

Mastering Payment for Stored Materials



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Disclaimer: This publication does not contain legal advice. The discussion is intended to provide information and guidance to individual subcontractors. Specific circumstances vary widely, so subcontractors may need to consult their attorneys before acting on the premises described herein. Each subcontractor should decide for itself the contract terms and conditions which it believes will best protect its interests. Subcontractors should not agree among themselves as to the form of contract terms and conditions they will use. Such agreements may violate federal or state antitrust laws and could result in the imposition of civil and/or criminal penalties.

Mastering Payment for Stored Materials

Introduction

Construction subcontractors that purchase and store materials in advance for their portion of a project face a special set of payment concerns. In practice, many subcontractors focus on assuring payment for work that they have properly performed. By contrast, in the case of stored materials, the subcontractor needs to focus on assuring payment for materials that it suitably stores before installation. Payment guarantees for stored materials are tied to factors such as the legal ownership of materials and the proper custody of materials. All but the most experienced subcontractors may need assistance from professional advisors to ensure that the proper payment guarantees are in place for stored materials.

Timely access to needed materials and equipment on the construction site is crucial for timely delivery of the project. Early delivery of materials and equipment is important from the perspective of both the subcontractor who performs the work and the owner who wants the project delivered on time. In addition to saving time, early ordering of materials can keep the project within budget by pre-empting price increases between bid time and the time that the materials and equipment are incorporated into the structure. Whether early ordered materials are delivered and stored at the project site, or on the subcontractor's own premises, the project benefits from a timely, adequate supply at a known price.

The main issue to address is the contractual and legal issue of payment. Payment for stored materials payments usually are made to the subcontractor before installation, as part of progress payments. The subcontractor and/or its advisor should research the prompt payment statutes that apply to the project. See the Foundation of ASA manual, [Prompt Payment in the 50 States](#), which is available on the [ASA Web site](#).

If the bid documents don't address payment for stored materials, a subcontractor may want to condition its bid on language assuring timely payment. Such language removes any ambiguity about whether stored materials are covered by the progress payment clause. Subcontract forms published by [ConsensusDocs](#) and the [American Institute of Architects](#) similarly provide that the subcontractor is entitled to payment for materials and equipment delivered to the site, or at another location if agreed in writing.

Even when a payment for stored materials clause is contractually in place, payment of the subcontractor is not unconditional. The payment clause generally applies specifically to "suitably stored" materials. So, what happens when there's a disagreement over whether materials were suitably stored? Subcontractors may consider approaching this problem by obtaining a written description of what "suitable storage" is from the owner or prime contractor. After all, each owner or prime contractor likely has a different interpretation of what "suitable" is.

A written document may offer some protection for the subcontractor in case a dispute arises. The subcontractor also may want to ensure that it has a clear, written understanding that it may store materials off-site.

The contractual risk of nonpayment is just one aspect of the payment risk of stored materials. For example, consider how the question of legal ownership of the materials may affect payment rights. Courts typically view the subcontractor as owning the materials until installation, but the owner may require a transfer of title when the subcontractor receives a progress payment for them (but still has not installed them). Suppose that the materials that the subcontractor is storing are damaged before the subcontractor transfers ownership to the construction owner or installs the work. Both the owner and the subcontractor's insurance company may wish to deny the subcontractor's claims for payment.

Most subcontractors would do well to have a frank discussion with their professional advisors to clarify whether their insurance coverage and contracts are adequate to cover all the nonpayment contingencies that stored materials involve.

For example, a subcontractor could use the ASA "Subcontractor Bid Proposal" to condition its bid on the ConsensusDocs Form 750, Standard Agreement Between Constructor and Subcontractor, which states:

"8.2.4 STORED MATERIALS Unless otherwise provided in the Subcontract Documents, applications for payment may include materials and equipment not yet incorporated in the Subcontract Work but delivered to and suitably stored on or off the Worksite including applicable insurance, storage, and costs incurred transporting the materials to an off-site storage facility. Approval of payment applications for such stored items on or off the Worksite shall be conditioned upon submission by Subcontractor of bills of sale and required insurance or such other procedures satisfactory to Owner and Constructor to establish Owner's title to such materials and equipment, or otherwise to protect Owner's and Constructor's interest including transportation to the Worksite."

The "Subcontractor Bid Proposal" is included in the ASA [Subcontract Documents Suite 2017](#), which is available on the [ASA Web site](#).

Subcontractor Concerns

Construction is a risky and expensive undertaking involving substantial credit and cash flow risks for the contractors and subcontractors involved.

One major reason that construction contracts provide for installment payments as construction proceeds is to supply the funds necessary for the agreed performance. Construction subcontractors regularly advance tens of thousands, or even hundreds of thousands of dollars of materials, equipment and labor every month that a construction project is active, all in exchange for a promise of future payment. Without sufficient cash

flow to continue such expensive operations, construction subcontractors face hardship or even bankruptcy.

