

The Legal Intelligencer

THE OLDEST LAW JOURNAL IN THE UNITED STATES 1843-2011

PHILADELPHIA, TUESDAY, AUGUST 16, 2011

VOL 244 • NO. 32 \$5.00 An **ALM** Publication

The Legal Intelligencer | Special Section | August 2011

Construction Law

The Costs of Withholding Payment:

Developments in Pa. Construction Payment Law For Owners, Contractors and Subcontractors

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Special to the Legal

The Pennsylvania Legislature has developed a two-pronged approach to regulating payment practices to subcontractors on privately funded construction projects. The Pennsylvania Mechanics' Lien Law of 1963 (MLL) and the Pennsylvania Contractor and Subcontractor Payment Act (CASPA) have regulated construction contractor payments for years.

However, recent holdings in the Pennsylvania courts have shed new light on the interaction between the two statutes, which parties have priority in recovering claims, and what steps owners should take to minimize litigation costs.

The MLL, 49 P.S. § 1101, et seq., provides that a contractor or subcontractor has the right to assert a lien on property for labor or materials furnished in the erection or construction of the property, or in the alteration or repair for improvements to the property, as long as the amount of the claim exceeds \$500. A subcontractor seeking relief under the MLL must provide notice to the owner of the property 30 days prior to filing a lien and the subcontractor must act quickly — a lien claim form must be filed within six months of the claimant's last work.

The mechanics' lien is powerful in that it typically relates back to the time in which the work visibly commenced, thus main-



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taining a more senior lien status than if the claimant sought judgment through ordinary channels. Likewise, an owner who has already paid for work performed runs the risk of having the property encumbered by a mechanics' lien, as payment is not an automatic defense. Remedies under the MLL, however, are limited to work per-

formed or material furnished.

In addition to the lien remedies offered under the MLL, payments made to subcontractors on privately funded projects are also subject to CASPA, 73 P.S. § 501, et seq. CASPA regulates the time periods for paying subcontractors and provides statutory relief, by way of interest, penalties and even attorneys' fees, to the substantially prevailing party if timely payments by the general contractor are not made.

CASPA was enacted in 1994 to address abuses within the building industry involving payments due from owners to contractors, from contractors to subcontractors, and from subcontractors to other subcontractors. At its basic level, CASPA operates to level the playing field and, in doing so, ensures prompt payments, discourages unreasonable withholding of payments, and addresses issues involving progress payments and retainages in ongoing construction projects.

Under CASPA, unless the parties agree otherwise, the owner must pay the contractor within 20 days of the end of a billing period or after delivery of the invoice, whichever is later. If, after a seven-day grace period, payment is not made by the owner, interest of 1 percent per month accrues. A contractor, however, must pay its subcontractors (and subcontractors must pay their subcontractors) for either the full or proportional amount received from the owner within 14 days of the progress or final payment, or after the receipt of the

invoice, whichever is later.

Reasonable attorney fees and an additional 1 percent per month penalty is also available to the unpaid contractor or subcontractor if arbitration or litigation is commenced to recover payment due and it is determined that the amount was wrongfully withheld. An amount is not deemed to have been wrongfully withheld, however, to the extent it bears a reasonable relation to the value of any claim held in good faith by the owner, contractor or subcontractor against whom the payment is sought. While the interest provision may be waived by contractual agreement, penalties and attorney fees may not be waived.

Consequently, there are separate methods for subcontractors to obtain relief under Pennsylvania law — a contract claim under the CASPA or a mechanics' lien claim under the MLL. The choice in claim, however, may alter the remedies an aggrieved party may obtain.

The Pennsylvania Superior Court recently made clear, for example, that a subcontractor filing a mechanics' lien against property cannot take advantage of the statutory remedies of CASPA without filing a separate contract claim. In *Wyatt Inc. v. Citizens Bank of Penn.*, the subcontractor plaintiff filed a mechanics' lien on the property after the general contractor filed for bankruptcy. The plaintiff attempted to refile separate lien complaints asserting additional interests, fees, costs and penalties

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attorney fees and expenses incurred in collecting the money owed.

The court reversed the trial court and remanded for a determination of the additional fees. Taking a lead from the U.S. District Court for the Eastern District of Pennsylvania, the court clarified the designation of who is deemed a "substantially prevailing party" under CASPA. In order to qualify as a "substantially prevailing party," the subcontractor must not only recover on its claim for damages, but must also prove that the contractor, without a good faith reason, failed to comply with CASPA's mandate of prompt payment.

Because the contractor in *Zimmerman*

recovered 100 percent of its claim, including interest, penalty, and attorneys' fees, the court held it to be the substantially prevailing party. Moreover, because the contractor was the substantially prevailing party, it could recover all fees and expenses for the post-award period because the court expressly held that CASPA's award of attorneys' fees and expenses incurred in order to collect the judgment are included in the statute.

The court also struck down the owner's argument that the award of attorneys' fees and expenses is discretionary with the court by holding that the award is a clear statutory mandate.

Following *Zimmerman*, the Commerce Court in Philadelphia recently vacated an order denying a contractor's request for additional fees incurred through the date of its original award in *Colony Metal and Glass*

Inc. v. Turcibi Inc. et al. The court held a hearing on the additional damages in which the plaintiff established that it reasonably incurred additional fees and costs through the date of the hearing and that it was entitled to additional penalty and interest amounts through that same date. The court agreed and ruled that under CASPA, the contractor is entitled to be made whole.

In *J.J. Deluca Company Inc. v. Toll Naval Associates, et al.*, the owner and contractor agreed to part ways before the completion of the project. This posed a unique question related to whether a contractor is a "substantially prevailing party." The court held that the contractor, although it was awarded a judgment for monies due, was not a substantially prevailing party because the defendant owner had discovered fraud on the part of the plaintiff contractor and,

as such, the contractor did not prevail on any of the fraud claims. On that basis, the court did not award attorney fees or penalties to the contractor.

In light of these developments, an owner, contractor or subcontractor who has had a breach of contract claim levied against it for violations of CASPA should consider the litigation costs, both in the initial trial or arbitration and in any appeal taken, before withholding payment.

As evidenced by these recent cases, the award of fees, costs and penalties are often a significant percentage of the amount claimed initially by the contractor or subcontractor. Unless the owner is confident that the claimant will not be deemed a substantially prevailing party, the litigation and appellate costs may simply be too prohibitive to defend the claim. •
