

# Payment Remedies in Construction Contracts

By Thomas More Buckley



Contractors typically have a number of powerful remedies to obtain payment for contracted construction services, either by forcing compliance with payment requests or elevating the matter into litigation or other disputes that results in payment. One of the best and surest ways to help in guaranteeing payment down the line is consistent and concurrent documentation of expenses, delays, and change orders for which payment will be sought. The kind of loose accounting practices which can prevail on construction projects have no consequence where payment is forthcoming. When disputes over payment arise, however, a lack of careful documentation of expenses, delays, and change orders can be a contractor's greatest enemy in obtaining payment for work performed. Of course, even the most careful documentation of such matters does not guarantee payment, so the following remedies, which are unique to the construction context, are typically available to a contractor who is not paid.

## STOPPING WORK

When a contractor is not paid, some contractual provisions and non-contractual legal principles might allow stoppage of work. AIA (American Institute of Architects) form contracts provide for work stoppage following a period of 7 days in which the owner is late with payment; the contractor may, upon an additional 7 days' notice, stop work. Assuming these requirements are complied with, the contractor would also be entitled to the extra costs associated with demobilization and remobilization upon such a work stoppage. Clauses such as these can be beneficial in clearly defining the parties' rights and responsibilities, but failure to abide by their express requirements can result in a contractor being liable for breach of contract for the work stoppage. Clauses allowing for the stoppage of work on a temporary basis are not equivalent to termination clauses, and work must resume once payment is received.

In any case, even absent an express provision in the contract, under general contract law principles, a contractor might well be entitled to stop work in response to non-payment of invoices. If the non-payment represents a material breach of contract, the party to whom payment is owed may terminate the contract or suspend work to wait for the non-payer to complete payment. If payment is made, and the contractor has not returned to work, the contractor might then be in a material breach of the contract itself, and therefore subject to damages to the owner.

## LIENS

Construction or mechanic lien statutes are intended to provide contractors, subcontractors, suppliers, architects, engineers, land surveyors, and others who have furnished labor, materials, service, and/or rental equipment in the improvement of real property for the means of collecting payment for such work. The property itself, in effect, acts

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as collateral security for such payment. A mechanics' lien claimant typically has a security interest beyond the rights of a general creditor.

Claims of lien often cannot be amended, so it is important to meet the time requirements set forth by the applicable statute. Statutes typically set forth a deadline for the filing of liens that runs from the date of last furnishing labor or materials. To preserve lien rights, the requirements of the state statute governing them need to be followed to the letter. Once the claim of lien has been filed, a lawsuit based on the lien typically must be filed within another strict deadline.

If a judgment is obtained based on the lawsuit filed to enforce the lien, the property may typically be sold at an execution sale. The party with the judgment is paid from the proceeds of the execution sale. Prior to that, the owner can usually discharge the lien by posting a bond, which replaces the lien to act as security for payment. As a practical matter, however, a lien can be of little value when weighed against a prior incurred security interest, such as a mortgage. For priority purposes, liens duly perfected under Chapter 44A relate back to the time of first visible furnishing of labor or materials. As between the statutory lien and the lien created by a deed of trust, the general rule is that the lien that is first in time has priority. In other words, where a deed of trust memorializing a lender's mortgage interest is recorded prior to the time the work on the property is begun, as is often the case where property is purchased pursuant to such a deed of trust prior to contracting for or beginning construction on the property, the deed of trust would typically have priority.

Accordingly, at the end of the day, even if a contractor correctly protects all of its lien rights, it might be faced with a situation in which it has done nothing but put itself in a position to take over the prior recorded mortgage and be subject to the owner's mortgage payments, since the mortgage must be satisfied by the sale proceeds before the contractor will be paid. Contractors who are not interested in taking over mortgage payments and, in effect, buying the property, may not be as interested in pursuing all of their lien rights to final enforcement. Nevertheless, a properly enforced lien represents a significant impairment to the marketability of the property, and represents a strong club that can be used in negotiations of disputes as to payment.

## CONCLUSION

Again, clear contracting and accurate record keeping remain a contractor's best method for ensuring payment of sums owed under a construction contract. When disputes or late payment issues arise, however, construction law provides some unique remedies to the construction

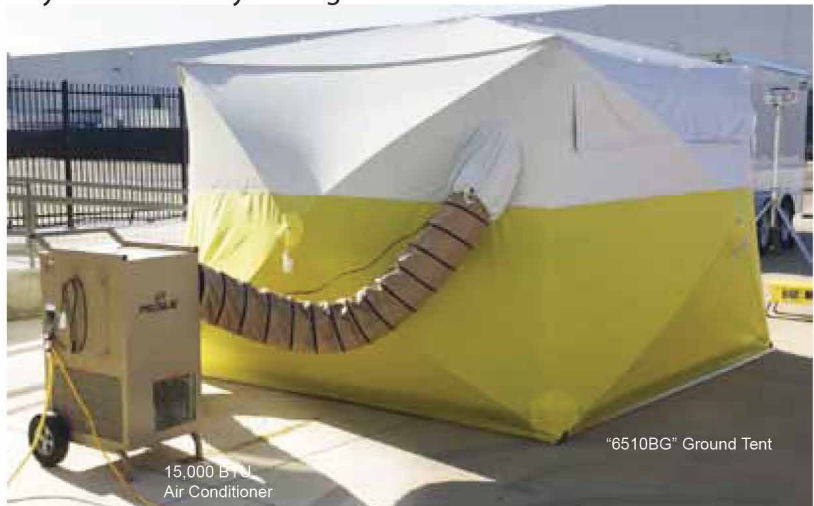
contractor, such as work stoppage and liens. These remedies need to be used with caution, and should only be pursued in strict compliance with the laws that allow them. When pursued in that manner, though, they can provide a powerful tool for a contractor seeking payment. ■



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