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Construction Law 2026

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USA – California

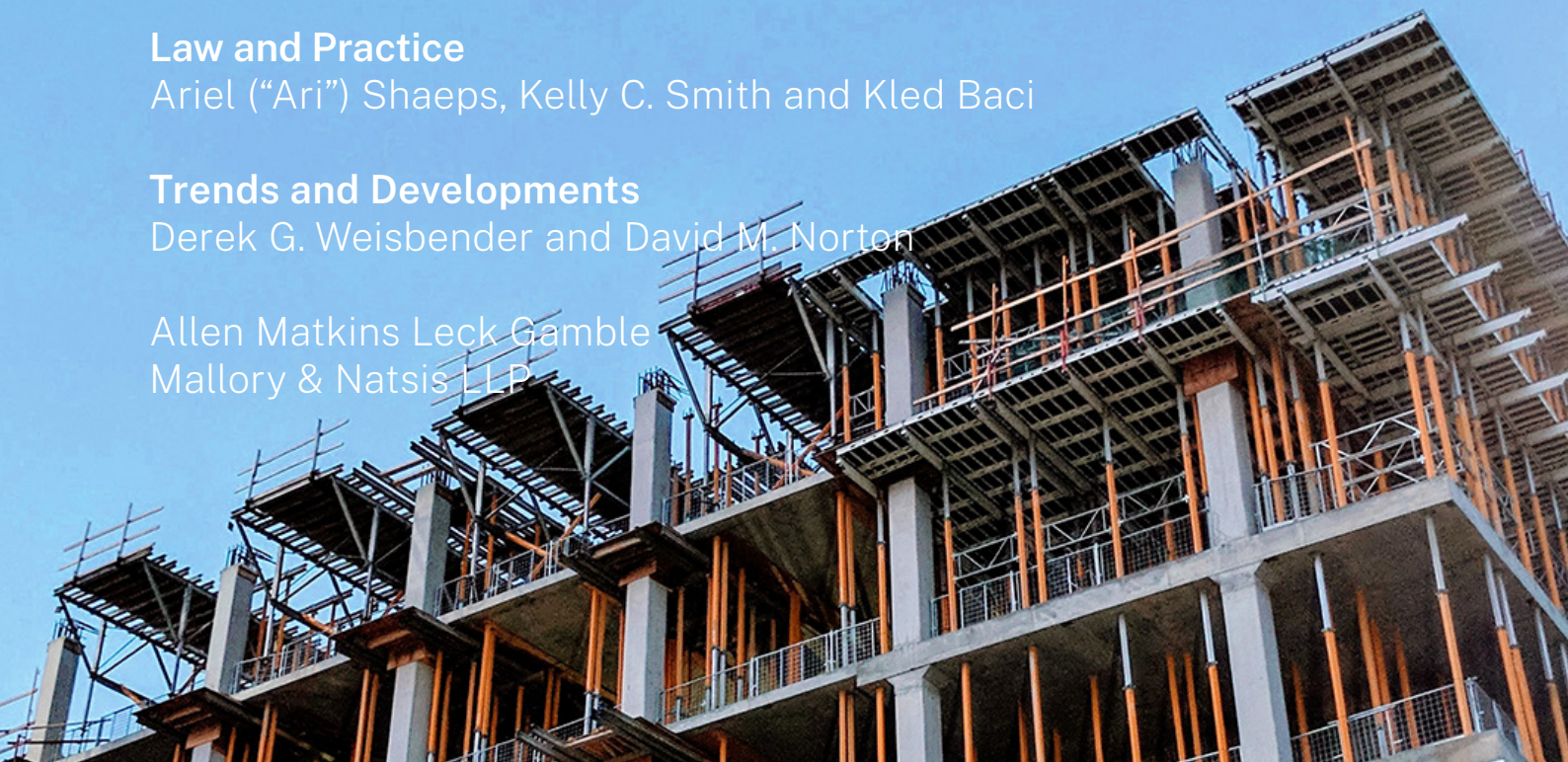
Law and Practice

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Law and Practice

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dle the full lifecycle of major projects – drafting and negotiating complex construction agreements, advising on construction lending, and representing clients in construction disputes and litigation. It serves national and international owners, investors, developers, financial institutions, REITs, landlords, tenants and construction managers on projects of every size and type. With deep industry knowledge and practical judgment, it helps clients manage risk, protect investments, keep deals moving and resolve conflicts efficiently when they arise.

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Allen Matkins

1. General

1.1 Governing Law

No content provided in this jurisdiction.

1.2 Standard Contracts

In California, the mandatory use of standard form construction contracts is generally limited to public works projects, where public agencies often use prescribed or agency-specific forms and procurement documents.

In the private sector, the use of standardised forms is not mandatory. Parties commonly start with AIA contracts or bespoke agreements that are tailored to the specific project, delivery method and financing structure.

Private construction projects most often follow one of two primary delivery frameworks, set out below.

Design-Bid Build

Under a design-bid build structure, the architect prepares the design for the project, and the contractor constructs the project based on the architect’s design. The owner contracts separately with the architect and the contractor.

Design-Build

Under a design-build structure, the contractor is responsible for both the design and construction of the project and provides the owner with a single point of responsibility.

Either delivery method may be paired with different pricing structures. In the development context, design-build projects are most commonly structured as guaranteed maximum price (GMP) construction contracts.

Private construction projects commonly use one of three pricing structures.

