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SJC gets crack at interpreting Prompt Pay Act

Decision will build upon Appeals Court ruling

Kris Olson//February 16, 2024//

It was big news in the construction industry in 2022 when the Appeals Court issued its ruling in ***Tocci Building Corporation v. IRIV Partners, LLC, et al.,*** the first appellate decision interpreting the Massachusetts Prompt Payment Act.

The main message in *Tocci* was that the act, G.L.c. 149, §29E, was not to be trifled with. Unless its requirements for rejecting a pay application were strictly adhered to, those applications would be deemed approved, the Appeals Court ruled.

The Supreme Judicial Court now has a chance to amplify or alter that message in ***Business Interiors Floor Covering Business Trust v. Graycor Construction Company, Inc., et al.***, which was argued on Feb. 7.

In its call for amicus briefs, the SJC framed the issue in *Business Interiors* as whether a general contractor loses its right to assert common law affirmative defenses when it has failed either to pay a subcontractor in a timely manner or complied with the statutory requirements for explaining its reasons for rejecting the subcontractor's payment claims.

While the general contractor in *Business Interiors* acknowledges that it has failed to comply with the Prompt Pay Act, it believes it has a viable impossibility defense to the subcontractor's breach of contract claim and should be allowed to retain the funds owed to the subcontractor until that claim is litigated.

But the subcontractor argues that the motion judge got it right when she applied *Tocci* and confined her inquiry to whether the contractor issued timely rejections of the applications.

Amicus briefs submitted by construction industry groups are generally supportive of the subcontractor's position in *Business Interiors*, though they believe the subcontractor has gone a step too far by suggesting that the contractor's affirmative defenses are gone for good.

To the extent those defenses are viable, the contractor can still make them, they say. But by missing its Prompt Pay Act deadlines, the contractor will have to make those arguments in the context of a recoupment action, after paying the money it owes to the subcontractor.

As was evident during oral argument, *Business Interiors* may not be the cleanest vehicle for the SJC to use in making new law regarding the Prompt Payment Act, which was enacted in 2010. The subcontractor argues that the contractor waived its common law affirmative defense of impossibility by not pleading it in its answer to the subcontractor's complaint and citing a contractual provision — rather than impossibility — as its "sole ground" for withholding payment.

The subcontractor also argues that the contractor failed to supply any admissible evidence that the project owner's financial difficulties made it impossible for the general contractor to perform its obligations under the contract, which should lead to a result like the one against the same contractor last fall in the Appeals Court's unpublished decision in Soep Painting Corp. v. Graycor Constr. Co., Inc.

At oral argument, the SJC justices seemed interested in exploring those alleged infirmities. Still, construction industry attorneys tell Lawyers Weekly they hope and expect the SJC will add meaningfully to the scant body of law interpreting the Prompt Pay Act when it issues its decision in *Business Interiors*.

Chance to reinforce 'Tocci'

Andrew R. Dennington of Boston, one of the attorneys for the appellee subcontractor, said his hope for the *Business Interiors* decision is that the SJC will reaffirm *Tocci*'s central holding, which is that the Prompt Pay Act "means what it says and says what it means."

The contractor seems to be arguing that there are some unwritten exceptions to the PPA, Dennington said.

"I'm hopeful that the court will reject that attempt to find unwritten exceptions to the reject-or-pay scheme that's set forth in the statute," he said.

One of the appellant's attorneys, Mark B. Lavoie of Salem, declined to comment.
But Bradley L. Croft of Boston, who represented the appellant in *Tocci*, agreed with Dennington about the decision's implications.

"A party receiving a payment request has a choice to make: communicate the reasons for non-payment to the requesting party or make the payment — it must do one or the other," he said. "To permit that party to fail both to communicate its basis for nonpayment and to make payment vitiates the purpose of the law, even if that party had great reasons for withholding the payment."

If a party could ignore the payment request and then argue its reasons for withholding during litigation, there would be no real consequences for ignoring the statute, Croft added.

Contractors and subcontractors are often left in the dark as to the reasons they are not being paid, which places an enormous financial burden on parties that are often least able to afford it, especially after providing work or materials, Croft noted.

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— Bradley L. Croft, Boston

Joseph A. Barra of Boston, who wrote an amicus brief on behalf of the Associated Subcontractors of Massachusetts, agreed that the right result would be for the SJC to "rubber stamp" the lower court's decision.

Barra's brief distinguishes between the right to withhold payment from a subcontractor, which is waived by failing to comply with the Prompt Pay Act's rejection requirements, and the right to assert more generally any duly preserved contract and common law defenses in subsequent proceedings.

"To the extent the Appellant has any viable contract or common law defenses to payment, such defenses are still available for presentation in a subsequent forum," Barra's brief reads. "However, it must first pay the funds purportedly owed and then seek to disgorge such funds in a succeeding adjudication."

That was the issue that the Construction Industries of Massachusetts and the Utility Contractors Association of New England wanted to highlight for the court, said one of the authors of their brief, Robert T. Ferguson Jr. of Boston.

