NEW YORK CONSTRUCTION LAW UPDATE

This article is written and published by Vincent T. Pallaci, Esq. Mr. Pallaci is a construction attorney with the law firm of Kushnick & Associates, P.C. and he practices construction law in New York State. Mr. Pallaci is also the publisher and author of the New York Construction Law Update blog (http://newyorkconstructionlawupdate.blogspot.com) and the New York Mechanic's Liens blog (http://nymechanicsliens.blogspot.com)

"PAY IF PAID" CLAUSE IS UNENFORCEABLE IN NEW YORK

In New York, unlike many other states, "pay if paid" clauses are void and unenforceable. West-Fair Elec. Contractors v. Aetna Cas. & Sur. Co., 87 N.Y.2d 148, 638 N.Y.S.2d 394 (1995). In Otis Elevator Co. v. Hunt Const. Group, 52 A.d.3d 1315, 859 N.Y.S.2d 850 (4th Dept. 2008) the plaintiff, Otis, sued for payment due from Hunt Construction Group. Hunt argued that payment from the owner was a condition precedent to the requirement to pay Otis. The Appellate Division held that the pay if paid clause in the contract was merely a timing mechanism and did not shift the risk of the owner's non-payment to the plaintiff. The Court therefore ruled that Otis was entitled to payment despite the owner's non-payment to Hunt. An identical result was reached in North Cent. Mechanical, Inc. v. Hunt Const. Group, Inc., 43 A.D.3d 1396, 843 N.Y.S.2d 894 (4th Dept. 2007).

Exactly what a pay-if-paid clause is may not be entirely clear. A contract provision stating that payment will occur upon a stipulated event is deemed to be a time for payment provision absent an express provision to the contrary. West-Fair. A true pay **if** paid clause specifically will state that payment to the general contractor by the owner is an express condition precedent (although it does not necessarily need to use those exact words) to the general contractor's obligation to pay the subcontractor. A pay if paid provision thus forces the subcontractor to assume the risk of non-payment from the owner and, as such, has been deemed to be void and unenforceable pursuant to Lien Law §34. On the other hand, a true pay **when** paid provision is simply a timing mechanism and does not pass the risk of non-payment on to the subcontractor. Pay when paid provisions are therefore routinely held to be valid. Part of the reasoning behind the prohibition against "pay if paid" clauses is that the subcontractor in effect has waived its right to ever enforce a mechanic's lien. A necessary element of enforcing a mechanic's lien is a showing by the subcontractor that there is presently an amount due and owing to it from the general contractor. However, a pay if paid clause means that payment would never become due to the subcontractor.

Notably, New York will enforce pay if paid clauses if the contract calls for the application of the law of a state that does allow pay if paid clauses. However, the Prompt Pay Act of 2003 (G.B.L. §757) specifically voids any contractual provision that calls for the law of another state to apply to a New York construction project. The Prompt Pay Act went into effect

on January 14, 2003 so any contract entered into before that date may still provide a valid and enforceable pay if paid clause. However, there are likely very few construction contracts in effect today that were entered into prior to January 12, 2003.

Sample "pay if paid" clause:

It is specifically understood and agreed that the payment to the trade contractor is dependent, as a condition precedent, upon the general contractor receiving payments, including retainage, from the owner.

 Mr. Pallaci can be reached at vtp@kushnicklaw.com or (631) 752-7100.