

Pay-If-Paid No Longer Enforceable in Virginia

On January 1, 2023, “pay-if-paid” clauses in new contracts became void as against public policy and unenforceable as a result of Virginia Senate Bill 550 (SB 550) going into effect. See Va. Code §§ 2.2-4354 and 11-4.6. Moreover, pay-when-paid clauses in some public and private construction contracts were also limited. As outlined below, now only pay-when-paid clauses with a reasonable time period for payment are enforceable.

In *New Virginia Law Prohibits Pay-if-Paid Clauses in Construction Contracts*, we discussed the impacts of SB 550 and the implications for project owners and contractors regarding the prohibition of pay-if-paid clauses. Under most pay-if-paid provisions, contractors (of all tiers) were contractually permitted to wait to pay their subcontractors until they themselves first received payment for work. These pay-if-paid clauses shifted the risk of non-payment to the project’s subcontractors as a result. In contrast, pay-when-paid clauses require a general contractor to make payment to its subcontractors within a reasonable time period, even if the general contractor does not first receive payment from the project owner. Pay-when-paid clauses have been viewed by courts as a timing mechanism as opposed to a contractual condition precedent.

Further, under the new law, project owners are required to pay their general contractors within sixty days of receipt of an invoice following the satisfactory completion of the work. Similarly, contractors are required to make downstream payments to their subcontractors within the earlier of seven days after receipt of amounts paid by the project owner or higher-tier contractor or sixty days of the satisfactory completion of work for which the subcontractor issued an invoice (whether or not payment is received from the owner).

The new law stops short of prohibiting retainage provisions, but if owners or contractors choose to withhold some or all of the invoiced amounts by a contractor or subcontractor, they are required to provide notice in writing of the withholding, including the amount being withheld and the reasoning or basis for the nonpayment. If a party fails to comply with these notice provisions, it may be liable for interest penalties.

It is important to note that the new law only applies to contracts entered into on January 1, 2023, or after—the law is not retroactive, and parties will not have to renegotiate previously executed contracts to be in compliance with the new law. That said, all parties should review the payment provisions in their existing construction contracts as well as those being negotiated and entered into after January 1, 2023, for compliance with the law’s new requirements.

For more information, or if you have questions on contract form modifications, please contact a member of the Cozen O’Connor Construction Team.



Lawrence M. Prosen

Member

lprosen@cozen.com
Phone: (202) 304-1449
Fax: (202) 861-1905



Jeffery R. Mullen

Member

jrmullen@cozen.com
Phone: (215) 665-6939
Fax: (215) 665-2013



Josephine M. Bahn

Associate

jbahn@cozen.com
Phone: (202) 280-6484
Fax: (202) 861-1905

Related Practice Areas

- Construction Law

Industry Sectors

- Real Estate & Construction