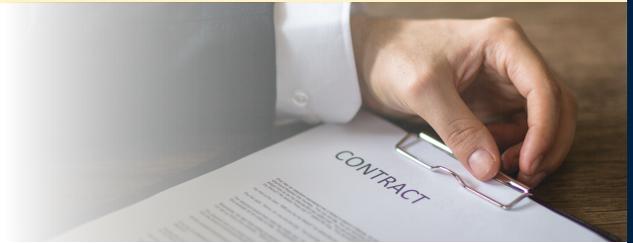


Understanding Contract Payment Provisions

By Aman Kahlon



Payment terms and conditions are an important piece of every construction contract. Taking some time to understand your payment obligations will help you successfully administer your project and, hopefully, avoid disputes. Although many construction projects utilize industry-standard form contracts with set payment terms, such provisions may, in practice, vary slightly or substantially from contract to contract, and it is important to understand the different obligations and rights that may arise under the payment section in any contract, regardless of the form used. Below is insight on how to navigate and apply some of the typical elements of payment provisions in construction contracts.

TIMING

Be aware of the payment timing requirements in your contract regardless of whether you are billing for or paying for the work. If you are a contractor contracting with a subcontractor, make sure your project manager understands the time period provided for review and approval of a subcontractor's payment application. Many contracts will require a contractor to dispute an application within a certain number of days; otherwise, the application will be deemed approved.

That same contractor will also want to know when payment on undisputed amounts is due in order to avoid any state prompt payment act violations. Many states use prompt pay acts to ensure timely payment from owners to contractors and contractors to subcontractors. Failure to adhere to the requirements of a particular state's prompt pay requirements can make the paying party liable for interest on past due payments, as well as payment of the billing party's attorneys' fees and costs incurred in order to collect on the past due payment.

For subcontractors, be mindful of "pay when paid" or "pay if paid" provisions in the contract. If your payment is tied to owner payments to the contractor and there is any delay in paying the contractor, you may experience delays irrespective of the timing requirements contained in your agreement. You need to plan your cash flow needs accordingly.

CONDITIONS FOR PAYMENT

Many contracts will require submission of a signed payment application before the obligation to review and approve billings accrues. Other contracts require additional documentation, which may come in the form of partial lien waivers or itemized schedule of values documenting

percentage of work completed. Before beginning work, you should make sure you understand what documentation is required, as failure to satisfy express documentation requirements is a simple way for a party to delay payment on a bill that is otherwise due and owing.

Pay particular attention to any partial lien waivers that an upstream party requires as a condition for payment. Aggressive upstream parties may draft broad lien waiver forms that effectively waive all claim rights through the date of partial payment on a particular payment cycle. Many courts will enforce the express terms of these waivers, so you should be weary of executing such forms, especially when you have pending claims or disputes with the owner or contractor you are billing. If an upstream party insists on submission of a broad waiver and you know you have change orders or other claims pending, one way to handle is to include a reservation of rights in the form before signing.

As mentioned above, an upstream party may also have review and approval authority over any payment application. As the upstream party, you should understand and try to adhere to any contractual notice requirements if you decide to dispute payment. As the billing party, you should recognize the contractual reasons that may be proffered for disputing or rejecting payment and be prepared to rebut in writing any such excuses for nonpayment.

CONCLUSION

Payment on construction contracts can be contentious. Owners are often dealing with lender financing issues that may complicate or delay payment, and contractors and subcontractors may encounter cash flow concerns if payment is withheld, which can impact the project schedule and progress of the work. If payment terms are properly dealt with through the parties' contract and the parties operate in good faith, most construction projects will achieve successful completion without substantial payment disputes arising.

However, if disputes regarding payment do arise, you should comply with your contract requirements as best you can. In the event that your dispute escalates to litigation, compliance with the contract payment terms will likely be given substantial consideration by whatever judge or arbitrator is hearing your case. If you have a substantively sound argument for disputing or demanding payment but fail to satisfy express payment terms under your contract, you may face an unfavorable outcome, so proceed diligently and carefully to avoid that result. ■

ABOUT THE AUTHOR

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