Construction Contracts:
Best Practices for Minimizing Risk

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Melissa Dewey Brumback

Ragsdale Liggett PLLC
2840 Plaza Place Suite 400
Raleigh, NC 27612

Phone: 919-881-2214 (direct)
Email: mbrumback@rl-law.com

Construction Law in North Carolina Blog:
www.constructionlawNC.com

CONSTRUCTION CONTRACTS:
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The only constant is change.

--- Heraclitus, Greek Philosopher

A. NEGOTIATING KEY CONSTRUCTION CONTRACT TERMS

Reducing risk starts before the ground is broken on a construction project. Construction contracts are unique in that they anticipate change will occur during the project for a multitude of reasons. However, not even the built-in change clause can anticipate every problem. That is why good communication and clear expectations of the parties up front are essential to minimizing or avoiding risk.

1. Scope of Work

The Scope of Services is the first place where parties can get sloppy. This is unfortunate, because the Scope of Services can be the place where any confusion as to who has what duties can be clarified and addressed. The more detail provided in the Scope of Services, the less confusion on the part of the owner as to what he is paying for, the less confusion on the part of the contractor as to what he actually contracted to provide, and the clearer understanding of the A/E's role on the project.

If, for example, your client is providing Construction Administration services, you should **specify the number of site visits** per week/month required and the number and nature of construction meetings that includes. If your contractor client's bid is based on an assumption of a certain quantity of material on site (such as rock) which must be removed, you should state **what quantify** of rock is included in the base bid or scope, and what levels will be deemed change condition or additional services. If you do not clarify this, your client may find that as the contractor he is responsible for unexpected conditions on the project.

It is also imperative that you have a list of Excluded Services. While it might seem obvious that anything not specifically admitted in the Scope of Services is automatically excluded, lawsuits have been filed over this very issue. Because Scope of Service terms tend to be broad or ill-defined, the owner may assume the A/E or contractor is agreeing to perform services which the A/E or contractor is not prepared to do. Agreements can and do erupt over whether or not a particular item is included in the Scope. Therefore, if your carefully drafted Scope of Services does not clarify the issue, you can have a fall back safety measure of the Excluded Services in which to resolve the issue amicably.

Furthermore, by having complete lists of both included and excluded services, there is much less chance that the parties will mistakenly have different ideas of what each parties' role is on the project. After all, "an ounce of prevention is worth a pound of cure," as the old saying goes.

Some specific items that should be addressed in the Scope of Services include:

- Additional Services: are they needed?
- The Proposal v. the Contract Description—which prevails?
- Compensation issues, including for changes or extended scope
- Value engineering issues, and who gets the credit?
- Unit Pricing, and when it applies?
- Extended construction: Is A/E paid for additional on-site administration?
- Delays: How will they be determined?
- Time considerations:
    - is time of the essence?
    - bonus for early completion?
    - Liquidated damages?
- Contingencies & Assumptions?
- Unforeseen conditions (i.e. bad soil)?
- Financing considerations of the Owner prior to Notice to Proceed?
- Timely delivery of Owner equipment (Fixtures, Furnishings & Equipment)?
- Safe harbor provisions for expected errors & omissions?

2. Responsibilities of the Parties

The responsibilities of each party should be clearly spelled out in advance. This is especially true on larger projects, where the Owner may have a representative on the site daily, while the A/E is only on-site weekly or less often. Schedules, drop-dead dates (particularly for time-sensitive projects such as student housing projects), and change procedures should all be addressed prior to the pre-construction conference.

- **Duties of Specific Parties**

On all projects there are standard duties and obligations of each of the parties:

The Owner's duties include access to the job site; allowance of a place to store of construction materials; ensuring that self-performed work does not interfere; furnishing surveys and site data, and complying with all payment terms of the contract. Unforeseen conditions also are the Owner's responsibility to pay for, as the Owner takes the risk for such conditions in the typical construction contract.

The Designer's duties include, first and foremost, workable plans & specifications (the Spearin doctrine). The Spearin doctrine states that if the contractor builds the project in accordance with the plans & specifications provided to him, he has no liability for any defects in those plans. Additionally, the designer acts as the owner's representative on the project, although his authority is limited by contract documents. Frequently, the designer's scope of work includes some on-site observation or construction administration; this should be clearly specified in detail in advance.

