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HOUSE OF REPRESENTATIVES  
146th GENERAL ASSEMBLY

HOUSE BILL NO. 109

AN ACT TO AMEND TITLE 6 RELATING TO BUILDING CONSTRUCTION AND PAYMENT.

BE IT ENACTED BY THE GENERAL ASSEMBLY OF THE STATE OF DELAWARE:

1           Section 1. Amend Chapter 35, Title 6 of the Delaware Code by striking existing sections 3501 through 3509 and  
2 inserting in place thereof the following:

3           § 3501. Title.

4           This Chapter shall be renamed the "Building Construction Procedures Act".

5           § 3502. Definitions.

6           As used in this chapter:

7           (1)     "Billing period" means the payment cycle agreed to by the parties, or, in the absence of an agreement, the  
8 calendar month within which the work is performed.

9           (2)     "Contractor" means a person who enters into any contract with the owner of land or the owner's agent to  
10 furnish labor, materials or services in connection with (i) the demolition, erection, construction, completion, alteration,  
11 addition or repair of any building or structure, (ii) improvement to land or (iii) other construction services. This definition  
12 includes architects, engineers, surveyors, construction managers, and all persons providing labor, materials or services in  
13 connection with subsections (i), (ii), and (iii) hereof.

14           (3)     "Moneys or funds" includes, but is not limited to, the entire amount of all moneys or funds received by a  
15 contractor or subcontractor, as defined in this section: (a) in connection with a contract for the sale of land and premises and  
16 for the labor, material or services provided in connection with the demolition, erection, construction, completion, alteration,  
17 addition or repair of any building or structure, improvement to land or relating to other construction services; (b) by way of  
18 a loan or advance upon the security of such lands and premises for the purpose of demolition, erection, construction,  
19 completion, alteration, addition, repair, improvement or other construction services; (c) from the other contracting party or  
20 vendee any deposit or sum of money on account of the purchase or contract price; or (d) by a contractor for labor, material  
21 or services provided in connection with the demolition, erection, construction, completion alteration, addition or repair of  
22 any building or structure, improvements to land or other construction services. No part of such moneys or funds shall be

deemed or construed applicable to the payment of the cost or selling price of land, unless that part of the contract price or selling price applicable to cost or selling price of land is specifically so stated in the contract.

(4) "Owner" means a person who has an interest in the lands or premises upon which a contractor has undertaken to provide labor, material or services in connection with the demolition, erection, construction, completion, alteration, addition or repair of any building or structure, improvements to land or other construction services.

(5) "Person" shall include a corporation, partnership, limited liability corporation or partnership, business trust, other association, estate trust, foundation or a natural person.

(6) "Subcontractor" means a person who enters into a contract to furnish labor, material, improvements to land or other construction services for a contractor or another subcontractor.

§ 3503. Contract Terms.

(a) If not otherwise specified in the contract, each construction contract awarded by an owner shall include:

(1) A payment clause which obligates the owner to pay the contractor all undisputed amounts within 30 days of the end of the billing period; and

(2) A clause which obligates the owner to pay the contractor interest equal to the prime lending rate plus five (5) percent per annum on all amounts not paid in accordance with the payment clause.

The payment clause required by this subsection shall not be construed to impair the right of the owner to include in its contract a provision allowing the withholding of a specified percentage of each payment, which is otherwise due to a contractor for satisfactory performance under the contract, as retainage to be paid after all work is approved by the owner, without incurring an interest penalty.

(b) If not otherwise specified in the contract, each construction contract awarded by a contractor shall include:

(1) A payment clause which obligates the contractor to pay all undisputed amounts to the subcontractor and each supplier for satisfactory performance under the subcontract within 30 days out of such amounts as are paid to the contractor; and

(2) An interest penalty clause which obligates the contractor to pay the subcontractor and each supplier interest equal to the prime lending rate plus five (5) percent per annum on all amounts not paid in accordance with the payment clause.

The payment clause required by this subsection shall not be construed to impair the right of the contractor to include in the subcontract a provision allowing the withholding of a specified percentage of each payment, which is otherwise due to a subcontractor and/or a supplier for satisfactory performance under the subcontract, as retainage to be paid after all work is approved by the owner, without incurring an interest penalty.

(c) Interest shall begin to accrue on the day payment is due under this section and end on the date upon which payment of the full principal amount is made. Any interest penalty which remains unpaid at the end of any 30 day period shall be added to the principal amount and interest penalties shall accrue on the whole amount.