- A stipulated sum (lump sum) construction contract is used where the project scope is fully or sufficiently designed and defined to enable the contractor to agree to fixed pricing.
- A cost of the work plus fee construction contract with a GMP is the most common structure in the development context. Under a GMP construction contract, the owner reimburses the contractor for actual, defined costs of the work plus an agreed fee, subject to a negotiated price cap. Contractor general conditions are often separately identified and subject to their own not-to-exceed limits to enhance transparency and cost control.
- Less commonly, projects may use cost-of-the-work plus fee contracts without a GMP, although these structures are less common in development transactions because lenders and capital partners typically require some form of cost certainty.

2. Parties

2.1 The Employer

In California, the “owner/employer” on construction projects commonly includes private real estate devel-

opers, institutional owners, private equity, corporate entities, healthcare systems, educational institutions and public agencies. In the private sector, ownership is often held through a special-purpose entity formed for a particular development or financing arrangement. Public works projects are typically sponsored by state agencies, municipalities, school districts or other public authorities and are subject to additional statutory and regulatory requirements.

Under a construction contract, the owner’s primary obligations generally include providing access to the project site, furnishing information necessary for performance, making timely payment in accordance with the construction contract and applicable prompt payment statutes, and co-ordinating between project participants where required. The owner customarily retains the right to approve the work, issue changes, enforce quality and schedule requirements, and terminate the construction contract for cause or convenience, subject to contractual notice, cure and dispute resolution provisions.

The owner’s contractual relationship is typically direct with the contractor who in turn contracts with subcontractors.

Lenders are not parties to the construction contract but often exert significant influence through loan documents and related collateral agreements. Lenders commonly require assignment of construction contracts following a default by the owner (as the borrower under the loan agreement), and consent rights over material amendments. The owner is generally responsible for structuring contractual relationships to align with financing requirements while maintaining clear allocation of risk and responsibility among project participants.

2.2 The Contractor

In California, construction projects are performed by general contractors that must be licensed with and are regulated by the California Contractors State License Board. Contractors may range from small, local residential builders to large national or international construction firms on commercial, infrastructure or hospitality developments. Subcontractors are retained by the general contractor to perform certain scopes of

work. On certain projects, a design-build contractor may provide both design and construction services.

California Business and Professions Code § 7026 broadly defines the types of work and activities that constitute acting as a “contractor” under California’s Contractors State License Law. Under these rules, parties co-ordinating or contracting for improvements should consider whether the person performing, offering to perform or managing the work is properly licensed for the applicable scope and classification of work, unless an exemption applies.

2.3 The Subcontractors

No content provided in this jurisdiction.

2.4 The Financiers

Financiers on construction projects in California most commonly include construction lenders that provide debt financing to project owners. Loans are typically documented through promissory notes secured by deeds of trust recorded against the property, and lenders focus heavily on lien priority, title and mechanics’ lien protections. Lenders do not have direct contractual relationships with contractors, subcontractors or the architect. Their relationship is usually with the borrower, and they may require completion guarantees or other credit support from a creditworthy party. Lenders commonly control construction disbursements by requiring third-party progress review, tying draw funding to approved payment applications, and conditioning payment on delivery of lien releases and supporting documentation. Owners are typically required to fund a portion of project equity before loan proceeds are advanced. Some development projects also include equity partners, which may retain approval rights over material project decisions and significant construction contract terms.

2.5 The Designer

In California, the designer is typically the architect of record (AOR). The AOR prepares the project design, stamps the drawings and responds to comments or directives from the local jurisdictions.

Rights and Obligations of AOR

- Design the construction documents to be consistent with (i) applicable laws and (ii) the owner’s

- budget for the project, and (iii) the appropriate standard of care for the design services.
- Modify the construction documents as requested by the owner and as required by the local jurisdiction.
 - In many circumstances, retain project consultants (ie, structural engineer, civil engineer, etc) for the design and co-ordinate the design of any consultants that the owner hires directly.

A key consideration is how the consultant team is structured and whether design professionals contract directly with the owner or the consultants are hired by the architect under the architect agreement, as this allocation affects co-ordination, responsibility and risk.

Architect agreements also commonly address ownership of design instruments and related intellectual property. In many private development transactions, these agreements are negotiated on a work-or-hire basis so that the owner owns the design work product and may continue using such works if the architect is terminated and engage another design professional to complete or revise the design, subject to negotiated indemnity and reliance limitations.

3. Works

3.1 Scope

In general, we frame the scope obligations to be performed by the contractor such that the contractor is to fully execute the work described in the contract documents and “inferable” therefrom. An item of work shall be “reasonably inferable” if it is a necessary component of a specific assembly and necessary for the proper execution and completion of the work to the extent consistent with the contract documents. For example, it shall be “reasonably inferable” for a sink to require proper plumbing, hardware and drain, regardless of whether or not shown on the construction documents.

3.2 Variations

In California, variations are typically addressed through change orders, and in representing owners/developers, we structure the construction contract to identify

and limit the circumstances under which a change order is permitted at the time of negotiation. Construction contracts usually establish a defined process for initiating, pricing and approving change orders.

When a potential change arises, if the owner directs additional or different work, the contractor typically submits a proposed change order describing scope, price and schedule impacts. Once executed, the change order amends the construction contract by modifying scope, price, time and/or other terms.

If a contractor requests a change order, it generally must demonstrate that the work falls within contractually permitted grounds, and such change order complies with the following:

- notice and documentation requirements; and
- price requirements for the change order work using the construction contract’s pricing mechanisms (for example, agreed unit prices, negotiated lump sums or cost-of-the-work pricing).

