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I. INTRODUCTION

This article surveys the law on the enforceability of the common construction contract provisions referred to as “pay-when-paid” and “pay-if-paid” provisions in each of the 50 states and the District of Columbia. This article also surveys the law on the statutory trusts enacted by some state legislatures regarding payments on construction projects, which statutes are commonly referred to as construction trust fund statutes. We asked our contributors to summarize the current state of the law on “pay-when paid” clauses separately from “pay-if-paid” clauses, as many courts treat the two differently. We further asked our contributors to describe any differences in the enforceability of such clauses in general contracts and in subcontracts and on public projects and on private projects. For states with construction trust fund statutes, we asked our contributors to address the types of projects to which the statute applies, the parties to whom the statute applies, the funds to which the trust attaches, the remedies available for violations of the trust, and whether the trustee is entitled to commingle the trust funds. Our original intent had been to develop a matrix, but as the reader will see the answers to these questions do not lend themselves to small boxes. We appreciate the efforts of the many contributors from around our great country who were willing to research and summarize the current law in their respective jurisdiction. The summaries are intended to be exactly that; they do not purport to address every nuance of the law or every possible fact pattern. Consultation with knowledgeable local counsel is, of course, advisable to understand the application of these general principles to any particular real life situation.

II. “PAY-WHEN-PAID” AND “PAY-IF-PAID” PROVISIONS

Parties are generally free to negotiate the terms of their contracts, and are generally permitted to negotiate and allocate the risks under their contracts, including the risk of non-payment. Many courts take a strict view of contracts. They see contracts as private law making and will not revise the terms of the contract to achieve “equity.” Other courts strictly construe risk shifting provisions that result in harsh outcomes for contracting party that is viewed as less capable of assuming the shifted risk. Those courts may find such provisions void as against public policy. Some state legislatures have enacted laws prohibiting provisions in contracts shifting the risk of non-payment. Alternative dispute resolution providers also address those clauses. The growing view of the industry is that condition
precedent clauses of all sorts are easily overcome in alternative dispute resolution, leading many owners or general contractors to abandon arbitration clauses altogether. vii

While the terms “pay-when-paid” and “pay-if-paid” are commonly used in the construction industry and are distinct clauses, commentators and courts have not universally applied these terms in discussing such provisions. Some courts refer to both provisions as “pay-when-paid" provisions and simply differentiate between those “pay-when-paid" provisions that act as reasonable timing provisions from those that act as conditions precedent. Therefore, it is critical to examine the actual contractual provision at issue in a case to determine the court’s actual holding – do not rely on the characterization of the clause in the opinion.

A typical “pay-when-paid” clause might read: “Contractor shall pay subcontractor within seven days of contractor’s receipt of payment from the owner.” Under a “pay-when-paid” provision in a construction subcontract, a contractor’s obligation to pay the subcontractor is triggered upon receipt of payment from the owner.viii Most courts hold that such a clause means that the contractor’s obligation to make payment is suspended for a reasonable amount of time for the contractor to receive payment from the owner.ix The theory is that a “pay-when-paid” clause creates a timing mechanism only. Such a clause does not create a condition precedent to the obligation to make payment and does not expressly shift the risk of the owner’s nonpayment to the subcontractor. We have seen no jurisdiction that treats a pure “pay-when-paid” clause as a condition precedent to payment. We saw no trends indicating a difference in the enforcement of “pay-when-paid” clauses on private projects as opposed to public projects or at different tiers of contractors.

A typical “pay-if-paid” clause might read: “Contractor’s receipt of payment from the owner is a condition precedent to contractor’s obligation to make payment to the subcontractor; the subcontractor expressly assumes the risk of the owner’s non-payment and the subcontract price includes this risk.” Under a “pay-if-paid” provision in a construction contract, receipt of payment by the contractor from the owner is an express condition precedent to the contractor’s obligation to pay the subcontractor. A “pay-if-paid” provision in a construction subcontract shifts the risk of the owner’s non-payment under the subcontract from the contractor to the subcontractor.x In many jurisdictions, courts will enforce a “pay-if-paid” provision if the provision is clear and unequivocal.xi Courts will generally find that a “pay-if-paid” provision does not create a condition precedent, but rather a reasonable timing provision, where the “pay-if-paid” provision is ambiguous.xii Some courts have held that the use of the term “condition precedent” in a “pay-if-paid” provision is sufficient to render the clause enforceable as a condition precedent.xiii At least one court has held that inclusion of the term “condition precedent” is not dispositive, and that the language of the “pay-if-paid” provision must include unequivocal language indicating that the monies owed under the subcontract are only to be paid out of the construction funds that the contractor is to receive from the owner.xiv

At least two jurisdictions have held that “pay-if-paid” provisions are void as against public policy because such provisions violate the anti-waiver provisions in the states’ mechanic’s lien statutes.xv While the “pay-if-paid" provisions involved in these cases did not expressly waive the subcontractors’ right to pursue a mechanic’s lien, the courts found that the “pay-if-paid" provisions effectively prevented the subcontractors from pursuing their mechanic’s
lien rights in violation of public policy. Under the statutes, the subcontractors’ mechanic’s lien rights are measured by the amounts due them under their subcontracts; therefore, if the “pay-if-paid” provisions were enforceable, the subcontractors would not have been due payment and could not pursue a remedy under the mechanic’s lien statutes. Some other jurisdictions have legislatively rendered “pay-if-paid” clauses inapplicable to mechanic’s liens on the theory that if the owner is not paying the general contractor, the subcontractors should be entitled to pursue the owner directly. Some states have legislatively prohibited conditional payment provisions all together. Other states have legislatively restricted their application, for example to permit a subcontractor to pursue a bond claim or lien action. We have seen no trends towards treating “pay-if-paid” clauses differently on public projects as opposed to private projects or at different tiers of contractors.

Parties attempting to utilize a “pay-if-paid” provision in a construction contract should be sure to research the applicable case law and statutes in their jurisdiction to determine whether such provisions are enforceable and whether there is any specific language that must be utilized in order for the provision to be deemed a condition precedent to payment. Likewise, parties presented with conditional payment provisions should be sure to research applicable case law and statutes to determine the risks that will be shifted to them as a result of such contractual language.

III. CONSTRUCTION TRUST FUND STATUTES

Several states have enacted construction trust fund statutes in an attempt to ensure that subcontractors, and in some cases sub-subcontractors and suppliers, are paid monies owed to them for labor and/or materials supplied to construction projects. A typical construction trust fund statute may provide as follows: “Any moneys paid under a contract by an owner to a contractor, or by the owner or contractor to a subcontractor, for work done or materials furnished, or both, for or about a building by any subcontractor, shall be held in trust by the contractor or subcontractor, as trustee, for those subcontractors who did work or furnished materials, or both, for or about the building, for purposes of paying those subcontractors.” Such a provision complies with all the necessary prerequisites for establishment of a trust under state law. The trustee is the party who receives the monies. The trust property or res is the moneys paid for work done or materials furnished, or both, for or about the building. The trust beneficiaries are the subcontractors who did the work or furnished the materials. The purpose of the trust and the means by which the trustee can discharge its obligations are clearly identified; the purpose of the trust is to pay the trust beneficiaries.

Construction trust fund statutes attach a trust to funds paid or to be paid to contractors, and in some cases subcontractors, for the benefit of those supplying labor and/or material to a construction project. Some construction trust fund statutes distinguish between public and private contracts and only apply to a specific class of project. Other constructive trust fund statutes apply only to claims that would be the proper subject of a mechanic’s lien. In such states, it follows that the statute would not apply on a public works project as such a project is not lienable.

The various states’ construction trust fund statutes vary widely with regard to the remedies provided under the statutes. Some states’ statutes provide for civil remedies such as
attorney’s fees or interest if the construction trust funds are misappropriated. Other states’ statutes do not provide civil remedies for misappropriation of construction trust funds; instead these statutes provide solely criminal penalties in an attempt to deter misappropriation. Some states construction trust fund statutes provide both criminal and civil penalties. Construction trust fund statutes that provide criminal sanctions for misappropriation of trust funds generally only apply to funds already paid to a contractor. The criminal trust fund statutes do not create private causes of action in favor of unpaid subcontractors.

A few states provide for personal liability for officers or directors of the contractor if the trust funds are misappropriated. This personal liability is usually only imposed on the officers or directors who controlled distribution of the trust funds. The statute may require proof of the officer’s or director’s intent to defraud the trust beneficiary. Such an officer or director may be personally liable even if the construction trust fund statute does not so provide.

A construction trust fund statute provides significant protection in the event that a contractor files for bankruptcy. When a contractor files bankruptcy, the owner, the subcontractors, and the contractor’s surety are understandably concerned. If the contractor can use the funds received from the owner for any purpose, the owner faces a dilemma. If it pays the contractor/debtor and the contractor/debtor fails to pay its subcontractors, those subcontractors may have lien rights under applicable state law. If the subcontractors obtain liens, the owner may pay twice for the work. The subcontractors are likewise worried that the contractor/debtor will redirect the funds and the subcontractors will need to incur the transaction costs of filing a lien or a claim on the contractor’s bond to obtain payment, or that such remedy may be barred by a notice or limitations provision. The trust fund statute resolves these problems. It protects the owner from liens, the subcontractors from non-payment, and the surety from claims by protecting the funds paid or to be paid by the owner from the claims of the contractor/debtor, its trustee, or its creditors. Pursuant to section 541(d) of the Bankruptcy Code, property in which a debtor holds only legal title and not equitable title becomes part of the debtor’s bankruptcy estate only to the extent of debtor’s legal title. If there is a valid trust in existence, “property of the debtor held in trust at the time of filing its bankruptcy petition is excluded from the bankruptcy estate.” To the extent that there is a valid trust in existence, construction trust funds paid to the debtor after the filing of bankruptcy are held by the debtor subject to the trust obligations.

Normally, a debt resulting from the debtor’s defalcation while acting in a fiduciary capacity can be exempted from discharge. The courts have consistently limited the meaning of “fiduciary capacity” to express or technical trusts. The requisite trust relationship must exist prior to and without reference to the act of wrongdoing. This requirement eliminates constructive, resulting, or implied trust from the scope of fiduciary obligations that will support a finding of non-dischargeability. Several courts have addressed the question of whether a violation of a construction trust fund statute can support a finding of non-dischargeability. For those statutes which provide solely criminal remedies, the courts have generally held that misappropriation of the trust funds does not support a finding of non-dischargeability. They view such statutes as closer to constructive or resulting trusts. For construction trust fund statutes that do not require segregated accounts but do create express trust requirements that arise before any wrongdoing, the courts generally hold that a misappropriation of the trust
funds will support a finding of non-dischargeability. Likewise, statutes that require the contractor to segregate and keep detailed records of the funds find the trust to be sufficient to support a determination of non-dischargeability. Thus, the terms of the statute must be closely analyzed to see if a sufficient fiduciary capacity is imposed upon the trustee to support a finding of non-dischargeability.

Most construction trust fund statutes set forth little or no procedural requirements for the maintenance of the trust funds and may expressly permit commingling of trust and non-trust funds. Other statutes require that detailed accountings be kept for each trust. If commingling is permitted, the funds do not lose their trust nature as a result.

It is important for owners, contractors and subcontractors to understand the applicable construction trust fund statute, assuming there is one that will govern a particular project as a construction trust fund statute may provide useful remedies and may also impose significant obligations and penalties. It is also important that the case law interpreting the applicable construction trust fund statute be carefully reviewed to determine how liberally or conservatively courts have applied the obligations and remedies provided by the statute.

IV. CONCLUSION

Payment provisions can have significant financial consequences for any party that has assumed the risk of non-payment, and can have significant financial benefits for the party that has shifted the risk of non-payment. Parties negotiating a construction contract should closely scrutinize conditional payment provisions to determine the effect of such provisions before entering into the contract. Likewise, construction trust fund statutes can provide useful remedies to owners, contractors, subcontractors, and sureties. The party charged with maintaining a construction trust fund should be familiar with specific requirements of the statute prior to the commencement of the construction project in order to ensure compliance with any procedural requirements and to avoid liability for remedies available under the statute.
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

A. To what extent are they enforceable on public projects?

The answer in Alabama is unclear. The only recent, authoritative case on subcontract payment clauses in Alabama, Federal Insurance Co. v. I. Kruger, Inc., 829 So. 2d 732 (Ala. 2002), dealt with what would normally be regarded as a “pay-when-paid” clause, stating that final payment would be made after the last of certain events, including payment by the owner to the contractor, but which the general contractor described in its briefing as a “pay-if-paid” clause, attempting to use it to preclude payment to the subcontractor indefinitely even thought the prime contract had been terminated, and citing authorities in support of its enforcement that clearly dealt with conditions precedent. The Supreme Court characterized the language as a “pay-when-paid” clause, and held that the clause could not be enforced as a condition precedent to the general contractor’s obligation to make payment to the owner, but merely provided a timing mechanism for payment. However, the language of the decision left some doubt as to whether a properly drafted “pay-if-paid” clause could be enforced, since it relied heavily upon the absence of any evidence in the record to indicate that the subcontractor “assumed the risk of nonpayment by the [owner] for events completely outside its control of influence,” id. at 739, and distinguished the instant case from a prior Alabama Supreme Court decision in which a subcontractor was held to be bound to avoid payment after the contractor received payment from the owner, since “the circumstances clearly indicated that the subcontractor assumed the risk of nonpayment.” Id. at 740. If the subcontract had been drafted, as many are, to provide that the owner’s payment to the general contractor was an absolute condition precedent to any payment to the subcontractor, and to include a recitation by the subcontractor that it was knowingly assuming the risk of owner non-payment, the Supreme Court might well have enforced the clause.

Although I. Kruger involved a public contract, the Court did not make any distinction between public and private contracts in its discussion of the issue and, in fact, relied in support of its holding on an ancient Alabama case involving a private contract. However, the Court did refuse to allow the general contractor’s payment bond surety to take advantage of the “pay-when-paid” clause as a defense to the subcontractor’s claim under Alabama’s “Little Miller Act,” Ala. Code § 39-1-1 (1975), at least without incorporating such a clause into the bond itself directly or by reference.
The Alabama Courts have decided no case in which a clear distinction of any sort between a subcontractor’s and a vendor’s right to payment is made.