"What we tried to do with our amicus brief on behalf of CIM and UCANE is caution the court against the situation where one slips past the goalie, so to speak," he said. "There's certain instances in which a payment application or change order request might not be fully and completely acted upon as contemplated by the statute."

Nothing in the statute precludes a contractor from being able to argue its affirmative defenses in a recoupment action, according to Ferguson. To find otherwise might open the door for an "unjustified windfall" for a party spared the implications of an opposing party's otherwise valid defense.

"That probably is not what the statute contemplated," he said.

With its requirement that a rejecting party provide a detailed description of the factual and legal basis of the rejection and certify that it is being made in good faith, the Prompt Pay Act encourages the parties to think carefully about whether there is a basis to reject and to communicate their beliefs to the other side, Dennington said.

As he tried to stress to the SJC justices, the Prompt Pay Act "is not just about prompt payment of invoices, but also prompt resolution of disputes," he said.

Whether "impossibility" can constitute a legal basis for rejection of a periodic payment application under the Prompt Payment Act or constitutes an improper end-run around the prohibition on "pay if paid" clauses in G.L.c. 149, §29E(e), is a novel question in which both sides of the argument have merit, Croft said.

"Unfortunately, where the contractor appears not to have relied on that reason as a basis for its rejection within the time and as required by the statute, it's hard to see how the SJC reaches that underlying question in this case," he said.

Unpaid invoices

Business Interiors involves a dispute between a general contractor and a subcontractor hired to perform carpeting work at a 13-screen theater complex located at the site of the old Boston Garden.

At issue in *Business Interiors* are three payment applications totaling $127,189 that Business Interiors Floor Covering submitted to Graycor Construction Co. between March 20 and Aug. 18, 2020, which remain unpaid.

Because Graycor is one "tier" below the owner of the project, Pacific Theatres Exhibition Corp., it had an extra seven days — 22 instead of 15 — to either approve or reject those applications. Under the Prompt Pay Act, if Graycor did not respond, the application would be "deemed approved."

Though it did not issue a rejection of the applications as prescribed by the statute, Graycor would now like to argue that the reason for its failure either to pay *Business Interiors* or reject the application was the lack of response from Pacific, given that *Business Interiors'* first two requests included payment for work on owner-requested changes.

Under the contract between Graycor and *Business Interiors,* Pacific was required to accept that work before payment could be made, Graycor argues.

But to Superior Court Judge Diane C. Freniere, what Graycor should have done was clear, considering *Tocci.*

"Here, Graycor did not issue rejections of Applications for Payment Nos. 19 and 20 or the Final Application," she wrote in her Feb. 8, 2023, decision. "Consequently, the applications are deemed approved, and Graycor wrongfully withheld payment under the PPA in violation of the Subcontract."

Graycor filed its notice of appeal a month later, and the SJC subsequently transferred the case sua sponte.

Ancillary issues

Beyond the central dispute in *Business Interiors*, there are ancillary issues on which the SJC could issue helpful guidance, attorneys say.

One involves what to make of the fact that the Prompt Pay Act defines the "contracts for construction" to which it applies by referencing the state's lien statute, G.L.c. 254, §2 and §4.

That reference opened the door to Graycor arguing that there is a triable issue of fact as to whether its contract with Business Interiors is, in fact, a "contract for construction," given that Pacific's lease had been terminated by the time Business Interiors filed its suit, rendering its mechanic's lien invalid and it unable to establish another lien on the leasehold interest.

In its brief, *Business Interiors* argues that Graycor did not raise the issue in a timely manner. But even if it engages with the argument on the merits, the SJC should reject it, lest it "create an inviting new loophole for owners to evade the statute" by creating a new limited liability company, leasing the property to that new company, and running construction contractors through that new entity, *Business Interiors* writes in its brief.

"The Legislature did not intend such an absurd result," the brief reads.

In its brief, the Associated Subcontractors of Massachusetts, which authored the Prompt Pay Act, agrees that Graycor's position misinterprets the PPA's reference to the lien law, which it says was "merely intended to provide a short-hand reference to the types of contracts to which the Prompt Pay Act applies."

"It is not, as suggested by the Appellant, a substantive prerequisite to receive the Act's protection," its brief reads.

While Graycor is appealing the substance of Freniere's ruling, it is also objecting to the fact that the judge entered a separate and final judgment, clearing the way for *Business Interiors* to collect what it is due, and the SJC devoted time to the issue at oral argument.

But attorneys do not think that aspect of the decision should be disturbed, either.

"The SJC seemed concerned about the potential impact that a separate and final judgment may have on the rights of the party withholding payment, but that's the precise power imbalance that this law was designed to remedy," Croft said. "The party holding the money is no longer the only party who gets to decide how or when funds flow downstream on a construction project."

Barra agreed that it would be a "Pyrrhic victory" for *Business Interiors* to prevail on its motion for summary judgment but not have separate and final judgment enter.

If the general contractor can just keep the money until all litigation is resolved, "the statute has no meaning," Barra said.