

## Town's Notice of Withholding Triggers Claim Notice Requirement

NELL M. HURLEY

A prudent contractor knows that limitations periods for suit against a non-paying owner can be set forth in several places. New York has a statutory six-year limitation period for breach of contract actions, but shorter limitations periods are common in construction contracts, particularly for public work, whether spelled out directly in the contract or by other laws relating to the public entity. There may also be notice provisions in the contract, or by law, that must be timely fulfilled by the contractor as a condition precedent to commencing a lawsuit. Failure to satisfy a condition precedent can result in dismissal of an otherwise valid contractor claim. Finally, there may be the issue of when the claim "accrues" thereby starting the applicable limitations period or notice provision "clock." Generally, for breach of contract, accrual occurs when the contract is breached. But in one recent case, the confluence of a short (6-month) notice of claim requirement, and a strict (and unexpected) interpretation of the claim's accrual date, meant early and complete dismissal of one contractor's claim.<sup>1</sup>

In that matter, William G. Prophy, LLC ("Prophy") contracted with the Town of Southampton ("Town") in April 2018 for stabilization and restoration construction of a museum. As required,

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## Private PPA Amendment: What Is All The Fuss About?

CAVAN S. BOYLE

Last November, New York's private Prompt Payment Act ("PPA") for commercial construction projects of more than \$150,000 was modified, making changes to General Business Law §§756-a and 756-c.<sup>1</sup> Legislative sponsors sought to rectify the prior law's failure to facilitate timely final payment to contractors or adequately limit retainage, which often subjected contractors (and subcontractors) to long wait-times for payment and caused costly, avoidable disputes.<sup>2</sup> Thus, the new PPA provisions endeavor to reduce retainage and permit final invoicing earlier than previously provided. While industry leaders generally support the amendment, some predict the new law will not achieve the desired results or may create new problems. Others suggest parties can "contract around" the new requirements to avoid the law's intended impact.

### Section 756-c: Retainage Reduced to 5%

The amendment limits retainage for owners (and upstream contractors) to no more than 5% of the contract sum. Prior law authorized parties to agree on a "reasonable amount" of retainage (typically 10%). Subcontract retainage is also capped at 5% but in no case may it exceed that of the prime contract, as it was with the prior law.

Lower retainage is always better for the contractor's cash-flow, though this reduction does not necessarily solve problems that can occur with various scenarios, such as retainage "bifurcation" where owners drop retainage to 0% halfway through the project, arguably preventing primes from withholding any retainage from later performing trades. This one example shows there may be a "learning curve" to these new mandates.

### Section 756-a: Final Invoice Timing

The amendment also adds that "[a] contractor shall be entitled to submit a final invoice for payment in full upon reaching *substantial completion*, as such term is defined in the contract or as it is contemplated by the terms of the contract." Final invoicing was previously permitted "upon the performance of *all the contractor's obligation[s]* under the contract."

In theory, submitting a "final invoice" earlier should get final payment, perhaps even retainage, to the contractor sooner. But will merely invoicing at "substantial completion" achieve this result? Not necessarily.<sup>3</sup>

First, because the statute does not define substantial completion, its occurrence is still determined by the contract, as the term is defined or "contemplated" therein. While some industry standard form contracts do reference a generally understood timing for substantial completion, revised forms and manuscripted documents often have terms defining (i.e. "contemplating") that substantial and final completion can be nearly the same.<sup>4</sup> Confusion and disputes will likely result because the contractual meaning of substantial completion may be unclear, particularly for subcontracts. The new law clearly invites parties to negotiate their own definition.<sup>5</sup>

Second, while the plain text of the amendment to §756-a provides for final invoicing

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at substantial completion, the existing text in §756-c states that retainage shall be released within 30 days of "final approval of the work," possibly leaving open the question of whether an owner must, in fact, remit full payment at substantial completion. After all, under the PPA, payment for final invoicing remains subject to all the usual conditions of any payment application, such as incomplete, defective, or disputed work, failure to pay subs, lack of design professional or other certification, or any other failure to comply with contract provisions. Thus, final invoicing under this section is no guarantee of true final payment, or timing of that payment.<sup>6</sup>

As a result, final invoicing may be insufficient to obtain retainage at substantial completion.<sup>7</sup> The requirement under GBL §756-c that retainage be released by the owner to the contractor within "30 days after final approval of the work" is unchanged. This appears to be the true deadline for final retainage, and it

imposes interest at 1% per month on parties who fail to comply.

