In the typical building process, a property owner hires an architect and/or engineer to design a building or other structure for the property and then a contractor to build the project. As the project nears completion, often the owner will begin to occupy the building and make use of it even though the contractor is not yet finished with the work that was contracted to be performed. Nonetheless, the contractor asks for payment and provides warranties, among other documentation, while continuing to finish up the work. The contractor's entitlement to payment will often depend on whether the contractor has reached Substantial Completion.

In the ordinary commercial contract setting, a party to a contract can only fulfill his or her obligations under the contract by establishing complete or full performance. In other words, a party is not entitled to the benefit of the contract if it has not fully lived up to its end of the bargain. In the construction industry, however, complete or full performance is often not required. Construction projects typically involve two different stages of completion – Substantial Completion and Final Completion. Any work that remains to be completed after the project has reached Substantial Completion is generally referred to as punch list work and its completion usually constitutes Final Completion.

The most common definition of Substantial Completion is the point in the project where the building is fit to be used for its intended purpose. What Substantial
Completion signifies, though, is what makes it important and the source of many construction project disputes. Typically, achieving Substantial Completion entitles the contractor to receive full payment for his work, less amounts the owner can retain to secure outstanding punch list work or to secure repairs for defective work. As a result, a contractor is entitled to payment even though the project is not fully complete. The parties to the contract, however, can define Substantial Completion differently in their contract and, thus, change the circumstances surrounding a particular project.

Here's why it's important to reach Substantial Completion:

1. It triggers the contractor's right to payment of the full contract amount minus offsets. This will include the owner's obligation to release any retention that may have been withheld as part of the payment process, which is often a significant amount;
2. The contractor likely is no longer subject to being found in material breach of the contract due to a performance failure;
3. The contractor may be subject to liquidated or other types of damages in the event of failure to meet a specific completion deadline, but, by achieving Substantial Completion, the contractor may eliminate any such liability;
4. Achieving Substantial Completion typically commences the time limitations associated with warranties, statues of limitations and statutes of repose;
5. Substantial Completion typically transfers responsibility for the project to the owner such that the owner becomes obligated to insure the property, as well as pay for utilities and routine maintenance.

When contemplating a building project, the owner and contractor should not overlook the importance of how Substantial Completion is defined in the contract. By ignoring this seemingly innocuous term of the agreement, the owner or contractor could be assuming financial risks and other obligations for which it failed to plan.

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