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Identify Contract Terms Early To Ensure You Get Paid

By Dan Goldberg



Everywhere one turns these days, the discussion focuses on the economy. Again and again, newspapers, financial journals and trade magazines are emphasizing that we

are in a housing slump, lending is off and commercial construction has slowed. The price of petroleum-based products is soaring. As a subcontractor or supplier, bidding labor and commodity materials on construction projects is becoming an increasingly difficult exercise. The rules seem to change every day.

It's a perfect time to reassess some of the fundamentals. If you are a subcontractor or a supplier, there are certain issues that come up daily, particularly when funds are tight. Whose contract controls the deal? How can you best secure your position on a job? And is there a way to get paid for your efforts and still have business for the next job?

One of the essentials at the beginning of a job is determining whose terms and conditions control. A typical job will have a standard contract chain: owner, general contractor, subcontractor, supplier. From the supplier's perspective,

the ball usually gets rolling when the subcontractor asks for a quote. The supplier responds by giving the quote. On the quote, the supplier may say "Supplier's terms and conditions control the sale of materials." What happens when the subcontractor gives a purchase order to the supplier with terms that are different than those on the quote? The short answer is that unless the supplier responds to the subcontractor by acknowledging the order and taking exception to the different terms, the supplier has married the new terms.

Sometimes, the subcontractor's terms can include language such as "All terms of the subcontractor's contract with general contractor are incorporated by reference into this purchase order." Seems simple, but that single phrase can upend an entire order. Unless the supplier is savvy enough to read all terms of the purchase order, the supplier may have married plans and specifications without reviewing them, may have committed to warranty obligations, liquidated damages for delay, retainage and who knows what else. The same issue can arise at the subcontractor level, when a general contractor incorporates by reference terms of its contract with the owner into its contract with the subcontractor.

The takeaway, as obvious as it sounds, is to read the contracts that are given to you, top to bottom, front and back. Look for references to other documents, ask for copies of them and understand the issues that are important to you ahead of time. Certain provisions that receive little attention in a stable market, such as escalation provisions, are receiving lots of attention now. If the cost of steel, copper

wire, or various petroleum-based products rises steadily during the course of the job, someone is bearing the risk of the price increase. You need to understand if you own that risk. It's better not to have a deal than to sign up the wrong one.

If you are a subcontractor or supplier, there are a number of other questions you should ask on the front-end of the job to assess the risks of getting paid for your work, and it is critical to understand whether the job is public or private. Depending on the answer to that single question, you may have a set of rights that stem from a payment bond on the job, a set of rights that stem from a mechanic's lien on the job, or both sets of rights.

If the job is a public job, for example, state or federal (school, wastewater treatment plant, post office), you generally will have payment bond rights but not mechanic's lien rights. Some tend to think of payment bonds as insurance policies, which they are not. Others attribute a certain mystique to payment bonds, but there is really nothing mysterious about them. A payment bond, quite simply, is a contract, nothing more and nothing less. If a job is bonded, you should try to follow Big Bond Rules:

- Get a copy of the bond;
- Determine who the parties are; and
- Review notices and deadlines.

Bond claims involve appropriate notice and documentation. In order to make a bond claim, it's necessary to determine who the "principal" is under the bond. Sometimes it will be the subcontractor and sometimes it will be the general contractor. Bonds generally are different from one another

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and, to be safe, it is best to assume that the bond in place on one job with a customer is not the same as a bond that may be in place on another job (even if it is the same customer). On a public bonded job (such as an elementary school or post office), as opposed to a private bonded job (such as a supermarket), it is also important to pay attention to local statutes to determine notice requirements not detailed in the bond itself.

A mechanic's lien generally involves asserting rights against the actual piece of real estate involving the construction project. For example, if a seller has not been paid for materials sold to a subcontractor and used in the building of a private office building, the seller may be able to assert a mechanic's lien in the land where the building sits.

Generally, if the job is a public job, the seller will not have mechanic's lien rights.

(This is because, in most states, the seller's ultimate remedy in exercising lien rights is to force a sale of the piece of property lienied—and state legislatures don't want ABC Electric owning and running the local elementary school.)

There are a number of issues that need to be considered in order to perfect a lien, and Massachusetts significantly amended its lien law in 1996. Generally speaking, however, no one wants a lien asserted. The owner will not want it because a lien may interfere with its construction financing, the general contractor will not want it because of lien-free provisions in its contract with the owner, and the electrical subcontractor will not want it because of its contract with the general contractor.

As the construction industry slows, it's necessary to continually address how to get paid. Equally as important is being aware that there is a process for ensuring payment.

Communication is key, and no one wants surprises. Unless there has been a complete breakdown in the relationship, it is always a good idea to call the party you have your contract with first, instead of leapfrogging to the next level. No general contractor wants a distributor to go directly to the owner, and no owner wants a creditor speaking to a surety because making a claim often can affect how easily the bonded party can get its next bond and whether it will be paying a higher premium.

The trick is to get in early and recognize a problem as quickly as possible. A party's position, leverage and security will depend on job completion, who has been paid, whether bond rights or lien rights exist, and whether or not timely notices can be given. The process can be done professionally and objectively, and knowing your bond and lien rights can help you get paid for your hard work. ■