

STATEMENT FROM STUART S. ZISHOLTZ

Over the years, I have written numerous articles about the pay-when-paid clauses that are regularly incorporated into construction contracts.

Until 1995, the pay-when-paid clause was enforceable and prevented subcontractors from receiving payment if the general contractor did not receive payment from the owner. In 1995, the Court of Appeals, the highest Court in New York, found that a contract provision that forces the subcontractor to assume the risk that the owner will fail to pay the general contractor was void and unenforceable.

Since that time, many attempts have been made to try and modify or overrule the Court of Appeals decision. Most attempts have failed.

Recently, the Appellate Division, First Department, found that a pay-when-paid clause was enforceable in the limited circumstances where a mechanic's lien was no longer an issue. In that case, the subcontractor was required to assess the level of damage incurred at various buildings and to prepare estimates of the costs to complete and repair the buildings as a result of the damages sustained by Hurricane Sandy. The subcontractor filed a mechanic's lien and, through various legal procedures, the mechanic's lien was ultimately vacated.

Thereafter, the general contractor sought dismissal of the case. One of the reasons for seeking dismissal was based on a pay-when-paid clause in the contract.

The lower court found that where the Lien Law was no longer relevant and the lawsuit was solely a breach of contract action, the express condition precedent for payment may be enforceable.

The Appellate Court agreed with the lower court and specifically stated that where a subcontractor no longer had lien rights, there was no basis for finding that the paid when paid clause was unenforceable.

Obviously, this decision could have serious consequences throughout the construction industry. General contractors will try and incorporate this clause in every contract. They will also continue to play games so that the time to file a mechanic's lien expires. Moreover, what the long-term effect will be is unknown. For instance, if some subcontractors on a particular project file mechanic's liens and others do not, is the same clause void for some parties and not void for others? What if the general contractor never gets paid from the owner? Is the general contractor off the hook and never has to pay the subcontractor?

I am recommending to everyone that they review their contracts carefully and strike the paid when paid clause. The filing of a valid mechanic's lien would render the pay-when-paid clause illegal and unenforceable. However, in the event you miss the deadline to file a mechanic's lien or if your mechanic's lien is vacated for any reason, you will be able to sleep at night knowing that the clause is not in your contract and that you are a little safer in collecting your outstanding receivable.

Never let your lien time run out!

For a free copy of a pamphlet pertaining to mechanic's liens and payment bond claims, kindly contact me.

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