Time-related costs and schedule impacts are addressed through delay provisions that distinguish between excusable/non-compensable delays (ie, contractor’s relief is for time only) and compensable delays (ie, contractor’s relief is for both time and money). To substantiate any such delay, the contractor must demonstrate, or provide, the following:

- the delay impacted the critical path;
- timely notice so the parties can evaluate and mitigate delay; and
- a time impact analysis.

3.3 Design

The architect typically serves as the AOR and is responsible for designing the project, while the contractor constructs the work in accordance with the design. The architect may retain subconsultants directly or the owner may contract directly with certain design professionals depending on the structure of the design agreements.

The architect’s contract typically includes formal processes to clarify and supplement the design, including responses to requests for information from the con-

tractor through which the contractor requests information necessary to build the work as designed by the architect. Design and construction agreements commonly specify response timeframes for RFIs, so the architect’s response obligations align with the contractor’s performance obligations and avoid unnecessary delay. A similar co-ordination framework applies to submittals for materials and systems prior to installation, where the architect reviews and aligns with specifications.

3.4 Construction

Responsibility for the construction of the work rests with the contractor. The contractor enters into a direct contractual relationship with the owner and assumes overall responsibility for constructing the project in accordance with the contract documents.

The contractor typically performs the work through subcontracts. Even prior to executing any subcontracts, the contractor engages the subcontractor market to obtain pricing based on the then-available project design and pricing. Subcontractors commonly submit proposals for their respective scopes of work, committing to perform the work at a specified price for a defined period of time, subject to the timely issuance of a subcontract. This process allows the contractor to lock in pricing and manage procurement risk before formal subcontract execution.

In the development context, certain large contractors will also self-perform portions of the work, rather than subcontracting those scopes. In these situations, the contractor not only oversees the work of subcontractors but also performs specific trades directly, either through the contractor’s own workforce or through affiliated or related entities. Some large contractors in California, particularly those operating at significant scale, have expanded self-performance capabilities across multiple trades.

3.5 Site

In California, responsibility for the construction site is generally allocated to the contractor, who assumes responsibility for site safety, site conditions and day-to-day control of the site, including liability for injuries occurring on the site, which are typically addressed through the contractor’s general liability insurance

and related coverages. This responsibility generally extends to the acts or omissions of the contractor’s subcontractors and their employees.

With respect to site conditions, including concealed or subsurface conditions, we generally structure risk allocation as follows.

- Owners provide the contractor with all available site information such as soils and geotechnical studies, environmental reports and other investigations, and the contractor is expected to review and have its price and schedule take into account such conditions disclosed or reasonably inferable therefrom.
- In an owner representative capacity, site condition risk is allocated to the contractor such that the contractor’s entitlement to a change order is limited to only those conditions that the contractor could not have reasonably discovered or anticipated based on an examination of the project site and all of the contract documents.

While some site-related obligations are influenced by regulatory requirements, allocation of responsibility and associated costs is largely governed by the negotiated construction contract.

3.6 Permits

Permitting is governed by the applicable local building department and related authorities. While the architect typically designs the drawings and specifications to be in compliance with applicable codes and regulatory requirements, the contractor is generally responsible for procuring required permits as part of the construction process.

3.7 Maintenance

In California, responsibility for maintenance of the works is typically separate from the construction contract and is commonly addressed through standalone maintenance agreements rather than through the general contractor’s construction obligations.

Maintenance often relates to specific systems or components, such as elevators, escalators, mechanical systems and other specialised equipment. Owners

commonly contract with the installer or specialty vendor for ongoing maintenance services.

These maintenance services generally include routine inspections, servicing, testing, repairs and all compliance-related activities defined in the maintenance contract, and are distinct from construction-phase warranty obligations.

3.8 Other Functions

No content provided in this jurisdiction.

3.9 Tests

In California, testing for completion is generally addressed through a process commonly referred to as commissioning and start-up. Completion is typically defined by substantial completion, meaning the point at which the work, or a designated portion of the work, is sufficiently complete in accordance with the contract documents, so that the owner can use or occupy the project for its intended purpose.

Once the contractor has substantially completed the work, the project and certain systems or components are tested and commissioned to confirm that they operate in accordance with the contract requirements and meet certain performance criteria to the extent so specified. This process commonly applies to building systems such as mechanical, electrical, plumbing and other operational components.

The contractor is generally responsible for performing and co-ordinating the testing and commissioning activities. These activities are carried out under the oversight of the owner, and often with the involvement of the design team. The purpose of the commissioning and start-up process is to ensure that the owner receives complete operational information necessary to use, operate and maintain the project after the contractor demobilises from the site.

3.10 Completion, Takeover and Delivery

In California, completion, takeover and delivery are primarily governed by the construction contract, and substantial completion is commonly defined as the point at which the work is sufficiently complete for the owner to use the project for its intended purpose. In an owner-representative capacity, substantial completion

is often defined more narrowly and tied to regulatory approval, typically requiring a certificate of occupancy or temporary certificate of occupancy.

Substantial completion triggers key contractual consequences, including release of retention (and in California, private project retention is capped at 5% as of 1 January 2026), commencement of warranty periods and transition of risk/insurance from builder’s risk to the owner’s property coverage. As a result, the substantial completion determination directly affects financial, risk and operational responsibility for the project.

3.11 Defects and Defects Liability Period

In California, the period during which a contractor may be held liable for defects depends on the claim asserted, but all construction defect claims are subject to an outer limit of ten years from substantial completion under California Code of Civil Procedure § 337.15.