B. To what extent are they enforceable on private projects?

It appears that Alabama law does not distinguish between public and private projects with respect to the enforceability of a “pay-if-paid” clause in a subcontract or supply contract (with the exception of the surety’s inability to take advantage of the clause, mentioned above).

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

A. To what extent are they enforceable on public projects?

The case of Federal Construction Co. v. I. Kruger, Inc., supra, involved a public project and, as discussed, the Supreme Court, in effect, refused to allow the general contractor to apply its “pay-when-paid” clause as a “pay-if-paid” clause. In its interpretation of the clause, however, the Supreme Court seemed to enforce it like what is often understood to be a “pay-when-paid” clause, meaning subcontract payment language which is “held to merely delay the final payment by a general contractor to a subcontractor; a general contractor’s duties to pay a subcontractor, within a reasonable time after subcontractor has completed performance, remains absolute, even if the general contractor never receives payment from an owner.” See Gerald B. Kirksey, “Minimum Decencies” - A Proposed Resolution of the “Pay-When-Paid”/”Pay-if-Paid” Dichotomy, 12:1 THE CONSTR. LAW. 1 (Jan. 1992).

For that matter, Alabama statutes approve of the concept of “pay-when-paid” in terms of timing. Alabama’s Prompt Payment Act, Ala. Code §§ 8-29-1, 8-29-8 (1975), imposes obligations on general contractors to pay their subcontractors, and subcontractors to pay their sub-subcontractors and material suppliers, timely in accordance with the payment terms agreed to but if no such terms have been agreed to, then within seven days of receipt of payment from their own customers. Id. § 8-29-3. This statute does not apply to state and local government contracts. Id. § 8-29-7. However, a similar requirement is imposed on state contractors by Ala. Code § 41-16-3 (1975).

B. To what extent are they enforceable on private projects?

In ruling on the defendant’s “pay-when-paid” clause in Kruger, the Court relied in part upon its own 1897 decision in Crass v. Scruggs, 115 Ala. 258, 22 So. 81 (1897), involving a subcontractor to a railroad contractor and holding that a promise to pay as soon as payment from the railroad had been received did not create a condition precedent to payment, but merely prescribed a time for payment. Accordingly, it does not appear that Alabama recognizes any distinction between public and private contracts and subcontracts with respect to the enforceability of “pay-when-paid” clauses, with the exception again of the effect of a Little Miller Act payment bond.
III. TRUST FUND STATUTES

Alabama does not have a construction trust fund statute.
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

A. To What Extent are They Enforceable in Public Projects

Alaska has no cases on “pay-if-paid” clauses. However, Alaska has a statute called the Public Construction Contract Prompt Payment Act, Alaska Stat. §§ 36.90.200, et seq., which governs general contractors’ payment obligations to subcontractors on public contracts. The act requires the State or public agency to pay the general contractor within 30 calendar days of receiving a properly executed and supported pay request as long as there is no issue over performance. If a basis for withholding exists, payment can be withheld without interest penalties, but must be paid within 21 calendar days after the grounds for withholding have been removed.

The same act requires the general contractor to pay the subcontractor within eight working days of receiving the agency’s payment for the subcontractor’s work. The statute preserves the general contractor’s ability to withhold amounts from the subcontractor for performance issues, but requires the general contractor to give notice to both the State as well as the subcontractor in the event of such a withholding. Retainage withheld from the subcontractor must be paid within eight working days of the receipt by the general of final payment from the State or its agency. Interest is due on the retainage at the rate of 10.5 percent per annum from the time the retainage is withheld.

B. To What Extent Are They Enforceable on Private Projects

There are no Alaska cases addressing the issue of “pay-if-paid” clauses on private projects. The Alaska Supreme Court would likely follow the weight of recent authorities from other states.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

A. To What Extent are They Enforceable in Public Projects

The only Alaska Supreme Court case dealing with a “pay-when-paid” clause is *Indus. Indem. Co. v. Wick Constr. Co.*, 680 P.2d 1100 (Alaska 1984) in which the court addressed a clause in a subcontract that required the general contractor to pay the subcontractor the final payment within five days of the contractor’s receipt from the owner of final payment for subcontractor’s portion of the work. The issue was when prejudgment interest (allowed in almost all cases in Alaska) should have commenced accruing. The court ruled that the prejudgment interest due for the retainage should have begun five days after the
general contractor received final payment from the owner for the subcontractor's portion of the work rather than when the subcontractor had actually earned that amount by final completion of its work. *Id.* at 1106. In essence the court enforced the clause.

As discussed above, Alaska has a statute, the Public Construction Contract Prompt Payment Act, Alaska Stat. §§ 36.90.200, *et seq.*, which deals with these issues on public contracts.

B. **To What Extent Are They Enforceable on Private Projects**

The Alaska Supreme Court has had no cases involving a “pay-when-paid” clause on a private project. The court in essence enforced such a clause dealing with final payments on a public project, *see, Industrial Co., supra.*, and is likely to follow the weight of recent authorities from other states on the issue of the enforceability of such clauses in a private construction setting.

III. **TRUST FUND STATUTES**

Alaska does not have a trust fund statute. Further, in *Donnybrook Bldg. Supply Co. v. Alaska Nat'l Bank*, 736 P.2d 1147 (Alaska 1987), the court held that the mechanic’s lien statute was intended to be “a complete remedy,” and thus preempted all common law and equitable remedies that might otherwise have been available to a contractor against third parties not in direct contract privity. Consequently, the theory that a construction lender holds the loan proceeds in trust for those working on the project is not available in Alaska under the *Donnybrook* decision. Construction lenders and others not in direct contractual privity with a contractor or subcontractor still face tort liability for tortious conduct such as misrepresentation toward a contractor. *See, Great W. Say. Bank v. George Easley Co.*, 778 P.2d 569 (Alaska 1989).
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

“Pay-if-paid” provisions are enforceable against subcontractors on both public and private projects where the language of the subcontract “plainly and unambiguously” indicates that receipt of payment by the contractor from a specified fund is a condition precedent to the contractor’s obligation to pay the subcontractor. See L. Harvey Concrete, Inc. v. Agro Construction & Supply Co., 189 Ariz. 178, 939 P.2d 811 (1997).

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS


III. TRUST FUND STATUTES

Arizona has a construction trust fund statute that applies to owner-occupied residential construction, Ariz. Rev. Stat. § 33-1005. The construction trust fund statute applies to monies paid by the owner to the general contractor. Violation of the statute can expose individual corporate officers or directors to personal liability for misappropriation of construction trust funds and such debts may not be dischargeable in bankruptcy. See Woodworking Enterprises, Inc. v. Baird, 114 B.R. 198 (9th Cir. 1990). There is no requirement under the statute that the trust funds be held in a separate account.
ARKANSAS

I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

A. To What Extent are They Enforceable in Public Projects

Arkansas has a Contractors’ Payment Protection Act codified at Section 22-9-205 of the Arkansas Code. It specifically states that “payment shall be made upon completion and approval” clauses in construction contracts are enforceable. The statute is applicable to contractors who perform work for any agency of the state, county, municipality, school district or other local taxing unit.

B. To What Extent Are They Enforceable on Private Projects

*Manuel v. Campbell*, 3 Ark. 324 (1841), involved a private project. The Supreme Court of Arkansas held that a payment clause in which the party agreed to pay the other “immediately on the completion of the work” was a condition precedent. The Court stated, “when the day or the time appointed for the payment of money, or performance of an act is to happen after the thing which is the consideration is to be performed, no action can be maintained before performance of the condition.”

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III. TRUST FUND STATUTES

Arkansas does not have a trust fund statute. Rather, Arkansas has a statute which imposes criminal liability on contractors who receive funds from an owner but fail to pay...
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

A. Public Projects

“Pay-if-paid” provisions are not enforceable against subcontractors on public construction projects as such provisions are contrary to public policy in that they act as an indirect waiver of a subcontractor’s right to assert a claim against a statutorily required payment bond. See Capitol Steel Fabricators, Inc. v. Mega Constr. Co, Inc., 58 Cal. App. 4th 1049 (1997).

B. Private Projects

“Pay-if-paid” provisions are not enforceable on private projects because they are contrary to public policy in that they act as an indirect waiver of a subcontractor’s constitutional right to assert a mechanic’s lien for unpaid labor and material. See William R. Clarke Corp. v. Safeco Ins. Co., 938 P.2d 372 (Cal. 1997).

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

A. Public Projects

“Pay-when-paid” clauses are likely enforceable on public projects if the language of the contract provides that payments are due when they are earned by not payable until the prime contractor receives payment from the owner, or upon completion of the project. See Capitol Steel Fabricators, Inc. v. Mega Constr. Co, Inc., 58 Cal. App. 4th 1049 (1997). However, payment must be made upon the subcontractor’s performance or within a reasonable time thereafter. See Yamanishi v. Bleily & Collishaw, Inc., 29 Cal. App.3d 457 (1972).

B. Private Projects

“Pay-when-paid” clauses are likely enforceable on private projects if the language of the contract provides that payments are due when they are earned by not payable until the prime contractor receives payment from the owner, or upon completion of the project. See Capitol Steel Fabricators, Inc. v. Mega Constr. Co, Inc., 58 Cal. App. 4th 1049 (1997). However, payment must be made upon the subcontractor’s performance or within a reasonable time thereafter. See Yamanishi v. Bleily & Collishaw, Inc., 29 Cal. App.3d 457 (1972).
III. TRUST FUND STATUTES

California does not have a construction trust fund statute; however, the 9th Circuit Court of Appeals Bankruptcy Appellate Panel has determined that a construction subcontract which contains a trust provision establishes a fiduciary duty on the part of the contractor receiving contract proceeds. *In re Gonzales*, 22 B.R. 58 (9th Cir. B.A.P. 1982).
COLORADO

I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

Colorado will enforce “pay-when-paid” and “pay-if-paid” clauses, although a contractual provision must unequivocally state the parties’ intent that payment be a condition precedent and that risk of owner or upstream contractor insolvency is shifted to the subcontractor in order to be construed as a “pay-if-paid” clause. See Main Elec., Ltd. v. Printz Servs. Corp., 980 P.2d 522, 527 (Colo. 1999).

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

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III. TRUST FUND STATUTES

Colorado has a construction trust law, Colo. Rev. Stat. Ann. §38-22-127. It provides that all funds disbursed to a contractor or subcontractor on a project subject to Colorado’s mechanics’ lien law are held in trust for downstream subcontractors who may have a lien against the subject property. Colo. Rev. Stat. Ann. §38-22-127(a). However, where the contractor or subcontractor to whom the disbursement was made has a good faith belief that the lien claim is invalid or is subject to setoff, no trust is created. Colo. Rev. Stat. Ann. §38-22-127(b). Colorado imposes personal liability upon those officers controlling the disbursement of funds who divert trust funds to other obligations of the contractor or subcontractor. See Flooring Design Assocs., Inc. v. Novick, 923 P.2d 216, 221 (Colo. App. 1995).
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

A. To What Extent are They Enforceable in Public Projects

1. Prime Contracts

Under Conn. Gen. Stat. § 49-41a (a)(1), every public works contract in an amount in excess of $50,000 is deemed as a matter of law to incorporate a provision requiring the contractor to pay its subcontractors for amounts included on the contractor’s payment application to the owner within thirty days after the public owner has paid the contractor for the particular payment application. There is no case law construing the statutory payment clause under circumstances where payment by the owner is delayed to the contractor for reasons unrelated to the work performed or services provided by a particular subcontractor. For consideration of this issue in regard to a contractual payment clause see R&L Acoustics v. Liberty Mutual Insurance Co., 2001 Conn. Super. Lexis 2854 (September 21, 2001).

2. Subcontracts.

Under Conn. Gen. Stat. § 49-41a (a)(2), every subcontract issued in connection with a “$50,000+” public works contract is deemed as a matter of law to incorporate a provision requiring the subcontractor to pay its sub-subcontractors for amounts paid by the contractor to the subcontractor for the sub-subcontractor’s work within thirty days after the contractor has paid the subcontractor for the sub-subcontractor’s work. There is no case law construing the statutory payment clause under circumstances where payment by the contractor is delayed to the subcontractor for reasons unrelated to the work performed or services provided by a particular sub-subcontractor. For consideration of this issue in regard to a contractual payment clause see R&L Acoustics v. Liberty Mutual Insurance Co., 2001 Conn. Super. Lexis 2854 (September 21, 2001).

3. Vendors

It appears that the terms of Conn. Gen. Stat. § 49-41a (a)(1) and (2) are fully applicable to agreements between vendors and contractors or subcontractors. See Connecticut Electric Equipment Co. v. Fidelity & Guaranty Insurance Co., 2002 Conn. Super. Lexis 3410 (2002). Assuming that this is the case: (a) every vendor agreement with a contractor issued in connection with a “$50,000+” public works contract is deemed as a matter of law to incorporate a provision requiring the contractor to pay its vendors for amounts included on the contractor’s payment application to the owner within thirty days after the public owner has paid the contractor for the particular payment application; and (b) every vendor
agreement with a subcontractor issued in connection with a "$50,000+" public works contract is deemed as a matter of law to incorporate a provision requiring the subcontractor to pay its vendors for amounts paid by the contractor to the subcontractor for the vendor’s materials within thirty days after the contractor has paid the subcontractor for the materials. There is no case law construing the statutory payment clause under circumstances where payment for the materials by the owner to the contractor or by the contractor to the subcontractor is delayed for reasons unrelated to the materials provided by the vendor.

