

Contractual Modifications For a Changing Marketplace

Though the construction industry has irrevocably changed during the past four years—with tighter project financing standards, owners struggling to stay solvent and subcontractors defaulting in record numbers—many firms continue to cling to outdated business practices and contractual provisions. In addition to seriously altering their bidding practices, staffing decisions, and even the means and methods by which they perform work, companies can protect themselves with relatively minor contractual revisions that redistribute the risk of nonpayment or nonperformance more equally among contracting parties.

CONTRACTORS' RIGHT TO VERIFY FINANCING

Lender involvement in construction projects has skyrocketed as investors seek to minimize their risks. As a result, lenders often are included in the construction contract as a third party. To account for lender activities, contractors should consider adding an express provision to their contracts that gives them the right to confirm sufficient financing exists at certain stages of the work.

For example, a contract that allows the contractor to confirm available funds for

owner-issued change orders increases the contractor's chances of timely payment for the work. Furthermore, projects scheduled to be built incrementally may benefit from a provision that allows the contractor to verify continued financing between phases.

BIMONTHLY PAYMENT APPLICATIONS

Contractors that shorten their payment periods are less likely to have significant exposure in the event of owner or lender

default. The traditional payment model requires payment applications every 30 days; a contractor that shortens this period to every 15 days can assess potential defaults earlier and faces less exposure in terms of unpaid labor and materials costs.

Although preparing payment applications twice as often presents an increased administrative burden, the benefit of significantly reduced risk may be worth the effort. This is especially true on projects with a highly condensed schedule, which can result in overhead and general conditions savings to the owner, but also requires the contractor to assume additional risk associated with the increased volume of labor and materials between payment applications. A contractual provision reserving the contractor's right to bill every two weeks can be highly advantageous in this marketplace.

SHORTENED NOTICE AND PAYMENT CYCLES

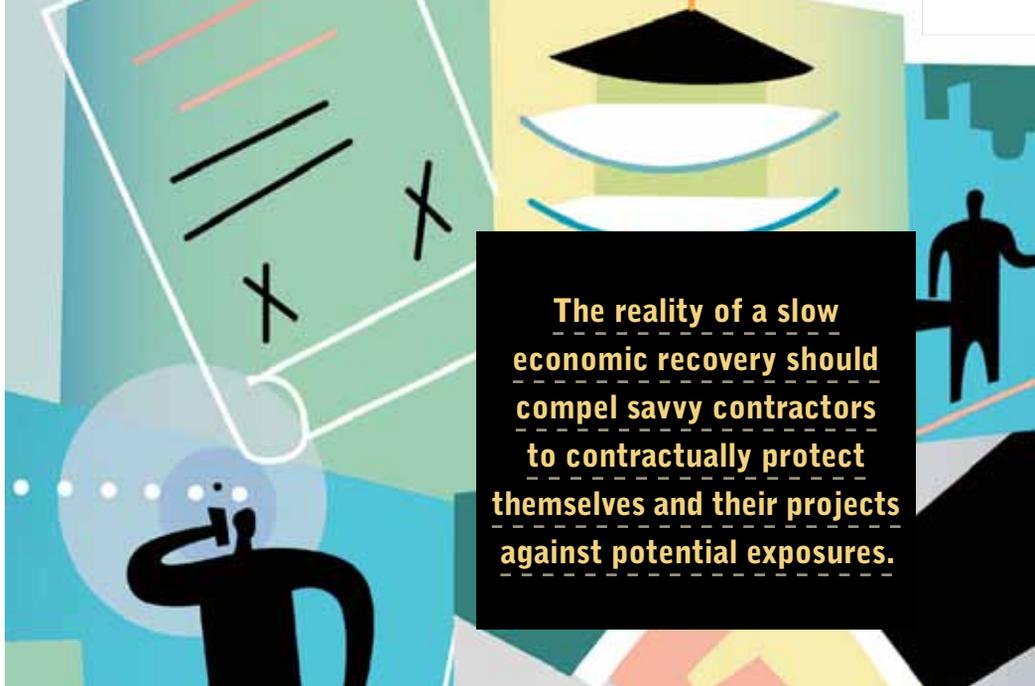
Traditional construction contracts require a contractor to submit a payment application for the previous month, wait 30 days for payment, provide 14 (or more) days notice of nonpayment, and then provide notice



LEGALLY SPEAKING

of default or termination. This outdated model can be found in virtually every standard form contract despite the fact it obligates a contractor to continue work without payment for 60 to 90 days at a minimum.

The remedy is relatively easy: Amend the contractual provisions to shorten these notice and payment periods. If a contractor moves to bimonthly payment applications, it's reasonable to shorten the time required for payment to a 15-day period and the notice for nonpayment to a seven-day period. These relatively minor revisions allow a contractor to shorten the time frame for stopping work after nonpayment and decrease its exposure in the event of owner default.



The reality of a slow economic recovery should compel savvy contractors to contractually protect themselves and their projects against potential exposures.

What I know:

- I know that at any one time, we may have 30 large construction projects underway all over the world.
- I know that by hiring 70 percent of our workers from the community in which we're building, we build more than just a project.
- I know the only way to run an international construction company is to delegate.
- I know that coaching a competitive soccer team relates to running a successful construction company in ways you might not realize.
- I know that working with people is supremely satisfying.
- I know our success is predicated upon allowing people to do what they know.
- I know we can allow Bradley Arant Boult Cummings attorneys to do what they know, and B.L. Harbert International will be well served.

That's what I know.


JIM REIN
CHIEF OPERATING OFFICER
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SUBCONTRACTOR DISCLOSURES

Diligent and responsible contractors often are forced into double payment situations by subcontractors or suppliers without a direct contract with the general contractor. Although some state lien laws offer protection from these types of lower-tier subcontractor claims, firms can secure additional protection with an express contractual provision in subcontracts requiring the subcontractor to disclose all of its lower-tier subcontractors and suppliers. Contractors can then use this provision to ensure the subcontractor has paid each of its lower-tier subcontractors and suppliers out of each payment draw.

Many contractors also require subcontractors to submit lien waivers from each lower-tier subcontractor or supplier with each payment application. This gives the contractor the right to demand evidence of payment from the subcontractor, and adds reassurance by knowing which lower-tier subcontractors and suppliers are working on the project to confirm payment and prevent claims.

As the construction industry leaves the chaos of the past four years behind, the harsh lessons imparted by the recession and the reality of a slow economic recovery should compel savvy contractors to contractually protect themselves and their projects against potential exposures.

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