Parties do not typically agree to contractual limitations on the time to discover defects. Rather, liability is governed by statute. Common limitation periods include:

- four years for breach of a written construction contract;
- three years for negligence causing property damage;
- four years for patent defects (from substantial completion);
- ten years for latent defects (from substantial completion); and
- one year for disgorgement claims based on improper licensure under California Business and Professions Code § 7031 (from completion or cessation of work).

Separate procedural requirements and timelines apply to new residential construction under California’s Right to Repair Act (SB 800).

If defects are discovered during construction, the owner may require correction and, where appropriate, withhold payment (see, eg, Cal. Civ. Code § 8800; Cal. Pub. Contract Code § 7107). After completion of the work, the owner may demand repair if the defect arises within the warranty period. After the warranty

period expires, remedies generally shift to litigation and/or filing a complaint with the California Contractors State License Board. SB 800 provides additional, structured pre-litigation remedies for qualifying residential projects.

There is no universal statutory deadline for notifying contractors of defects on commercial projects. Instead, notice requirements during construction and the warranty period are typically governed by contract. For new residential construction, California Civil Code § 910 requires pre-litigation notice to the contractor and an opportunity to repair.

Failure to comply with contractual or statutory notice requirements may limit available remedies. Once applicable statutes of limitation or repose expire, defect claims are generally barred.

4. Price

4.1 Contract Price

In California private construction contracts, the construction contract price is most commonly established as a lump sum (stipulated sum) or as cost of the work plus a fee, often with a guaranteed maximum price (GMP).

The construction contract price is typically composed of the direct cost of the work (including subcontracted trade costs and materials), plus general conditions and general requirements, contractor fee, insurance and bonds, and agreed allowances and contingencies where applicable. For GMP structures, parties commonly negotiate how savings are treated, how contingencies may be used, and whether certain categories (eg, general conditions) are subject to separate not-to-exceed caps to support cost control and transparency.

4.2 Indexation

Indexation is not universally used in California private construction contracts, but price escalation concepts are increasingly addressed by negotiation, particularly for labour and long-lead materials or equipment. Where owners require price certainty, the risk of price fluctuation is often priced into the contractor’s bid or

managed through allowances, contingency structures or narrowly drafted escalation provisions for defined categories. Where indexation or escalation is used, parties commonly define the triggering events, documentation required, and caps or sharing arrangements to prevent open-ended exposure.

4.3 Payment

Construction contracts typically manage late or non-payment through defined payment timing (eg, monthly progress payments), notice and cure procedures and remedies that may include interest on late amounts and, in some circumstances, work suspension or termination rights following required notices. Progress payments are common through periodic pay applications supported by backup documentation such as subcontractor invoices, conditional and unconditional lien releases, and other draw requirements that may be driven by lender conditions.

Advance payments are less common in traditional building projects but may be negotiated for early procurement, mobilisation or owner-furnished/contractor-installed scopes, and any advance payment is typically paired with security and documentation requirements.

4.4 Invoicing

Invoicing on California private projects is most commonly handled through monthly pay applications. A contractor’s pay application is typically based on the schedule of values that allocates the construction contract price across scopes of work. Pay applications generally include amounts earned to date, retainage withheld, amounts previously paid and the net amount currently due. Pay applications are commonly required to be supported by subcontractor and supplier backup, lien releases and other documentation required by the construction contract and, where applicable, the construction lender. Many contracts also require updated schedule reporting with each pay application to align payment with progress and to support project administration. Final invoicing typically occurs at substantial completion or final completion, together with closeout documentation and final lien releases.

5. Time

5.1 Planning and Programme

Planning is typically established through a baseline project schedule prepared by the contractor (often after construction contract execution) and updated periodically throughout performance. The contractor is responsible for preparing the schedule, including sequencing, procurement planning and co-ordination of subcontractor activities, while the owner typically has review and approval rights for key milestones, long-lead procurement decisions and change-related schedule impacts.

Schedules are safeguarded through contractual requirements for regular updates, notice of events affecting the critical path, and integration of schedule impacts into the change order process. Milestones are commonly used to manage the project (eg, permit milestones, procurement releases, substantial completion and turnover), and while milestone payments are sometimes used, many projects rely on progress payments with milestone dates functioning primarily as schedule and performance controls rather than payment triggers.

5.2 Delays

Delay processes are primarily governed by the construction contract, but follow a consistent framework. In the event of a delay that is entirely outside of the contractor’s control, the contractor must provide the owner with prompt written notice of the delay, an updated project schedule, and a request for a time extension demonstrating impact (ie, a time impact analysis) to the project’s critical path. The contractor is generally obligated to mitigate delays and accelerate work.

Whether the contractor is entitled to a time extension and/or additional compensation depends on the cause of the delay. In the event of a contractor-caused delay, the contractor is not entitled to additional compensation or a schedule extension. In the event of an excusable delay (commonly defined as acts of God, labour disputes (not directed at the contractor), inclement weather, etc), the contractor is typically entitled to a schedule extension, but not additional compensation.

In the event of a compensable delay (commonly defined as changes in the work, concealed conditions or a delay caused by owner), the contractor is entitled to both a schedule extension and additional compensation (eg, extended general conditions). If the compensable delay is concurrent with any contractor-caused delay, the contractor is typically entitled to a time extension, but no additional compensation.

5.3 Remedies in the Event of Delays

See 5.2 Delays.