B. To What Extent Are They Enforceable on Private Projects

1. Prime Contracts

In the absence of explicit payment terms between a contractor and subcontractor, every prime contract is deemed as a matter of statute to incorporate a provision requiring that the contractor pay its subcontractors and vendors within fifteen days after the contractor is paid by the owner for the subcontractor’s work or the vendor’s materials. See Conn. Gen. Stat. § 42-158j(a)(2). A contractor is barred by statute from withholding payment from a subcontractor because of a dispute with another contractor, subcontractor or vendor. See Conn. Gen. Stat. § 42-158j(c). There is no case law construing the statutory payment clause under circumstances where the owner delays payment to the contractor for reasons unrelated to the work performed or services provided by a particular subcontractor. To the extent that there is a contractual “pay-if-paid” clause, the Connecticut courts may require payment to the subcontractor within a reasonable time frame of when the subcontractor should have been paid, irrespective of whether the contractor has been paid by the owner for the subcontractor’s work. R&L Acoustics v. Liberty Mutual Insurance Co., 2001 Conn. Super. Lexis 2854 (September 21, 2001). See DeCarlo & Doll, Inc. v. Dilozi (45 Conn. App. 633, 642-43 (1997). Compare Blakeslee Arpaia Chapman, Inc. v. EL Constructors, Inc., 239 Conn. 708 (1997).

2. Subcontracts

In the absence of explicit payment terms between a contractor and subcontractor, every subcontract is deemed as a matter of statute to incorporate a provision requiring that the subcontractor pay its sub-subcontractors and vendors within fifteen days after the subcontractor is paid by the contractor for the subcontractor’s work or the vendor’s materials. See Conn. Gen. Stat. § 42-15 8j(a)(2). A subcontractor is barred by statute from withholding payment from a sub-subcontractor because of a dispute with another contractor, subcontractor or vendor. See Conn. Gen. Stat. § 42-158j(c). To the extent that there is a contractual “pay-if-paid” clause, the Connecticut courts may require payment to the sub-subcontractor within a reasonable time frame of when the sub-subcontractor should have been paid, irrespective of whether the subcontractor has been paid by the contractor for the sub-subcontractor’s work. R&L Acoustics v. Liberty Mutual Insurance Co., 2001 Conn. Super. Lexis 2854 (September 21, 2001). See DeCarlo & Doll, Inc. v. Dilozi, 45 Conn. App. 633, 642-43 (1997). Compare Blakeslee Arpaia Chapman, Inc. v. EL Constructors, Inc. 239 Conn. 708 (1997).
3. Vendor

In the absence of explicit payment terms between a contractor and vendor or a subcontractor and vendor, every prime contract and subcontract is deemed as a matter of statute to incorporate a provision requiring that the contractor pay its vendors and the subcontractor pay its vendors within fifteen days after the contractor is paid by the owner or the subcontractor is paid by the contractor for the vendor’s materials. See Conn. Gen. Stat. § 42-158j(a)(2). A contractor or subcontractor is barred by statute from withholding payment from a vendor because of a dispute with another contractor, subcontractor or vendor. See Conn. Gen. Stat. § 42-158j(c). There is no case law construing the statutory payment clause under circumstances where payment by the owner for the materials is delayed to the contractor for reasons unrelated to the materials furnished to the contractor by the vendor. To the extent that there is a contractual “pay-if-paid” clause, the Connecticut courts may require payment to the vendor within a reasonable time frame of when the vendor should have been paid. R&L Acoustics v. Liberty Mutual Insurance Co. 2001 Conn. Super. Lexis 2854 (September 21, 2001). See DeCarlo & Doll, Inc. v. Dilozir. 45 Conn. App. 633, 642-43 (1997). Compare Blakeslee Arpaia Chapman, Inc. v. EL Constructors, Inc., 239 Conn. 708 (1997).

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

A. To What Extent are They Enforceable in Public Projects

1. Prime

Under Conn. Gen. Stat. § 49-41a (a)(1), every public works contract in an amount in excess of $50,000 is deemed as a matter of law to incorporate a provision requiring the contractor to pay its subcontractors for amounts included on the contractor’s payment application to the owner within thirty days after the public owner has submitted payment to the contractor for the particular payment application. There is no case law construing the statutory payment clause under circumstances where payment by the owner is delayed to the contractor for reasons unrelated to the work performed or services provided by a particular subcontractor. For consideration of this issue in regard to a contractual payment clause, See S&L Acoustics v. Liberty Mutual Insurance Co., 2001 Conn. Super. Lexis 2854 (September 21, 2001).

2. Subcontracts

Under Conn. Gen. Stat. § 49-41a (a)(2), every subcontract issued in connection with a “$50,000+” public works contract is deemed as a matter of law to incorporate a provision requiring the subcontractor to pay its sub-subcontractors for amounts paid by the contractor to the subcontractor for the sub-subcontractor’s work within thirty days after the contractor has paid the subcontractor for the sub-subcontractor’s work. There is no case law construing the statutory payment clause under circumstances where payment by the contractor is delayed to the subcontractor for reasons unrelated to the work performed or services provided by a particular sub-subcontractor. For consideration of this issue in regard to a contractual payment
3. Vendors

It appears that the terms of Conn. Gen. Stat. § 49-41a (a)(1) and (2) are fully applicable to agreements between vendors and contractors or subcontractors. See Connecticut Electric Equipment Co. v. Fidelity & Guaranty Insurance Co. 2002 Conn. Super. Lexis 3410 (2002). Assuming that this is the case: (a) every vendor agreement with a contractor issued in connection with a “$50,000+” public works contract is deemed as a matter of law to incorporate a provision requiring the contractor to pay its vendors for amounts included on the contractor’s payment application to the owner within thirty days after the public owner has paid the contractor for the particular payment application; and (b) every vendor agreement with a subcontractor issued in connection with a “$50,000+” public works contract is deemed as a matter of law to incorporate a provision requiring the subcontractor to pay its vendors for amounts paid by the contractor to the subcontractor for the vendor’s materials within thirty days after the contractor has paid the subcontractor for the materials. There is no case law construing the statutory payment clause under circumstances where payment by the contractor is delayed to the subcontractor for reasons unrelated to the material provided by the vendor.

B. To What Extent are They Enforceable on Private Projects

1. Prime Contracts

It the absence of explicit payment terms between a contractor and subcontractor, every prime contract is deemed as a matter of statute to incorporate a provision requiring that the contractor pay its subcontractors and vendors within fifteen days after the contractor is paid by the owner for the subcontractor’s work or the vendor’s materials. See Conn. Gen. Stat. § 42-158j(a)(2). A contractor is barred by statute from withholding payment from a subcontractor because of a dispute with another contractor, subcontractor or vendor. See Conn. Gen. Stat. § 42-158j(c). There is no case law construing the statutory payment clause under circumstances where payment by the owner is delayed to the contractor for reasons unrelated to the work performed or services provided by a particular subcontractor. To the extent that there is a contractual “pay-when-paid” clause, the Connecticut courts may require payment to the subcontractor within a reasonable time frame of when the subcontractor should have been paid. R&L Acoustics v. Liberty Mutual Insurance Co., 2001 Conn. Super. Lexis 2854 (September 21, 2001). See DeCarlo & Doll. Inc. v. Dilozir, 45 Conn. App. 633, 642-43 (1997). Compare Blakeslee Arpaia Chapman. Inc. v. EL Constructors. Inc., 239 Conn. 708 (1997).

2. Subcontracts

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3. Vendor

In the absence of explicit payment terms between a contractor and vendor or a subcontractor and vendor, every prime contract and subcontract is deemed as a matter of statute to incorporate a provision requiring that the contractor pay its vendors and the subcontractor pay its vendors within fifteen days after the contractor is paid by the owner or the subcontractor is paid by the contractor for the vendor's materials. See Conn. Gen. Stat. § 42-158j(a)(2). A contractor or subcontractor is barred by statute from withholding payment from a vendor because of a dispute with another contractor, subcontractor or vendor. See Conn. Gen. Stat. § 42-158j(c). There is no case law construing the statutory payment clause under circumstances where payment by the owner for the vendor's materials is delayed to the contractor for reasons unrelated to the materials furnished to the contractor by the vendor. To the extent that there is a contractual “pay-if-paid” clause, the Connecticut courts may require payment to the vendor within a reasonable period of time of when the subcontractor should have been paid. *R&L Acoustics v. Liberty Mutual Insurance Co* 2001 Conn. Super. Lexis 2854 (September 21, 2001). See *DeCarlo & Doll. Inc. v. Diloziir,* 45 Conn. App. 633, 642-43 (1997). Compare *Blakeslee Arpaia Chapman. Inc. v. EL Constructors. Inc.,* 239 Conn. 708 (1997).

III. TRUST FUND STATUTES

Connecticut does not have a construction trust fund statute.
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

“Pay-if-paid” provisions are not enforceable in Delaware on private projects. Del. Code Ann. tit. 6, § 3507(e). Subsection (f) of section 3507 states that section 3507 does not apply to public projects. There is no case law construing these statutory provisions, which were only adopted in 2002.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

Del. Code Ann. tit. 6, § 3507 does not prohibit “pay-when-paid” language; however, inasmuch as “pay-if-paid” language is prohibited, presumably a Court will hold that “pay-when-paid” only implies a reasonable time for payment, but payment must ultimately be made. Again, note that subsection (f) of section 3507 states that section 3507 does not apply to public projects. Note again also that section 3507 was only adopted in 2002 and to date there is no case law construing its provisions.

III. TRUST FUND STATUTES

Delaware has a construction trust fund statute that appears to apply to all types of projects. Del Code Ann. tit. 6, § 3502. The statute applies to any contractor, subcontractor, or any other person who enters into contract to supply labor or materials. The statute doesn’t apply to owners. The statute applies to funds received. Violation of the statute can result in interest penalties, Del. Code Ann. tit. 6, § 3506, and a violator may also be subject to criminal fines and possible imprisonment, Del Code Ann. tit. 6, § 3505. If a payment is not withheld “in good faith for reasonable cause,” then a court may also award reasonable attorneys’ fees. There are no restrictions or limitations on commingling under the statute.
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

In the only treatment of “pay-when-paid” and “pay-if-paid” clauses under the law of the District of Columbia, the court assumed but did not decide that a “pay-if-paid” clause was enforceable. *See Urban Masonry Corp. v. N&N Contractors, Inc.*, 676 A.2d 26 (D.C. 1996). The court went on to hold that the clause did not prevent the subcontractor from recovering interest under the facts presented.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

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III. TRUST FUND STATUTES

The District of Columbia does not have a construction trust fund statute.
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

In Florida, there is no bright line separating “pay-when-paid” and “pay-if-paid” decisions. See Kriksev & Brown. The “Pay-When-Paid”/“Pay-If-Paid” Dichotomy and the Florida Trilogy - Bright Line or Murky Fog?, 11 The Constr. Law 8 (Oct. 1991). Both types of payment provisions are enforceable in Florida although such provisions are generally referred to only as “pay-when-paid” clauses. As a general rule, provisions attempting to shift risk of non-payment to the subcontractor so that the subcontractor is not entitled to receive any payment at all until the general contractor is paid by the owner must be clear and unambiguous to be enforceable. Any ambiguity in such provisions is resolved against the general contractor and interpreted as establishing a reasonable time for the general contractor to pay the subcontractor even if the general contractor has not received payment from the owner.

There are no Florida statutes or any case law specifically prohibiting “pay-if-paid” clauses. However, as a general presumption, “the intent in most cases is that payment by the owner to the general contractor is not a condition precedent to the general contractor’s duty to pay the subcontractors.” Peacock Constr. Co., Inc. v. Modern Air Conditioning, Inc., 353 So.2d 840, 842 (Fla. 1977). Pay-if-paid provisions, sometimes referred to as contingent pay provisions, are enforceable in Florida to the extent such provisions clearly and unambiguously express the intention that payment to the subcontractor is not earned and is not payable at all unless the condition precedent of the general contractor’s receipt of payment from the owner is first satisfied. Moreover, the burden of expressing such clear intention to shift the risk of payment is on the general contractor and any ambiguities are resolved against the contractor. DEC Electric, Inc v. Raphael Constr. Corp., 558 So.2d 427 (Fla. 1990); Robert F. Wilson, Inc. v. Post-Tensioned Structures, Inc., 522 So.2d 79 (Fla. 3d DCA 1988); Peacock Constr. v. Modern Air Conditioning, Inc., 353 So.2d 840 (Fla. 1977); Snead Constr. Corp. v. Langerman, 369 So.2d 591 (Fla. 1st DCA 1978); Aetna Casualty & Sur. Co. v. Warren Bros., 355 So.2d 785 (Fla. 1978); Charles R. Pen-v Constr., Inc. v. C. Barry Gibson & Assoc., 523 So.2d 1221 (Fla. 1st DCA 1988); Team Land Dev. Inc. v. Anzac Contractors, Inc., 811 So.2d 698 (Fla. 3d DCA 2002).

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

Pay-when-paid clauses are enforceable in Florida. Where such clause exists, the subcontractor is entitled to payment after a reasonable time even if the general contractor has not received payment from the owner, so long as the reason for nonpayment is not the fault of the subcontractor. Peacock Constr. Co. v. Modern Air Conditioning, Inc., 353 So.2d 840 (Fla. 1977). Any ambiguities in a contract provision where a general contractor has
attempted to shift the risk of nonpayment onto the subcontractor will be resolved against the general contractor and such provision will generally be deemed a “pay-when-paid” or “time of payment” clause and interpreted as establishing a “reasonable time” for the general contractor to pay the subcontractor. G.E.L. Recycling, Inc. v. Atlantic Env., Inc., 821 So.2d 431 (Fla. 5th DCA 2002); Harris Air Systems, Inc. v. Gentrac, Inc. 578 So.2d 879 (Fla. 1st DCA 1991); OBS Co., Inc. v. Pace Constr. Corp., 558 So.2d 404 (Fla. 1990); Snead Constr. Corp. v. Langerman, 369 So.2d 591 (Fla. 1st DCA 1978); Peacock Constr. v. Modern Air Conditioning, Inc., 353 So.2d 840 (Fla. 1977).

