee's own negligence
- Applies to architectural, engineering, surveying, or landscape architectural services
- Cannot be waived by contract — prohibited provisions are void and unenforceable
- Chapter does not apply to Insurance Contracts or Workers' Compensation Agreements

#### **Tex. Ins. Code §151.101**

- Voids indemnity provisions to indemnify, hold harmless, or defend for claims arising from the indemnitee's own negligence or fault, the breach or violation of a statute, ordinance, governmental regulation, standard, or rule, or the breach of contract
- Applies to construction contracts
- Exception for employee claims (i.e., workers compensation claims)



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## 05 | Statutory Indemnity — The Anti-Indemnity Statute

### What Is Prohibited

- Broad indemnity: indemnify Owner for any and all claims, including those caused by Owner's negligence
- For A/E, defense obligations that do not carve out the indemnitee's own fault
- Insurance endorsements that effectively require the insurer to cover Owner's negligence

### What Remains Permissible

- Proportionate fault indemnity: A/E indemnifies for A/E's or its subconsultants' own negligence
- Proportionate fault indemnity: Contractor indemnifies for contractor's or its subcontractors' own negligence or fault, the breach or violation of a statute, ordinance, governmental regulation, standard, or rule, or the breach of contract
- Proportionate Attorneys' Fees
- Broad form Workers' Compensation indemnification



## 05 | Statutory Indemnity — Drafting Compliant Provisions

### Sample Compliant Indemnity Language

- "A/E shall indemnify Owner from and against claims, damages, losses, and expenses to the extent caused by the negligent acts or omissions of A/E, A/E's consultants, or anyone for whose acts A/E may be liable"
- Key phrase: 'to the extent caused by' — proportional, fault-based, and enforceable

### Limitation of Liability (LOL) Provisions

- Separate from anti-indemnity — LOL provisions capping A/E liability are generally enforceable in Texas
- Common form: limit A/E total liability to amount of available insurance proceeds
- Public policy debate: should public owners agree to LOL caps? Practice varies by entity and project size

### Professional Liability Insurance Implications

- CGL contractual liability coverage does NOT cover professional errors — a separate PL policy is required
- Additional insured status on professional liability policies is generally unavailable
- Owners should require A/E's PL policy to be maintained after the expiration of the contract (2 or 4 years after)
- Require extended reporting period (tail) endorsement if the policy is cancelled or non-renewed



# 06

## Contractual Notice Requirements



### 06 | Notice Requirements — Conditions Precedent to Claims

#### Why Notice Provisions Matter

- Notice provisions serve dual purposes: alert the owner to act and mitigate, and preserve an evidentiary record
- Courts may treat notice as a condition precedent — failure to give timely notice may waive the claim entirely

#### Common Notice Provisions in Public Construction Contracts

- Differing site conditions notice: typically 7–21 days from discovery (See AIA; EJCDC)
- Claim or dispute notice: typically 21 days from the event giving rise to the claim
- Change order/equitable adjustment notice: often 14–21 days after the event giving rise to the change
- Statutory pre-suit notice under Tex. Gov't Code §311.034 — required before suing any governmental unit
- Statutory pre-suit notice under Tex. Gov't Code §2272.003 – Report of Defects before suing contractor

#### Consequences of Non-Compliance

- Meritorious claims may be barred — Texas courts have enforced this, but check for substantial compliance
- Owner's actual knowledge of the condition may excuse non-compliance under equitable waiver
- Owner's conduct (e.g., directing work to continue) may constitute waiver of the notice requirement



## 06 | Notice Requirements — Drafting and Compliance Strategy

### Drafting Recommendations for Owners

- Include clear, unambiguous notice periods — specify form (written), addressee, and delivery method
- State expressly that failure to give timely notice waives the claim — do not leave this implied
- Require notice to a specific title (e.g., City Manager) with a copy to legal counsel

### Compliance Best Practices

- Make sure City is complying with notice requirements
- When in doubt — give notice; a protective notice does not harm your negotiating position
- Preserve all written communications
- Include the surety when necessary

