



# Construction Industry Payment Protection Act

## SB2681/HB2706

Sponsored by Senator Paul Rose and Representative Ron Gant

### Identification of the Problem

1. The construction industry needed adequate payment protections.
2. Statutes affecting the construction industry are intertwined and provided some protection but were inconsistent and insufficient.
3. The risk of nonpayment was not borne by party best able to manage risk or fairly allocated.

### How Did We Resolve the Payment Dilemma?

1. Made applicable statutes Internally consistent.
2. Reduced applicability loopholes.
3. Ensured acts have adequate timing, notice, and penalty provisions to protect industry.



## Summary of Changes

1. Modified statutory language to reflect consistent definitions and terminology throughout lien laws, Truth in Construction Act, Prompt Pay Act, and construction defect statutes to maintain internal consistency.
  - a. Tennessee Lien Laws – T.C.A. §§66-11-101, *et. seq.*
  - b. Truth in Construction – T.C.A. §§66-11-201, *et. seq.*
  - c. Prompt Pay Acts of 1985, 1991 – T.C.A. §§12-4-701, *et seq.*; 66-34-101, *et seq.*
  - d. Construction Defect Statute – T.C.A. §§66-36-101, *et seq.*
  
2. Modified statutes to ensure they have adequate timing, notice, and penalty provisions to protect industry.
  - a. Prompt Pay Act
    - i. Clarified existing law that all contractors may recover funds owed to them from the party holding the construction proceeds through an equitable action regardless of any arbitration requirement (T.C.A. §§66-34-104, -205, -602).
    - ii. Raised interest rate to statutory rate (1 ½% per month) applicable to purchases by the State of Tennessee (T.C.A. §66-34-601).
    - iii. Introduced a “stop work” notice procedure that largely mirrors the common law “notice and opportunity to cure” requirement to allow contractors to stop work when they are not paid (T.C.A. §66-34-602).
    - iv. Introduced a “Demand for Reasonable Assurances” that provides all contractors assurance that the owner has obtain sufficient funding to pay for all labor and materials on a project (T.C.A. §66-34-603).



3. Provided forms for use by contractors to serve notice of their rights under Tennessee's construction statutes (T.C.A. §66-34-602, -603).
4. Reduced applicability loopholes by requiring lenders and insurance companies to comply with the Prompt Pay Act on projects where they serve as the Owner. Lenders must now comply with a court order requiring them to deposit funds held in trust for contractors into the court's registry (T.C.A. §66-34-703).
5. Clarified the applicability of the statute of repose by modifying the definition of the term "action."
  - a. Included arbitration within the definition of "action" to clarify that the statute of repose for construction applies equally in litigation and arbitration (T.C.A. §28-1-101)
  - b. Amended terminology used in lien statutes to eliminate "action" and reflect requirement of court proceeding to enforce lien (T.C.A. §§66-11-126, -130, -133, -134, -135, -136, -139, -142)
6. Affirmed that limitations of liability in construction contracts are not against the public policy of the State of Tennessee (new statute).
7. Eliminated unnecessary notice provisions (and associated criminal liability) for commercial construction contracts (T.C.A. §§66-11-201, *et seq.*).

### **Practical Application (How does it Work?)**

1. Tennessee Lien Laws – T.C.A. §§66-11-101, *et seq.*

There are no major practical changes in the way liens are asserted or enforced. General contractors have one year to enforce their lien. Remote contractors must still send notices of nonpayment within 90 days of the last day of each month where they perform work, but are not paid, and also record a lien within 90 days of completion. A remote contractor must file suit on its lien within 90 days of serving/recording the lien.



2. Truth in Construction – T.C.A. §§66-11-201, et. seq

Historically, all contractors were required to serve a pre-construction notice to the owner advising them of potential lien rights. Noncompliance could result in criminal liability but did not affect lien rights. This is a consumer protection statute and primarily protected homeowners that were unfamiliar with the construction process. The concerns supporting the statute for homeowners are not present in commercial construction, which involves sophisticated transactions between parties that understand the industry. Accordingly, commercial contractors are no longer to serve this notice, which simply advised the owner of rights they already understood.