Under section 713.245(1), Fla. Stat. (2003), a general contractor can provide a conditional bond which limits the contractor's (and its surety's) obligation to pay the subcontractor until the general contractor receives payments from the owner. Such bonds have been described as "pay-when-paid" bonds. WMS Constr., Inc v. Palm Springs Mile Assoc., LTD., 762 So.2d 973 (Fla. 3d DCA 2000). However, in order for a surety to restrict its duty to pay lienors under section 7 13.245, the contractor must have a valid “pay-when-paid” clause in all its subcontracts. North American Specialty Ins. Co. v. Hughes Supply, Inc., 705 So.2d 616 (Fla. 4th DCA 1998). [Note: the courts referred to the bonds as pay-when-paid, but such bonds are understood to mean "pay-if-paid" bonds.]

Under Chapter 255, Florida Statutes (2003), sureties cannot issue conditional payment bonds for public projects. Because a conditional payment bond cannot be used on a public project, a surety cannot raise the “pay-if-paid” defense. Everett Painting Co., Inc v. Padula & Wadsworth Constr., 856 So.2d 1059 (Fla. 4th DCA 2003).

III. TRUST FUND STATUTES

Florida is not a trust find state per se, except for the limited purpose concerning insurance proceeds as provided in section 713.32, Fla. Stat. (2003). Section 713.32 states that any insurance proceeds payable to the owner or a lienor because of fire or other insured casualty are liable to liens or demands for payment for labor, services, or materials furnished. The named insured who receives any such insurance proceeds is considered a trustee of those proceeds and such proceeds are deemed trust funds for the purposes of this section for one year from the date of receipt of the proceeds.

Chapter 713 governs only private projects. Even though Florida is not considered a “trust” state, there are provisions in Chapter 713 that mandate proper disbursement of payments. For example, section 713.345 provides that any person or entity that receives any payment on account of improving real property must pay all undisputed amounts that are due for services, labor, or materials. Anyone who fails to pay the undisputed amounts due and owing is guilty of a felony.

Additionally, under section 713.246, any person or entity that fails to pay undisputed obligations for labor, services, or materials within 30 days entities any person providing such labor, services, or materials to file a verified complaint. The section further explains the remedies available for the person providing the labor, services, or materials to the
extent of the undisputed amount due. The prevailing party in any proceeding under section 713.346 is entitled to recover costs including reasonable attorneys’ fees.

Section 713.31 further provides legal recourse against anyone that attempts by fraud or collusion to deprive any lienor of its benefits or rights.
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

A. To What Extent are They Enforceable in Public Projects

Generally speaking, the law is unsettled in Georgia in terms of cases explicitly addressing “pay-if-paid” provisions. The general rule in Georgia regarding conditions, however, is: “When the existence of a debt is conditional on the happening of some event, payment cannot be enforced until that event happens; but when payment of an existing liability is postponed until the happening of an event which does not happen, payment must be made within a reasonable time.” Rosing v. Dwoskin Decorating Co., 141 Ga. App. 617, 619, 234 S.E.2d 128, 130 (1977) (quoting MacLeod v. Belvedale, Inc., 115 Ga. App. 444, 446, 154 S.E.2d 756, 759 (1967)).

Based on that language, a Georgia court would probably find that a “pay-if-paid” clause is only enforceable for “a reasonable time.”

The language cited below under “pay-when-paid,” however, certainly does not make this distinction.

B. To What Extent Are They Enforceable on Private Projects

No distinction has been drawn in Georgia cases between public or private projects. Nor has any distinction been made between prime contracts, subcontracts, and contracts with vendors.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

A. To What Extent are They Enforceable in Public Projects

Although no Georgia cases specifically hold that a “pay-when-paid” clause is enforceable, the cases can certainly be read to endorse the concept, and a Georgia federal case and a North Carolina federal case both state that “pay-when-paid” clauses are enforceable in Georgia. The language those cases rely on is:

A provision in a contract may make payment by the owner a condition precedent to a subcontractor’s right to payment if the contract between the general contractor and the subcontractor should contain an express condition showing that to be the
intention of the parties’. ...The condition is clearly expressed in this subcontract.


B. To What Extent Are They Enforceable on Private Projects

No distinction has been drawn in George cases between public or private projects. Nor has any distinction been made between prime contracts, subcontracts, and contracts with vendors.

III. TRUST FUND STATUTES

Georgia does not have a construction trust fund statute. However, Georgia has a criminal statute that makes it a crime for a contractor that has been paid by the owner to fail to pay for labor, services, or material while any amount for which the contractor is liable for such labor, services, or materials remains unpaid. Ga. Code Ann. § 16-8-15. Further, Georgia has recognized a constructive trust fund in narrow circumstances: “Georgia law recognizes the constructive trust fund doctrine with respect to payments owed materialmen by their contractors for improvements made to a third party’s realty,” but only to the extent that payments do not exceed amounts owing to materialmen, and that payments are made to the general contractors at time when materialmen have either a valid lien on the owner’s property or a right to file lien. See Bethlehem Steel Corp. v. Tidwell, 66 B.R. 932, 939-40 (M.D. Ga. 1986).
HAWAII

I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

The Hawaii courts have not addressed the issue of “pay-if-paid” provisions.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

The Hawaii courts have not addressed the issue of “pay-when-paid” provisions.

III. TRUST FUND STATUTES

Hawaii does not have a construction trust fund statute.
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

The enforceability of “pay-if-paid” clauses in construction contracts on public and private projects has not been addressed by Idaho courts.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

The enforceability of “pay-when-paid” clauses in construction contracts on public and private projects has not been addressed by Idaho courts.

III. TRUST FUND STATUTES

Idaho does not have a construction trust fund statute.
ILLINOIS

I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS


II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS


III. TRUST FUND STATUTES

Illinois has a construction trust statute, but it is only applicable to projects on which lien waivers are required. 770 ILCS 60/21.02. The statute provides that where an owner, contractor, subcontractor, or supplier of any tier requires the execution of a lien waiver from any person supplying labor or materials to a project governed by the mechanics’ lien law, any earned but unpaid funds for work for which the lien was waived are held in trust for the party executing the waiver.
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

There is no Indiana statute addressing this issue. There is also a dearth of case law on point. However, Midland Engineering Co., et al. v. John A. Hall Constr. Co. and United States Fidelity & Guaranty Co., 398 F.Supp. 981 (N.D. Ind. 1975) is widely accepted as establishing that “pay-if-paid” and “pay-when-paid” clauses are not enforceable in Indiana. The contract clause at issue in Midland read:

...the last payment, which the said contractor shall pay to said subcontractor immediately after said material and labor installed by said subcontractor to have been completed, approved by said architect, and final payment received by the contractor...” Id. at 993.

The court rejected contractor’s claim that it was not obligated to pay its subcontractor until such time as it received payment from the owner. The court opined that:

Clauses such as Paragraph 15 are not intended to provide the contractor with an eternal excuse for nonpayment. They have been construed by the courts on several occasions to simply provide the contractor with a reasonable time within which to obtain payment from the owner before he is contractually bound to the subcontractors for immediate payment. Id. at 993.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

There is no Indiana statute addressing this issue. There is also a dearth of case law on point. However, Midland Engineering Co., et al. v. John A. Hall Constr. Co. and United States Fidelity & Guaranty Co., 398 F.Supp. 981 (N.D. Ind. 1975) is widely accepted as establishing that “pay-if-paid” and “pay-when-paid” clauses are not enforceable in Indiana. The contract clause at issue in Midland read:

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Clauses such as Paragraph 15 are not intended to provide the contractor with an eternal excuse for nonpayment. They have been construed by the courts on several occasions to simply provide the contractor with a reasonable time within which to obtain payment from the owner before he is contractually bound to the subcontractors for immediate payment. *Id.* at 993.

III. **TRUST FUND STATUTES**

Indiana does not have a trust fund statute.
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

In Grady v. S.E. Gustafson Constr. Co., 251 Iowa 1242, 103 N.W.2d 737 (1960), the Supreme Court of Iowa addressed a contingent payment provision the defendant contractor alleged was a “pay-if-paid” provision. Id. at 1245, 103 N.W.2d at 739. The Court ultimately held that the plaintiff subcontractor was entitled to payment within a reasonable amount of time after it completed its labor as the defendant contractor was responsible for the non-payment of the owner in that the general contractor was refusing to accept final payment from the owner in order to preserve a claim against the owner unrelated to the plaintiff subcontractor’s claim. Id. at 1245-46, 103 N.W.2d at 739. Some of the language in the Court’s opinion could arguably be interpreted as recognizing the enforceability of “pay-if-paid” provisions. Id. at 1246, 103 N.W.2d at 739. There is also one unreported decision of the Iowa Court of Appeals that addressed a “pay-if-paid” contract clause on a private construction project between a general contractor and a sub-contractor, Booth v. Pilot Corp., 2001 WL 726364 (Iowa Ct. App. June 29, 2001). The Iowa Court of Appeals found in Booth that the general contractor had in fact been paid by the owner, and therefore the “condition precedent” was satisfied. Id. at *4. No argument was raised that the “pay-if-paid” clause was unenforceable as a matter of public policy. Accordingly, the law in Iowa on these topics is “unsettled.”

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

Based upon the Supreme Court of Iowa’s decision in Grady v. S.E. Gustafson Constr. Co., 251 Iowa 1242, 103 N.W.2d 737 (1960), Iowa courts will most likely enforce “pay-when-paid” provisions.

III. TRUST FUND STATUTES

Iowa does not have a construction trust fund statute.
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

There do not appear to be any Kansas authorities addressing the issue. However, generally, in the absence of statutory provisions or recognized public policy to the contrary, Kansas decisions normally enforce contracts as written.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

There do not appear to be any Kansas authorities addressing the issue. However, generally, in the absence of statutory provisions or recognized public policy to the contrary, Kansas decisions normally enforce contracts as written. There is one unpublished federal court case in which a "pay when paid" clause was held not to be a condition precedent to a contractor's downstream payment obligation to a subcontractor, but only to have the effect of postponing the payment obligation for a reasonable period of time in which payment may be received from the owner, after which the contractor's obligation may be enforced notwithstanding non-payment by the owner. Shelley Electric, Inc. v. United States Fidelity & Guaranty Co., 1992 WL 31964 (D. Kan. Oct. 16, 1992).

III. TRUST FUND STATUTES

Kansas does not have a trust fund statute.
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

No Kentucky case directly addresses them, but “pay-if-paid” clauses seem to be enforceable in the Kentucky as a matter of narrow contract interpretation and a matter of the parties' intentions. See Dyer, 303 F.2d 655 at 660. Although not specifically addressing a “pay-if-paid” clause, Dyer seems to uphold the enforceability of such provisions by stating that they must be expressly and unambiguous stated. See id. If not so stated, the clause will be interpreted as a "pay-when-paid" provision that simply sets the time for performance. See id.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

The law of Kentucky is sparse concerning this issue and does not seem to make a distinction between public or private contracts and subcontractors or vendors. However, Thos J. Dyer Co. v. Int'l Engineering Co., 303 F.2d 655 (6th Cir. 1962) addressed the effect and enforceability of a “pay-when-paid” clause in a Kentucky contract. The court held that “unless the contract shows clearly that such an action is an express condition,” (emphasis added) these clauses fix the time of payment. Id. at 660. They do not make payments by an owner to the general contractor a condition precedent to payment of subcontractors. Id. In other words, the clauses are simply treated as a promise to pay “within a reasonable time.” Id. Even if the general contractor is not paid, he or she still has the obligation to pay vendors and subcontractors. Id.

III. TRUST FUND STATUTES

Kentucky has not expressly created a statute providing for the creation of a trust fund for proceeds under construction contracts. However, Kentucky places a statutory obligation upon contractors to pay all suppliers of material or labor, including both vendors and subcontractors. Ky. Rev. Stat. Ann. § 376.070. This obligation extends to all situations when a mechanic's or materialman's lien may be filed, even if one has not yet been imposed. Id. One case applying Kentucky law has determined that the statute impliedly creates a trustee relationship. In Re D & B Electric, Inc., 4 B.R. 263 (Bankr. W.D. Ky. 1980). Later cases, however, have rejected this analysis. In Re Sigler, 196 B.R. 762 (Bankr. W.D. Ky. 1996); Kentucky v. Laurel County, 805 F.2d 628 (6th Cir. 1986).
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

A. To What Extent are They Enforceable in Public Projects

Prime Contracts - No authority.

Subcontracts - No authority on point but presumably enforceable.

Vendors - No authority on point but presumably enforceable.

B. To What Extent Are They Enforceable on Private Projects

Prime Contracts - No authority.


Vendors - No authority on point but presumably enforceable.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

A. To What Extent are They Enforceable in Public Projects

Prime Contracts - No authority.


Vendors - No authority on point but presumably enforceable.

B. To What Extent Are They Enforceable on Private Projects

Prime Contracts - No authority.

Vendors - No authority on point but presumably enforceable.

III. TRUST FUND STATUTES

Louisiana does not have a construction trust fund statute.
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

Maine has not addressed the issue of the enforceability of “pay-if-paid” provisions in construction contracts on private or public projects.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS UNSETTLED

Maine has not addressed the issue of the enforceability of “pay-when-paid” provisions in construction contracts on private or public projects.

III. TRUST FUND STATUTES

Maine does not have a trust fund statute.
I. **ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS**


II. **ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS**


III. **TRUST FUND STATUTES**

Maryland has a construction trust law, Md. Code Ann., Real Prop. §§ 9-201, et seq. It requires that any funds paid under a contract by an owner to a contractor or by an owner or contractor to a subcontractor shall be held in trust for those subcontractors who did the work or furnished the materials for purposes of paying those subcontractors. Md. Code Ann., Real Prop. § 9-201. The trust nature of the funds extends to the benefit of lower tiers of subcontractors. *Id.* The law applies to private projects and to those under the Little Miller Act, but not to federal projects within the state or single home residential contracts. Md. Code Ann., Real Prop. § 9-204; *United States ex rel. Allied Bldg. Prods. Corp. v. Federal Ins. Co.*, 729 F. Supp. 477, 478 (D. Md. 1991).
I. ENFORCEABILITY OF “PAY-IF-PAID” CLauses IN CONSTRUCTION
CONTRACTS

A. To What Extent are They Enforceable in Public Projects

1. Non-Filed Sub-bidders

The Massachusetts public construction statutes require that seventeen separate sub-trades must file their sub-bids directly with the owner. See Mass. Gen. Laws Ch. 149, § 44F(1). As a general proposition, if a subcontractor on a public project is not a “filed sub-bidder,” its relation with the general contractor is essentially the same as on a private project. This analysis could be altered if a public owner “approved in writing” a non-filed sub-bidder, in which case the subcontractor would be treated as a statutory subcontractor. Absent such approval, however, it is likely that the relations between non-filed sub-bidders and a general contractor will be treated the same as private contracts.

