

Betting the Farm? – Three Rules in Construction Disputes  
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In a recent ruling by the United States District Court in the Eastern District of Philadelphia<sup>1</sup>, a metal panel subcontractor learned a hard lesson about walking off a job in the midst of a dispute with the contractor. In the case of LBL Skysystems (USA) Corp. v. APG-America, Inc. (and their respective sureties), LBL was a contractor obliged to install curtain wall, windows, louvers and metal panel in the new USAirways International Terminal in the Philadelphia Airport. It subcontracted the metal panel work to APG. After performing for nearly two years and recognizing that they were operating at a loss, APG attempted to reduce its scope of work by claiming that it had been erroneously supplying the support steel necessary to attach its panels to the building structure. Accordingly, in the middle of a change order meeting between LBL and USAirways, APG delivered an ultimatum to LBL: Either pay approximately \$5MM for the design, engineering, fabrication and installation of the support steel already in place, or APG would leave the job.

Stunned by this ultimatum,<sup>2</sup> LBL investigated and confirmed that the support steel was part of APG's contractual scope. APG had contracted with its independent structural engineer to design the steel that it now protested was deserving of a change order. APG's bid documents, design drawings, purchasing and pay applications, to that point, all confirmed that APG had indeed included the support steel in the scope.

LBL tried to dissuade APG from taking the drastic step of walking off. However, despite the at-best-questionable position being taken by APG, it followed through on its

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<sup>1</sup> 2006 WL 2590497 (E.D.Pa.)

<sup>2</sup> The authors were counsel for LBL and its payment bond surety. As a result, the presentation of the facts is susceptible of a justified accusation of bias.

threat and reduced its manpower nearly to zero, where its work could not progress at the rate needed to keep LBL from itself being placed into contractual default by USAirways. At this critical stage of construction, LBL could not afford to lose its key subcontractor, but equally could not afford to pay an extra \$5MM for work it had already purchased within the existing LBL/APG subcontract. It called upon APG's performance bond surety, to seek a solution. APG's surety delayed any decision, ultimately declining either to step in and complete APG's work or to fund LBL's completion of it. LBL was left with no choice but to do the work itself at its own cost. It did so. Not surprisingly, it cost LBL a lot more to complete APG's scope than it would have cost APG itself. LBL was not in the metal panel business, did not have the job experience or work force that had gone through the necessary learning curve, and could not be nearly as efficient in completing the work. It deducted the cost it incurred from the balance remaining in the subcontract and sued APG to collect the difference. After a bitter, hard-fought trial, the United States District Court agreed with LBL, finding that the support steel was in APG's subcontracted scope of work. The Court awarded LBL a judgment against both APG and its surety for nearly \$2MM (including interest). In addition, LBL is now seeking to recover its fees from APG and its surety, which could more than double APG's loss. The disastrous miscalculations and missteps by APG now threaten to close the doors on this third generation business. Why did this happen? How could it have been avoided?

Putting aside for a minute APG's dubious position on the disputed scope of work, perhaps the fatal step taken by APG was acting on its threat without considering thoroughly the full implications of the terms of the subcontract. As is common, the prime contract, between USAirways and LBL, was incorporated into the LBL/APG subcontract.

During negotiation of the subcontract, a provision that would have authorized APG to stop work during a dispute was stricken. That left APG bound to a provision in the prime contract that expressly required APG to continue “working expeditiously” during a dispute. In light of that obligation, the Court ruled that APG’s abandonment was inexcusable – even without considering the merit of its position on APG’s scope. APG’s abandonment, in light of the subcontract prohibition against stopping work during a dispute, was ruled to be a material breach of the subcontract – entitling LBL to recover its costs of completing APG’s work – even where the cost to LBL exceeded what it might have cost APG.

What lessons should contractors and subcontractors take from the Philadelphia Airport debacle? Three come to mind: (1) read and understand the entire contract; (2) avoid taking irrevocable positions that may excuse performance by your adversary; and (3) be willing to explore and accept a reasonable compromise.

Almost always, construction agreements incorporate documents that are physically separate from the one single “contract” that is signed by the parties. Most contractors are aware that building plans and specifications form a material part of the agreement. Beyond this, however, subcontracts usually incorporate the terms of prime contracts, and general and special conditions, all of which are embodied in separate writings. Also, bonds and insurance policies required by the contract language, impact upon the rights and obligations of the parties. The total package of interrelated documents composing the subcontract must be carefully studied as an integrated agreement to appreciate the meaning and intent of each provision, when it might come into play and how it is interpreted with other provisions of the contract. The time to

understand the agreement is not after a dispute has materialized; , , but before it is signed, before work begins and before disputes arise. .

In the Philadelphia Airport case, APG should not have walked off, no matter how valid its position on scope might have been.<sup>3</sup> The subcontract anticipated that disputes might arise and unequivocally prohibited APG from ceasing its work notwithstanding the existence of the dispute. Had APG recognized the importance of this contractual requirement, it may not have acted so rashly and may have considered other alternatives for resolving the dispute. As it was, APG's failure to perform during the dispute was ruled to be a breach that excused LBL from making any further payments to APG until the project was completed and an accounting of the cost to complete could be performed.

APG also ignored the second lesson by taking an irrevocable position that left LBL no choice but to terminate. The terms of APG's performance bond required that LBL terminate APG before LBL could pursue a claim against APG's surety. Thus, when APG throttled down its forces, LBL was compelled to terminate APG as a condition of invoking the surety's obligation under its bond. APG's throwing down the gauntlet gave LBL no option, because it had to achieve performance of APG's subcontract scope or risk being in default of its own obligation to USAirways.

Finally, APG rejected all entreaties to resolve the dispute short of abandoning the work – requiring termination and the beginning of a declaring “shooting war.” When LBL was confronted with APG's ultimatum, LBL disagreed with APG's position and tried to convince APG to back off. When that failed, LBL proposed several compromises, which would have allowed the project to be completed, while preserving

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<sup>3</sup> APG's position lacked merit, but the consequences of the position might not have been so devastating had it understood, before acting, the ramifications of the contract provisions that were used to attack its actions.

the APG's right to fight over compensation.<sup>4</sup> LBL offered to supply the disputed support steel, if only APG would continue to perform the installation. LBL then sought just to have APG deliver fabricated panels for which it had already been paid, so that LBL could itself install them. Again, APG refused and actually required LBL to pay for them a second time as a condition of their release.

All reasonable efforts at compromise were rejected by APG, which insisted that it would walk off the job unless LBL paid the millions of dollars APG claimed to have incurred performing "out-of-scope" work. This position left LBL no alternative. It did not have the cash to front APG such a large, unanticipated sum and logically looked to APG's surety to advance APG the funds that would allow it to avoid default and termination. Instead, the surety supported APG's intransigence, and refused to step in, and left LBL the only course open to it, terminating APG and suing both APG and its surety. What should have been a negotiable dispute over half a million dollars became a liability for millions – spelling ruination for APG. APG violated the three rules in a construction dispute: It failed to read and understand the contract provisions brought into play by its actions. It took an unreasonable, irrevocable position, and it refused to accept a reasonable compromise.

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<sup>4</sup> APG could even have commenced a lawsuit to resolve the dispute while continuing to perform under protest.