

Owner Required to Arbitrate Under New York's Prompt Payment Act

By: Michael J. Rosenthal, Esq.

The New York Prompt Payment Act, which applies to private construction projects, remains an under-utilized tool to be used by unpaid contractors.

Among other things, the Prompt Payment Act mandates the procedure for the submission and payment of contractor invoices. Specifically, upon receiving an invoice, the owner must timely "approve or disapprove" the invoice. Grounds for disapproval include "[u]nsatisfactory or disputed job progress" and "[f]ailure to comply with other material provisions of the construction contract." An owner must not, however, "unreasonably withhold approval or "in bad faith disapprove all or a portion of an invoice," and must "prepare and issue a written statement" justifying any refusal.

The Prompt Payment Act provides several remedies for an owner's noncompliance. First, if the owner fails to pay within the mandated time period, interest begins to accrue. Second, if the owner fails to approve or disapprove an invoice on time, or fails to pay "the undisputed invoice amount" on time, the contractor may suspend performance. Finally, "[u]pon receipt of a written complaint ... that an owner has violated the provisions of this article ... the parties shall attempt to resolve the matter giving rise to such complaint." If they cannot agree on a resolution, "the aggrieved party may refer the matter ... to the American Arbitration Association for an expedited arbitration."

In a recent case, a general contractor submitted an interim invoice to the owner and four days later the owner stated that it would not pay the invoice because the amount owed was less than the amount of a lien that the general contractor asserted against the property. The general contractor then issued a notice of complaint alleging the owner was withholding payment unreasonably and in bad faith in violation of the Prompt Payment Act.

After the parties failed to resolve the dispute, the general contractor served a demand for expedited arbitration. The owner then started an action in court seeking an emergency order staying the arbitration. The question the court was ultimately required to determine was whether the parties' dispute was subject to mandatory arbitration under the Prompt Payment Act.

It was undisputed that the parties' contract did not provide a basis for compelled arbitration; rather, it permitted arbitration only "[u]pon mutual agreement of the parties."

The Prompt Payment Act declares that any contractual provision "stating that expedited arbitration as expressly provided for and in the manner established by [the statute] is unavailable to one or both parties" is "void and unenforceable."

The general contractor argued that the Prompt Payment Act's arbitration provision applies. The owner disagreed, arguing that the Prompt Payment Act's arbitration provision applies only as to undisputed invoices.

Analyzing the cases interpreting the Prompt Payment Act, the court held that the statute's arbitration provision does not, by its terms, limit the availability of arbitration to statutory violations related to undisputed invoices. Rather, it applies broadly to any "violat[ion]" of "the provisions of this article." The court further held that an owner could violate the Prompt Payment Act regarding a disputed invoice by, for example, disapproving the invoice in bad faith or simply by refusing to approve it for a reason that is not sanctioned by the statute. Indeed, the general contractor's allegation in this case is that the owner withheld payment in bad faith.

The predicate for arbitration is a "complaint," which in legal terminology refers to an allegation. The court held that it is not necessary for the general contractor to prove, in the early stage of the dispute, that the owner is actually in violation of the statute, only to claim as much. The court reasoned that it is unthinkable that the New York Legislature intended to subject every demand for arbitration under the Prompt Payment Act to gatekeeping merits litigation in court before any arbitration could proceed.

The court ultimately denied the owner's request to stay the arbitration and held that the dispute is subject to the Prompt Payment Act's arbitration provision. Moreover, any further disputes, including whether the owner in fact violated the Prompt Payment Act, are questions reserved for the arbitrator.

Commentary

The Court in this recent case did a thorough job reviewing the Prompt Payment Act and the cases interpreting the statute to find that the parties' dispute of the unpaid invoice could be submitted to expedited arbitration. Indeed, the court noted that only a handful of cases have addressed the arbitration provision of the Prompt Payment Act.

Ultimately, the court reasoned that the Legislature's decision to limit one remedy to undisputed invoices strongly suggests that other remedies, which contain no such limitation, are available regardless of whether the invoice is disputed.

The Prompt Payment Act's expedited arbitration provision to resolve payment issues is a lower cost and quicker alternative to litigation in court. A contractor, however, must properly comply with the statute in order to properly invoke arbitration.

Feel free to call me to discuss New York's Private Prompt Payment Act.