# 07

## Change Order Limitations

*Tex. Gov't Code Chapter 252*

## 07 | Chapter 252 — Competitive Bidding Requirements

### Chapter 252 Framework

- Tex. Loc. Gov't Code §252.001 requires competitive bidding for municipal purchases over \$100,000
- Gov't. Code Ch. 2269 & §252 apply to contracts for construction, services, and goods
- Purpose: prevent favoritism, ensure value for taxpayers, and maintain public confidence

### Change Orders and the Competitive Bidding Problem

- Substantial changes in scope may constitute a new contract requiring competitive bidding
- Tex. Loc. Gov't Code §252.048(d) – cannot increase more than 25% of original contract price or decrease more than 25% without the contractor's consent
- A change order adding significant new scope may be an unauthorized modification void under Ch. 252

### Texas AG Opinions and Case Guidance

- AG opinions: changes within the original scope and specifications are generally permissible
- Changes adding entirely new scope or materially increasing cost may require re-procurement
- City charter provisions may impose additional restrictions beyond state law



## 07 | Chapter 252 — Managing Change Orders in Practice

### Permitted Change Order Mechanisms

- Owner contingency allowances built into the original bid — reduces risk of later re-bidding (exceeding 25%)
- Bid alternates priced in the original solicitation — can be added/deducted without a new bid

### Proper Authorization of Change Orders

- City council approval required above \$50,000 or \$100,000 if pop. over 240,000 (Tex. Loc. Gov't Code §252.048(c), (c-1))
- City manager typically has delegated authority for changes up to a stated amount
- All changes must be in writing and authorized before work proceeds — oral directives create significant risk

### Documentation Best Practices

- Include detailed scope description and pricing justification in every change order package
- Track cumulative change order total against original contract amount
- Document the time impact in each change order and contractor should incorporate it into the project schedule



# 08

## Insurance Coverages & Limits



### 08 | Insurance — Core Required Coverages

#### **Commercial General Liability (CGL)**

- Covers bodily injury and property damage from operations and completed operations
- Minimum for public projects: \$1M per occurrence / \$2M aggregate — scale upward with project size
- Completed operations coverage - extend through statute of repose (recommend 8 years)

#### **Workers' Compensation & Employers' Liability**

- Mandatory for contractors with employees in Texas — Tex. Labor Code Ch. 406
- Confirm coverage via TWCC certificate; employers' liability minimum \$500K per occurrence

#### **Commercial Auto Liability**

- Require 'any auto' endorsement covering owned, hired, and non-owned vehicles
- Minimum \$1M CSL for all vehicles used in project operations



## 08 | Insurance — Core Required Coverages

### Professional Liability (E&O) — for Design Professionals & Contractors with Design Scopes

- Required for all A/E firms or contractor with design scope — covers design errors and omissions
- Claims-made policy: require extended reporting period (tail) of at least 3 years post-project completion
- Minimum limits: \$1M/\$2M–\$2M/\$4M depending on project complexity and A/E scope

### Excess Liability/Umbrella Policy

- include \$5M to \$10M excess policy depending on project complexity



## 08 | Insurance — Limits, Additional Insured, and Common Pitfalls

### Calibrating Limits to Project Size

- Rule of thumb: CGL limits should approximate 10–20% of contract value for larger projects
- Builder's Risk: insure 100% of completed project value including soft costs and owner-furnished equipment

### Additional Insured Requirements

- Owner and A/E should be named additional insureds on contractor's CGL
- Primary and non-contributory language — contractor's policy pays first before owner's policy
- Waiver of subrogation endorsement — prevent insurer from suing the additional insured after paying a claim

### Common Pitfalls to Avoid

- Certificates of insurance are not policies — do not rely on the certificate alone
- Require 30-day notice of cancellation endorsed into the policy
- Request and review actual policy endorsements — confirm they are attached, not just promised
- Gap risk: contractor demobilizes or goes out of business, coverage lapses — require continuous coverage provisions



