Whether your outfit is a huge regional general contractor or a tiny sub or supplier, getting fully paid – on time – is not always easy. There are a bunch of reasons this is the case, and it won’t likely ever change. That being said, if you want an edge the next time the owner or the contractor who hired you won’t pay like it should, knowledge of the Tennessee Prompt Pay Act could really help.

Construction-related payment disputes, like most negotiations, usually turn on three factors: power, information and time. If you or your lawyer understands the Act, you can use it to try to assist on all three fronts. Together you can neutralize your adversary’s strengths, get your money quickly, and hopefully avoid the high legal expense associated with some collection efforts.

Introduction

In the late 1970s Congress came to the realization that complete and timely payment on federal construction projects was becoming infrequent. This presented a real hardship for the contractors and suppliers building our roads and public structures. Congress’ solution was a new law, the Prompt Payment Act of 1982.

Tennessee lawmakers eventually came to the same realization that Congress did, and in 1991 passed the Tennessee Prompt Pay Act.1 As its name implies, the Act is designed to provide its users with a tool to make sure they get paid fairly within a reasonable time. Although the Act is short, it packs a punch, and effective use of it can give a builder or supplier leverage that it would never have without it. What follows is a question and answer explanation of the Act’s features.

To what types of Projects does the Prompt Pay Act apply?

The Prompt Pay Act’s coverage is very broad. It applies to all private construction projects in Tennessee except those involving residential construction. In addition, and unlike the state’s lien statutes, the Act applies to all construction contracts with the state and any other “subdivision,” including the University of Tennessee, and all county and municipal governments. The Act cannot be waived by contract, and thus can’t be bargained away in the bidding or contract formation process. It is important to point out, however, that regardless of whether the project is private or public, you must have a written contract to take advantage of the Act’s protections.

Who does the Prompt Pay Act protect?

The Act is designed to protect contractors, subcontractors, suppliers, architects and engineers from the parties they con-
Continued from pg. 32

contract with directly. For example, a subcontractor who has a written contract with a contractor can use the Act against that contractor if the sub performs in accordance with the written contract. The subcontractor cannot, however, under the Act recover payment from the project owner unless the sub also had a contract with the owner. The Prompt Pay Act thus allows you to pursue one party – the outfit with whom you contracted. Of course this is in addition to any contract or other rights you might have under payment bonds or lien statutes, etc.

What obligations does the Prompt Pay Act impose on owners and general contractors (or other hiring parties)?

The Act establishes a presumption that a contractor (or any other party owed money) who performs under a written construction contract with another party is entitled to payment. Indeed, the Act states that the owner is under a duty to pay the contractor within the time periods provided in the contract after the owner receives a timely application for payment. Failure of an architect, engineer or other person hired by the owner to review and approve an application for payment, does not excuse the owner from making the earned payment. While an owner may withhold payment or a portion of payment under contract terms, it must release that retained amount once it has: (1) received an occupancy permit; (2) received a certificate of substantial completion; or (3) begun to use or could have begun to use the improvement.

While the presumption and duty described above are valuable for those seeking payment, the Act also states that the sums intended as payment are to be held in trust for the benefit and use of the party due the money. While a discussion of the law concerning money held “in trust” is beyond the scope of this article, this trust feature is a significant advantage for an unpaid party, and creates obligations on the party holding the money that they probably wished they did not have. This “trust” feature does not apply to the State of Tennessee or its subdivisions, however.

What does one need to do to recover under the Prompt Pay Act?

A contractor, for example, seeking relief under the Act must first inform the party failing to make payment (by registered or certified mail, return receipt requested) that it intends to
seek the remedies available under the Act. The party receiving the notice then has 10 calendar days within which it can (1) either make payment or (2) provide an adequate legal reason for failing to do so.

If the notified party fails to respond in either of the acceptable ways, the notifying party can then file a lawsuit in the Chancery Court in the county where the project is located. In its lawsuit the contractor in our example can ask the court for injunctive relief, ordering the notified party to pay the owed funds at the outset of the lawsuit before trial. The availability of an injunction to compel payment prior to trial is an unusual right and it gives the Act real teeth. As a practical matter, an owner or contractor ordered by a court to pay owed funds early on in a case usually has little stomach for a continued court battle and is likely to want to compromise the case and get it dismissed.

Without this right, a contractor trying to recover monies owed might be left to wage a court battle that could take more than a year to conclude. Of course, during the litigation the contractor would not only have to get by without the monies it is due, but also incur attorneys’ fees and other litigation expenses. Unless this contractor has a “prevailing party” clause in its contract, the litigation effort might greatly diminish the value of its recovery – even if it did get awarded everything to which it was entitled. Recognizing this reality, the Act makes clear, reasonable attorney fees may be awarded against the losing party on the Prompt Pay Act claim if that losing party had acted in bad faith in not making payment. While bad faith is not always easy to prove, the threat of this sanction is valuable in and of itself. Finally, the Act allows that any payment not made in accordance shall accrue interest.

**Conclusion**

As mentioned earlier in the article, effective and knowledgeable use of the Prompt Pay Act allows an unpaid builder or supplier to enhance its chances of success in resolving payment dispute negotiations/litigation. Remember what the Act can do for you the next time your labor, services or material doesn’t get the payment it should under a written contract on a Tennessee project.

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**Footnote:**