The Contractor's duties include means & methods of construction (techniques, sequences, procedures) for both himself and his subcontractors. Additionally, he impliedly warrants his work for merchantability and, at times, fitness for a particular purpose. The contractor must exercise good workmanship, and must warrant that materials are new and free of defect. He must also warrant that he has complied with the contract documents. The contractor is further charged with site supervision, scheduling, and proper staffing of the job.

- **Mutual Duties of all Parties**

All of the parties on a construction project have an implied, nondisclaimable duty **not to hinder** one another. The parties also have a mutual duty to **disclose material facts**. If one party has knowledge pertinent to the project, he is required to disclose it to other parties. For example, if the owner knows about unfavorable former site usage, he should disclose that to both the civil engineer and to the bidding contractors. Similarly, if a contractor learns of conflicts in the plans and specifications, he has a duty to disclose those discovered conflicts to the design professional.

All parties must perform in accordance with the **Standard of Care** for their industry. That is, each party is liable to perform in acceptance with the standard of care of others employed in the same profession in the same locale. An

architect must act as other architects would in the same situation; a contractor must act as other contractors would.

The parties sometimes attempt to add **indemnity provisions** to their contract whereby one party (usually the designer or contractor) indemnifies the other in the event of any third party lawsuit. Indemnity provisions are fraught with potential liability issues, including the potential that by agreeing to such an indemnity provision you might inadvertently waive your insurance coverage.

3. Dispute Resolution Procedures

Dispute resolution procedures should be discussed during negotiation, when everyone is still working well together. In addition to determining the forum for any matters in dispute, the contract negotiation phase is also the time to consider limiting damages, consequential damages, and/or incidental damages.

The ultimate arbitrator of any construction disputes will be either court or arbitration. Court could be a bench trial or a trial in front of 12 jurors. Arbitration can be AAA or private arbitration. There are different opinions as to which venue is more favorable to which type of case.

In AIA contracts, litigation is the default unless the parties explicitly choose arbitration by checking the appropriate box. In ConsensusDocs, the parties choose which ADR mechanism to use up front. In EJCDC contracts, a complex system of steps are outlined, starting with the Engineer's initial determination as the condition precedent.

Litigation has several advantages, including a large body of substantive law, set procedures to govern disputes, the right to appeal, and the better chance to get punitive damages. Disadvantages include the length of time to get to court, the minimal limitations to discovery, costly legal fees, schedules controlled by courthouse, the lack of finality due to the right to appeal, and the chance that the trier of fact (judge or jury) may not have knowledge of construction law and issues.

Arbitration also has pros and cons. It is generally more informal than litigation, and usually (but not always) faster and cheaper. The arbitrators are likely to be knowledgeable in construction law, parties have more control over the process and schedules, and parties can control the amount of discovery. Additionally, the hearing is confidential and as such there is no

public record. Disadvantages of arbitration include no right to appeal (except in limited circumstances), no right to discovery, no reasoned opinion (unless specifically consented to), and a very high probability of a compromise verdict, aka "splitting the baby".

One option that provides the benefits of arbitration while minimizing some of its concerns is that of **private arbitration**. A private arbitration, instead of an AAA arbitration, can be much less costly, extremely fast, and final. While private arbitration can be negotiated once a dispute arises, it is often easier to negotiate such a provision up front, before the project begins. Private arbitration considerations include: abbreviated discovery procedures; one person versus panel arbitration; and whether or not dispositive motions will be considered prior to the hearing.

B. MANAGING CONSTRUCTION CHANGES

1. Construction Administration & Supervision

Administration of Construction Contract is not construction supervision. The A/E who agrees to administer the contract is agreeing to provide management, budgeting, handling pay applications and change orders. The A/E is not agreeing to have authoritative control over the general contractor or his subcontractors.

Administration of the construction contract includes:

- Reviewing and certifying Applications for Payment
- Rejecting work that does not conform to the Contract
- Reviewing, approving, or taking appropriate action on shop drawings, samples, etc.
- Acting as initial arbitrator of disputes

On-site observation is "to become generally familiar" with the work. This is periodic observation, not inspection. Parties should document up front how often and under what circumstances the A/E will visit the site.