(d) It shall be against public policy and shall be void and unenforceable for any provision of a construction contract to:

- (1) Require a contractor to assume the risk of nonpayment of the owner;
- (2) Require a waiver of any statutory or other legal right to commence litigation or arbitration until payment is made by the owner or by a general or prime contractor;
- (3) State that payment, of any kind, to a subcontractor or supplier shall be subject to payment from the owner;
- (4) State that a contractor relies on the credit of the owner and not on the credit of the general or prime contractor or of a bonding company; or
- (5) Require the contract, subcontract, agreement or understanding between a contractor and subcontractor to be subjected to the laws of a State other than Delaware or require litigation, arbitration, mediation or other dispute resolution procedures to occur in or be governed by the laws of a State other than Delaware.

(e) Once a contractor has made payment to the subcontractor or supplier according to the payment clause of the contract or the provisions of this section, future claims for payment against the contractor or any surety of the contractor by party's owed payment from the subcontractor or supplier shall be barred.

(f) This section shall not apply to:

- (1) Public works contracts awarded under Chapter 69 of Title 29, except for § 3503(d)(5) which shall apply to all contracts;
- (2) Contracts for the erection of six (6) or fewer residential units which are under construction simultaneously, or for the alteration or repair of any single residential unit; or
- (3) Contracts for the purchase of materials by a person performing work on that person's own real property.

§ 3504. Payments to contractor impressed with trust.

All moneys or funds received by a contractor in connection with a contract for the demolition, erection, construction, completion, alteration, or repair of any building or structure or additions to a building or structure, including improvements to the land upon which the building is situated, and all moneys or funds received by a contractor in connection with a contract for the sale of land and the demolition, erection, construction, completion, alteration, or repair of any building or structure or addition thereon, including improvements to the land upon which the building is situated, shall be trust funds in the hands of the contractor.

§ 3505. Use or application of money received by a contractor.

No contractor, or agent of a contractor, shall pay, use or appropriate any moneys or funds described in 3504 of this title until such moneys or funds first have been applied to the payment of the full amount of all moneys or funds due and owing by the contractor to all persons (including surveyors and engineers) furnishing labor, material (including fuel) and supplies (including rental equipment) for the demolition, erection, construction, completion, alteration or repair of, or for additions to such building or structure, including improvements to the land upon which the building is situated, regardless of whether the labor, entered into material or supplies entered into or became a component part of any such building, structure or addition and regardless of whether they were furnished on the credit of the building, structure or addition or on the credit of such contractor.

§ 3506. Contractor's failure to use or apply money in accordance with § 3505.

Failure of a contractor, or of an agent of a contractor, to pay or cause to be paid in full the lawful claims of all persons, firms, association of persons or corporations, including surveyors and engineers, furnishing labor, material (including fuel) or supplies (including rental equipment), as required by § 3505 of this title, within 30 days after the receipt of any moneys or funds for the purposes of § 3504 of this title, shall be *prima facie* evidence of the payment, use or appropriation of such trust moneys or funds by the contractor in violation of the provisions of this chapter.

§ 3507. Procedure for disputes of payment claims.

(a) If an owner or contractor disputes an amount stated in an invoice such owner or contractor must notify the party submitting the invoice of the dispute within 15 days of receipt of the invoice, state with specificity the item(s) disputed, the basis for the dispute, and any other information that supports the withholding of the disputed amount; and

(b) If written notice is not given within 15 days of the receipt of the disputed invoice as provided in section (a), the invoice shall be deemed to be accepted and payment shall be made by the owner or contractor. Despite payment of an invoice, the owner or contractor shall retain the right to challenge the quality of work covered by any undisputed invoice.

(c) This section shall not apply:

(1) Public works contracts awarded under Chapter 69 of Title 29 of the Delaware Code;

(2) Contracts for the erection of six (6) or fewer residential units which are under construction simultaneously, or for the alteration or repair of any single residential unit;

(3) Contracts for the purchase of materials by a person performing work on that person's own real property; or

(4) Where the terms of a contract specify a different procedure for disputing claims for payment; provided, however, that no contract shall contain a provision in contravention of § 3505(d)(5) unless the parties explicitly agree otherwise in the contract.

§ 3508. Attorneys' fees and litigation costs.