2. Filed Sub-bidder

Mass. Gen. Laws Ch. 149, § 44F provides a statutory form of subcontract for filed sub-bidders on public projects. Mass. Gen. Laws Ch. 30, § 39F governs the manner in which subcontractors receive periodic and final payments on public projects. While there appears to be no reported decision on the issue, with regard to periodic payments, it has been argued that the language of Mass. Gen. Laws Ch. 30, § 39F itself operates as a “pay-when-paid” provision. See Mass. Gen. Laws Ch. 30, §39F (“Forthwith after the general contractor receives payment on account of a periodic estimate, the general contractor shall pay to each subcontractor the amount paid for the labor performed and the materials furnished by that subcontractor....“). With regard to final payments, however, Bayer & Mingolla Industries, Inc. v. A.J. Orlando Contracting Co., Inc., 6 Mass. App. Ct. 1, 370 N.E.2d 1381 (1978) holds that release of retainage on a public project is not contingent upon final payment from the owner.

B. To What Extent Are They Enforceable on Private Projects

“Pay-when-Paid”/”Pay-if-Paid” provisions are enforceable on private projects where the contractual language contains a “clear provision that payment to the subcontractor is to be directly contingent upon the receipt by the general contractor of payment from the owner.” A.J. Wolfe Co. v. Baltimore Contractors, Inc., 355 Mass. 361, 244 N.E.2d 717 (1969); Bayer & Mingolla Industries, Inc. v. A.J. Orlando Contracting Co., Inc., 6 Mass. App. Ct. 1, 370 N.E.2d 1381 (1978) (reaffirming holding in Wolfe that to be enforceable a "pay-if-paid" provision must be stated as a clear condition precedent); Canam Steel Corp. v. Bowdoin Construction Corp. 34 Mass. App. Ct. 943, 613 N.E.2d 121 (1993) (“A provision tying payment to a subcontractor to receipt of payment by the general contractor from the owner is, however,

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

A. To What Extent are They Enforceable in Public Projects

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B. To What Extent Are They Enforceable on Private Projects


III. TRUST FUND STATUTES

Massachusetts does not have a trust fund statute.
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

In *Berkel & Co. v. Christman Co.*, 533 NW.2d 838 (1995), the Michigan Court of Appeals, in interpreting a “pay-when-paid” clause in the contract between Christman Company and its subcontractor Berkel & Company Contractors (“Berkel”), affirmed the trial court’s decision that Christman Company was not required to pay Berkel until it received payment from the owner. In so holding, the court looked to the language of the contract and determined that the receipt of payment by Christman Company from the owner was a condition precedent to payments to the subcontractor. The court also rejected Berkel’s argument that the “pay-when-paid” clause merely postponed payment for a reasonable amount of time finding that the contract contained no language limiting the condition precedent.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

Based upon the Court’s holding in *Christman Co.*, supra, Michigan courts will most likely enforce “pay-when-paid” provisions on public and private construction projects.

III. TRUST FUND STATUTES


The MBCFA imposes civil liability for violation of the statute. *See People v Whipple*, 202 Mich App 428; 509 NW2d 837 (1993), *James Lumber Co., Inc. v J & S Constr., Inc.*, 107 Midi. App. 793; 309 N.W.2d 925 (1981). The MBCFA also imposes criminal liability for violation of the statute, Mich. Comp. Laws Ann. § 570.152, and personal liability where a defendant personally mis-appropriated the funds after they have been received by the
MINNESOTA

I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

“Pay-if-paid” provisions are enforceable under Minnesota law; however, the language of such provisions must clearly, unequivocally and unambiguously shift the risk of the owner’s insolvency to the subcontractor in order for the provisions to be enforced. See Mrozik Constr., Inc. v. Lovering Assoc., Inc., 461 N.W.2d 49, 52 (1990).

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

“Pay-when-paid” provisions are enforceable under Minnesota law. See Mrozik Constr., Inc. v. Lovering Assoc., Inc., 461 N.W.2d 49, 51 (1990).

III. TRUST FUND STATUTES

Minnesota has a construction trust fund statute that applies to “payments received by any person contributing to an improvement to real estate within the meaning of section 514.01 shall be held in trust by that person for the benefit of those persons who furnished the labor, skill, material, or machinery contributing to the improvement.” Minn. Stat. Ann. § 514.02 (2003). If a person uses trust funds knowing that the funds are owed to a supplier of labor or material and if the person has not provided the person making payment a valid lien waiver in accordance with Minn Stat. Ann. § 514.07, or has not furnished the person making payment with a payment bond in the basic amount of the contract price, such person is guilty of theft. If the misappropriation of trust funds is related to residential real estate, a “shareholder, officer, director, or agent of a corporation who is responsible for the theft shall be guilty of theft of the proceeds.” Minn. Stat. Ann. § 514.02 (2003). A person injured by a misappropriation of trust funds may bring a civil action for “costs, disbursements, including costs of investigation and reasonable attorney’s fees” and may receive other relief as determined by the court. Minn. Stat. Ann. § 514.02 (2003).
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

A. To What Extent are They Enforceable in Public Projects

“Pay-if-Paid” and “Pay-When-Paid” clauses generally are not an issue on public projects in Mississippi. For all public projects over $50,000, Mississippi law requires that a payment and performance bond be posted by the general contractor. Under Mississippi’s “Little Miller Act,” the payment bond covers all subcontractors and vendors through the second tier - those who have a contractual relationship with the prime contractor or with a subcontractor of the prime contractor. Miss. Code Ann. § 31-5-51. Specifically, those covered are identified by the statute as follows:

(i) Subcontractors & Material Suppliers of the Contractor;
(ii) Subcontractor and Material Suppliers and Subcontractors of the Prime Contractor; and
(iii) Laborers who perform work at the Project Site.

With the payment bond in place, there should not be a non-payment issue due to lack of funds.

B. To What Extent Are They Enforceable on Private Projects

The seminal Mississippi case on “pay-when-paid” clauses is Nicholas Acoustics & Specialty Company v. H. M Construction Co., Inc., 695 F.2d 839 (5th Cir. 1983). In that case, the court found that the contractual documents were in conflict and construed them in favor of the unpaid subcontractor. The subcontract provided that the subcontractor would be paid when the contractor was paid. However, the General Contract between the owner and the contractor provided that the contractor would pay the subcontractors upon receiving a release of liens from the subcontractors. The court found that this created a classic “Catch 22” situation—“the owner will not pay until the subcontractors have been paid, and the subcontractors cannot be paid until the owner is paid.” These provisions were found to be conflicting. Accordingly, the United States Court of Appeals for the Fifth Circuit concluded that the “pay-when-paid” clause would be construed as allowing the contractor to delay payment to the subcontractors only for a reasonable time after the subcontractors completed their work.
II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

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III. TRUST FUND STATUTES

Mississippi is not a trust fund state. However, Mississippi does have prompt payment statutes for both public and private projects. Prompt payment is required by contractors to subcontractors on public contracts by Miss. Code Ann. § 31-5-27. Under the statute, the prime contractor on a public project must pay its subcontractor within 15 days of the prime contractor’s receipt from the public owner of that portion of payment, attributable to the subcontractor’s work.
Prompt payment is required by contractors to subcontractors on private projects by Miss. Code Ann. § 87-7-5. Contractors on private projects must pay their subcontractors and suppliers within 15 days of the prime contractor’s receipt of payment for the work completed by each subcontractor and supplier.
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

“Pay-if-paid” claims are enforceable in both private and public construction contracts under Missouri law, but only if clear and unambiguous in both private and public, at least no distinction in case law. Latest case (Meco) makes it difficult to prove provision is unambiguous. *Meco Sys., Inc. v. Dancing Bear Entertainment, Inc.*, 42 S.W.3d 794 (Mo. App. 1981); *American Drilling v. City of Springfield*, 614 S.W.2d 266 (Mo. App. 1981).

No distinction is made between primes, subs, suppliers or vendors. Again, if the “pay-if-paid” provision is clear and unambiguous, it should be enforceable. However, Missouri statute prohibits a waiver of mechanic's lien rights or bond rights by the operation of a “pay-if-paid” clause. Mo. Rev. Stat. § 431.183.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

“Pay-when-paid” provisions are enforceable in both private and public construction contracts. If “pay-if-paid” provision is invalid due to ambiguity, then clause sets reasonable time (i.e., reverts to pay-when-paid). See *Meco Sys., Inc. v. Dancing Bear Entertainment, Inc.*, 42 S.W.3d 794 (Mo. App. 1981); *American Drilling v. City of Springfield*, 614 S.W.2d 266 (Mo. App. 1981).

No distinction is made in case law as to prime contractors, subcontractors, suppliers or vendors.

III. TRUST FUND STATUTES

Missouri does not have a construction trust fund statute.
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

The Montana Supreme Court has not addressed the issue of whether a “pay-if-paid” clause or a “pay-when-paid” clause in a construction contract is enforceable, either with regard to public or private contracts. The Montana Legislature has, however, enacted several statutes that appear relevant to the issue of the enforceability of “pay-if-paid” and “pay-when-paid” clauses in construction contracts.

Section 28-2-723 of the Annotated Code of Montana suggests that “pay-if-paid” and “pay-when-paid” provisions are enforceable under Montana law. Section 28-2-723 provides:

A construction contract may not contain provisions requiring a contractor, subcontractor, or material supplier to waive the right to a construction lien or a right to a claim against a payment bond before the contractor, subcontractor, or material supplier has been paid for the labor, materials, or both labor and materials, furnished by the contractor, subcontractor, or material supplier.

Although this statute has not been interpreted by the Montana Supreme Court, it appears to invalidate any contractual provision that waives a subcontractor's lien rights except in such cases where the lien waivers are executed in conjunction with payment for work performed. Jurisdictions outside of Montana with anti-waiver statutes similar to Mont. Code. Ann. § 28-2-723 have utilized such statutes to strike down “pay-if-paid” and “pay-when-paid” provisions, reasoning that both have the practical effect of acting as a waiver of lien rights, and therefore violate the public policy underlying the anti-waiver statutory provisions pertaining to mechanic's liens. See Wm.R.Clarke Corp. v. Safeco Ins. Co. of America, 938 P.2d 372, 376-377 (Cal. 1997); Capitol Steel Fabricators, Inc. v. Mega Const. Co., Inc., 68 Cal.Rptr.2d 672, 680 (Cal.App.2.Dist., 1997); See also West-Fair Elec. Contractors v. Aetna Cas. & Sur. Co., 661 N.E.2d 967, 971 (N.Y.1995) (wherein the court held that a “pay-if-paid” provision is volatile of New York’s anti-waiver of mechanic’s lien statute). Despite the similarities of Montana's anti-waiver statute to those found in California and New York, it is unclear whether the Montana Supreme Court will utilize Mont. Code. Ann. § 28-2-723 to find “pay-if-paid” and “pay-when-paid” provisions unenforceable.
II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

Other statutory sections provide conflicting authority regarding the enforceability of “pay-when-paid” provisions.

Montana statutes pertaining to construction contracts for residential and commercial projects over $400,000.00 also support the conclusion that “pay-if-paid” and “pay-when-paid” provisions would be unenforceable under Montana law. In particular, Mont. Code. Ann. § 28-2-2102 provides:

performance by a subcontractor of a subcontract entitles the subcontractor to payment from the contractor.

This statute appears to state that a subcontractor’s payment may not be contingent upon payment (or the timing of payment) by the owner to the subcontractor, but instead is due upon performance under the contract. Interestingly, however, at the same time that it enacted Mont. Code. Ann. § 28-2-723-2102 (providing that payment is collectable upon performance), the Montana Legislature enacted additional statutes related to the payment of general contractors and subcontractors that seem to indicate that “pay-when-paid” clauses may be valid and enforceable, with certain limitations. For example, Mont. Code. Ann. § 28-2-2103(2)(a) provides:

Within 7 days after a contractor receives a periodic or final payment from an owner or a state agency, the contractor shall pay the subcontractor, if any, the full amount due the subcontractor in accordance with the subcontract for work performed or materials provided in accordance with that subcontract.

Section 28-2-2104 of the Annotated Code of Montana provides that a contractor may collect interest from an owner for delayed payment by the owner, and shall distribute the pro rata share to the subcontractors. Finally, Mont. Code. Ann. § provides that a subcontractor may suspend (and later terminate) performance under a construction contract if the owner fails to pay the contractor and the contractor then fails to pay the subcontractor for the approved work under the construction contract.

These statutes seem to contemplate the legitimacy of a “pay-when-paid” provision in a construction contract. It is unclear, however, how these statutes should be reconciled with the directive of Mont. Code. Ann. § 28-2-2102 that “performance . . . entitles a subcontractor to payment.” The above described statutes have not yet been interpreted by the Montana Supreme Court.

III. TRUST FUND STATUTES

In reviewing this issue, we examined trust fund statutes of other jurisdictions, such as Colorado Statute, Colo. Rev. Stat. Ann. § 38-22-127, and Maryland Statute, Md. Code Ann., Real Prop., § 9-201 as points of reference. Our research revealed that Montana does
not have a trust fund statute that would require a general contractor to hold in trust payments received on a project for payment to subcontractors and suppliers.
NEBRASKA

I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

    The Nebraska courts have not addressed the issue of “pay-if-paid” provisions in construction contracts.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

    The Nebraska courts have not addressed the issue of “pay-when-paid” provisions in construction contracts.