In contrast to the A/E, the **contractor has the role of supervising** the project. This includes supervision of subcontractors. Generally, the construction supervisor for the GC should be present every day there is activity on site.

2. Change Orders & Construction Change Directives

The contract "change" clause allows flexibility for the inevitable changes that arise in construction projects. If the parties agree on the change, it is documented through a written change order. It is imperative that the change order be in writing and be signed by all parties

When the parties can agree to the appropriate change to compensation and/or time for a change on the project, it is fairly straight-forward to execute a change. If the owner initiates the change, the design professional usually prepares the documentation. If the contractor initiates the change, to which the owner consents, the contractor typically prepares the documentation, which is then reviewed by the design professional.

To be effective, a change order should include:

- description of the additional or changed work to be performed;
- number of days the work is extended for this additional/changed work;
- amount of money contractor is to be compensated for the additional/changed work;
- signature and date of owner, architect, and contractor; and
- back-up proposals, invoices, logs, etc. to support the change order requested.

No other information is necessary to execute an enforceable change order. If the price is not yet determined but the parties have agreed to a unit price, the agreement for the unit price should be included in the change order. A follow-up revised change order can then include the actual number of units, and compensation, involved in the changed work.

When the terms cannot be agreed upon, either a **Construction Change Directive** (CCD) is issued (on AIA and ConsensusDocs projects), or a form of change order is issued (on EJCDC documents). Partial payment for such work is also contemplated by AlA A201, as set forth below:

> *7.3.3 If the Construction Change Directive provides for an adjustment to the Contract Sum, the adjustment shall be based on one of the following methods:*
>
> > *.1 Mutual acceptance of a lump sum properly itemized and supported by sufficient substantiating data to permit evaluation;*

.2 Unit prices stated in the Contract Documents or subsequently agreed upon;

.3 Cost to be determined in a manner agreed upon by the parties and a mutually acceptable fixed or percentage of fee; or

.4 As provided in Section 7.3.7.

7.3.9 Pending final determination of the total cost of a Construction Change Directive to the Owner, the Contractor may request payment for Work completed under the Construction Change Directive in Applications for Payment. The Architect will make an ***interim determination*** *for purposes of monthly certification for payment for those costs and certify for payment the amount that the Architect determines, in the Architect's professional judgment, to be reasonably justified. The Architect's interim determination of cost shall adjust the Contract Sum on the same basis as a Change Order, subject to the right of either party to disagree and assert a Claim in accordance with Article 15.*

If the contractor fails to promptly respond to or expresses disagreement with the method of calculating an adjustment, the adjustment is made by the architect on the basis of reasonable expenditures and savings attributed to the change, including a reasonable allowance for overhead and profit. (§7.3.6).

Similarly, the ConsensusDOCS 200 provide for changed work to be performed in the absence of complete agreement on the compensation terms. Moreover, it also provides for partial payment of that disputed work, to prevent the contractor from, in effect, providing the owner with a cost-free loan.

8.2.1 The Owner may issue a written Interim Directed Change directing a change in the Work prior to reaching agreement with the Contractor on the adjustment, if any, in the Contract Price or the Contract Time.

8.2.2 The Owner and Contractor shall ***negotiate expeditiously and in good faith for appropriate adjustments****, as applicable, to the Contract Price or the Contract Time arising out of an Interim Directed Change. As the Changed Work is performed, the Contractor shall submit its costs for such work with its application for payment with beginning with the next application for payment within thirty (30) Days of the*

issuance of the Interim Directed Change. ***If there is a dispute as to the cost to the Owner, the Owner shall pay the Contractor fifty percent (50%) of its estimated cost*** *to perform the work. In such event, the parties reserve their rights as to the disputed amount, subject to the requirements of Article 12.*

