

# CONSTRUCTION AND THE LAW IN TEXAS

## Prompt Pay Act for Public Works

The Texas Prompt Pay act has two forms: the government code contains the prompt pay act that applies to public works and the property code contains a similar act that applies to private projects. Under both, the failure to promptly pay downstream entities on construction projects carries interest obligations and other penalties. Because the vast majority of heavy construction projects are publicly funded and owned, this article only addressed the public prompt pay act.

The prompt pay act for public works applies to any contract for goods or services entered into by the state or local governmental entities as well as any subcontracts or purchased orders under such public contracts. The act applies to all state agencies and local governmental entities. Unlike other statutes governing public construction in Texas, the prompt pay act does not carve out the Texas Department of Transportation from its reach.

One potentially confusing element within the statute is that it defines vendors as a person providing goods or services to the public entity. It further defines subcontractors as a person who contracts with a vendor. The definition of vendor in the statute differs from typical construction industry vernacular in that a vendor under the statute is the prime contractor.

The act applies to all public construction contracts and only has four limited exceptions. Those exceptions are 1) if a bona fide dispute exists between the public owner and the prime or subcontractors about the goods or services that caused the

payment to be late, 2) if a bona fide dispute exists between a subcontractor and its downstream suppliers, 3) if the terms of a federal grant prevent the public owner from making payment timely, or 4) if the invoice requesting payment is not mailed to the proper party in strict accordance with any instructions contained in the contract or purchase order.

Of note, included with the broad application of the law, this statute is one that may not be waived by contract.

Most contractors working on public jobs submit written pay applications for payments owed by a governmental entity. When using pay applications, the payment to the prime contractor becomes overdue on the 31st day after receipt of the invoice. If no written invoice is submitted, payment becomes overdue on the 31st day after the delivery of any goods or the performance of services is completed. One caveat is that the payment period is extended to the 46th day after payment becomes due for any governmental entity whose governing body meets only once per month or less frequently.

For prime contractors making payments to their subcontractors and suppliers, the payment of the portion of the funds received from the public owner must be made within 10 days of receipt. That portion due to any subcontractor or supplier is overdue following the 11th from receipt. This same 10-day period transfers downstream for any subcontractors paying sub-subcontractors or suppliers.

Under the prompt pay act, all overdue payments begin to accrue interest on the

date the payment becomes overdue. The applicable interest rate is determined by the prime rate of interest in effect for the fiscal year in which the payment becomes overdue, plus one-percent of additional interest. The act looks to the prime rate of interest as published by the Wall Street Journal on the first business day of July from the year preceding the start of the then applicable fiscal year.

To translate this relatively confusing legislative mandate into practical terms, one can search the web for “WSJ prime rate July 1” and a number of websites will be provided with a history of the prime rate of interest. For July 2016, the prime rate was 3.5 percent. Therefore, under the act and for the current fiscal year, the interest rate on overdue payments for public works is 4.5 percent. The interest that begins to accrue the day the payment becomes overdue will cease to accrue, under the act, on the day the payment is mailed or electronically transmitted to the payee.

For payments that are disputed, the governmental entity is required to notify its prime contractor of any error in an invoice not later than 21 days after receipt. If the dispute is resolved in favor of the contractor, then interest is due as calculated from the 31st day. If the dispute is resolved in favor of the public owner, then the contractor is required to resubmit the invoice and the time would begin to run as of the resubmittal. The section in the act addressing disputed payments and incorrect invoices may be viewed as separate from the exemptions addressed in the beginning of this article.

Where an invoice contains mistakes, the disputed payment provision controls. However, where there is a bona fide dispute as to whether payment is due, then the exemption controls. If an administrative hearing or litigation is required to resolve either a disputed payment or bona fide dispute, the act provides that the prevailing party, whether it be the public owner or the contractor, is entitled to recover its reasonable attorney’s fees for the other party.

A contractor who is not being paid by the public owner may suspend its performance due to the nonpayment. The act provides that a contractor, upon written notice to the governmental entity that payment has not been received and warning of a suspension, may suspend performance after 10 days from the notice. These same rights extend to downstream subcontractors and suppliers.

On state highway contracts, the act does



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provide that a contractor or subcontractor may not suspend performance before the 20th day after giving notice of nonpayment. That notice must be sent to the executive director, the director of construction, and the person designated in the contract as the recipient of notice for the Texas Department of Transportation.

Finally, the act concludes with a section providing that the rights and remedies available to contractors and downstream subcontractors and suppliers is not exclusive and that the interest penalties and attorney’s fees available under the act are in addition to any other rights available to claimants under the law.