III. TRUST FUND STATUTES

    Nebraska does not have a construction trust fund statute. Although the language of Neb. Rev. Stat. § 52-123 is consistent with other state’s trust fund statutes, the Supreme Court of Nebraska has held that the statute does not create a trust fund or a fiduciary duty on the part of the contractor. State v. McConnell, 266 N.W.2d 219, 222 (Neb. 1978).
NEVADA

I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

Nevada courts have not addressed the issue of “pay-if-paid” provisions in construction projects on private or public projects.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

Nevada courts have not addressed the issue of “pay-when-paid” provisions in construction projects on private or public projects.

III. TRUST FUND STATUTES

Nevada does not have a construction trust fund statute.
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

New Hampshire law on “pay-if-paid” and/or “pay-when-paid” provisions is unsettled. New Hampshire case law has not specifically interpreted “pay-if-paid” and/or “pay-when-paid” contract provisions. As a general matter, conditions precedent are not favored in New Hampshire, and courts look for specific language such as ‘if’, ‘on condition that’, ‘subject to’, and ‘provided’ before holding that a contract contains a condition precedent. Holden Engineering and Surveying, Inc. v. Pembroke Road Realty Trust 137 N.H. 393, 396 (1993). Accordingly, the language of the contract provision likely would have to clearly indicate that payment by the owner is a condition precedent to payment of the subcontractor based on New Hampshire case law. The reason for withholding payment is also likely to affect the enforceability of a “pay-if-paid” or “pay-when-paid” clause in New Hampshire. See D.M. Holden, Inc. v. Contractors’ Crane Service, Inc. 121 N.H. 831 (1981) (holding contract provision conditioning subcontractor’s right to payment on approval of subcontractor’s work should not be enforced where Crane Service, Inc. failed to properly seek the architect’s approval).

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

New Hampshire law on “pay-if-paid” and/or “pay-when-paid” provisions is unsettled. New Hampshire case law has not specifically interpreted “pay-if-paid” and/or “pay-when-paid” contract provisions. As a general matter, conditions precedent are not favored in New Hampshire, and courts look for specific language such as ‘if’, ‘on condition that’, ‘subject to’, and ‘provided’ before holding that a contract contains a condition precedent. Holden Engineering and Surveying, Inc. v. Pembroke Road Realty Trust 137 N.H. 393, 396 (1993). Accordingly, the language of the contract provision likely would have to clearly indicate that payment by the owner is a condition precedent to payment of the subcontractor based on New Hampshire case law. The reason for withholding payment is also likely to affect the enforceability of a “pay-if-paid” or “pay-when-paid” clause in New Hampshire. See D.M. Holden, Inc. v. Contractors’ Crane Service, Inc. 121 N.H. 831 (1981) (holding contract provision conditioning subcontractor’s right to payment on approval of subcontractor’s work should not be enforced where Crane Service, Inc. failed to properly seek the architect’s approval).

III. TRUST FUND STATUTES

New Hampshire does not have a trust fund statute. New Hampshire law does provide that a lien arises automatically upon performing labor or furnishing material in private
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

A. To What Extent are They Enforceable in Public Projects

New Jersey state courts have not addressed the issue of “pay-if-paid” clauses in public construction contracts.

B. To What Extent Are They Enforceable on Private Projects

New Jersey state courts have not addressed the issue of “pay-if-paid” clauses in private construction contracts.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

A. To What Extent are They Enforceable in Public Projects

New Jersey state courts have not addressed (in a reported opinion) the issue of “pay-when-paid” clauses in public construction contracts.

B. To What Extent Are They Enforceable on Private Projects

New Jersey state courts have not addressed (in a reported opinion) the issue of “pay-when-paid” clauses in private construction contracts. The only reported case applying New Jersey law to this issue is Seal Title Corp. v. Ehret, Inc. where the U.S. District Court for the District of New Jersey held that the contract clause did not contemplate that the bankruptcy of the owner would exonerate the contractor forever from paying the subcontractor the sums that were due. 589 F. Supp. 701 (D.N.J. 1984).

III. TRUST FUND STATUTES


Public Projects:

N.J. Stat. Ann. § 2A:44-148 applies to all money paid by a public entity to a contractor for any type of public improvement. The money is to be treated as a trust fund in
the hands of the contractor until “all claims for labor, materials and other charges incurred” in connection with the improvement are fully paid. This trust fund statute only “protects those who have a direct contractual relationship with the prime or general contractor”, and does not extend its benefits to those “who have furnished labor or materials for the project through contract with any subcontractors down the ladder.” Universal Supply Co. v. Martell Constr. Co., Inc., 156 N.J. Super. 327 (App. Div. 1978). The trust fund is created by any public entity in New Jersey paying any Contractor for “public improvements.” N.J. Stat. Ann. § 2A:44-148. The trust attaches whenever money is paid by a public entity to a contractor and remains until all claims for labor, materials and other charges incurred with the construction have been paid. N.J. Stat. Ann. § 2A:44-148.


Private Projects:

NEW MEXICO
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I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

New Mexico has not addressed the issue of the enforceability of “pay-if-paid” provisions in construction contracts on private or public projects.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS UNSETTLED

New Mexico has not addressed the issue of the enforceability of “pay-when-paid” provisions in construction contracts on private or public projects.

III. TRUST FUND STATUTES

New Mexico does not have a trust fund statute.
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

A. To What Extent are They Enforceable in Public Projects


Prime Contracts:

Enforceable if tied to availability of appropriated funds. A party in privity with a public entity may not file a lien under a contract for public improvement. Under State Finance Law § 136, the aggregate amount of all contracts for a State project may not exceed the amount appropriated and a contractor may be unable to recover for base contract work that exceeds the amount appropriated. Similar statutes affect the right to payment for municipal projects. N.Y. State Fin. Law § 136 (McKinney 2002).

Subcontracts and Vendors:


B. To What Extent Are They Enforceable on Private Projects

Unenforceable. “Pay-if-paid” clauses that make the contractor’s receipt of payment a condition precedent to the subcontractor’s right to payment are unenforceable on private projects in New York because they would void the non-waivable right to file and enforce a lien. In addition, under New York’s Construction Contracts Act, a party may suspend performance if another party to the contract fails to make prompt payment. See West-Fair Elec. Contrs. v. Aetna Cas. & Sur. Co., 87 N.Y.2d 148, 661 N.E.2d 967, 638 N.Y.S.2d 394.
Prime Contracts, Subcontracts, Vendors:


II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

A. To What Extent are They Enforceable in Public Projects


Prime Contracts:

Enforceable if payment is made within 30 days of a proper invoice, with some statutory exceptions. N.Y. State Fin. Law § 179-f (McKinney 2002).

Subcontracts and Vendors:

Time for payment generally runs from prime contractor’s receipt of payment from municipal agency. N.Y. Gen. Mun. Law § 106-b (McKinney 1999) (within 15 days); New York City, N.Y. Rules, Tit. 9, §4-06 (within seven days).

B. To What Extent Are They Enforceable on Private Projects

Prime Contracts:

Payment due 30 days after invoice is approved, unless contract specifies longer period. If payment is contingent on receipt of funds from lender, payment due 7 days after owner receives “good funds” from lender. Enforceability of Construction Contracts Act if Owner never receives “good funds” is unsettled there are no cases construing this new statute. N.Y. Gen. Bus. Law §§ 756-a, 756-d (McKinney Supp. 2004).

Subcontracts and Vendors:


III. TRUST FUND STATUTES

A. New York does have a construction trust fund statute.


B. If so, what type of projects does it apply to (e.g., public/private, residential/commercial, projects over a size limit)? The statute applies to all projects for improvement to real property or construction of public improvements.


C. To what parties does it apply (owner, general contractor, subcontractor, lower-tier subcontractor, vendor)? The statute applies to:

Owners, as trustees of funds received by Owner


Contractors and Subcontractors, as trustees of funds received by Contractors and Subcontractors respectively


Contractors, Subcontractors, Vendors as beneficiaries of the Owner’s trust and beneficiaries of trust funds received by upper tier contractors


Governmental entities with claims such as employment taxes

D. To what funds does it apply (e.g., when does the trust attach — in some jurisdictions it may only apply to funds once they are paid by the owner to the GC)?

The trust arises when trust asset comes into existence (first payment) and continues until all claimants have been paid or the trust is exhausted.

I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS


II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS


III. TRUST FUND STATUTES

North Carolina does not have a construction trust fund statute.
NORTH DAKOTA

I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

There is no North Dakota case law addressing “pay-if-paid” or “pay-when-paid” clauses.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

There is no North Dakota case law addressing “pay-when-paid” or “pay-when-paid” clauses.

III. TRUST FUND STATUTES

North Dakota does not have a Trust Fund Statute
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

In Ohio there are no cases distinguishing between public and private projects when the enforceability of “pay-if-paid” clauses are in dispute. It would be reasonable to expect that there would not be any difference given the clear state of the law currently existing. Such clauses are enforceable under certain specific conditions. If undeniably clear and unambiguous as to the true intent and meaning of the clause a “pay-if-paid” clause will be enforceable. Kalkreuth Roofing & Sheet Metal, Inc. v. Bogner Const. Co., 1998 WL 666765, *3 (Ohio Ct. App. Aug. 27, 1998) (dispute between general contractor and subcontractor); North Market Ass’n v. Case, 132 N.E.2d 122, 122-23 (Ohio Ct. App. 1955). Such clauses need to be stated as a clear condition precedent to payment. Although the noted authority does not specifically address vendor and sub-tier subcontractors, it would be reasonable to expect similar treatment.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

No authority distinguishes the treatment of “pay-when-paid” clauses between public and private projects. In the context of private contracts such clauses are enforceable and are to be construed as a promise to pay within a reasonable time. Power & Pollution Services, Inc. v. Suburban Power Piping Corp., 598 N.E.2d 69 (Ohio Ct. App. 1991) (dispute between general contractor and subcontractor); Thomas J. Dyer Co. v. Bishop Int'l Eng. Co., 303 F.2d 655 (6th Cir. 1962) (dispute between general contractor and subcontractor). Although the noted authority does not specifically address vendors and sub-tier subcontractors, it would be reasonable to expect similar treatment.

III. TRUST FUND STATUTES

Although on public projects there is a requirement for the escrowing of retained funds by the public owner, such are not construed as creating a trust fund and no other statute provides for “trust fund” treatment.
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

There are no Oklahoma appellate court decisions on target. However, there are two federal decisions which decide Oklahoma law as it applies to private works projects.

There are no true “pay-if-paid” Oklahoma cases, yet one federal court decision suggests that Oklahoma would follow the general rule to the effect that courts look with disfavor upon contractual provisions which condition payment upon the happening of a future event (such as payment by the project owner or the prime contractor), and will not find that a condition precedent to payment exists unless required to do so by plain and unambiguous contractual language. Byler v. Great American Insurance Company, 395 F.2d 273 (10th Cir. Okl. 1968). There is no statutory prohibition against “pay-if-paid” clauses.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

“Pay-when-paid” provisions are enforceable for a reasonable length of time following the date upon which payment should have been made to the party relying on the clause. Such provisions are designed only to delay payment for a reasonable time during which the party relying thereon is afforded a fair opportunity to collect the contract earnings from the owner (or perhaps the general contractor). Such provisions do not shift the credit risk downstream or otherwise affect one’s obligation to pay. Byler v. Great American Insurance Company, 395 F.2d 273 (10th Cir. Okl. 1968); followed in Moore v. Continental, Casualty Company, 366 F. Supp. 954 (W.D. Okla., 1973), both of which involve private works projects.

Note: Oklahoma has recently enacted a “Fair Pay for Construction Act” which becomes effective November 1, 2004. However, it does not appear that the Act will preclude either “pay-if-paid” or “pay-when-paid” provisions; rather, it primarily governs progressive payment applications and the time within which such payments must be made by the owner, contractor and others progressing down the contractual chain. See, Senate Bill No. 1561, to be codified as Okla. Stat. tit. 15, §§ 621-627.

III. TRUST FUND STATUTES

The Oklahoma trust fund statutes are Okla. STAT. tit. 42, §§ 152 and 153. Because they create trusts for the benefit of those with “lienable claims” the statutes apply solely to private works projects since lien claims cannot be asserted against public property.
The amount payable under any building or remodeling contract shall, upon receipt by any contractor or a subcontractor, be held as trust funds for the payment of all "lienable claims" due and owing or to become due and owing by such contractors or subcontractors. Similarly, funds received pursuant to a mortgage executed for the purpose of constructing or remodeling any structure are deemed to be trust funds for the payment of all valid lienable claims due and owing or to become due and owing by the mortgagor. Likewise, the amount received by a seller of real property under a warranty deed must be held as trust funds for the payment of all valid lienable claims due and owing or to become due and owing by the seller or his predecessors in title which arise out of improvements made upon the real property within four months (the lien filing period in Oklahoma for a prime contractor) prior to the delivery of the warranty deed. Okla. Stat. tit. 42, § 152.

There is no mandate that the "trust funds" be deposited to a separate or special bank account, although doing so might be the safest method of avoiding an alleged breach of trust and criminal prosecution for embezzlement by trustee under OKLA. STAT. tit. 21, § 1451. Section 153 specifically provides that such "trust funds. . . shall be applied to the payment of said valid lienable claims and no portion thereof shall be used for any other purpose until all lienable claims due and owing or to become due and owing shall have been paid." If the party violating the trust fund law is an entity having the characteristics of limited liability pursuant to law, both the entity and the natural persons having the legally enforceable duty for the management of the entity shall be liable for the proper application of the trust funds, and are subject to punishment for criminal embezzlement by trustee in the event of misuse. For criminal prosecution purposes the "natural persons" subject to punishment include the managing officers of a corporation and the manager(s) of a limited liability company. Okla. Stat. tit. 42, § 153.