8.3.3 ***If the Owner and the Contractor disagree as to whether work required*** *by the Owner is within the scope of the Work, the Contractor shall furnish the Owner with an estimate of the costs to perform the disputed work in accordance with the Owner's interpretations. If the Owner issues a written order for the Contractor to proceed, the Contractor shall perform the disputed work and* ***the Owner shall pay the Contractor fifty percent (50%) of its estimated cost*** *to perform the work. In such event, both Parties reserve their rights as to whether the work was within the scope of the Work, subject to the requirements of Article 12. The Owner's payment does not prejudice its right to be reimbursed, should it be determined that the disputed work was within the scope of Work. The Contractor's receipt of payment for the disputed work does not prejudice its right to receive full payment for the disputed work, should it be determined that the disputed work is not within the scope of the Work.*

While the EJCDC C-700 does not have a separate construction change directive mechanism, it incorporates such owner-dictated changes into its work change order process. Where unit prices or lump sum fees are provided for in the contract, they are applied. Otherwise, a set percentage of the cost of the changed work is allowed by the contractor under §12.01.C.2:

1. if a fixed fee is not agreed upon, then a fee based on the following percentages of the various portions of the Cost of the Work:

a. for costs incurred under Paragraphs 11.01.A.1 [payroll and labor charges] *and 11.01.A.2* [material and equipment costs]*, the Contractor's fee shall* ***be 15 percent****;*

b. for costs incurred under Paragraph 11.01.A.3 [payment to subcontractors]*, the Contractor's fee shall* ***be five percent****;*

c. where one or more tiers of subcontractors are on the basis of Cost of the Work plus a fee and no fixed fee is agreed upon, the intent of paragraph 12.01.C.2.a and 12.01.C.2.b is that the Subcontractor who actually performs the Work, at whatever tier,

*will be paid a fee of **15 percent of the costs incurred** by such Subcontractor under Paragraphs 11.01.A.1 and 11.01.A.2 and that any higher tier Subcontractor and Contractor will each be paid a fee of five percent of the amount paid to the next lower-tier Subcontractor.*

In all cases of changes to the project, timely notice is required. The amount of time varies by the form contract:

Document	**Number of days for Notice**	**Pertinent contract section(s)**
ConsensusDOCS 200	14 days	§3.16.2 (site conditions); §8.4 (claims)
AIA A201	21 days	§3.7.4 (site conditions); §15.1.2 (claims)
EJCDC C-700	30 days	§10.05

Failure to comply with the notice provision under the contract can bar a delay claim.[1] However, courts sometimes, but not always, take a lenient view with regard to this provision.

Verbal change orders given in the field **should be documented as soon as possible** to avoid a "he said/she said" situation later on. Once any litigation occurs, it is a guarantee that many verbal conversations will be in hot dispute. To the extent that an oral change or directive is given, you should attempt to have it reduced to writing. At the minimum, you (or your client) should write a letter to all parties to confirm the oral change order and agreed upon price, even if you have to send the letter at the end of the day to confirm the conversation and work that took place that day. Meeting minutes are good, but an actual stand-alone letter is better.

Oral change orders can be enforced under the legal theory that the owner waived the written change order requirement of the contract, or under theories of equity such as *quantum meruit*. However, the equitable remedy is the fair market value for the services performed, not the agreed-upon price for those services. Even where a contract states that no oral modification is allowable, if the parties act consistent with an oral modification the court will allow the contractor compensation.[2]

In one North Carolina case, a contractor was ordered to utilize stronger 18 gauge material in lieu of the 20 gauge material originally specified in the contract. The Court held that the contractor **was entitled to make a claim for the oral change order despite the requirement of written change orders** specified in the contract. "The provisions of a written contract may be modified or waived by a subsequent parol [oral] agreement, or by conduct which naturally and justly leads the other party to believe the provisions of the contract are modified or waived . . . [3] In another case, the court held that the owner was required to pay where (1) the owner had ample notice of the "changed conditions" and the "extra work;" (2) the architect had ordered the work to be performed; and (3) the contractor notified the owner of the price estimates prior to performing the extra work.[4]

The Court may also find that the parties made a mutual mistake or encountered unforeseen conditions such that compensation should be made regardless of the contract terms.[5] . An example of a differing site condition case occurred in the *Davidson & Jones* case.[6] In that case, the contractor encountered four times the amount of anticipated rock (based on the owner's own figures). The court found that 10-15% was a reasonable variation, and it allowed compensation for the extreme conditions on site. In another case, excessive wetness which requires a large overrun in undercut excavation was deemed a changed condition for which compensation was justified.[7]

In some cases, though, the courts have refused to allow a claim based on an oral change order, **strictly adhering to the language of the express contract** where no "waiver" was found.[8] Therefore, no party should rely on an oral change order; instead, he should insist upon a writing for all changes to contract time, scope, or amount.

