

# Surviving the Current Economic Crises in the Construction Industry

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It seems clear that the economic climate for the construction industry will not return to the pre-recession level for some time. However, if you work in, conduct business in, or are a part of the construction industry, there are techniques and best practices that not only will help you survive the current recession, but also may allow you to emerge from it stronger. Many of these practices are "best" practices to embrace regardless of the economic situation.

## **Measure Three Times, Mark Twice, Cut Once**

Planning is an integral part of the construction process. During a recession, planning is all that much more important and can make the difference between profit and loss, or even between survival and failure.

Make sure you record things in writing. This is particularly true of contracts and change orders. The terms of your agreements and contracts should be clear and set out in writing. The advantage of a written contract is that the terms can be determined with certainty. There are no "fuzzy" or "convenient" memory issues. You should read your contract. That sounds basic, but it is all too common to be lulled into the "that's just needless boilerplate, and I can't waste time reading it" mindset. It's really not "boilerplate"; it's "details," and the "devil is in the details." Don't stop at just reading your contract; be familiar with every term, conduct yourself consistently with each term, and let the other parties know that you expect compliance from them as well.

Change orders are perhaps the most common source of disputes on construction projects. At the end of the project, there can be multiple viewpoints on what changes were agreed to during the course of construction. If those changes are in writing, it's easy to determine what the parties intended. Otherwise, it's a swearing match.

The advantage of a written contract is lost if you don't - or can't - rely on that contract. Conducting yourself consistently with the terms of a contract is important as it avoids any implication that you have breached it or that certain terms have been waived or altered by your conduct.

Negotiate all the terms in your contracts. Although the contract amount is the most obvious term that you want to negotiate in your favor, there are other terms or provisions in your contracts that can be almost as important and may be easier to negotiate:

- Less or more retainage;
- Less or more frequent progress payments;
- Dispute resolution provisions;
- Notice provisions;

- Change order process; and,
- Backcharge process.

Regardless of what terms you are able to negotiate, be sure you read, understand, and rely on the contract you sign.

## **Cash is King**

Money on construction projects is not flowing as freely as it once was, and the security that a lien on real property provides is not as great as it once was. Remaining profitable, or even surviving, requires that you manage your work so that you're neither advancing monies for work not yet performed nor performing a significant amount of work without receiving progress payments. If you are an owner, general contractor, or upper-tier subcontractor, make sure that you pay your general contractors or subcontractors only for work that has actually been performed and performed properly.

If you are a general contractor or subcontractor, closely monitor the work you are performing and the amount you are being paid. Be careful not to perform significant amounts of work for which you are not getting paid promptly. The further ahead of your pay that you get, the harder the hit you will take if the stream of money dries up. You should never be in the situation where you owe your subcontractors for work they've performed, but you are not being paid for that work by the owner or your upper-tier contractor. Submit your payment applications promptly; follow-up on getting paid; and, if the owner or your upper-tier contractor gets behind on paying you, don't blindly continue working. Be prepared, if necessary, to suspend work.

Whatever your role, maintain a healthy relationship with your lender. This includes communicating forthrightly and frequently. Now, more than ever, ready access to capital, for whatever purpose, is an important strategic asset. Having a lender who understands the need and benefit of advancing funds at the critical moment can be the determining factor of whether a project succeeds or fails.

## **Tools**

There are various tools available to the parties in a construction project for forcing payment. There is a lien on the real property available to the general contractor and to subcontractors through the concept known as subrogation. Subcontractors also have the right to assert a lien on funds in the hands of upper-tier contractors and the owner.

Bonds are sometimes available to insure certain payments and performance:

- Public projects, and some private projects, require the general contractor, and sometimes subcontractors, to obtain payment bonds which insure payment for work performed and materials furnished by lower-tier subcontractors.
- Public projects, and some private projects, require the general contractor to provide a performance bond which assures the owner that the general contractor will perform.
- Bid bonds are sometimes available to provide assurance to the owner that the owner can rely on a bid made by a contractor.

Like any tool, these only work if used correctly with a comprehension of the full extent of their capabilities.

Liens on real property and liens on funds have requirements as to form and how and when they are filed and served. Failure to meet these requirements can eliminate or interfere with the associated lien rights, regardless of the substantive merit of the underlying claim. Likewise, there are certain requirements for asserting and pursuing claims against payment bonds, performance bonds, and bid bonds; failure to comply

with these requirements can eliminate or interfere with the protected party's ability to assert and pursue a claim against these bonds.

These requirements also can create a defense for the party defending against a claim. In addition, there may be requirements for asserting a defense to a contract, lien, or bond claim. Therefore, a party defending or opposing a claim – like the party asserting the claim – has a strong interest in understanding and being able to comply with these requirements. Being vigilant, acting early and decisively, and understanding the rules will help minimize the likelihood of errors or omissions that could be detrimental to your position.

### **Sharpen the Knife**

Unfortunately, a result of the current recession is that there is simply less construction work being performed and, therefore, less revenue and profit to be earned. Like a rain day on a construction site, periods of time with less work than necessary to satisfy your capacity provide excellent opportunities to:

- Maintain, repair, or upgrade your equipment;
- Relearn, update, and improve your processes;
- Provide training to your employees;
- Focus on areas for efficiency gains;
- Review your strategic plan; and,
- Identify problem areas in your organization that require attention.

### **Conclusion**

By embracing and implementing certain best practices – which provide benefits in any economic climate – you can increase your chances of surviving until better times while also putting yourself in a much better position to thrive once those times arrive.

*For further information regarding the issues described above, please contact Jason T. Strickland.*

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