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Texas Lien Statute Significantly Alters Subcontract Management Practices for Contracts Executed After January 1, 2012

Recent revisions to the Texas lien laws, Tex. Prop. Code Ann. § 53.001, *et seq.*, mandate the use of statutory lien release forms. Because the statute voids, as a matter of public policy, agreements that “adversely affect” payment bond or lien claims, many standard release forms previously employed by general contractors may be unenforceable. As a result, a general contractor’s subcontract administration practices should be carefully tailored to the statute if it wishes to resolve outstanding subcontractor claims during the course of a construction project.

The New Statutory Scheme Invalidates Many Prior Contracting Practices

The required statutory forms for the release of lien rights and payment bond rights raise significant contracting issues for Texas general contractors. The new Texas statute significantly impairs a general contractor’s freedom to contract insofar as it relates to a subcontractor’s release of lien or payment bond rights.

Tex. Prop. Code Ann. § 53.281(a) provides that “[a]ny waiver and release of a lien or payment bond claim under this chapter is unenforceable unless a waiver and release is executed and delivered in accordance with this subchapter.” Tex. Prop. Code Ann. § 53.282 provides that a “statement purporting to waive, release, or otherwise adversely affect a lien or payment bond claim is not enforceable” unless it complies with the statutory form prescribed by Section 53.284 (emphasis added.)

Under the statute, in order to be effective to release the owner, the owner’s property, the general contractor and any payment bond surety, a waiver and release must “substantially comply” with the statutory forms, and must be signed by the claimant or the claimant’s authorized agent and notarized. In the case of a conditional release, there must be evidence that the payment contemplated by the release was, in fact, made. Tex. Prop. Code Ann. § 53.281(b).

Many general contractors include a broad release of claims in their forms for progress payments. When enforced, these releases are highly effective claims avoidance tools. With the adoption of this mechanic’s lien statute for contracts executed after January 1, 2012, Texas has significantly limited the circumstances in which a contractual release of claims can be enforced.

Currently there is no case law under the statute determining the extent to which, if any, a general contractor can require a periodic release of contract rights as opposed to lien or payment bond rights under the revised statute. The statutory form for the release of lien and payment bond rights includes a “carve-out” on the form “for unpaid retention, pending modifications and changes, or other items furnished” (emphasis added). Because lien and payment bond rights are usually dependent upon contract rights, a subcontractor that seeks to enforce its lien or payment bond rights on a project could conceivably argue that any release of its contract rights that goes beyond the statutorily mandated release form is void and unenforceable because it would “adversely affect a lien or payment bond claim” and would not “substantially comply” with the mandatory form. In particular, a periodic release form with a broad release of claims would likely modify the statutorily mandated carve-out for “unpaid retention, pending modifications and changes, or other items furnished.” Because the carve-out itself is relatively

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broad and includes “pending modifications and changes or other items furnished,” a subcontractor that also seeks to enforce a lien or payment bond claim might argue that any release of its contract rights is unenforceable and void as against public policy under the statutory scheme because it would “adversely affect” lien or payment bond rights.

A subcontractor that allows its lien or payment bond rights to lapse by not timely asserting those rights can nonetheless assert contract rights against a general contractor. Thus, under the Texas statute, so long as a subcontractor in Texas also seeks to enforce either lien or payment bond rights, it might argue that the Texas statute changes Texas public policy insofar as it relates to the enforceability of a periodic release of contract rights in exchange for progress payments. The statute also provides that any contract or agreement “purporting to waive the right to file or enforce any lien or claim created under this chapter is void as against public policy.” Tex. Prop. Code Ann. § 55.286 (emphasis added.)

Because contract rights are not rights that are “created under this chapter,” there is a good argument that Texas public policy nonetheless continues to allow a release of contract rights as a part of periodic applications for payment under certain circumstances. Under circumstances in which the subcontractor has failed to properly exercise its lien rights or payment bond rights (if, for example, the general contractor is not bonded on a private project), then a release of contract rights should be enforceable.

It seems unlikely that the Texas legislature intended to modify contract law outside the context of lien and payment bond releases. Nevertheless, a subcontractor could conceivably argue that even a change order with broad release language is unenforceable (assuming that the subcontractor wanted to renegotiate the change at a later date) because it would “adversely affect” the subcontractor’s lien or payment bond rights. While there is no authority construing the statutory provisions, a fair reading of the statute indicates that the legislature intended to address releases in connection with progress payments and final payment and that the legislature did not intend to invalidate change orders with release provisions because of their effect on a subcontractor’s lien or payment bond rights. There is, however, no statutory provision excepting change orders from the scope of the statute.