3. Schedule Delays

Projects inevitably experience some delay, often multiple delays from multiple sources. As the saying goes, "time is money," and on construction projects, every party has a duty to not delay or get in the way of any other party to the project.

The most crucial time issue on a construction project is, of course, the critical path. Many, though not all, construction projects begin with a critical path method (CPM) schedule at the start of the project. It is important that all parties review and understand their obligations under the CPM. If the delay affects the critical path, a milestone, or the date of substantial completion, the parties need to determine whether or not the delay is excusable and/or compensable.

a. Excusable delay

An excusable delay is one that is **not foreseeable and is not in control** of either of the contracting parties. If, for example, the steel market suddenly dries up causing delays in fabrication of key building components, this was likely unforeseeable (and not controllable) and, therefore, an excusable delay.

An excusable delay may entitle the contractor to a time extension. However, it **does not allow the contractor monetary damages**. For example, under AIA A201, Article 4.3.8.2, extremely adverse weather conditions may be an excusable delay where the weather is not foreseeable and it effects the scheduled construction. Other examples include "acts of God", labor strikes, and differing site conditions.[9]

b. Compensable delay

If a delay is not excusable, then by definition it is one that has been caused by one of the parties. If the delay is the owner's fault (or that of another contractor or the designer), the contractor is entitled to money damages. Likewise, if the delay is the contractor's fault (or its subcontractor), the owner is entitled to money damages if it delays the date of substantial completion.

Actual damages have to be proven by the party claiming damages. This is accomplished through the careful documenting of costs, invoices, time sheets, and related damages. If there is a valid liquidated damages provision, it will determine the amount of compensation for a compensable delay.

Indirect damages may be recoverable, if they are allowed under the contract and can be proven with a reasonable degree of certainty. These can include extended overhead, interest, lost profits, rents, equipment idle time, labor idle time, mobilization and demobilization fees, increased material costs, and related damages.[10] While such damages must be proved to a reasonable degree of certainty (i.e., they cannot be speculative), there is no requirement of complete or absolute certainty.

It is important to note that, left unaltered, "consequential damages" are limited or waived in the standard form contracts. Consequential damages include the indirect damages listed above.

Document	**Cite**	**Parties**	**Language**
AIA A201	§15.1.6	Owner-Contractor	Claims for Consequential

			Damages—mutual waiver
AIA B101	§8.1.3	Owner-Architect	Consequential Damages Waiver
ConsensusDOCS 200	§6.6	Owner- Contractor	Limited Mutual Waiver of Consequential Damages
ConsensusDOCS 240	§5.4	Owner-Architect/Engineer	Limited Mutual Waiver of Consequential Damages
EJCDC C-700	§12.03	Owner- Contractor	No damages paid to Contractor by Owner or Engineer
EJCDC E-500	§6.10.E	Owner-Engineer	Mutual Waiver of Consequential Damages

Some contracts contain "no damages for delay" clauses, in which a contractor's right to recover for time delays is limited. [Standard construction contracts typically do not contain explicit, all-encompassing, no-damages-for-delay clauses.] In those cases where a **"no damages for delay"** clause is present, the contractor's remedy is time extension only, and not money. Even with such a clause, money may be recovered if the contractor can show that the owner was grossly negligent, the delays were not anticipated, or the delays were so unreasonable that they essentially changed the scope of the entire project.

To establish a delay claim, the key is detail. You must demonstrate both the extent of the delay and the extent of the direct damages with a reasonable degree of accuracy.

c. Concurrent delay

Concurrent delays, where both parties are at fault, are generally not compensable in North Carolina unless otherwise provided for within the contract itself.[11]

C. TERMINATING THE CONSTRUCTION CONTRACT & PREPARING FOR A CLAIM

1. Termination & Suspension

Termination is the ultimate threat in a construction project. The owner may threaten termination of a contractor who fails to perform; conversely, a contractor who is not being paid in accordance with the contract documents may threaten termination.