# 09

## Statutory Bonds

*Tex. Gov't Code Chapter 2253*



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### 09 | Statutory Bonds — Framework and Requirements

#### Chapter 2253 — Public Work Bonds Act

- Applies to all public work contracts valued at more than \$100,000 (performance), \$50,000 (payment) (§2253.021)
- Requires two bonds: a Performance Bond and a Payment Bond, each equal to 100% of the contract amount
- Bonds must be executed by a surety authorized to do business in Texas and rated by an acceptable rating organization

#### Performance Bond

- Secures the contractor's obligation to complete the work in accordance with the plans, specifications, and contract documents
- Triggers: contractor default, abandonment, or material failure to perform
- Surety's options: finance the contractor, complete directly, tender a replacement contractor, or pay the penal sum
- Owner must formally declare default and give an opportunity to cure before terminating

#### Payment Bond

- Secures payment to subcontractors, material suppliers, and laborers on the public project
- Texas has no mechanic's lien rights against public property — the payment bond is the exclusive remedy
- Claimants must strictly comply with notice requirements and filing deadlines under §2253.041



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## 09 | Statutory Bonds — Claims, Notice, and Enforcement

### Bond Forms & Contract Provisions

- City should specifically tailor bonds forms pursuant to Gov't Code Ch. 2253
- Revise contract to remove requirement for notice to surety of all contract changes
- Check limitations period in bond form (statutorily 1 year from termination, abandonment or final completion)

### Performance Bond Claims

- Owner must formally declare contractor in default and give a cure opportunity
- Notice to the surety of default is critical
- Common surety defenses: owner-caused breach (payment failure, differing conditions); limitations

### Avoiding Bond Disputes

- Verify bond form complies with Ch. 2253 before project commences — reject deficient bonds immediately
- Require bonds from Treasury-listed, A-rated sureties only
- Maintain current list of subcontractors and suppliers — contact info for potential claimants



# 10

## Liquidated Damages

*Including Key Texas Caselaw*



## 10 | Liquidated Damages — Legal Framework

### What Are Liquidated Damages?

- A pre-determined sum payable per day of delay in achieving a defined completion milestone
- Serve as an alternative to proving actual delay damages — critical where damages are inherently speculative

### Texas Enforceability Standard

- Step 1: At the time of contracting, actual damages must have been difficult or impossible to estimate
- Step 2: The stipulated LD amount must be a reasonable forecast of just compensation — not a penalty
- Phillips v. Phillips, 820 S.W.2d 785 (Tex. 1991) – landmark case
- Atrium Medical Center, LP v. Houston Red LLC, 595 S.W.3d 188 (Tex. 2020) - applied “second-look” approach
- Step 3: If LD provisions is facially reasonable, determine whether, at the time of the breach, an “unbridgeable discrepancy” exists between the actual and liquidated damages

### The Penalty Distinction

- If the LD amount is 'grossly disproportionate' to actual damages, courts will void it as an unenforceable penalty



## 10 | Liquidated Damages — Drafting and Practical Guidance

### Setting the LD Rate — Documentation Is Critical

- Identify anticipated delay costs: owner overhead, extended inspection/administration, financing costs, lost revenue from delayed opening
- Perform and document the calculation methodology to determine daily rate — retain analysis in the permanent contract file

### Key Drafting Provisions

- Never refer to LDs as a 'penalty' in the contract
- Define completion milestones triggering LDs with precise specificity
- Address excusable delay: weather, force majeure, owner-caused delays — provide for time extensions without cost
- Consider bonus/incentive provisions as a complement to LDs

### Common Contractor Defenses

- Owner prevention or hindrance — if owner-caused delay contributed, LD clause may not apply
- Concurrent delay — if both parties contributed, courts struggle with apportionment
- Waiver by owner — continued acceptance of late work without assessing LDs can constitute waiver



# Questions

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