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Condominiums and the Mass. "Prompt Payment" law

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Massachusetts governor Deval Patrick recently signed into law Chapter 293 of the Acts of 2010, An Act Promoting Fairness in Private Construction Contracts (codified as Massachusetts General Laws Chapter 149, Section 29E). M.G. L. Ch. 149, Section 29E ("the Prompt Payment Law") which includes a number of very significant provisions which will alter the way owners, contractors, subcontractors and suppliers do business in Massachusetts. The new statute governs how and when contractors, subcontractors and suppliers will apply for payments and proposed changes and how and when owners will pay contractors for their work under private construction contracts and related subcontracts and lower tier agreements entered into as of November 8th, 2010.

The Prompt Payment Law prohibits parties from agreeing to waive or to modify the requirements set forth in the new statute and generally precludes the enforcement of certain kinds of contractual provisions aimed at making a payment to a subcontractor or supplier conditioned on the receipt of payment from a third party - usually an owner (also known as "pay if paid" and "pay when paid" clauses). It is important to note, however, that the Massachusetts Prompt Payment Law does not universally apply to all construction related agreements and that it includes restrictions that would exclude construction projects of the scope commonly undertaken by condominium trusts and homeowners' associations. The statute expressly provides that it is not applicable to contracts for construction if the original project contract price is less than \$3 million or if the project at issue contains "or is designed to contain at least 1 but not more than 4 dwelling units." In other words, if the original contract price is less than \$3 million or is a project of any cost that involves a structure housing four (4) dwelling units or less, the requirements of the Prompt Payment Law do not apply. Therefore, only contracts for construction projects of relatively large scope will be affected by the new statute.

Payments and Change Orders

As to those contracts to which it does apply, the Massachusetts Prompt Payment Law requires that contracts for construction projects which are subject to the new statute provide for reasonable time periods within which (i) applications for payment shall be submitted; (ii) the person receiving the application must approve or reject the application for payment; and (iii) the person approving the application must pay the amount of the approved application.

The Prompt Payment Law also governs the submission and approval of change orders which would result in an increase to the contract price.

Pay If Paid and Pay

When Paid Clauses

The other major provision of the Prompt Payment Law substantially limits the use of "pay when paid" clauses and "pay if paid" provisions in construction contracts to which it applies. "Pay when paid" provisions allow a contractor to delay a payment to a subcontractor or supplier until the contractor has received payment for the subcontractor's work or the suppliers equipment or material from a third party not a party to that contract (in the case of a general contractor, that third party would likely be the owner). While a "pay when paid" clause is generally interpreted as governing only the timing of such payment, a "pay if paid" provision governs whether the payment to the subcontractor supplier is ever due. In other words, if the third party, for whatever reason, fails to pay a general contractor, a subcontractor with a "pay if paid" clause in its subcontract would never be entitled to be paid for its work on the project by the general contractor.

The Prompt Payment Law makes such contract provisions void and unenforceable except under two specific circumstances - (1) if the third party's failure to pay is based on the failure of the subcontractor or supplier requesting payment to perform under its contract or to timely cure a default under that agreement; or (2) if the third party is or becomes insolvent within ninety (90) days of the application for payment and the party enforcing the "pay when paid" or "pay if paid" clause has perfected a mechanic's lien and pursued all reasonable legal remedies in an effort to recover from the insolvent third party. Other than these exceptions, the Prompt Payment Law essentially outlaws the use of "pay when paid" and "pay if paid" provisions in private construction contracts to which the statute applies.

Because the new statute radically modifies the way private contraction contracts in Massachusetts are drafted, interpreted and enforced, all parties involved in construction projects covered by the Prompt Payment Law - owners, general contractors, subcontractors and suppliers - should consult with their legal counsel with regard to how to ensure that their construction contracts and procedures comply with the new statute.

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