5.4 Extension of Time

Construction contracts typically specify circumstances that entitle the contractor to an extension of time, such as acts of God, labour disputes, inclement weather, adverse weather days, delivery delays, changes in the work, concealed conditions or a delay caused by the owner, and similar events. When an extension event occurs, the contractor provides a notice of delay. Generally in the event of a delay noted above, an extension of the project schedule shall require that contractor demonstrate the following: that the delay (i) impacts components of the work on the critical path indicated in the project schedule; (ii) is not caused by, or could have been avoided or mitigated by contractor, or its subcontractors (of any tier), exercising its standard of care (including by re-scheduling activities after the occurrence of the event causing delay), or reasonably avoided by contractor; and (iii) has an impact of at least one day.

5.5 Force Majeure

See 5.2 Delays and 5.4 Extension of Time.

5.6 Unforeseen Circumstances

In California, unforeseen circumstances are primarily addressed through negotiated contractual risk allocation, often supported by owner-provided reference documents such as environmental reports, geotechnical studies, soils reports and surveys.

The owner-side approach commonly aims to narrow relief to conditions that could not reasonably have been identified through review of the reference documents and available site information. Where relief is available, remedies may include time and monetary adjustments consistent with the construction con-

tract’s differing site conditions and change order framework.

5.7 Disruption

See 5.2 Delays and 5.4 Extension of Time.

6. Liability

6.1 Exclusion of Liability

Certain liabilities cannot be contractually waived or excluded in California, including:

- licensure requirements – a contractor or subcontractor must be properly licensed and cannot contract around this requirement;
- mechanics lien rights – advance waivers of mechanics lien rights are unenforceable under California Civil Code § 8122;
- prompt payment rights – certain statutory payment rights and dispute procedures cannot be waived in advance under California Civil Code § 8800;
- indemnity limitations – construction contracts cannot require a party to indemnify another for that party’s sole or active negligence or wilful misconduct under California Civil Code § 2782; and
- fraud and wilful misconduct – a party cannot exempt itself from liability for fraud, willful injury to person or property, or violation of law under California Civil Code § 1668.

6.2 Wilful Misconduct and Gross Negligence

Both concepts are recognised under California law and arise from common law and public policy. Gross negligence is generally defined as “want of even scant care” or “an extreme departure from the ordinary standard of conduct”. Wilful misconduct involves intentional conduct or a conscious or reckless disregard of known risks.

These concepts act as limitations on risk allocation. For example, under California Civil Code § 1668, parties may not contractually limit or exclude liability for their own fraud or wilful misconduct, and, in many contexts, limitations on liability are also unenforceable in the face of gross negligence. Further, there is an exception to the ten-year statute of repose set forth in

Section 337.15 of the California Code of Civil Procedure for wilful misconduct or fraudulent concealment.

6.3 Limitation of Liability

In California, parties are generally permitted to contractually limit their liability, particularly on private construction projects. Limitation of liability provisions are most commonly used by general contractors and design professionals and commonly show up as caps on liability, waivers of consequential damages and delay-related limitations (ie, providing a grace period before liquidated damages apply).

Under California law, limitation of liability provisions are generally enforceable in breach of contract claims unless they are unconscionable or contrary to public policy. However, such provisions are not enforceable against negligence claims to the extent the party seeking to employ the provision was actively or grossly negligent. In no circumstance will limitations of liability protect a party from its own fraud or wilful misconduct.

7. Risk, Insurance and Securities

7.1 Indemnities

Indemnities are commonly used in California construction contracts to allocate risk and address third-party claims arising out of the work. In an owner representative capacity, the indemnity is generally drafted to be as broad as permitted by applicable law and include the following:

- claims arising out of the contractor’s performance of the work;
- liabilities sustained on account of a breach or the failure of the contractor or its subcontractors to perform their obligations in accordance with the construction contract and applicable laws;
- liabilities sustained on account of a breach of any representation or warranty of contractor or subcontractors in the construction contract;
- any and all liens and stop notices filed or claimed against the project; and
- employment-related claims brought by employees of the contractor and any subcontractor.

California law limits construction indemnities that attempt to shift responsibility for the owner’s sole or active negligence or wilful misconduct and in connection with defects in design furnished by the owner.

7.2 Guarantees

No content provided in this jurisdiction.

7.3 Insurance

Construction contracts in California typically require insurance intended to cover bodily injury, property damage and related losses arising out of the contractor’s work, with the required programme tailored to the project’s scope and risk profile. Common requirements include commercial general liability on an occurrence basis (typically including products and completed operations), workers’ compensation and owners’ liability, and automobile liability for owned, hired and non-owned vehicles used in connection with the work.

Nearly all projects also require builder’s risk (course of construction) coverage for physical loss or damage to the work during construction, and professional liability where design services are part of the delivery method. Construction contract requirements frequently include additional insured provisions in favour of the owner or public entity (limited to work performed under the contract) and require proof of coverage through certificates of insurance and endorsements before commencement.

7.4 Insolvency

No content provided in this jurisdiction.

7.5 Risk Sharing

No content provided in this jurisdiction.

8. Contract Administration and Claims

8.1 Personnel

A common approach is to identify key personnel or the contractor’s project team either in the construction contract body or in an exhibit. Construction contracts often prohibit changing project team members without the owner’s written consent, and that consent is often required not to be unreasonably withheld. The project

team is critical to a project’s success. If the contractor changes the project team without owner’s approval, this may be a triggering event for termination.

In large transactions and limited circumstances, construction contracts may include a key personnel clause where removing or changing a particular individual from the project team could trigger immediate liquidated damages. Those consequences typically would not apply if the person is no longer employed, but rather when the contractor shifts that person to another project.