In most cases, termination is a losing proposition for both parties. If your client terminates, such termination will most likely cost him money, even if the termination is proper. Therefore, it is vitally important to understand when and how a termination can legally occur and how to handle such termination threats.

Termination can be for default or for convenience. Termination for convenience is solely available for the owner, while either party can terminate for default:

Action	**Form Contract**	**Section**	**Details**
Suspension by Owner for Convenience	AIA A201	§14.3	No more than 100% of total days or 120 days in any 365 day period (whichever less, after which Contractor may terminate- see 14.1.2)
	ConsensusDOCS 200	§11.1	Up to 30 days (after which Contractor may terminate- see 11.5.1.2)
	EJCDC C-700	§15.01	Up to 90 consecutive days
Termination by Owner for Convenience	AIA A201	§14.4	Requires written notice
	ConsensusDOCS 200	§11.4	Requires written notice
	EJCDC C-700	§15.03	Requires 7 days written notice
Termination by Owner for Cause/Default	AIA A201	§14.2	Requires Architect certification that cause exists & 7 days written notice (14.2.2)
	ConsensusDOCS 200	§11.3	Requires 7 days notice to cure; 14 day additional notice (11.3.1)
	EJCDC C-700	§15.02	Requires 7 days notice of intent (15.02B); if Contractor corrects within 30 days cannot terminate (15.02D)
Termination by Contractor for Cause/Default	AIA A201	§14.1	Requires 7 days notice (14.1.3; 14.1.4)
	ConsensusDOCS 200	§11.5	Requires 7 days notice (11.5.1)
	EJCDC C-700	§15.04	Requires 7 days notice (15.04 A)

Termination/Suspension for Convenience

Regardless of which standard form contract is being used, only the owner can terminate, or suspend, the contract for convenience. This power is completely discretionary with the owner; however, contract sum and time are adjusted for increases caused by suspension, delay, or interruption.

Termination for Default

Both the contractor and the owner have a right to terminate for default.

Owner's Termination for Default

Under AIA A201 §14.2.1, the owner can terminate for cause, if the contractor materially breaches the contract in one or the following ways:

- persistently fails to supply enough properly skilled workers or proper materials;
- fails to make payment to Subcontractors for materials or labor in accordance with the respective agreements;
- persistently disregards laws, ordinances, or rules, regulations or orders of a public authority having jurisdiction; or
- otherwise is guilty of substantial breach of a provision of the Contract Documents.

Termination for cause must be for breaches which are "so material as in effect to defeat the very terms of the contract."[12]

Under ConsensusDOCS 200 §11.3, the owner can terminate for default if:

- Within 7 days of notice to cure, Contractor fails to commence and satisfactorily continue correction of the default. Owner may notify Contractor it intends to terminate for default absent correction within 14 additional days, after which it may provide written notice of termination.

Under EJCDC C700 §15.02, the owner can terminate for cause for:

- Contractor's persistent failure to perform Work in accordance with Contract Documents (including supplying skilled works, suitable materials, equipment, and following Progress Schedule)

- Contractor's disregard of Laws or Regulations of any public body having jurisdiction
- Contractor's repeated disregard of the authority of Engineer
- Violation in any substantial way of any provision of the Contract documents.

The Owner must provide contractor and surety 7 days written notice of its intent to terminate. (15.02C). If contractor beings within 7 days of notice of intent to terminate to correct its failure to perform and proceeds diligently to cure within 30 days of receipt of notice of intent to terminate, the Contractor's services will not be terminated. (15.02D).

Contractor's Termination for Default

A contractor may terminate the contract for a material breach in the following circumstances:

Under AIA A201 §14.1.1: if the Work is stopped for 30 or more days through no fault of the Contractor, for specified reasons only, which include:

- issuance of a governmental stop-work order;
- an act of government such as declaration of national emergency;
- failure of prompt payment or failure to issue a Certificate of Payment with no notified reason for the failure to issue such a certificate; or
- failure of the owner to show financial capability upon request.