The trust fund statutes do not prohibit the filing or enforcement of a statutory labor, mechanic or materialman’s lien by a lien claimant, nor does the filing of a lien claim release the holder of the trust funds from the statutory trust obligations. Okla. Stat. tit. 42, § 153. In fact, a properly perfected mechanic’s and materialman’s lien claim is necessary in order to create a "lienable claim," thus invoking the constructive trust fund statutes. In re Tefertiller, 1989 Ok. 60, 772 P.2d 396.

If someone other than a statutorily identified recipient of trust funds is found to have actually exercised control over disbursement of the funds, knowing it to be a part of the trust res, such person may be regarded pro tanto as an involuntary trustee. Sandpiper North Apartments, Ltd. v. American Nat. Bank and Trust Co. of Shawnee, 1984 OK 13, 680 P.2d 983.

One charged with knowledge of the source of trust funds is required to inquire as to the source, and thereafter make proper distribution by paying valid lienable claims, rather than applying the payment to the oldest debt due. McGlumphy v. Jetero Const. Co.. Inc., 1978 Ok. 154, 593 P.2d 76.
OREGON

I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

Oregon has not addressed the issue of the enforceability of “pay-if-paid” provisions in construction contracts on either public or private construction projects.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

Oregon has not addressed the issue of the enforceability of “pay-when-paid” provisions in construction contracts on either public or private construction projects.

III. TRUST FUND STATUTES

Oregon does not have a construction trust fund statute.
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

A. To What Extent are They Enforceable in Public Projects


Pennsylvania’s Public Prompt Payment Act (the “Act” (62 Pa. C.S. § 3901 et seq.) also suggests that “pay-if-paid” clauses are enforceable on public projects. Although subsection 3933(a) of the Act provides that “[p]erformance by a subcontractor in accordance with the provisions of the contract shall entitle the subcontractor to payment from the party with whom the subcontractor has contracted,”1 subsection 3933(c) of the Act requires only that a contractor or subcontractor pay its subcontractors “the full or proportional amount received for each subcontractor’s work and material … 14 days after receipt of a progress payment.” 14. § 3933(a) & (c) (emphasis added). Thus, under Pennsylvania law, a contractor or subcontractor on a public project need only pay its subcontractors if it has received payment for their work.

Although “pay-if-paid” clauses are enforceable on public projects under Pennsylvania law, contractors and subcontractors must be aware of subsection 3933(b) of the Act, which requires a contractor or subcontractor to “disclose to a subcontractor, before a subcontract is executed, the due date for receipt of progress payments from the government agency.” 62 Pa. CS. § 3933(b). If the contractor or subcontractor fails to do so, “the contractor or subcontractor shall be obligated to pay the subcontractor as though the due dates established in subsection (c) were met by the government agency.” Id. Thus, if a contractor or subcontractor does not disclose to a subcontractor the due date for receipt of progress payments from a government agency, the Act assumes that payment from the government agency has been made and requires the contractor or subcontractor to pay its subcontractor.

B. To What Extent Are They Enforceable on Private Projects

1 The Public Prompt Pay Act defines a “contractor” as “[a] person who enters into a contract with a government agency,” a “subcontractor” as “[a] person who has contracted to furnish labor or materials to or has performed labor for a contractor or another subcontractor in connection with a contract,” and a “government agency” as “any State-aided institution.” 62 Pa. C.S. § 3902. A “contract” is a construction contract exceeding $50,000. Id. Thus, the Public Prompt Pay Act covers subcontractors and vendors.
Pay-if-paid clauses are enforceable on private projects. See *Earthdata Int’l v. STV Inc.*, 159 F. Supp. 2d 844 (E.D. Pa. 2001) (applying Pennsylvania law and holding that there was an issue of fact regarding whether the parties intended a payment clause in subcontract to be construed as a “pay-if-paid” or a “pay-when-paid” clause).

Pennsylvania’s Contractor and Subcontractor Payment Act (the “PCSPA” (73 P.S. 501 et seq.)) also suggests that “pay-if-paid” clauses are also enforceable on private projects. Although the PCSPA provides that “[p]erformance by a contractor or subcontractor in accordance with the provisions of a contract shall entitle the contractor or subcontractor to payment from the party with whom the contractor or subcontractor has contracted,” subsection 507(c) of the PCSPA, entitled “Contractor’s and subcontractor’s payment obligations,” provides, in relevant part, that “[w]hen a subcontractor has performed in accordance with the provisions of the contract, a contractor shall pay to the subcontractor, and each subcontractor shall in turn pay to the subcontractor’s subcontractors, the full or proportional amount received for each subcontractor’s work and materials ... 14 days after receipt of each progress or final payment or 14 days after receipt of the subcontractor’s invoice, whichever is later.” 73 P.S. §§ 504, 507 (a) & (c) (emphasis added). Thus, under the PCSPA, a contractor or subcontractor on a private project need only pay its subcontractors after it has received payment for their work.

Although “pay-if-paid” clauses are enforceable on private projects under Pennsylvania law, contractors and subcontractors must be aware of subsection 507(b) of the PCSPA, which requires a contractor or subcontractor to “disclose to a subcontractor, before a subcontract is executed, the due date for receipt of payments from the owner.” 73 P.S. § 507(b). If the contractor or subcontractor fails to do so, “the contractor or subcontractor shall be obligated to pay the subcontractor as though the due dates established in [73 P.S. § 507(c)] were met by the owner.” Id. Thus, if a contractor or subcontractor does not disclose to a subcontractor the due date for receipt of progress payments from a government agency, the Act assumes that payment from the owner has been made and requires the contractor or subcontractor to pay its subcontractor.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

A. To What Extent are They Enforceable in Public Projects


2 The PCSPA defines a contractor as “[a] person authorized or engaged by an owner to improve real property,” a “subcontractor” as “[a] person who has contracted to furnish labor or materials to, or has performed labor for, a contractor or another subcontractor in connection with a contract to improve real property,” and an “owner” as “[a] person who has an interest in the real property that is improved and who ordered the improvement to be made.” 73 P.S. § 502. Thus, the PCSPA applies to contractors, subcontractors and vendors.
Dist LEXIS 4604 (E.D. Pa Apr. 2, 1991) (construing clause in subcontract on public project as a “pay-when-paid” clause, rather than a “pay-if-paid” clause).

B. To What Extent Are They Enforceable on Private Projects


III. TRUST FUND STATUTES

My research has not uncovered a “Trust Fund Statute” in Pennsylvania. My sense is that the Public Prompt Pay Act and PCSPA, discussed above, serve the purposes that a “Trust Fund Statute” would, and, therefore, Pennsylvania does not have one.
I. ENFORCEABILITY OF “PAY-IF-PAID” OR “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

There are no state or federal court decisions, or any statutes, rules or regulations in Rhode Island that mention or treat “pay-if-paid” or “pay-when-paid” clauses in construction contracts. Rhode Island does observe, however, general principles of contract law relating to conditions precedent. Thus, for example, where a maker’s obligation to pay the holder of a promissory note was conditioned upon the prior payment of a related mortgage, and the condition was not satisfied, no payment on the promissory note was deemed due. Absent some strong public policy to the contrary, there is no reason to believe that, given its demonstrated adherence to the enforceability of conditions precedent, Rhode Island would not enforce a “pay-if-paid” or “pay-when-paid” clause. While Rhode Island’s mechanics’ lien law does generally evidence a strong state interest in securing payment to subcontractors and suppliers, it does not contain any provision that bars or modifies the effect of such clauses. In fact, prior efforts to pass legislation banning such clauses have not met with any success.

II. TRUST FUND STATUTES

Rhode Island does not have a statutory or other form of trust fund that applies to public or private construction projects.


4 The 2004 session of the Rhode Island General Assembly has generated another such attempt in the form of proposed Senate Bill S-2440. The proposed bill provides:

9-1-53. Contractors/subcontractors agreements. -- Any provision of any contract, agreement, or understanding, whereby payment from a contractor to a subcontractor or supplier, is conditioned upon receipt of such payment from any other party including an owner, shall be void and against public policy; provided, however, this section shall not prohibit any claim, cause of action or defense that a contractor may have directly against its subcontractor or supplier. This act shall apply to contracts entered into on or after August 1, 2004.

As of June 2004, the proposed law had not been enacted.
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

South Carolina has a Subcontractors’ and Suppliers’ Payment Protection Act codified at Section 29-6-210 of the South Carolina Code. It specifically states that “pay-if-paid” or “pay-when-paid” clauses in the contract are not enforceable. The statute is applicable to both public and private projects.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

South Carolina has a Subcontractors’ and Suppliers’ Payment Protection Act codified at Section 29-6-210 of the South Carolina Code. It specifically states that “pay-if-paid” or “pay-when-paid” clauses in the contract are not enforceable. The statute is applicable to both public and private projects.

III. TRUST FUND STATUTES

Does the state have a trust fund statute?

South Carolina has a “First Lien on Funds” statute found at Section 29-7-10 of the South Carolina Code.

If so, what type of projects does it apply to (e.g., public/private, residential/commercial, projects over a size limit)?

The statute applies to projects involving the “erection, alteration, or repairing of buildings in this State...”

To what parties does it apply (owner, general contractor, subcontractor, lower-tier subcontractor, vendor)?

It applies to general contractors, subcontractors, lower tier subcontractors and materialmen. It does not apply to the owner.

To what funds does it apply (e.g., when does the trust attach in some jurisdictions it may only apply to funds once they are paid by the owner to the GC)?
It applies to funds paid to the contractor or to any subcontractor.

What remedies are available for breach of the trust under state law (civil, criminal, specific enforcement, interest, attorneys’ fees, personal liability, etc.)?

The contractor or subcontractor who fails to pay a lower tier entity from funds received is guilty of a misdemeanor and may face up to 6 months imprisonment.

Is the trustee entitled to commingle?

There is no prohibition against commingling.
SOUTH DAKOTA

I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

South Dakota does not have a Pay-if-Paid statute or any cases relating to such clauses.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

South Dakota does not have a Pay-When-Paid statute or any cases relating to such clauses.

III. TRUST FUND STATUTES


The statute applies to “any improvement of real estate, mines or purviews.”

The statute applies to “any contractor, subcontractor or supplier.”

The statute applies to funds in excess of five hundred dollars of the proceeds from the project used for non-project-related purposes when there are still project-related outstanding costs. “It is not a violation of this section to withhold funds from a contractor, subcontractor or supplier pending the completion and approval of his final work or product.”

The statute makes such use of the funds a criminal offense: the individual “is guilty of theft of the proceeds of such payment.”

The statute does not mention commingling.
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

Tennessee courts have not directly addressed the issue of enforceability of “pay-if-paid” clauses. The guiding principle seems to be that conditions precedent are not favored in contract law and will not be upheld unless there is clear language to support them. Harlan v. Hardaway, 796 S.W.2d 953, 958 (Tenn. App. 1990). Given the court’s discussion in the Koch case, discussed below, and assuming the “pay-if-paid” clause is worded sufficiently to unambiguously create a condition precedent to a payment obligation (thereby shifting the burden of nonpayment to the subcontractor), the courts probably will enforce the clause. The law is unsettled as to whether this would apply to contracts other than subcontracts or on projects other than the type addressed in Koch (Memphis Housing Authority project), but there is no reason to think it would not.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

Koch v. Construction Tech, Inc., 924 S.W.2d (Tenn. 1996) dealt with a “pay-when-paid” clause (holding that the clause in question did not create a condition precedent such that the contractor was permanently relieved from paying the subcontractor because of nonpayment by the owner). Implicit in the Koch decision is that “pay-when-paid” clauses will be enforced such that the payment obligation from the contractor to a subcontractor awaits receipt of the owner’s payment, but probably only for a reasonable time. Koch directly addresses a subcontract on a Memphis Housing Authority project. The law is unsettled as to whether the Koch holding would apply to other contracts or projects, but there is no reason to think it would not.

III. Trust Fund Statutes

Tennessee does not have a trust fund statute per se. To the extent that similar protection is offered in Tennessee, it is through the Prompt Pay Act, Tenn. Code Ann. §§ 66-34-101 et. seq. The Prompt Pay Act does not apply to residential projects of four single-family units or less. Tenn. Code Ann. § 66-34-702. The Act further provides that it shall not apply to any regulated financial institutions or insurance companies. Tenn. Code Ann. § 66-34-703. With the one exception of Term. Code Ann. § 66-34-205, the Act as it is pertinent to this survey applies to public projects. With the few exceptions noted above, the Act applies to private projects.

Specifically § 66-34-205 and § 66-34-3 04 offer protection to contractors, subcontractors and suppliers. Section 66-34-205 provides that payments due to a contractor
under a contract between owner and contractor shall be held in trust by the owner or third party, if such party provided or committed such sums to the owner, and shall be subject to all legal and equitable remedies. This section does not apply to the State of Tennessee, including its departments, boards or commissions, or to any institution of higher education. Section 66-34-304 states that “any sums received by the contractor as payment for work, services, equipment and materials supplied by the subcontractor, materialman or furnisher for improvements to real property shall be held in trust ... and subject to all legal and equitable remedies.”