8.2 Subcontracting

Given the extent to which most commercial development projects are performed through subcontracted scopes of work, it is critical for the contractor to correctly manage subcontractor buyout and engagement. Contractors have an array of broad rights and meaningful responsibilities with respect to subcontracting and subcontractor buyouts on commercial development projects.

Accordingly, contractors are often contractually required to develop bidder interest, run a competitive bidding process (generally a three-bid process), tabulate bids and provide recommendations, and ultimately be responsible for the performance of the awarded subcontractors.

In engaging subcontractors, contractors must comply with all applicable terms of the construction contract (between owner and contractor) and ensure consistency among its responsibilities and those of its subcontractors. Doing so means understanding and syncing up critical contractual requirements ranging from administrative (eg, obligations around applications for payment, permissible retention, scheduling deliverables and notice requirements) to risk allocation (eg, liquidated damages exposure, dispute resolution, contingent assignment, indemnification and insurance obligations).

Working through the buyout process successfully is always a major early project milestone and can set the stage for a successful project. Failure to do so can result in unanticipated price escalation as quotes

expire, or risks to timely completion of the work as schedules shift.

Moreover, even after buyout, contractors still own the performance risk of selected subcontractors which is why in more recent years there has been a growing use of products like subcontractor default insurance (SDI) to help hedge such exposure, and often to generate an additional revenue driver for contractors. Payment and performance bonds can also be used to mitigate default risk for contractors and avoid costly delays.

8.3 Intellectual Property

No content provided in this jurisdiction.

9. Remedies and Damages

9.1 Remedies

No content provided in this jurisdiction.

9.2 Restricting Remedies

It is common practice in California for construction contracts to contractually limit or define the remedies available to the parties. These limitations frequently take the form of waivers of consequential damages, sole remedy provisions, no damage for delay clauses, caps on liability and provisions converting certain claims into time extensions as the exclusive relief. Parties also routinely agree to structured dispute resolution processes that condition access to remedies on compliance with notice, claim submission and escalation procedures.

While California law generally enforces negotiated limitations on remedies in private construction contracts between sophisticated parties, such provisions remain subject to statutory and public policy constraints. Remedies cannot be restricted to the extent they waive non-waivable statutory rights, including certain prompt payment protections, mechanic’s lien rights, or liability for fraud or wilful misconduct. Courts will also scrutinise remedy-limiting provisions for clarity and may refuse enforcement where a limitation renders the construction contract illusory or causes a remedy to fail of its essential purpose.

9.3 Sole Remedy Clauses

Sole remedy clauses are commonly used in private construction contracts in California, particularly for claims tied to discrete risks such as defective work, design errors in design-build arrangements, or delay-related impacts. These clauses are typically negotiated as part of broader risk-allocation provisions and are often paired with limitations of liability and waivers of certain categories of damages.

California courts will generally enforce sole remedy clauses as written, provided they are clear, unambiguous and the result of arm’s length negotiation. Enforcement is more likely where the parties are sophisticated and represented by counsel. However, sole remedy provisions may not be enforced if they are found to be unconscionable, violate public policy, or attempt to eliminate statutory rights that cannot be waived, such as certain prompt payment or mechanic’s lien protections. Courts may also limit enforcement where the exclusive remedy fails of its essential purpose.

9.4 Excluded Damages

Construction contracts in California commonly exclude categories of consequential or indirect damages. Typical exclusions include loss of use, loss of profits, loss of business opportunities, loss of financing and other similar economic damages not directly tied to the cost of repair or completion of the work. Delay-related damages are also frequently limited or waived, particularly where delay is addressed through extensions of time or liquidated damages provisions.

These exclusions are usually reciprocal and negotiated in conjunction with caps on liability, carve-outs for gross negligence or wilful misconduct and insurance requirements. While California law generally permits contractual waivers of consequential damages, such provisions will not be enforced to the extent they conflict with non-waivable statutory rights or attempt to shield a party from liability for fraud or intentional misconduct.

9.5 Retention and Suspension Rights

Retention and suspension rights are not typically waived entirely in California construction contracts, but they are frequently modified or contractually constrained in private projects. Owners commonly retain

the right to withhold a portion of progress payments as retainage, subject to statutory limits and timing requirements, while contractors often negotiate detailed conditions governing payment withholding to limit discretionary or indefinite retention.

Suspension rights are similarly addressed through negotiated provisions rather than outright exclusion. Contractors may agree to limit their right to suspend work to non-payment scenarios that continue beyond a specified cure period, while owners often retain suspension rights for convenience, subject to compensation for demobilisation costs and time impacts.

Any contractual modification of retention or suspension rights remains subject to California’s prompt payment statutes and related public policy considerations, which restrict the extent to which these rights can be waived or eliminated.

9.6 Termination

Construction contracts in California typically provide for both termination for cause and termination for convenience, with the specific rights and consequences defined by construction contract and informed by general principles of contract law. Termination for cause is commonly available where a party materially breaches the construction contract, such as by failing to perform the work in accordance with the construction contract documents, failing to make required payments or abandoning the project. These provisions usually require notice and an opportunity to cure before termination becomes effective, and improper termination may itself constitute a breach.

Termination for convenience is frequently included in owner-drafted agreements, particularly in private development projects, allowing the owner to terminate the construction contract without cause. In such cases, the terminated contractor is typically entitled to payment for work properly performed to date, approved costs incurred as a result of the termination and, depending on the construction contract, a portion of demobilisation costs. Anticipatory or lost profits on unperformed work are often expressly excluded.

