

CONSTRUCTION AND THE LAW IN TEXAS

Resolving Performance Disputes in a Joint Venture

In the June 2015 edition of *Texas Contractor*, I wrote a column addressing the Keys to a Successful Joint Venture. Assume that the hypothetical joint venture discussed in that column was formed, a project was awarded, and the Work has just been completed. Now, after substantial completion, the owner submits a claim notice letter to the joint venture that it will withhold retainage due to delay and that there are suspected construction defects that require funds in excess of the contract balance to correct and complete.

In that situation, what should joint venture partners do to address the claims and resolve the internal conflicts that necessarily arise when one party may be solely or more responsible than another? This column will address that conflict.

In crafting joint venture language, parties may want to consider the following: How is the joint venture structured so that it and its members can receive necessary compensation from the owner for claims it may assert for changes and increases to the cost of the work. Alternatively, what if the owner alleges performance errors by one or both partners? The joint venture agreement should be drafted in a way to address allocation of funds or responsibility where appropriate.

Consider a situation where a claim is asserted to offset payment of final contract balance and the Owner pursues that claim into litigation. In that situation, insurance may not be available to provide a defense and lessen the financial impact on the joint venture and its members. Does the joint venture agreement have terms to address allocation of responsibility? Does the agreement have terms that cover internal disputes so that the partners can overcome the challenge and continue performance for the owner to protect against default?

The June 2015 column offered the following terms that a joint venture agreement should include to ensure a sufficient understanding of performance expectations:

- Governance: How will the parties

allocated responsibilities such as control of the entity's resources and activities

- Capital Contributions: Both initial and recapitalization, if necessary, should be considered and addressed as well as bonding capacity
- Operational Concerns: Project management, safety training and oversight, subcontractor selection and direction, among others
- Procurement: How will the joint venture secure projects

That list was not intended to cover the situation where an owner has submitted a claim that implicates each joint venture partner. If the owner's claim has merit and the responsibility for the events giving rise to the claim is shared equally by the joint venture partners, resolving the claim is fairly straight forward. On the other hand, if the responsibility for the claim falls more heavily on one partner or there are multiple incidents which give rise to liability and the responsibility is not evenly distributed, the joint venture is liable in full but one partner may become adverse to another due to the unequal division of responsibility.

In addition to the terms listed above, parties should also consider language that will allow them to address situations where claims may arise against the joint venture. For example, provisions addressing mutual insurance policies that provide additional insured status for the other joint venture partners as well as the owner can be beneficial for certain claims. Furthermore, the joint venture should be sure to include a requirement that subcontractors provide additional insured status to the joint venture and its individual members.

In the example where construction defects are alleged, having each subcontractor name the joint venture, and each partner, as additional insureds on the policy will assist in securing coverage even if the offending subcontractor is not responsive to a demand for cure.

Another term that would benefit a situ-

ation where conflicts may arise between joint venture partners would be a dispute resolution provision that provides a mechanism to determine percent responsibility by partner. If such a mechanism exists, then the subsequent terms should determine how liability to the Owner and each other is resolved. One way would be to offset claim-resolution costs from distributions or reduce the responsible member's capital contribution by a corresponding amount to fairly compensate the other partner.

If the joint venture is one where the joint venture partners have divided scope by segments and there are defects in the areas where each segment ties together, then the above dispute resolution and compensation provisions may be fairly easily applied. But where scopes intersect or may be mingled, then the allocation may be less clear.

In every joint venture, each partner brings something unique to the table. The contributions of each partner may vary based on the needs of the venture and characteristics of the project. In each event, careful consideration should be given to the possibility that friends today may become adversaries tomorrow. While no one enters into a joint venture expecting the relationship to fall apart mid-project, things happen and partners can have their common interest diverge from one another. That is not to say that the relationship and joint venture will collapse. Certainly, have language in the agreement that can address the situations addressed above can ease conflict and allow that parties to resolve a single situation while preserving the overall success and goals of the joint venture.

If a conflict arises that is so severe that the joint venture cannot continue with the original members or in its original form, the parties should include exit provisions and align those to the terms of the prime contract with the owner. Regardless of what might happen between joint venture partners internally, the owner will expect and has the right to demand full perfor-



Jeff Chapman is the founder of The Chapman Firm, a construction law boutique serving clients throughout Texas. Chapman practices construction law with a focus on the heavy industrial, water and wastewater, transportation and municipal sectors of the industry. Chapman provides his clients with the full range of construction representation, ranging from transactional, project management, dispute resolution, and general counsel services. He can be reached at Jeff@ChapmanFirmtx.com or 512.872.3838



A Balanced Approach to Construction Law.

mance by the joint venture. Accordingly, the joint venture agreement should also include terms that anticipate the possibility that the partnership may come to an end. If that happens, the joint venture agreement should address how that split might affect the prime contract and the joint venture agreement.