(a) If arbitration or litigation is commenced to recover payment and it is determined that the owner, contractor or subcontractor has failed in good faith to comply with the payment terms of the contract or this title, the arbitrator or the Court, whichever applicable, may award the amount determined to have been wrongfully withheld, plus an amount equal to the amount wrongfully withheld, as additional damages. An amount shall not be deemed to have been wrongfully withheld to the extent that it bears a reasonable relationship to the value of any disputed amount or claim held in good faith by the owner, contractor or subcontractor against whom the contractor or subcontractor is seeking to recover payment.

(b) The party commencing arbitration or litigation shall have the burden of proof that payment has been wrongfully withheld.

(c) Absent any agreement to the contrary between or among the parties, the arbitrator or the Court in any proceeding arising under this chapter may award to the substantially prevailing party its reasonable attorneys' fees, arbitration or court costs and expenses, and expenses for expert witnesses if applicable. Any award of attorneys' fees shall not be limited by 10 Del. C. § 3912.

(d) This section shall not apply to:

(1) Public works contracts awarded under chapter 69 of Title 29 of the Delaware Code;

(2) Contracts for the erection of six (6) or fewer residential units which are under construction simultaneously, or for the alteration or repair of any single residential unit; or

(3) Contracts for the purchase of materials by a person performing work on that person's own real property.

(e) This section shall not apply where the terms of a contract between a general or prime contractor and subcontractor specifies different terms regarding the award of attorneys' fees and litigation costs in arbitration or judicial proceeding.”.

Section 2. Amend Chapter 35, Title 6 by redesignating “§ 3505” as “§ 3509.”

#### SYNOPSIS

The primary purpose of this Act is to provide a party (a contractor, a subcontractor or a material supplier) with the right to file a legal action against a contractor or an owner who has improperly withheld the payment of money to force settlement or for other reasons unrelated to a lawful dispute. Often the value of these claims and the cost of litigation do not justify filing litigation. Moreover, the current statute is often unclear and confusing, which has resulted in difficulties for the Courts in applying the statute and overseeing the related litigation.

The Act further seeks to provide clear language that will allow parties to pursue claims under the statute and recover an amount equal to the amount wrongfully withheld plus attorneys fees, if it is determined that the contractor or owner withheld payment in bad faith. Additionally, this Act seeks to expand the applicability of the Chapter to encompass various construction services offered on present day projects which may not have been offered when the Chapter was originally enacted.

In sum, the revisions to the Chapter are primarily focused on three areas: (1) applying the Chapter to all services provided on construction projects; (2) coordinating the various sections so they work cohesively, making such sections easier to apply; and (3) addressing relevant issues that the Courts have historically struggled with in applying the statute.

In particular, the revisions to current Chapter 35, Title 6, on a section by section, basis are as follows:

First, existing Section 3501 was amended to cover relationships between contracting parties in three categories: (1) demolition, erection, construction, completion, addition or repair of any building or structure; (2) improvements to land; and (3) other construction services. The current version of the statute covered only the first category.

Section 3503 amends the existing statute by combining the contract clauses in current §§ 3506 and 3507 into one section. This section also seeks to harmonize the timing of events under the two sections, which are currently inconsistent. This section also adds a clause in section (d)(5) that makes it against public policy to require any agreement to be subject to laws of any State other than Delaware or to require any legal action, arbitration, mediation or other resolution procedure to take place outside the State of Delaware. Finally, the title was changed from "Payments to Contractor" to "Contract Terms" to reflect the combination of the two sections.

Prior Section 3502, now embodied in Section 3504, was amended to reflect the three categories of projects covered by the Act.

Prior Section 3503, now embodied in § 3505, was amended to reflect the three categories of projects covered by the Act.

Prior Section 3504, now embodied in § 3506, was amended to reflect the three categories of projects covered by the Act and reference the correct new sections of the Act.

New Section 3507 embodies former sections 3506 and 3507. In addition, the first subsection was revised to allow a contractor or subcontractor 15 days to dispute an invoice and thereby avoid the situation where the invoice is designated as accepted. This is a more reasonable timeline for all types of construction projects than the current 7 days.

Prior Section 3508 was revised to clarify when attorneys' fees and litigation costs could be awarded, the standard to award such fees, and to exclude attorneys' fees from the limitation provided for in 10 Del. C. § 3912.

Prior Section 3505 was merely renumbered as Section 3509.