

Contract Language and Documentation

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Agenda

- Payment issues.
- Warranties.
- Change orders.
- Project delays and inefficiencies.
- Pay-when-paid clauses.



Full-Price Lien

- Ala. Code § 35-11-210.
- Lien for full amount of materials regardless of whether value of materials exceeds unpaid balance due by owner to general contractor.
- To defeat, owner must object to services or materials.

Form of Notice to Owner

“Take notice, that the undersigned is about to furnish _____, your contractor or subcontractor, certain material for the construction, or for the repairing, altering, or beautifying of a building or buildings, or improvement or improvements, on the following described property:

and there will become due to the undersigned on account thereof the price of the material, for the payment of which the undersigned will claim a lien.”



Tenant Lien

- Ala. Code § 35-11-212.
- Has limited practical application
- When contractor contracts with tenant (instead of landlord), lien applies to leasehold interest or to improvements if improvements can be removed without damage.
- *Matador Holdings, Inc. v. HOPO Realty Investments, LLC*, 77 So.3d 139 (Ala. 2011); *Lloyd v. Stewart*, 60 So.2d 911 (Ala. 1952); cf. *Kirkpatrick Concrete Company, Inc. v. Birmingham Realty Co., Inc.*, 598 So.2d 796 (Ala. 1992)

Alternative Avenues for Payment

- Surety bonds:
 - Performance bonds.
 - Payment bonds.
- Federal Miller Act (40 U.S.C. § 3131).
- Alabama “Little Miller Act” (Ala. Code § 39-1-1).
- Prompt Payment to Contractors and Subcontractors Act (Ala. Code § 8-29-1).

Surety Bonds

- Usually requirement for general contractor (GC) as part of contract.
- Generally, guarantees performance by principal (usually GC).

Surety Bond \neq Insurance Policy

- Surety bonds cover economic damages from breach of contract; insurance policies don't.
- Surety has indemnification rights against principal; insurance carrier cannot assert **subrogation rights** against insured.



Performance Bond

- Inure to benefit of owner.
- Surety will not assume GC's role OR pay claims asserted by owner unless—
 - **GC defaults** and
 - GC refuses to remedy default.
 - If dispute arises of whether there is default, surety will typically tender their defense to GC.

Payment Bonds

- Inure to benefit of “downstream” parties: subcontractors, laborers, suppliers, etc.
- Guarantees all payments due for services or materials furnished for project.
- Benefits owner because owner doesn't have to worry about liens being filed against property.

Federal Miller Act

- When contract exceeds \$100,000, contractor must post performance and payments bond.
- Surety must be on U.S. Treasury list of qualified sureties.
- Civil action to enforce claim after 90 days.
- Second-tier subcontractor must provide notice to prime contractor within 90 days.
- Statute of limitations: 1 year.

Alabama “Little Miller Act”

- When contract exceeds \$50,000, contractor must have—
 - Performance bond (100% of prime contract amount).
 - Payment bond (50% of prime contract amount).
- No distinction between first- and second-tier subcontractors or suppliers. Applies to “any person.”

Alabama “Little Miller Act” (cont.)

- Notice requirement: 45 days.
- If surety fails to pay within 45 days, claimant can recover attorney fees and interest on unpaid principal.
- Statute of limitations: 1 year.

Prompt Payment Act

- Owner required to pay—
 - According to contract terms.
 - **If no terms, within 30 days after request for payment.**
- Contractor has to pay—
 - According to contract terms.
 - **If no terms, within 7 days after receiving payment from owner.**
- Interest at 12% a year.
- Possible attorney fee.

Retainage

- Retainage on private projects capped at 10% of estimated amount of properly performed work until work is 50% complete.
- After 50% complete, **no additional retainage.**
- “Downstream” retainage **may not** exceed “upstream” retainage.

Right to Retain Payments

- Applies when “bona fide dispute” exists over claimant’s right to receive payment.
- Withholding party must provide written notice of dispute within 5 days of request for payment.

Exempt Parties

- Residential homebuilders.
- Improvements to residential property consisting of 16 or fewer residential units.
- Contractors, subcontractors, and sub-subcontractors when contract is worth \$10,000 or less.
- Contracts with state or local governments.

Warranties

- Implied warranty of habitability (residential only).
- Express warranty provided by contractor or builder.



Implied Warranty of Habitability

- An action alleging a breach of warranty is a subset of a breach-of-contract action and each new house constructed within the State of Alabama carries with it an implied warranty of habitability.
- This implied warranty may, however, be waived or disclaimed via contract.
- Does not apply to commercial projects.

