



New Virginia Prompt Payment Statutes Invalidate Most 'Pay When Paid' Clauses

By: W. Alexander Burnett

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On April 27, 2022, the Virginia General Assembly passed Senate Bill 550, which makes "pay when paid" and "pay if paid" clauses unenforceable in most circumstances and requires both public and private construction contracts to include certain payment clauses that obligate the contractors to be liable for the entire amount owed to any subcontractor with which it contracts. The requirements below will apply to all future public and private construction contracts executed on and after January 1, 2023.

The key provisions of SB 550 are broken down into two sets of requirements, one for construction contracts within the private sector and one for state agencies and local governments. Any provision in a construction contract executed after January 1, 2023 that runs counter to these requirements will be void and unenforceable.

Contracts between Owners and General Contractors on Private Projects

For any construction contract between an owner (private sector entity) and a general contractor:

- The owner and general contractor shall include a provision that requires the owner to pay such general contractor within 60 days of the receipt of an invoice following satisfactory completion of the portion of the work for which the general contractor has invoiced.
- An owner shall not be required to pay amounts invoiced that are subject to withholding pursuant to the contract for the general contractor's "noncompliance with the terms of the contract." However, in the event that an owner withholds all or a part of the amount invoiced by the general contractor under the terms of the contract, the owner shall notify the general contractor, in writing and with reasonable specificity, of his intention to withhold all or part of the general contractor's payment with the reason for nonpayment.
- Failure of an owner to make timely payment as provided in this subsection shall result in interest penalties.
- Nothing shall be construed to apply to or prohibit the inclusion of any retainage provisions in a construction contract.

Contracts between Higher Tier Contractors and Subcontractors on Private Projects

For subcontracts between a higher tier contractor and subcontractor on a private sector project:

- All contracts between a higher-tier contractor and subcontractor shall be deemed to include a provision under which that higher-tier contractor is liable to the lower-tier subcontractor with whom the higher-tier contractor contracts for satisfactory performance of the subcontractor's duties under the contract.
- Such contract shall require such higher-tier contractor to pay such lower-tier subcontractor within the earlier of (i) 60 days of the satisfactory completion of the portion of the work for which the subcontractor has invoiced or (ii) seven days after receipt of amounts paid by the owner to the general contractor or by the higher-tier contractor to the lower-tier contractor for work performed by a subcontractor pursuant to the terms of the contract.
- Payment by the party contracting with the contractor (the contractor's customer) shall not be a condition precedent to payment to any lower-tier subcontractor, regardless of whether that contractor has received payment for amounts owed to that contractor, unless the contractor's customer (e.g., the owner) is insolvent or a debtor in bankruptcy. This statutory provision overrides any "pay if paid" or "pay when paid" clauses in a subcontract.
- Such contractors shall not be liable for amounts otherwise reducible pursuant to the subcontractor's "noncompliance with the terms of the contract." "Noncompliance" is not defined or limited in the new statute, but it could include nonconforming or deficient work by the subcontractor, or subcontractor's failure to provide documentation or lien waivers required under the contract.
- In the event that a contractor withholds all or a part of the amount invoiced by any lower-tier subcontractor under the contract, the contractor shall notify the subcontractor, in writing, of his intention to withhold all or a part of the subcontractor's payment with the reason for nonpayment, specifically identifying the contractual noncompliance, the dollar amount being withheld, and the lower-tier subcontractor responsible for the contractual noncompliance.
- Note that the definition of "subcontractor" expressly excludes "persons solely furnishing materials," so these requirements and limitations, including restrictions on pay if paid clauses, do not apply to subcontracts with material suppliers.
- Any provision in a contract contrary to this section shall be unenforceable.

Contracts between General Contractors and Subcontractors on Public Projects

For any construction contract awarded by a state agency or local government:

- Contracts between general contractors and subcontractors are required to include a payment clause that makes a contractor liable for the entire amount owed to any subcontractor with which it contracts.

- Payment by the party contracting with the contractor shall not be a condition precedent to payment to any lower-tier subcontractor, regardless of whether that contractor received payment for amounts owed to that contractor. This statutory provision overrides any "pay if paid" or "pay when paid" clauses in a subcontract. Also, note that, unlike private projects, there is no exception for insolvent or bankrupt subcontractors.
- Contractors will not be liable for amounts otherwise reducible due to the subcontractor's noncompliance with the terms of the contract.
- In the event the contractor withholds all or a part of the amount promised to the subcontractor under the contract, the contractor shall notify the subcontractor, in writing, of his intention to withhold all or a part of the subcontractor's payment with the reason for nonpayment.

Conclusion

A full version of the enacted legislation can be found [here](#).

While this law has a delayed effective date and applies to all construction contracts executed on or after January 1, 2023, the bill also requires the Department of General Services to convene the Public Body Procurement Workgroup to review whether the issue of nonpayment between general contractors and subcontractors necessitates legislative corrective action. The Workgroup is required to report its findings and any legislative recommendations to the General Assembly on or before December 1, 2022. Our attorneys will be closely monitoring this Workgroup and attending meetings over the summer. Please be on the lookout for any further updates this summer and after the Workgroup issues its report. More information on the Workgroup can be found [here](#).

All prime contracts and subcontracts that contain pay if paid or pay when paid clauses, or that do not contain the requirements described above, will need to be updated before January 1, 2023.

For more information, or if you have questions on contract form modifications, please contact Alex Burnett, Patrick Cushing or a member of the Williams Mullen Construction Team.

Related People

- W. Alexander Burnett ? 804.420.6481 ? aburnett@williamsmullen.com

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