

BILL ANALYSIS

Senate Research Center
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C.S.H.B. 1146
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Business & Commerce
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Committee Report (Substituted)

AUTHOR'S/SPONSOR'S STATEMENT OF INTENT

Contingent payment clauses are payment provisions in construction contracts that shift financial risks of non-payment from one party to another and make the payment for work performed by a contractor or subcontractor conditional upon receipt of payment by another person. Typically, the general or prime contractor includes a provision in the subcontract agreement that makes its obligation to pay the subcontractor conditional upon the general or prime contractor's receipt of payment from the owner. The intent of the clause in a subcontract is that general or prime contractors not be required to pay the subcontractor until and unless the contractor receives payment from the owner.

These clauses are commonly used in the construction industry by general contractors and some subcontractors in order to spread their credit risk downstream and have the potential to be used by unscrupulous contractors to avoid payment to subcontractors where the owner has legitimately withheld payment from the contractor due to the contractor's default. Under those circumstances, the subcontractor would be precluded from seeking payment from the contractor even though the subcontractor properly performed its subcontract obligations.

C.S.H.B. 1146 clarifies the circumstances in which contingent payment clauses will not be enforceable under Texas law.

RULEMAKING AUTHORITY

This bill does not expressly grant any additional rulemaking authority to a state officer, institution, or agency.

SECTION BY SECTION ANALYSIS

SECTION 1. Amends Subchapter D, Chapter 35, Business & Commerce Code, by adding Section 35.521, as follows:

Sec. 35.521. AGREEMENT FOR PAYMENT OF CONSTRUCTION SUBCONTRACTOR. (a) Defines "contingent payee," "contingent payment clause," "contingent payor," "improvement," "obligor," and "primary obligor."

(b) Prohibits a contingent payor or its surety from enforcing a contingent payment clause to the extent that the obligor's nonpayment to the contingent payor is the result of the contractual obligations of the contingent payor not being met, under certain circumstances.

(c) Prohibits a contingent payor or its surety from enforcing as to work performed or materials delivered, under certain circumstances. Authorizes the contingent payee to send written notice only after the 45th day after the date the contingent payee submits a written request for payment, as specified.

(d) Sets forth specifications regarding when the written notice becomes effective, for the purposes of Subsection (c).

(e) Provides that a notice given by a contingent payee under Subsection (c) does not prevent enforcement of a contingent payment clause under certain circumstances.

(f) Provides that a written notice given by a contingent payee under Subsection (c) does not prevent the enforcement of a contingent payment clause under certain circumstances. Sets forth actions not included in this subsection.

(g) Provides that on receipt of payment, as specified, the contingent payment clause is reinstated as to work performed or materials furnished after the receipt of the payment, subject to provisions of this section.

(h) Prohibits a contingent payor or its surety from enforcing a contingent payment clause if, under Section 53.026, Property Code, the contingent payee is considered to be in direct contractual relationship with the obligor.

(i) Prohibits a contingent payment clause for being used as a basis for invalidation of the enforceability or perfection of a mechanic's lien under Chapter 53, Property Code.

(j) Prohibits a contingent payor or its surety from enforcing a contingent payment clause if the enforcement would be unconscionable. Provides that the party asserting that a contingent payment clause is unconscionable has the burden of proving that the clause is unconscionable.

(k) Provides that the enforcement of a contingent payment clause is not unconscionable if the contingent payor meets specific criteria.

(l) Provides that a cause of action brought on an assignment made under Subsection (k)(2)(B) is enforceable by a contingent payee against an obligor or a primary obligor.

(m) Provides that a contingent payor is considered to have exercised diligence for purposes of Subsection (k)(1) under a contract for a private project governed by Chapter 53, Property Code, under certain circumstances.

(n) Provides that a contingent payor is considered to have exercised diligence for purposes of Subsection (k)(1) under a contract for a public project governed by Chapter 2253, Government Code, under certain circumstances.

(o) Provides that a contingent payor is considered to have exercised diligence for purposes of Subsection (k)(1) under a contract for a public project governed by 40 U.S.C. Section 3131, under certain circumstances.

(p) Requires a primary obligor to furnish the information described by Subsection (m) or (n), as applicable, to the contingent payor, not later than the 30th day after the date the primary obligor receive a written request for the information. Provides that the contingent payor, the contingent payee, and their sureties are relieved of the obligation to initiate or contingent payor and contingent payee, under certain circumstances.

(q) Provides that the assertion of a contingent payment clause is an affirmative defense to a civil action for payment under a contract.

(r) Provides that this section does not affect a provision that affects the timing of a payment in a contract for construction management or for the construction of improvements to real property if the payment is to be made within a reasonable period.

(s) Prohibits a person from waiving this section by contract or other means. Provides that a purported waiver of this section is void.

(t) Prohibits an obligor or a primary obligor from prohibiting a contingent payor from allocating risk by means of a contingent payment clause.

(u) Sets forth specified types of contractual agreements to which this section does not apply.

SECTION 2. Makes application of Section 35.521, Business & Commerce Code, as added by this Act, prospective.

SECTION 3. Effective date: September 1, 2005.