Finally, some posit that the PPA amendment only applies where the parties have not otherwise contracted, subject only to certain limited statutory exceptions.<sup>8</sup> Submission of a final invoice and the amount of retainage are not among the exceptions. As such, these new PPA provisions may be superseded by negotiated contract terms, including different retainage amounts and/or payment terms. This interpretation could ultimately be decided by the courts.

For now, conformity with the new law is recommended, with careful contractor (and counsel) review of all contract language (both upstream and down) related to retainage, substantial completion, and conditions for final approval and final payment spelled out clearly. Strive for consistency of these terms across all contracts for the project to avoid confusion or surprises and expect a few bumps in the road. **E&D**

- 1 Certain private residential construction contracts are also impacted by the PPA. While not expressly stated, the monetary threshold is likely the total construction cost for the project, not individual subcontracts.
- 2 The PPA is far from perfect and failed to operate as originally intended.
- 3 Notably, an earlier version of the amendment required the release of retainage upon substantial completion. The final version did not.
- 4 Standard AIA contracts, for example, often treat substantial completion synonymously with beneficial use/occupancy.
- 5 Whether a prime contract's definition of substantial completion governs subcontracts is unclear under this law, thus the statute's language may leave that open to judicial or arbitral interpretation. An explicit negotiated term, however, should control.
- 6 There is not even an explicit requirement for a punchlist to be generated as there is in the public Prompt Payment Law.
- 7 Final invoicing under the new law would typically not include uncompleted/punchlist work, though might permit release of retainage for work completed, subject to final approval provisions.
- 8 GBL §757 mandates certain "Void Provisions" that parties cannot modify by contract.



Michael F. Higgins

## Experienced Attorney Joins Ernstom & Drete

E&D is excited to announce the addition of Michael F. Higgins to our team as an Associate. Mike brings a wide array of legal experience from over a decade of professional practice, most recently as a litigator in a respected mid-size Rochester area firm. He uses that expertise to provide counsel and exceptional advocacy for clients, delivering legal service and advice in all areas of construction and surety claims, and other complex commercial litigation. Mike's practice includes all aspects of claim evaluation, management, and resolution, including ADR, and litigation processes such as pleadings, discovery, motion practice, trial, and appeal. He is a graduate of Brooklyn Law School and University of Rochester.

With over a decade of legal experience, Mike's varied work experience also includes service teaching at two New York law schools, and positions related to civil and disability rights, and first amendment freedoms.

Mike earned his Juris Doctor degree at Brooklyn Law School in 2011, having obtained his Bachelor of Arts in Economics from the University of Rochester in 2008.

### Court Admissions:

- New York
- U.S. District Court, Southern and Western Districts of New York

### Practice Areas:

- Construction Law
- Surety Law
- Commercial Litigation

### Education:

- Brooklyn Law School, J.D. *cum laude* 2011
- University of Rochester, B.A. *magna cum laude* 2008

### Contact:

mhiggins@ed-llp.com  
(585) 473-3100 (Ext. 160)

CONTINUED "TOWN'S NOTICE OF WITHHOLDING TRIGGERS CLAIM NOTICE REQUIREMENT"

Prophy's contract was bonded by its surety. Contract work was performed by Prophy through April 2019, with payments made by the Town. On April 16, 2019, the surety sent a "stop-payment" request to the Town asking that:

"...no further funds be released [on the contract] without the expressed [sic] written consent and direction of [the surety]. We hope this will be a temporary stop notice...[Surety] endeavors only to ensure that project funds are utilized properly...on bonded contracts.<sup>2</sup>

In response to the surety's direction, the Town sent a letter the same day to Prophy advising of a "Notice of Withholding of Contract Payments" ("Notice of Withholding") based upon the surety's letter. It also alleged contract violations but stated "the Town... would be happy to...meet in an attempt to settle a dispute regarding this Notice." There was no stop work order issued or termination of the contract.