Express Warranty by Contractor or Builder

- In many cases, a homebuilder will warrant its work in accordance with the standard “2-10” home buyer’s warranty which covers workmanship defects for 1 year, systems defects for 2 years, and structural defects for 10 years.
- Commercial warranties are typically 1 year from “substantial completion.”
- Manufacturer’s warranties typically inure to owner.

Changes to Work: Change Orders

- Most, if not all, contracts allow an owner to make changes to the project, even after the GC and its subcontractors have commenced construction.
- Problems rarely arise out of minor changes which do not affect the project schedule or contract amount.
- On the other hand, changes that involve additional work or require additional time to perform will normally entitle the GC and affected subcontractors to additional compensation and an extension of time to complete the work.
- In an ideal situation, the effect of such changes will be agreed upon ahead of time and memorialized within a written **change order**.
- Without a written change order, disputes are **very** common.

Changes to Work: Owner Directive

- If an Owner and GC cannot agree upon the effect of a proposed change ahead of time, some contracts provide for an owner directive.
- This document requires the GC to implement the change in exchange for a “reasonable” adjustment in the contract amount or an extension of time.
- This procedure works best when the GC is contractually entitled to full reimbursement of its costs to implement the change and can include those costs within its normal applications for progress payments.

Changes to Work: Practical Note

- Changes to the work or project schedule are **hotbeds for litigation** if the written change order or owner directive procedures are not used.



Project Delays and Labor Inefficiencies

- Owners, contractors, and subcontractors budget a project in accordance with the project schedule.
- When a project is delayed and is, thus, not completed within the allotted time, claims for economic losses related to the delay are common.

Claims by Owner

- Delays to revenue-producing projects will often result in lost profit opportunities for the project owner.
- **Liquidated Damages:** Most construction contracts anticipate such delays and allow the owner to recover “liquidated damages” for each day the project is delayed beyond the anticipated or scheduled date of completion.
- **Re-sequencing or acceleration:** If delay occurs during project, some construction contracts grant the owner or GC the right to demand that remaining work be re-sequenced or accelerated to “make up” for lost time. In the absence of a contractual right to re-sequence or accelerate the work, such changes will often result in requests for additional compensation from the GC and or its subcontractors.

Claims by Contractors and Subs

- **For delay:** When a project is delayed through no fault to the GC or its subcontractors, the GC and its subs may have claims for extended labor and field office overhead during the delay period. The justification for such claims is that the delays increase the contractors' costs and, therefore, renders their work less efficient. If these extra costs are not reimbursed, the contractors' anticipated profits are diminished.
- **Weather and other acts of god:** Most contracts allow for delay or inefficiency claims related to extend periods of bad weather or other natural events (for example, hurricanes, tornadoes, lightning damage, earthquakes, etc.).
- **Concurrent delay:** When a contractor contributes to the alleged delay by its own actions or non-actions, the casual link between its damages and the otherwise compensable delay may be broken.
- **No-damage-for-delay-clauses:** Many construction contracts limit a contractor's recourse for delays to an extension of time to complete the work, thereby requiring the contractor to waive claims for additional funds related to the delay.

Claims for Labor Inefficiencies

- If the GC or its subcontractors, through no fault of their own, are required to **accelerate** their work schedule, the resulting increase in labor costs often gives rise to labor inefficiency claims against the owner.
- These claims are usually based upon the increased labor burden from additional workers or overtime required to comply with the compressed or accelerated schedule.

Pay-When-Paid Clauses

- Requirement that subcontractor is not paid until condition precedent has been met, such as the owner pays the GC

OR

- Mere timing mechanism for subcontract payment.



Pay-When-Paid Clauses (cont.)

- **Condition precedents** are not favored in contract law and will not be upheld unless there is clear language to support them.
- If two parties knowingly, clearly, and unequivocally enter into an agreement whereby they agree that the respective liability of the parties will be determined by some type of agreed-upon formula, Alabama law permits the enforcement of that agreement as written.

Example: Pay-If-Paid Clause

- “Notwithstanding anything else in this subcontract or the contract documents, the obligation of contractor to make any payment under this subcontract . . . is subject to the express and absolute condition precedent of payment by owner.
- It is expressly agreed that contractor and its surety shall have no obligation to pay for any work done on this project until contractor has received payment for such work from owner.
- **Subcontractor expressly assumes the risk of non-payment by owner.”**

Example: Pay-When-Paid Clause

- “Final payment, consisting of the unpaid balance of the price, shall be made within 45 days after the last of the following to occur:
 - a. . . . ;
 - b. . . . ;
 - c. Final payment by owner to contractor under the contract on account of the work.”

Payment Within Reasonable Time

If pay-when-paid clause applies, payment must be made within a **reasonable time**.



Questions?

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