3. Prompt Pay Act of 1991 – T.C.A. §§66-34-101, et seq.

- a. Interest – In the absence of a contractual rate, interest shall accrue on amounts due under a written construction contract at the rate of 1 ½% per month (TCA §66-34-602).
- b. Equitable/Injunctive Relief – Clarifies that a court may order all parties, including a bank, to deposit all funds held in trust into the court's registry pursuant to an injunction. When a contractor is not paid, it may file a motion for injunctive relief and obtain an order requiring the payment (T.C.A. §§66-34-104; -205; -602; -703).
- c. Applicability to Banks/Insurance Companies – Removed blanket exemption these industries held, which prevented contractors from being able to recover construction proceeds. Under the new law, banks must comply with the Prompt Pay Act when they serve in the capacity of an owner and comply with court orders requiring them to pay funds held in trust into the court's registry.
- d. Stop Work Notice – If an owner or contractor fails to make payment to the prime contractor or a remote contractor, the contractor may serve a notice of its intent to stop work ten (10) days after the notice is received and until payment is made. If the owner or contractor from whom payment is sought fails to make payment or provide a response setting forth adequate



legal reasons for the failure to make payment within ten (10) days, the contractor make stop work until receiving payment. If a contractor validly stops work and payment is eventually made or an adequate response is received, the contractor is entitled to an equitable adjustment of the contract schedule when it returns to work (T.C.A. §66-34-602).

- e. Demand for Reasonable Assurance – Similar to many form contracts, a new statute allows a prime contractor to evidence the owner made adequate financial arrangements to pay for the improvements being constructed. After visible commencement, if an owner fails to make payments, contractors may again demand reasonable assurances the owner is capable of paying all amounts due under the construction contract. The request may be included within a contractor's Stop Work Notice. If the owner does not provide an adequate response within 10 days, the contractor may stop work.

#### 4. New Forms

- a. Prompt Pay Act Notice (Tenn. Code Ann. §66-34-602)

This letter shall serve as notice pursuant to the Tennessee Prompt Pay Act, Tenn. Code Ann. §§ 66-34-101, et seq., of [prime contractor or remote contractor]'s intent to seek relief under the Prompt Pay Act. [Prime contractor or remote contractor] furnished [description of labor, materials, or services furnished] in furtherance of improvements to real property located at [property description] pursuant to its written contract with [owner, prime contractor, or remote contractor]. [Prime contractor or remote contractor] first furnished labor, materials, or services on [insert first date] and ["is still continuing to perform" or "last furnished labor, materials, or services on (insert date)"]. If [owner, prime contractor, and/or remote contractor] fail(s) to make payment, arrange for payment, or provide a response setting forth adequate legal reasons for the failure to make payment to [prime contractor or remote contractor] within ten (10) days of your receipt of this letter, then [prime contractor or remote contractor] may, in addition to all other remedies at law or in equity, file a lawsuit for equitable relief, including injunctive relief, for continuing violations of this chapter.



b. Demand for Reasonable Assurances (Tenn. Code Ann. §66-34-603)

[Prime contractor or remote contractor] furnished labor, materials, or services in furtherance of improvements to real property located at [property description] pursuant to its written contract with [owner, prime contractor, or remote contractor]. As of the date of this letter, [owner, prime contractor, or remote contractor] owes [prime contractor or remote contractor] the sum of [amount past due], which is past due or for which [prime contractor or remote contractor] asserts it has not been paid from [owner]. Such amounts were due on or before [insert due date] pursuant to the written contract between the parties. Pursuant to T.C.A. § 66-34-603, [prime contractor or remote contractor] demands [owner] furnish reasonable evidence that [owner] has made financial arrangements sufficient to fulfill its obligation to make all payments in accordance with the written contract or setting forth adequate legal reasons for your failure to make payment, within ten (10) days of your receipt of this letter.

5. Statute of Repose

The statute clarified what the industry previously understood: the statute of repose in Tennessee applies to all claims arising out of a construction project regardless of whether the claim is resolved through litigation or arbitration.

6. Limitations of Liability

The new statute confirms that a limitation of liability provision in a construction contract does not violate the public policy of Tennessee. Provided the amount is reasonable, courts should enforce those provisions as written.