Prophy billed for work completed but was not paid. No further work was performed by Prophy, and the balance of the contract work was ultimately finished by someone else. During that time, and for the next year, the parties negotiated, but an agreement on the amount due was not reached. On July 21, 2020, Prophy filed a notice of claim against the Town, and a lawsuit was initiated on October 30, 2020. The Town moved to dismiss, contending that the notice of claim was untimely, and the motion court agreed. Prophy appealed.

The appellate court sided with the Town, relying on Town Law §65(3) which states:

"no action shall be maintained against a town upon or arising out of a contract entered into by the town...unless a written verified claim shall have been filed with the town clerk within six months after the cause of action shall have accrued."<sup>3</sup>

At issue, said the court, was when Prophy should have viewed its claim as

actually or constructively rejected. That date, it determined, was when the April 16, 2019 Notice of Withholding was sent by the Town to Prophy. Thus, the July 21, 2020 notice of claim was untimely, requiring dismissal of Prophy's case.

The court was unconvinced by Prophy's argument that the Notice of Withholding contained no indicia of a permanent withholding of payments and failed to even mention the invoices then or later in dispute, much less reject them. Likewise, the actions and representations by the Town during the year of negotiations did not impact the court's conclusion as to the date Prophy's claim accrued. Prophy should have viewed its claim for payment of the amount due under the contract as constructively rejected by the Notice of Withholding, said the court.

Many lessons can be learned from this case. At the outset, it is important that a contractor knows the limitations period for filing suit related to the contract, preferably at the time the contract is executed. Any contractual limitations periods must be identified and the legal suit

limitation or notice provisions applicable to the owner/public entity determined.<sup>4</sup> If unsure, consult with counsel. Next, be certain to follow all notice provisions to the letter. Never rely on owner negotiations or assurances, mistakenly thinking that the claim will not accrue, or notice provisions be triggered, until the final hard "no" is received from the owner. Finally, be aware that limitations and notice provisions are strictly enforced, and important time-sensitive events are subject to interpretation by the courts.

**E&D**

- 1 *William G. Prophy, LLC v. Town of Southampton*, 219 AD3d 1378 (2d Dept 2023).
- 2 Although not directly addressed in the decision, it appears that the surety "stop-payment" notice was security for losses incurred or expected on Prophy's other bonded projects, not the contract at issue here.
- 3 N.Y. Town Law §65(3) also requires actions against a town to be commenced within eighteen months of accrual.
- 4 As a further example, N.Y. Public Authorities Law contains a shortened limitations period and strict notice provisions applicable to all construction contracts with public authorities.



Brian Streicher attended the 2023 Gilbane Upstate New York Annual Charity Golf Tournament in September, held at Bellevue Country Club in Syracuse. Shown here are Brian (L) and Nick Schuler of Schuler-Haas Electric Corp. E&D was a Hole Sponsor.





925 Clinton Square  
Rochester, New York 14604

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## FIRM NEWS

John Dreste has earned the highest possible Martindale-Hubbell® distinction, AV Preeminent Peer Rating, 2023 Judicial Edition™. The award is based on receiving the maximum rating in both legal ability and ethical standards, reflecting confidential opinions of members of the Bar and Judiciary.

Kevin Peartree authored updates to the ConsensusDocs Handbook for the 2024 Cumulative Supplement, including the addition of Chapter 22, ConsensusDocs 755: Standard Master Subcontract Agreement between Constructor and Subcontractor and ConsensusDocs 756: Standard Work Project Order (pursuant to Master Subcontract Agreement).

Brian Streicher presented on the topic of "Contracts, Cost, and Compliance Buyout" on March 6, 2024 for the Junior Builders Exchange's *JBX Breaking Ground: Perspectives on Project Teamwork* series in Rochester, NY.

Todd Braggins was a panelist at the January, 2024 ABA/TIPS Fidelity & Surety Law Committee Midwinter Conference in New Orleans. He spoke regarding select surety claims handling considerations related to different contract delivery methods. Brian Streicher also attended.

Cavan Boyle was admitted to the New York Bar on November 8, 2023. Cavan is also licensed to practice in Massachusetts and New Hampshire, where he practiced law before joining E&D.

Kevin Peartree recently became Chair of the Board of Trustees for Our Lady of Mercy School for Young Women in Rochester, NY.

Clara Onderdonk participated in the national Association of Legal Administrators Executive Leadership Summit, September 28-30, 2023 in San Diego, CA.