Most well-drafted construction subcontracts expressly recognize the general contractor’s right to terminate the subcontract upon the default of the subcontractor. Typically, the specific events and circumstances that constitute a default are enumerated in the subcontract. A typical subcontract, for example, may provide that the subcontractor shall be deemed in default if the subcontractor (a) fails to prosecute the work with promptness and diligence, (b) fails to prosecute the work in a workmanlike, skillful, cooperative, safe, and careful manner, (c) fails to supply sufficient, adequate or competent supervision, (d) fails to furnish a sufficient number of properly skilled workmen, (e) fails to supply sufficient materials and equipment of the proper quality and quantity, (f) fails to promptly correct defective or deficient work, (g) fails to promptly pay its sub-subcontractors or suppliers or otherwise fails to faithfully discharge its financial obligations on the project, (h) fails to maintain the project schedule or otherwise materially delays the work of the contractor or other subcontractors, or (i) fails to submit any required progress, procurement, and man-hour completion schedules.

Most well-drafted construction subcontracts also provide the subcontractor with an opportunity to cure a default before the contractor is allowed to exercise its right to terminate the subcontract. Termination is an option not to be invoked lightly. Given that a termination for default is the construction industry equivalent of capital punishment, it is important that the subcontractor be given an opportunity to cure a default. Similarly, alternatives to termination should be carefully considered in advance and addressed in the subcontract. The extreme act of termination should not be the contractor’s only option in dealing with a subcontractor’s default.

Most well-drafted construction subcontracts will give a contractor several different options if the subcontractor fails or refuses to cure a default within the contractually specified time period. Such options might include (a) supplementing the subcontractor’s workforce, (b) having a second subcontractor take over a portion of the subcontractor’s work, (c) making direct payments to the subcontractor’s material and equipment suppliers, subcontractors, and laborers, or (d) accelerating the subcontractor’s work.

Against the possibility that termination may become inevitable if the subcontractor fails or refuses to perform or otherwise cure a default, the subcontract should give the contractor the express right to terminate the subcontract in whole or in part. The termination provision should allow the contractor to take possession of the subcontractor’s drawings (including as-built drawings), materials, tools and equipment as may be necessary or desirable to complete the subcontractor’s work with the contractor’s forces or with another subcontractor. It would also be prudent to have the subcontract language clarify that the contractor’s decision to first pursue one or more alternatives to termination does not prejudice the contractor’s right to later terminate the subcontractor or to claim damages against the subcontractor or the subcontractor’s surety.
The subcontract should also provide that if the contractor opts to pursue one or more of these alternatives to termination then the contractor may deduct its costs, together with resulting losses or damages, from any money due or that may become due to the subcontractor under the subcontract. The subcontract should make clear that in the event the unpaid balance due under the subcontract exceeds the contractor’s cost of supplementing or completing the subcontract work then the difference shall be paid to the subcontractor; but if such cost exceeds the balance due, then the subcontractor must promptly pay the difference to the contractor.

The facts and circumstances of construction contract defaults vary widely and are oftentimes both factually and legally complex. Given the potentially harsh results and consequences of a default termination and the death sentence that a default termination suggests, it is prudent to contact an experienced construction lawyer at the first sign of trouble and certainly well before taking the extreme action of terminating a construction contract.

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