



Proactive Measures to Mitigate Payment Disputes on Construction Projects



Strengthen your contracts to prevent litigation & delays

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Wednesday, June 12, 2024



Contractors, like any skilled professional, expect to be paid for their work. In exchange, owners expect to receive a completed construction project that is done in compliance with the project's specifications and applicable codes, and in accordance with any applicable deadlines under the governing contract. While this concept is relatively basic and understood, construction projects can become incredibly complicated, and things often do not go as planned. The last thing any

party to a construction project wants is a dispute that leads to litigation; however, they are increasingly common, and often lead to costly and complex litigation. The good news: Many disputes are avoidable if both sides take proactive measures at the start of a construction project.

Proactive measures can be as simple as including certain procedures in the governing contract and actually following those procedures. For example, it regularly surprises me how many contractors, large and small, do not take advantage of the payment procedures outlined in their contracts. Some of those payment procedures might force the contractor to fill out some extra paperwork and may seem inconvenient at times, but if those procedures are strictly followed, it places the contractor in a better position to receive both progress payments during the project and the final payment at the end of the job.

In today's South Florida construction climate, we are seeing many old buildings being forced to undergo both small and massive construction projects to satisfy the ever-demanding local building departments, who have been quick to attach building code violations to buildings and levy corresponding fines. Oftentimes, these old buildings are run by property management companies and/or voluntary condominium association boards of directors whose members are not construction professionals or developers. This often results in these sorts of construction projects proceeding rather informally; often, the contractor can become complacent and begin to treat the procedures outlined in the contract as "guidelines" rather than firm rules. When contractors do this and fail to take advantage of the procedures included in their contract, they run into problems.

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The payment and dispute resolution procedures in construction contracts, if crafted a specific way, can help avoid or mitigate many common disputes. For example, robust construction contracts typically set forth progress payment and final payment procedures that require the contractor to complete certain tasks prior to being entitled to payment, which can include a) providing subcontractor and material supplier lien releases; b) providing the owner with any material or labor warranties for the completed work; c) securing any necessary permits or local authority building department approvals; and d) securing payment approval from a third-party design professional, inspector or owner's representative.

When contractors skip these steps during the construction project and simply send pay applications or invoices directly to the owner, an unsophisticated and/or inexperienced owner might just make the payment without raising an objection. While that might seem convenient for certain progress payments during the course of the project when there are no disputes between the parties, ignoring the contractual requirements can create big problems for the contractor when there is a dispute or when final payment is due.

It is much easier to simply follow the contract, rather convincing a judge or jury that the owner "waived" its right to these pre-payment requirements. Following these steps and collecting documentary evidence that those steps were followed (such as securing all the required documentation) might cause the payment to arrive a little later than by taking the shortcut, but it sets the contractor up to be in a stronger position to be entitled to payment, undisputedly, under the contract.

Another common issue arises when the owner claims the contractor's work is defective. How does that play into payment? Defect claims can be standard procedure for construction project payment disputes. If the contractor skips the step of securing the approval of the third-party design professional, inspector or owner's representative (which can be included as a requirement under the contract), it places the parties in limbo. The owner will not make a payment if it believes the work is defective, and the contractor will not simply waive its right to payment because the owner is unhappy with the work. Securing the approval of the third-party design professional, inspector or owner's representative places the contractor in a much stronger position to be entitled to payment.

Another proactive measure to address the inevitable "defect" claim is to include a procedure in the contract where a neutral third party could serve to be the arbitrator of defect claim. If the parties follow that procedure, the defect claim can be addressed promptly during the project, rather than in a drawn-out payment dispute that could stretch into subsequent litigation. Most contractors have no opposition to correcting their own defective work and/or punch list items. That is not the issue. The issue is this: Who is making the determination that the work is defective? Of course, the owner has an interest in making a defect claim if it allows the owner to withhold all or a portion of a significant payment. If, however, there is a neutral, agreed-upon third party making that determination, the contractor will be much more likely to voluntarily correct the work.



Similar dispute resolution procedures can be instituted on a project to deal with delay claims, which are typically incredibly fact-intensive and require the review of thousands of project documents such as critical path schedules, change orders, daily reports, requests for information (RFIs) and documents detailing events affecting the schedule during the course of a project, which can include weather events, material or labor shortages, or other unforeseen issues. Similarly, because it may be in the owner's interest to assert a delay claim, a contractor will likely not be willing to simply take the owner's word for it if a delay claim is made. Involving a neutral third party could mitigate the potential dispute and/or avoid it entirely.

These are just a few procedures that can be written into a construction contract to help mitigate payment disputes during construction projects. However, while every possible mitigation procedure can be included in the contract, those procedures only work if they are followed. Although it might seem easier for the contractor to ignore the procedures outlined in the contract, ignoring those procedures could lead to a construction project payment dispute that could delay payment by months or years or potentially preclude any payment whatsoever.

Jacob A. Epstein is board certified in construction law by the Florida Bar and concentrates his practice in the areas of construction litigation, construction law and real estate litigation. Epstein regularly represents community associations and property owners during all phases of investigations and claims concerning defective construction and building code violations at high-rise buildings, homeowners' associations and condominiums. He has assisted his clients in recovering millions of dollars in multiparty, complex construction defect litigation disputes and regularly provides counsel prior to and during active construction and repair projects.

In addition, Epstein represents property owners, contractors, and design professionals in matters involving delay claims, construction contract disputes, Chapter 713 construction liens, bond claims, disputes arising out of preconstruction and post-construction purchase agreements and contract negotiations. He also has experience representing clients in matters involving community association law, collections and foreclosures, aviation fuel liens and business torts.