The consequences of termination are heavily driven by the construction contract terms. Following termination for cause, the non-defaulting party may seek completion costs, damages resulting from the breach, and offsets against unpaid construction contract balances, subject to any contractual limitations on remedies. California courts generally enforce negotiated termination provisions, provided they are clear and do not violate public policy, but closely scrutinise whether the procedural and substantive requirements for termination were properly followed.

10. Dispute Resolution

10.1 Regular Dispute Resolution

Unless they proceed through ADR, most construction disputes in California are adjudicated in superior court. Superior courts are California’s trial courts of general jurisdiction. They handle breach of contract claims, construction defect actions, delay claims, indemnity disputes and related claims. Complex construction matters may be assigned to specialised complex departments. It is possible, but less common, for construction cases to be tried in federal district court.

10.2 Alternative Dispute Resolution

ADR is widely used in California construction disputes. Parties typically mediate their dispute at least once and may agree in their construction contracts that formal or informal mediation is a condition precedent to litigation or arbitration. Additionally, it is common (especially on private projects) for parties to agree to arbitrate their dispute through providers like JAMS or the American Arbitration Association, rather than litigate in court. Arbitration is governed by the California Arbitration Act, the Federal Arbitration Act and the rules of the arbitration provider. While arbitration involves added costs, it proceeds faster than litigation, and arbitration awards are widely enforceable with limited grounds for judicial review.

Trends and Developments

Contributed by:

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Allen Matkins Leck Gamble Mallory & Natsis LLP is a national law firm with over 280 attorneys and offices in California and New York. Founded with deep roots in real estate, it has leveraged that foundation to build prominent litigation, corporate, tax, labour and employment, land use, and environmental practices, partnering with clients across industries and markets. For nearly 50 years, clients have relied on its market-leading solutions, pragmatism, exemplary quality, approachability and unparalleled network in business and government. Its construction law attorneys han-

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Trends in Data Centre Construction

Introduction

The rate of growth in the data centre construction market has been staggering. At their core, data centres are heavy industrial buildings with unique needs. Once land, power, fibre, water and design have been checked off the list, a data centre owner or developer (whether building for its own use, or to serve tenants; we use the terms interchangeably) turns to construction and its contractor. Although there is indeed much overlap with traditional commercial construction projects, data centres have their peculiarities, and especially in light of the extreme values at play (billions of dollars at a single campus) and the market forces demanding faster, bigger and more. These peculiarities change quickly. Even year-to-year, there have been shifts in business priorities that ultimately drive the key provisions in a construction agreement. Below, we have gathered some key observations from over the last year. These observations are applicable to projects in California and, excepting the California-specific items, other states, as well as other provinces and countries.

Build a bench before you need one

For data centre developers of moderate size or larger, there is tremendous value and time savings in negotiating baseline commercial terms and construction agreement terms (in a project-neutral form), in advance, among a bench of contractors for a given region. Contractors are not committed to a project at this stage but, conversely, neither is the developer. Developers use this approach in other sectors such as office and multifamily, but the best dividends are found in the data centre space, largely due to the frenetic pace at which new projects are coming online. By negotiating and establishing a bench of potential contractors ahead of time, RFP responses are more predictable, developers can pivot more quickly if a preferred contractor lacks capacity, and surprise deviations from the negotiated terms are quashed at the business level, all without the pressure of a looming start date. This simultaneous negotiation strategy also highlights unreasonable asks. If only one of five contractors demands a certain unpalatable term, it is readily identified as an outlier.

Although generally beneficial for all developers, this approach is most practicable for developers with programmatic consistency, where contract-to-contract deviations are largely limited to project-specific details. The approach works equally well for developers that operate in multiple states (and even multiple countries), incorporating local law changes only as necessary, to preserve as much of the original deal as reasonably possible. For others, such as joint venture developers that frequently partner with different investors with their own unique requirements, there may be more variation requiring further negotiations at the project level, but the core value remains and the return is almost certainly worth the up-front investment of time and effort.

One caveat: As tempting as it may be to develop and negotiate a single, all-purpose construction agreement that works for design-bid-build or full design-build, GMP or lump sum, any state in the union, and any possible scenario, we recommend against it. With ultimate flexibility comes ultimate complexity. The 141-function, 9-inch-wide, 2-pound Wenger Swiss Army Knife known as the “Giant” may do everything, but good luck trying to unscrew a light switch cover. Sometimes you just need a good screwdriver. Likewise, the programmatic negotiation should involve the most typical baseline approaches but still allow for narrow adjustments as needed to conform at the project level.

Allow for incremental builds

For those that build in response to demand, particularly owners that build for their own use, consider structuring construction agreements with optionality for phased releases of work (often tied to design hold-points, so long as logical and practicable). The simplest versions merely allow the owner to release portions of the project as the need arises, such as fitting-out more of a data hall when demand is signalled. The more complex versions lock commercial terms and perhaps a floating schedule (a fixed schedule but without a known start date) for a period of time, for whole buildings on a campus.

As the pace of new compute infrastructure continues to accelerate (with new products and configurations frequently evolving), a phased release of the work

also helps developers incorporate the latest technology and best practices into their projects, mid-stream. What was the latest and greatest for the first phase of a project may be one (or two) cycles behind by the time the final phase is released for construction. This is particularly true for larger projects involving multiple buildings or fit-outs.

A phased release of the work has also become increasingly useful for larger projects supported by modular data centre units. These modular units are often deployed in the earlier phases of the project (largely due to their reduced costs, activation timelines, and flexibility to function with existing power at the site), and help developers bring projects online (partially, at least) even while the larger stick-built buildings or additional electrical infrastructure are still under construction.