The “Safe Harbor” Provisions Provide An Opportunity for Legally Effective Subcontractor Releases in Appropriate Circumstances

There are three enumerated exceptions in the statute in which releases that deviate from the statutory form are enforceable: (i) a release provision that is part of an accord and satisfaction of an “identified dispute”; (ii) a release provision in any action pending in any court or arbitration proceeding; and (iii) any release provision that is executed after an affidavit claiming the lien has been filed or a payment bond claim has been made. Tex. Prop. Code Ann. § 53.287. The last two exceptions regarding pending lawsuits or arbitrations and lien or bond claims that have already been filed do not provide a general contractor with the opportunity to obtain a legally enforceable release as a part of its routine administration of a subcontract in the ordinary course of business. The first exception – “an accord and satisfaction of an identified dispute” – offers what amounts to a “safe harbor” for obtaining a legally enforceable release under certain circumstances.

Resolving claims during the course of a project is almost invariably less expensive than resolving such claims in court or arbitration. For that reason, obtaining a legally enforceable release of claims when such claims are resolved during a project is particularly important. A general contractor should structure its administration of subcontracts to take advantage of this “safe harbor” accord and satisfaction exception whenever it has the opportunity to do so.

Because the safe harbor exception is applicable to an accord and satisfaction for an “identified dispute,” it is unlikely that a general contractor could invoke the statutory exception in every change order by including a boilerplate provision in all of its subcontract change orders reciting that the change order constituted an accord and satisfaction of an identified dispute. Many routine change orders are undisputed, such as change orders adjusting quantities upward or downward for items covered by unit price provisions. Under circumstances in which a general contractor has resolved a genuine dispute with a subcontractor (an “identified dispute” under the language of the statute), a general contractor should take steps to ensure that the change order includes a full release of all contract, lien, and payment bond rights and an express provision indicating that the change order constitutes an “accord and satisfaction of an identified dispute.”

Nothing in the express terms of the statute indicates that the scope of the safe harbor accord and satisfaction exception is limited to a release of only the identified dispute. Thus, any change order that does resolve an “identified dispute” should also include a list of all items that comprise the subcontract balance to that point in time.

Nothing in the statute defines or describes what constitutes an “identified dispute.” Thus, where a general contractor and a subcontractor have a genuine dispute on either entitlement to a change or the pricing associated with the change, the resolution of the matter should constitute an accord and satisfaction of an identified dispute and should be eligible for the “safe harbor” exception.

The Execution of the Statutory Forms

The statutory forms enclosed with this Legal Alert include provisions for both conditional and unconditional releases for both progress payments and final payment. For contracts executed after January 1, 2012, a subcontractor’s first payment application should include the “Conditional Waiver and Release on Progress Payment.” After receiving payment for the initial progress payment and beginning with its second progress payment application, a subcontractor should provide both a “Conditional Waiver and Release on Progress Payment” for the second payment application and an “Unconditional Waiver and Release on Progress Payment” governing the first payment application in order to reflect the fact that the first progress payment application has been paid and that the subcontractor’s lien and payment bond rights are being unconditionally released for the first payment application. The subcontractor would then follow the same procedure for each subsequent payment application.

The statutory forms include a similar two-step procedure for final payment. The statutory form includes a “Conditional Waiver and Release on Final Payment.” The subcontractor would provide this form as a part of its final payment application to indicate that when final payment has been received and the check has cleared, the subcontractor would thereby have waived any right to file a mechanic’s lien or payment bond claim. The statute also includes an “Unconditional Waiver and Release on Final Payment.” The subcontractor should execute and provide this form once final payment has been received and the check has cleared the bank. With the execution of this document, the subcontractor would then release any right to file a mechanic’s lien or payment bond claim on a private improvement. Although the final release forms indicate that the subcontractor has received payment in full, the mandatory statutory final release forms (both conditional and unconditional) do not, by their express terms, include a release of the general contractor.

Contracting Practices Potentially Available to General Contractors Under the Statute

Nothing in the statute prohibits a general contractor from requesting a release in addition to the statutorily mandated forms. For the reasons stated above, however, any additional release must be carefully

drafted, and the statutory scheme unfortunately limits the circumstances in which a general contractor can obtain a legally enforceable release that is broader than the statutory form. Thus, in addition to the statutory forms (which are attached), a general contractor may wish to modify any periodic release forms that it used prior to the adoption of the statute so that it “carves out” from the release those rights that the statute requires while simultaneously seeking a release of all rights not governed by the statute.



If you have any questions about this Legal Alert, please feel free to contact any of the attorneys listed below or the Sutherland attorney with whom you regularly work.

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NOTICE:

This document waives rights unconditionally and states that you have been paid for giving up those rights. It is prohibited for a person to require you to sign this document if you have not been paid the payment amount set forth below. If you have not been paid, use a conditional release form.