Construction subcontractors need to fully appreciate their cash flow concerns and be willing to pay for materials and equipment that are delivered and suitably stored at either the project site or at another, agreed location.

ASA, the Associated General Contractors of America and the Associated Specialty Contractors endorse the following [Guideline on Payment for Stored Materials and Equipment](#):

Advance procurement of construction materials and equipment is a prudent practice that saves money and promotes the timely completion of construction projects. The Associated General Contractors of America, the American Subcontractors Association, and the Associated Specialty Contractors, suggest that construction project owners garner the full benefit of advance procurement by allowing progress payments to include payment for materials and equipment that are stored at the construction site or some other agreed-upon location. As a matter of careful construction practice, contractors and subcontractors often purchase and request delivery of construction materials and equipment soon after a contract is executed and well before the equipment or material is needed. The purpose of advance purchases is to assure that specified materials and equipment are available for installation or use in accordance with the construction schedule. Early procurement of materials and equipment also guards against escalating costs, particularly in long-term contracts, and enables the contractor and its subcontractors to make timely purchases when shortages may be a problem.

The contractor's and subcontractor's progress payments for suitably stored material or equipment should not be withheld until the material or equipment is actually installed in the work. Owners that fail to provide for payment of stored materials and equipment discourage prudent business practices and prompt schedule compliance. Safeguards can be taken to assure that the owner's interests are protected from diversion, destruction, theft, or damage to stored materials or equipment that the contractor or subcontractor is holding for future installation.

Similarly, the federal government's Federal Acquisition Regulation's clause for "Payments under Fixed-Price Construction Contracts," published at [48 C.F.R. § 52.232-5](#), provides:

"In the preparation of estimates, the Contracting Officer may authorize material delivered on the site and preparatory work done to be taken into consideration. Material delivered to the Contractor at locations other than the site also may be taken into consideration if-

(i) Consideration is specifically authorized by this contract; and

(ii) The Contractor furnishes satisfactory evidence that it has acquired title to such material and that the material will be used to perform this contract.”

Protecting Your Business

Contract terms permitting payment for materials delivered and stored either on-site or off-site universally use subjective terminology such as “suitably” to describe the way the materials must be stored, require that off-site locations for storage be approved in writing, in advance, and universally require subjectively-described “satisfactory evidence” that title is transferred and that the materials are properly insured. Regular communication with the prime contractor, in advance of ordering materials for which early payment will be sought, is therefore vital.

When a specific acquisition of such materials or equipment is contemplated, talk to the prime contractor ahead of time to be certain that your arrangements will be “suitable” and “satisfactory.” A written document prepared by either yourself or the prime contractor, with the signature or initials of a person in authority, will serve as the best guarantee for any subcontractor’s expectation of being paid for materials not scheduled to be immediately incorporated into the work. Even an email exchange with the proposed arrangement and a response accepting the arrangement can serve this purpose.

A discussion with an insurance agent knowledgeable of the terms of the builder’s risk policy for the project may also save expense and time.

Ordinarily, materials which are stored to be incorporated into a building, structure or improvement are covered under an installation floater policy (inland marine coverage) procured by the trade contractor. However, the stored materials are the property of the trade contractor until they are incorporated into the work.

The builder's risk policy generally covers the materials after they become part of the work; however, the owner’s or prime contractor's builder's risk policy can include coverage for suitably stored materials at temporary locations and in transit. The policy should be reviewed to determine coverage for stored materials whether they belong to the owner or contractor.

When it is necessary to transfer title to the owner or prime contractor for materials stored at the subcontractor's yard, the required coverage generally changes. The subcontractor no longer has ownership interest but has a care, custody and control exposure for property belonging to others. Coverage for that liability exposure may be arranged with the subcontractor’s insurance carrier if coordinated in advance.

Advance payment for materials and equipment not yet incorporated into the structure requires planning and communication.

Conclusion

Advance procurement of construction materials and equipment, soon after a contract is executed and well before the equipment or material is needed, is a prudent practice which assures that specified materials and equipment are available for installation or use in accordance with the construction schedule. Advance procurement also guards against escalating costs, particularly in long-term contracts, enabling the contractor and its subcontractors to make timely purchases when shortages may be a problem. Practical owners and prime contractors will encourage the prudent practice of early materials acquisition by making payment for such materials an easily available option. Even when advance payment is permitted, however, subcontractors should be cautious and expect that the prime contractor and the owner will require observation of reasonable requirements for storage, title and insurance which will vary depending on the circumstances. As is often the case when project issues arise, early and frequent communication are the keys to a satisfactory result.