Any payment not paid in accordance with the Prompt Pay Act shall accrue interest from date due until date paid. Term. Code Ann. § 66-34-601. After nonpayment and upon proper notification, a contractor, subcontractor or supplier may sue for injunctive relief, and reasonable attorneys’ fees may be awarded to the prevailing party if nonpayment was in bad faith.
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

A. To What Extent are They Enforceable in Public Projects

Prime Contracts: Enforceable
Subcontracts: Enforceable
Vendors: Enforceable

B. To What Extent Are They Enforceable on Private Projects

Prime Contracts: Enforceable
Subcontracts: Enforceable
Vendors: Enforceable

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

A. To What Extent are They Enforceable in Public Projects

Prime Contracts: Enforceable
Subcontracts: Enforceable
Vendors: Enforceable

B. To What Extent Are They Enforceable on Private Projects

Prime Contracts: Enforceable
Subcontracts: Enforceable
Vendors: Enforceable

Both “pay-if-paid” and “pay-when-paid” clauses are enforceable in Texas on both public and private projects. However, because of their harsh results, the courts will avoid holding a clause is a condition precedent if the contractual language will possibly allow it. See Wiszina v. Wilcox 438 S.W. 2d 874 (Tex. Civ. App. - Corpus Christi 1969, writ ref’d n.r.e.) (conditional language pertained to timing of payment when contingency failed to occur); Prickett v. Lendell Builders, Inc., 572 S.W. 2d 57 (Tex. Civ. App. - Eastland 1978, no writ) (conditional language merely applied to when payments would be made, not whether they would be made); Gulf Constr. Co., Inc. v. Self 676 S.W. 2d 624 (Tex. App. - Corpus Christi 1984, writ ref’d n.r.e.) (contingent payment clause merely provides terms of payment and not a
condition precedent); Sheldon L. Pollack Coro. v. Falcon Industries, Inc., 794 S.W.2d 380 (Tex. App. — Corpus Christi 1990, writ denied)(clause reading “contractor will pay...) for work... for which payment has been made by owner or lender to contractor” does not constitute condition precedent); North Harris, etc. v. Fleetwood Constr. Co., 604 S.W. 2d 247 (Tex. Civ. App. — Houston [14th Dist.] 1980, writ ref’d n.r.e.) (clause reading “final payment shall be made... after... full payment therefore by owner...” required payment from owner before contractor’s obligation to pay subcontractor arose).

In order to make payment from owner an enforceable condition precedent, great care should be taken to state that payment to contractor is “an express condition precedent” to contractor’s obligation to pay subcontractor in every clause addressing payment.

III. TRUST FUND STATUTES

Texas does have a construction trust fund statute:

Tex. Prop. Code Chapter 162

If so, what type of projects does it apply to (e.g., public/private, residential/commercial, projects over a size limit)?

Public, private commercial, residential. Residential project; over $5,000. must be deposited in a construction account. Tex. Prop. Code §162.006

To what parties does it apply (owner, general contractor, subcontractor, lower-tier, subcontractor, vendor)?


To what funds does it apply (e.g., when does the trust attach - in some jurisdictions it may only apply once they are paid by the owner to the GC)?

Construction payments. Tex. Prop. Code §162.001(a)

Loan receipts for the purpose of improving specific real property secured by a lien on the property. Tex. Prop. Code §162.001(b)
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

“Pay-if-paid” provisions in construction contracts are enforceable on both private and public projects; however, such provisions are not a defense to most claims to enforce a mechanic’s lien filed under Utah’s mechanic’s lien statute. Utah Code Ann. § 13-8-4 (2004). Such provisions are a defense to a claim to enforce a mechanic’s lien on a “private construction work for the building, improvement, repair, or remodeling of residential property consisting of four units or less.” Utah Code Ann. § 13-8-4(3)(b).

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

“Pay-when-paid” provisions in construction contracts are enforceable on both private and public projects; however, such provisions are not a defense to most claims to enforce a mechanic’s lien filed under Utah’s mechanic’s lien statute. Utah Code Ann. § 13-8-4 (2004). Such provisions are a defense to a claim to enforce a mechanic’s lien on a “private construction work for the building, improvement, repair, or remodeling of residential property consisting of four units or less.” Utah Code Ann. § 13-8-4(3)(b).

III. TRUST FUND STATUTES

Utah does not have a construction trust fund statute.
VERMONT

I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

Vermont does not have a Pay-if-Paid statute or any cases relating to such clauses.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

Vermont does not have a “pay-when-paid” statute or any cases relating to such clauses.

III. TRUST FUND STATUTES

Vermont’s trust fund statute is Vt. Stat. Ann. tit. 9, § 4003, “Contractor’s and subcontractor’s payment obligations.”

This statute applies to the project specified in a contract. It does not specify what type.

This statute applies to contractors and subcontractors.

This statute applies to the payment of subcontractors, and requires that the due date for receipt of payments from the owner be disclosed to the subcontractor. Additionally, when a subcontractor has performed in accordance with the provisions of its contract, a contractor shall pay to the subcontractor, and each subcontractor shall in turn pay to its subcontractors, the full or proportional amount received for each such subcontractor’s work and materials based on work completed or service provided under the subcontract, seven days after receipt of each progress or final payment or seven days after receipt of the subcontractor’s invoice, whichever is later.

If there is a delay in payment,

“the contractor or subcontractor shall pay its subcontractor interest, beginning on the next day, at an interest rate equal to that established by 12 V.S.A. § 2903(b), on such unpaid balance as may be due.”

The statute does not mention commingling.
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

A. To What Extent are They Enforceable in Public Projects

Virginia courts have not addressed whether “pay-if-paid” provisions in construction contracts on public projects are enforceable. However, see generally Galloway Corp. v. S.B. Ballard Construction Co., et al., 250 Va. 493, 464 S.E.2d 349 (1995) (freedom to contract); Virginia Public Procurement Act, Article 4. Prompt Payment, Va. Code Ann. §§ 2.2-4347, et. seq.

B. To What Extent Are They Enforceable on Private Projects

Virginia courts have not addressed whether “pay-when-paid” provisions in construction contracts on private projects are enforceable. However, see generally Galloway Corp. v. S.B. Ballard Construction Co., et al., 250 Va. 493, 464 S.E.2d 349 (1995) (freedom to contract).

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

A. To What Extent are They Enforceable in Public Projects


B. To What Extent Are They Enforceable on Private Projects


### III. TRUST FUND STATUTES

I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

Washington has no statute governing “pay-if-paid” clauses in construction contracts. The one applicable case is *Amelco Electric v. Donald M. Drake Company*, 20 Wash. App. 899, 583 P.2d 648 (1978), review denied 91 Wash.2d 1020. That case interpreted a clause stating that the subcontractor’s right to payment was only “to the extent that Contractor has received payment for said work from Owner”. The court held that this language did not create a condition precedent but merely postponed payment “for a reasonable period of time after the work was completed”, during which time the prime contractor had an opportunity to obtain payment from the owner. It is unsettled whether express “condition precedent” language might result in a different ruling, but the language in *Amelco* (“to the extent that”) seems very similar to “condition precedent”.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

Washington State has no statute governing “pay-when-paid” clauses in construction contracts. Under the *Amelco Electric* case referenced above, it seems probable that a “pay-when-paid” clause will be enforced only to the extent of postponing payment for a reasonable time.

III. TRUST FUND STATUTES

Washington has a “trust fund” statute codified at Wash. Rev. Code § 60.28.010. It applies only to “contracts for public improvements or work, other than for professional services, by the state, or any county, city, town, district, board, or other public body.” By its terms, the statute requires retention of up to 5% of moneys earned “as a trust fund for the protection and payment of any person or persons, mechanic, subcontractor or materialman who shall perform any labor upon such contract or the doing of said work, and all persons who shall supply such person or persons or subcontractors with provisions and supplies.” The statute also protects “the state with respect to taxes” due from the contractor. The 5% retainage is subject to reduction after 50% of the original contract work has been completed.

Construing an earlier version of the statute, the Washington Supreme Court has held that the trust fund statute is also intended to provide protection for sureties. *United States Fidelity and Guaranty Co. v. City of Montesano*, 160 Wash. 565, 571, 295 Pac. 934 (1931) (also indicating that contract retainage clauses may create claim rights by unpaid contractors/suppliers/sureties against an owner who fails to withhold the promised percentage). In *Norris Industries v. Halverson-Mason Constructors*, 12 Wash. App. 393, 400,
529 P.2d 1113 (1974), the Washington State Court of Appeals confirmed that a materialman to a second-tier subcontractor had rights against the “trust fund”, i.e. there seems to be no limit on how many tiers of privity may exist between the owner and the claimant. In *Puget Sound Electrical Workers Health and Welfare Trust Fund v. Merit Co.*, 123 Wash.2d 565, 568, 870 P.2d 960 (1994), the Washington Supreme Court held that a union welfare trust also had standing to assert claims against the project retainage even though they are not listed as protected parties under the statute.

Wash Rev. Code § 60.28.010(1) literally imposes the trust fund requirement only on the project owner, but Wash. Rev. Code § 60.28.010(3) adds that if contractors withhold corresponding sums from their own subcontractors and suppliers, they must pay interest at the same rate that the prime contractor receives (if any).

As demonstrated in *United States Fidelity and Guaranty Co. v. City of Montesano*, 160 Wash. 565, 575, 295 Pac. 934 (1931), the remedy for an owner’s breach of its obligation to hold retained funds for the specified period is the owner’s liability for the amount of the retained fund that was wrongfully released. Washington has a statute obligating public owners to pay interest at a rate of 1% per month on “amounts due on written contracts for public works”, Wash Rev. Code § 39.76.011, and another general statute authorizes interest at a rate of 1% per month on liquidated obligations between parties, Wash Rev. Code § 19.52.010.

The “trust fund” statute only applies to public works, and there does not appear to be any restriction on a public agency mixing retention balances from multiple projects in a single account.
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

West Virginia has no case law or statutes addressing the enforceability of “pay-if-paid” in construction contracts on private or public projects.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

West Virginia has no case law or statutes addressing the enforceability of “pay-when-paid” in construction contracts on private or public projects.

III. TRUST FUND STATUTES

West Virginia does not have a construction trust fund statute.
I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

“Pay-if-paid” provisions in construction contracts for public and private projects are void per Wisconsin statute. Wis. Stat. § 779.135(3) (2003).

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

“Pay-when-paid” provisions in construction contracts for private and public projects are enforceable.

III. TRUST FUND STATUTES

Wisconsin has a trust fund statute that applies to private projects, Wis. Stat. § 779.02(5) (2003), and public projects, Wis. Stat. § 779.16 (2003). The statute is not limited to only certain tier levels. The trust attaches to funds that have been paid out, See Capital City Sheet Metal, Inc. v. Voytovich, 217 Wis. 2d 683, 578 N.W.2d 643 (Ct. App. 1998), or funds paid into the court, See Wis. Dairies, Corp. v. Citizens Bank, 160 Wis. 2d 758, 467 N.W.2d 124 (1991), or funds paid into the bank, See Kraemer Bros. v. Pulaski State Bank, 138 Wis. 2d 395, 406 N.W.2d 379 (1987). The trust fund statute provides for civil penalties and criminal penalties. See Wis. Stat. §§ 779.02(5), 779.16 (civil penalties); Wis. Stat. § 943.20 (criminal penalties); Tri-Tech Corp. of America v. Americomp Services, Inc., 254 Wis.2d 418, 646 N.W.2d 822 (2002) (criminal penalties). Specific enforcement, interest, attorneys’ fees, personal liability – yes on private projects per Wis. Stat. §779.02(5).

Is the trustee entitled to commingle?

Yes, see Simonson v. McInvaille, 42 Wis. 2d 346, 166 N.W.2d 155 (1969).
WYOMING

I. ENFORCEABILITY OF “PAY-IF-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

A. To What Extent are They Enforceable in Public Projects

Wyoming courts have not addressed whether “pay-if-paid” provisions in construction contracts are enforceable on public projects. However, Wyoming does protect contractors in public contracts from the risk of untimely payment by its Prompt Pay Statute, Wyo. Stat. Ann. § 16-6-602 (Michie 2003). The statute provides for the contractor to be paid within forty-five days of receipt of the invoice. Additionally, Wisconsin protects subcontractors on public projects from the risk of contractors not paying them by mandating that contractors furnish a bond when the contract price exceeds seven thousand five hundred dollars ($7500.00). Wyo. Stat. Ann. § 16-6-112. The bond is for the use and benefit of any person performing work or labor during the execution of the contract.

B. To What Extent Are They Enforceable on Private Projects

Wyoming courts have not addressed whether “pay-when-paid” provisions in construction contracts are enforceable on private projects.

II. ENFORCEABILITY OF “PAY-WHEN-PAID” CLAUSES IN CONSTRUCTION CONTRACTS

Wyoming courts have not addressed whether “pay-when-paid” provisions in construction contracts on public or private projects are enforceable.

III. TRUST FUND STATUTES

Wyoming does not have a trust fund statute.
The authors gratefully acknowledge Mr. David T. Peitsch of Hayward Baker and Division 11 of the Forum on the Construction Industry for his key assistance in organizing this survey.


See id.


See id.


There are other reasons for this trend, including the rising cost of arbitration, the increased willingness of arbitrators to grant broad discovery, the increased time to resolution, and the lack of appeal rights.


See id.

Id.


See Restatement of the Laws 2d (Trusts), § 17.


See, e.g. Woodworking, supra, 114 B.R. 1981.
The mechanics of what must be done in the bankruptcy court (e.g., filing a motion for relief from automatic stay or to prohibit use of cash collateral) are beyond the scope of this article. These rights can usually be enforced by the debtor's surety as well. See 11 U.S.C. § 362(d) (party in interest can move for relief from automatic stay); 11 U.S.C. § 363(e) (party in interest may move to condition or prohibit debtor's use of cash collateral).


Ragsdale v. Haller, 780 F.2d 794, 796 (9th Cir. 1986).

Davis, 293 U.S. at 333.

In re Pedrazzini, 644 F.2d 756 (9th Cir. 1981) (California law); In re Cross, 666 F.2d 873 (5th Cir. 1982) (Georgia law); In re Angelle, 610 F.2d 1335 (5th Cir. 1980) (Louisiana law); In re Dloogoff, 600 F.2d 166 (8th Cir. 1979) (Nebraska law); but see In re Romero, 535 F.2d 618 (10th Cir. 1976).

See In re Baird, 114 B.R. 198 (BAP 9th Cir. 1990) (Arizona law); Carey Lumber Co. v. Bell, 615 F.2d 370 (5th Cir. 1980) (Oklahoma law); In re Johnson, 691 F.2d 249, 251 (6th Cir. 1982) (Michigan law); and In re Martin, 35 B.R. 982 (Bankr. E.D. Pa. 1984) (Delaware law). But see Boyle, 819 F.2d 583 (5th Cir. 1987) (Texas law); and In re Rausch, 49 B.R. 562 (Bankr. D.N. J. 1985) (New Jersey law).


See N.Y. Lien Law § 75 (McKinney 1993).