Additionally, a contractor can terminate the Contract if it experiences repeated suspensions, delays or interruptions of the Work more than 100% of the total number of days scheduled for completion, or 120 days in any 365 day period, whichever is less. (14.1.2). Finally, a contractor can terminate for cause if work is stopped for 60 consecutive delays through the fault of the owner. (14.1.4).

Under ConsensusDOCS 200 §11.5.1: a Contractor an terminate for cause upon 7 days written notice, if the Work is stopped for 30 or more days through no fault of the Contractor, for the following reasons:

- under court order or order of other governmental authorities having jurisdiction;
- as a result of the declaration of a national emergency during which materials are not available; or
- suspension by Owner for convenience.

Additionally, a contractor may terminate with 7 days written notice if the Owner fails to furnish evidence of sufficient funding for the project, assigns the Agreement over contractor's reasonable objection , fails to pay the Contractor, or the Owner otherwise "materially breaches" the Agreement. (11.5.2).

Under EJCDC C700 §15.04 A: a contractor may terminate for cause upon 7 days written notice to Owner and Engineer, provided Owner/Engineer do not remedy the failure during that time, if:

- Work is suspended for more than 90 consecutive days by Owner or by order of Court or other public authority;
- Engineer fails to act on an Application for Payment within 30 days of submission; or
- Owner fails for 30 days to pay any sum finally determined to be due.

The contractor may, alternatively, stop the work in the issue is failure to pay within 30 days, until such time as payment is made of all amounts due, including interest. (15.04.B.)

Wrongful Termination

Wrongful Termination of Contract by Owner

If a contractor is terminated without cause, but the owner states that the termination is "for cause," the contractor can sue to recover for wrongful termination. The contractor would be entitled not only for compensation for work performed prior to termination, but also the net profit the contractor anticipated making on the unperformed portion of the contract.

Termination for failure to complete on time would be wrongful, unless the contract contains valid "time is of the essence" language. Without a "time is of the essence" clause, failure to complete on time would not give the owner the right to terminate for cause.[13]

Moreover, it would be wrongful for the owner to terminate after substantial performance of the contract by the contractor. That is, once the contractor has substantially performed his part of the work, the owner is not allowed to rescind or terminate the contract based on immaterial breaches.

Wrongful Termination of Contract by Contractor

If a contractor wrongfully terminates a contract and leaves the job, he will be held liable for the difference between the owner's cost to complete and the remaining contract balance. He would also be required to pay reasonable extra costs associated with the delay and the hiring of a new contractor.

For example: Owner and contractor enter into a lump-sum contract in the amount of $500,000 for the construction of a building. After 75% of the building is completed, and $375,000 has been paid to the contractor, the contractor terminates the contract by walking off the job. Owner has to hire another contractor to finish the remaining 25% of the work. Instead of costing $125,000 (the remaining contract balance), the new contractor charges the owner $200,000 due to the rushed conditions and half-finished status of the building. Additionally, the owner incurs $5,000 in direct actual delay costs and $10,000 in increased materials costs. The owner is entitled to obtain the extra $75,000 contractor fee, as well as the $15,000 in substantiated extra costs, from the original, defaulting contractor.

Steps to Proper Termination

To ensure no charge can be made for wrongful termination, you should be sure that (1) cause exists for termination; and (2) procedures are followed to terminate properly.

Contractor's Proper Termination

Prior to termination, the contractor can often elect to suspend the work if timely payments are not made by the owner (AIA A201 §9.7.1; EJCDC C-700 §15.04.B.). This is a safer course of action than termination, and it allows the owner a chance to cure. If the contractor must terminate for cause, he must provide a 7 day written notice to the owner regardless of which form contract he is utilizing.

Owner's Proper Termination

Although not required prior to termination, the owner can elect to exercise its right to stop work prior to taking the more drastic remedy of termination. The owner can stop the work if it is not proceeding in accordance with the plans, and the contractor's breach is substantial. (See AIA A201 §2.3.1). This is a recommended first step prior to termination. Further, the owner can elect to carry out portions of the work itself, provided it follows the notice requirements and gives the contractor an opportunity to comply.