UNCONDITIONAL WAIVER AND RELEASE ON PROGRESS PAYMENT

Project: _____

Job No.: _____

The signer of this document has been paid and has received a progress payment in the sum of \$ _____ for all labor, services, equipment, or materials furnished to the property or to _____ (person with whom signer contracted) on the property of _____ (owner) located at _____ (location) to the following extent: _____ (job description). The signer therefore waives and releases any mechanic's lien right, any right arising from a payment bond that complies with a state or federal statute, any common law payment bond right, any claim for payment, and any rights under any similar ordinance, rule, or statute related to claim or payment rights for persons in the signer's position that the signer has on the above-referenced project to the following extent: _____ (job description).

This release covers a progress payment for all labor, services, equipment, or materials furnished to the property or to _____ (person with whom signer contracted) as indicated in the attached statement(s) or progress payment request(s), except for unpaid retention, pending modifications and changes, or other items furnished.

The signer warrants that the signer has already paid or will use the funds received from this progress payment to promptly pay in full all of the signer's laborers, subcontractors, material men, and suppliers for all work, materials, equipment, or services provided for or to the above referenced project in regard to the attached statement(s) or progress payment request(s).

Date: _____

(Company Name)

By: _____
Signature

Title: _____

NOTICE:

This document waives rights unconditionally and states that you have been paid for giving up those rights. It is prohibited for a person to require you to sign this document if you have not been paid the payment amount set forth below. If you have not been paid, use a conditional release form.

UNCONDITIONAL WAIVER AND RELEASE ON FINAL PAYMENT

Project: _____

Job No.: _____

The signer of this document has been paid in full for all labor, services, equipment, or materials furnished to the property or to _____
(person with whom signer contracted) on the property of _____
_____ (owner) located at _____
_____ (location) to the following extent: _____
_____ (job description). The signer therefore waives and releases any mechanic's lien right, any right arising from a payment bond that complies with a state or federal statute, any common law payment bond right, any claim for payment, and any rights under any similar ordinance, rule, or statute related to claim or payment rights for persons in the signer's position.

The signer warrants that the signer has already paid or will use the funds received from this final payment to promptly pay in full all of the signer's laborers, subcontractors, material men, and suppliers for all work, materials, equipment, or services provided for or to the above referenced project up to the date of this waiver and release.

Date: _____

_____(Company Name)

By: _____
Signature

Title: _____

CONDITIONAL WAIVER AND RELEASE ON PROGRESS PAYMENT

Project: _____

Job No.: _____

On receipt by the signer of this document of a check from _____ (maker of check) in the sum of \$_____ payable to _____ (payee or payees of check) and when the check has been properly endorsed and has been paid by the bank on which it is drawn, this document becomes effective to release any mechanic's lien right, any right arising from a payment bond that complies with a state or federal statute, any common law payment bond right, any claim for payment, and any rights under any similar ordinance, rule, or statute related to claim or payment rights for persons in the signer's position that the signer has on the property of _____ (owner) located at _____ (location) to the following extent: _____ (job description).

This release covers a progress payment for all labor, services, equipment, or materials furnished to the property or to _____ (person with whom signer contracted) as indicated in the attached statement(s) or progress payment request(s), except for unpaid retention, pending modifications and changes, or other items furnished.

Before any recipient of this document relies on this document, the recipient should verify evidence of payment to the signer.

The signer warrants that the signer has already paid or will use the funds received from this progress payment to promptly pay in full all of the signer's laborers, subcontractors, material men, and suppliers for all work, materials, equipment, or services provided for or to the above referenced project in regard to the attached statement(s) or progress payment request(s).

Date: _____

_____(Company Name)

By: _____
Signature

Title: _____

CONDITIONAL WAIVER AND RELEASE ON FINAL PAYMENT

Project: _____

Job No.: _____

On receipt by the signer of this document of a check from _____
(maker of check) in the sum of \$ _____ payable to _____
_____ (payee or payees of check) and when the check has
been properly endorsed and has been paid by the bank on which it is drawn, this document becomes
effective to release any mechanic's lien right, any right arising from a payment bond that complies with a
state or federal statute, any common law payment bond right, any claim for payment, and any rights
under any similar ordinance, rule, or statute related to claim or payment rights for persons in the signer's
position that the signer has on the property of _____
(owner) located at _____ (location) to the
following extent: _____
_____ (job description).

This release covers the final payment to the signer for all labor, services, equipment, or materials
furnished to the property or to _____ (person with
whom signer contracted).

Before any recipient of this document relies on this document, the recipient should verify evidence of
payment to the signer.

The signer warrants that the signer has already paid or will use the funds received from this final payment
to promptly pay in full all of the signer's laborers, subcontractors, material men, and suppliers for all work,
materials, equipment, or services provided for or to the above referenced project up to the date of this
waiver and release.

Date: _____

_____(Company Name)

By: _____
Signature

Title: _____