A phased approach, however, does require some trade-offs, and reasonably so: The more of the stage that is set (waiting for the owner to yell “action” with a notice to proceed), the greater the commercial risk to the contractor with respect to inflation, demand spikes, employment overhead, availability of materials and equipment, and the like. So, depending on the circumstances, it may be fair to lock some aspects for a longer period, while others may be open to renegotiation after an agreed period of time. For example, subcontractor pricing may be locked for six months after pricing is established but, after that, the contractor may re-bid the subcontracted scope, whereas the contractor may not revisit its general conditions, general requirements or fee. It is likewise reasonable to allow the contractor to exit if there is an extended period between completion of one phase and commencement of the next; otherwise, the contractor may be in a position of indefinitely preserving capacity, the cost of which is likely to be transferred to the owner, in one way or another.

Pricing subcontractor risk

The hallmark of a general contractor is that, unlike a construction manager, it is responsible for (liable for) the quality of the work of its subcontractors – the contractor is on the hook for defective work even if the subcontractor can’t or won’t remedy the problem. Traditionally, the contractor is compensated for this

risk with its fee. In the last decade, and particularly on large-scale projects, contractors have sought to convert this from a contractor risk to an owner cost, in the form of subcontractor default insurance (SDI), bonds or other mechanisms, the cost of which is passed on to the owner.

For an apples-to-apples comparison, data centre developers should tease out these details in the negotiation process, and address whether the contractor will seek to avoid some of that liability, or, if not avoiding such liability but instead compensating with insurance, what the proposed costs of insurance will be. At the most basic level, this is a commercial point, as a contractor with a 2.5% fee is less expensive than a contractor with a 2% fee that also charges 1% for SDI (assuming equally reliable contractors). Bonds are often more expensive than SDI, but may provide better protection. If a contractor demands SDI, data centre developers are well-served to shop SDI policies through their own insurance brokers, particularly if they develop at scale, as mere tenths of a percent can equal significant amounts.

Nevertheless, in all cases, the commercial and legal terms should be negotiated almost contemporaneously or with the legal terms slightly staggered behind the commercial terms. Otherwise, the initial commercial terms may reflect differing expectations about the contractor’s world of liability, leading to renegotiation of commercial terms too far down the runway or unfavourable legal compromises.

Owner-furnished equipment

Data centres are equipment-heavy industrial and technical facilities, requiring generators, switchgear, cooling systems, servers and a myriad of other widdets. Developers can find value in creating their own relationships with suppliers and procuring equipment directly, rather than through the contractor, so long as the design is stable or at least predictable. A developer can order items early enough (and even before a contractor is engaged) to combat long lead times, secure volume discounts (particularly if purchasing for multiple projects) and save costs by not paying the contractor a fee on top, though still paying the contractor to receive, store and install the item. By supplying the item, a developer is taking on some risk

of a failed delivery or a change in design, for example, but the savings in cost and time may be worthwhile. The developer should inform the contractor of manufacturer requirements for handling and installation, so as not to impair the warranty.

In the office world, comparatively, the cost of equipment relative to the rest of the project is significantly less than with a data centre, meaning that the fee avoided on data centre equipment is more significant, and some contractors may seek a separate fee on that owner-sourced equipment, ostensibly for the added risk in handling that equipment. But because the equipment is typically protected by insurance already in place (such as the builder's risk policy), the added risk is relatively low. For that reason, some have moved away from that fee model.

Alternatively, some developers have moved towards a modified fee structure, paying contractor a lower fee on contractor-procured (ie, traditionally procured) equipment, reasoning that, dollar-for-dollar, the risk associated with the cost of a widget is less than with an equally-priced scope of subcontracted labour. At that lower rate, the balance of risk and savings may tip towards having contractor procure all of the equipment.

California five percent retention

As of 1 January 2026, California Civil Code Section 8811 limits retention on new private project construction contracts in California to 5%, subject to exceptions for certain residential projects. Previously, there was no established maximum, though developers and contractors typically agreed to 10%. This new limitation applies to data centres as equally as other commercial projects. Given the relatively high value of data centre builds, developers should carefully consider whether to tighten other controls on retention, such as not allowing early retention releases for certain subcontractors or reductions in the retention percentage once the project has achieved a certain level of completion. Where 10% may have allowed enough wiggle room to accommodate early release of retention on rough grading subcontractors, for example, 5% does not provide the same margin.

California prevailing wages on renewable energy projects

Data centres are frequently paired with photovoltaic (solar) or other renewable energy systems. Often-overlooked California Public Utilities Code Section 769.2 requires that the contractor pay prevailing wages (similar to a public work) when a project includes a renewable electrical generation facility and uses net energy metering (NEM; selling electricity to the utility). There are other criteria, and exceptions apply for certain residential projects. Many data centres are likely to consume renewable energy generated on-site and may not use NEM, likely avoiding application of Section 769.2. But for those that do use NEM, pre-contract planning is essential to evaluate the impact Section 769.2 may have. Note that the California requirement is discrete from prevailing wage and apprenticeship requirements related to electricity production tax credits under the Inflation Reduction Act.

The take-away

Data centres – once a subset of the industrial building market – are indeed their own category now, given the monumental demand. Traditional commercial and legal terms applicable to commercial construction, generally, have become stale and insufficient in the world of high-value, need-it-tomorrow data centres. Data centre owner-developers are well-advised to make sure their construction agreements are properly adapted to data centre builds and the current state of the contracting market.

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