Prior to termination, the owner must give a 7 day written notice to the contractor and, depending on the contract used, an opportunity to cure. After termination, the owner is generally permitted to choose any reasonable method for completing the work and charge that cost to the defaulting contractor, whether or not that method is the best method or the cheapest method.

2. Documentation & Preparation for Litigation

Documentation is the key to favorable resolutions to construction disputes. Daily, contemporaneous reports should be made, and all decisions should be documented in some manner, even if only in an email.

Any letters which state facts that your client disagrees with should be followed by a letter stating that he disagrees. Even though this can sometimes result in a "paper war," **nothing is worse than having claim after claim against your client made by the other side with no denials on your client's part**. A jury will not understand why your client did not defend himself from claims of wrongdoing at the time such charges were first leveled.

Your client should maintain all project documentation in a uniform matter, including proposals, contracts, invoices, time sheets, emails, letters, etc. The only exception is contact with the insurance carrier and lawyers. Remind your client that these communications should be placed in a SEPARATE physical location so they are not inadvertently disclosed in discovery.

If a possible claim is anticipated, it should be reported to the insurance carrier as soon as possible. Put your client to work in creating a timeline of key events and people so you can get quickly up to speed. Also consult your client about early expert retention to secure the most desirable experts.

CONCLUSION

Proper planning in advance of a construction project can ensure its success. Just as your client spends time reviewing owner requirements or the design plans, you and your client should spend time reviewing the contract documents. It is also vital your client follows all proper notification, documentation, and other requirements to ensure he obtains the time and money to which he is entitled in the event of changes to the scope or project schedule.

ENDNOTES

[1] *See D.W.H. Painting Co., Inc. v. D.W. Ward Construction Co., Inc.,* 174 N.C. App. 327, 620 S.E.2d 887 (2005); *American Nat'l Electric Corp. v. Poythress Commercial Contractors, Inc.,* 167 N.C. App. 97, 604 S.E.2d 315 (2004).

[2] *See Inland Const. Co. v. Cameron Park II, Ltd,* LLC, 181 N.C. App. 573, 640 S.E.2d 415, aff'd by 181 N.C. App. 573, 640 S.E.2d 45 (2007); *Triangle Air Conditioning, Inc. v. Caswell County Ed. of Educ.,* 57 N.C. App. 482, 291 S.E.2d 808 (1981); rev. denied by 306 N.C. 564, 294 S.E.2d 376 (1982).

[3] *Metric Constructors, supra*. *See also Centex-Rodgers Construct. Co. v. Wake County*, 993 F.2d 228, 1993 WL 147487 (4th Cir. 1993 (N.C.)) (unpublished disposition).

[4] *Centex-Rodgers, supra.*

[5] *S.J. Groves & Sons*, *supra.*

[6] *Davidson & Jones, Inc. v. North Carolina Dep 't of Admin.,* 315 N.C. 144, 337 S.E.2d 463 (1985).

[7] *Ray D. Lowder, Inc v. Highway Comm'n*, 26 N.C. App. 622, 217 S.E.2d 682, *cert. denied* 288 N.C. 393, 218 S.E.2d 467 (1975).

[8] *See, e.g., Brokers, Inc. v. High Point City Board of Education*, 33 N.C. App. 24, 234 S.E.2d 56, *rev denied by* 293 N.C. 159, 236 S.E.2d 702 (1977).

[9] *See, e.g., Lea Co. v. N.C. Bd of Transp.,* 308 N.C. 603, 304 S.E.2d 164 (1983).

[10] *See*, *e.g.*, *Biemann and Rowell Co. v. Donohoe Companies, Inc.*, 147 N.C. App. 239, 556 S.E.2d 1 (2001).

[11] *Terry's Floor Fashions, Inc. v. Crown General Contractors, Inc.*, 184 N.C. App. 1, 645 S.E.2d 810 (2007) (subsequent history omitted).

[12] *Opsahl v. Pinehurst, Inc.*, 81 N.C. App. 56, 64, 344 S.E.2d 68, 73 (1986), *quoting Childress v. Trading Post*, 247 N.C. 150, 156, 100 S.E.2d 391, 395 (1957).

[13] *Opsahl v. Pinehurst Inc.*, 81 N.C. App. 56, 344 S.E.2d 68 (1986).