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Putting the short into short sales

Philip J. Vacco

In response to pressure to simplify the short sale and deed-in-lieu of foreclosure processes, in August of this year the Federal Housing Finance Authority [FHFA] announced a new set of short sale guidelines[1] that will be standardized across both the Fannie Mae (FNMA.OB) and Freddie Mac (FMCC.OB) platforms designed to assist struggling homeowners.[2] Effective November 1, 2012, Fannie Mae's and Freddie Mac's new and improved preforeclosure sales program will officially be known as "Standard Short Sale/HAFA II." It is hoped that this amended short sale program, which will consolidate the existing short sale programs into a single uniform program, will provide servicers with more clear and consistent guidelines with the goal of making it easier to process and execute short sales and provide a much needed alternative to borrowers facing foreclosure.

Under the prior guidelines, Fannie Mae and Freddie Mac did not allow a borrower facing imminent default of their mortgage obligation to qualify for preforeclosure relief.[3] In fact, to qualify for assistance a borrower had to be seriously delinquent; this meant that the borrower had to have at least two payments that were 31 days or more in arrears. Unfortunately this rule resulted in some homeowners, who were meeting their

Continued on page 2

The leaky "pay-if-paid" clause: A fluid story of the "if's" and "when's" of contingent payments

By Nicholas J. Johnson

Ideally, payments in a construction project are intended to resemble the flow of a diverging river. Payments are designed to originate from the owner, and then flow through the general contractor to the various subcontractors, and ultimately trickle down to the various suppliers and laborers. In reality, however, the process is rife with opportunities for the payment stream to become disrupted, slowed, or simply run dry.

In an effort to lessen the impact of any such disruptions, it is common practice in the construction industry for contractors to include conditions in their contracts that will protect them from having to pay third parties until they themselves have been paid. These provisions are commonly referred to as "pay-if-paid" clauses. If implemented throughout the length of the payment stream, such provisions constitute an effective risk management tool that distributes any potential loss associated with non-payment amongst numerous parties. In practice, however, the application of "pay-if-paid" clauses can be devastating to down-stream parties.

In most projects, a subcontractor has no choice but to agree to a contractor's contingent payment provision, but due to lack of negotiating leverage, the subcontractor is frequently incapable of securing similar protection from its suppliers. Thus, if any upstream party on the project becomes insolvent, this partial imple-

Continued on page 5

INSIDE

Putting the short into short sales

Continued from page 1

mortgage obligations even though they were upside down and in financial distress, making ill-advised decisions to voluntarily default on their payments in a desperate attempt to qualify for relief. Regrettably, such actions typically only exasperated the borrower's financial distress buy forcing them to incur additional late fees and penalties, damaging their credit, and adding the additional stress and uncertainty associated with a foreclosure action; all without any certainty that a short sale would be approved by their servicer.

In addition, every borrower was required to submit a completed Borrower Response Package in which the borrower provided a thorough and detailed financial disclosure of all of the borrower's assets, complete a Hardship Affidavit,[4] and supply an array of documents supporting the borrower's claims.[5] The gathering and reviewing of these documents took time which resulted in typical delays of several months before the servicer would be in a position to approve of the sale.

Further adding to the uncertainty of completing a short sale were the additional road blocks created by second lien holders who refused to release their lien claim unless they received amounts that were much higher than what the servicer would approve. And when junior lien holders held out for more money, the short sale was often jeopardized.

Under the new guidelines the Federal Housing Financing Agency attempts to address many of these shortcomings by consolidated existing short sales programs into one streamlined standard short sale program intended to enable lenders and servicers to quickly and easily qualify eligible borrowers for a short sale.[6]

Perhaps the two most significant changes contained in the new guidelines are that they now permit servicers of Fannie Mae or Freddie Mac loans to allow homeowners who are current on their mortgage obligation, but deemed to be in a position where default is imminent, to sell their home in a short sale before they become delinquent; as long as they have an eligible hardship.[7] And the adoption of a streamlined short sale process for borrowers deemed most in need, which permits servicers to approve of a short sale without obtaining any additional approval from Fannie Mae or Freddie Mac.[8] A principal component of the streamline process is that it abolishes the need for a qualifying borrower to make a financial contribution to the short sale. This in turn eliminates the obligation for the borrower to provide a Borrower Response Package; reducing the time necessary to approve a short sale by eliminating the time expended on gathering, submitting, reviewing and ultimately qualifying the borrower.

Qualifying borrowers who are current on their mortgage obligations

As of November 1, 2012 there will now be a mechanism in place for Fannie Mae and Freddie Mac servicers to offer relief to mortgagors who are current on their payments but are otherwise facing financial hardships. Under the new guidelines as long as the homeowner can demonstrate that they are suffering a recognized "hardship,"[9] servicers can expedite the short sale process without any additional approval from Fannie Mae or Freddie Mac. The hardships enumerated by FHFA are as follows:

- Death of a borrower or death of the primary or secondary wage earner in the household.
- Unemployment.
- Increased housing expenses (i.e. ARM loan rate adjustment).
- Disaster (natural or man-made).
- Business failure.
- Long-term or permanent illness or disability of borrower, co-borrower or dependent family member.
- Divorce or legal separation of a borrower or co-borrower.
- Employment transfer / relocation (including Permanent Change of Station order for military personnel) greater than 50 miles from current primary residence.
- NOTE: If a borrower faces a hardship not listed above and provides relevant documentation to the servicer, the servicer must review the Borrower Response Package and make a determination if the short sale request is legitimate. It must then submit that recommendation to Fannie Mae / Freddie Mac for approval.[10]

Streamlined short sale approach for borrowers most in need

For borrowers that are 90 days or more delinquent in their mortgage payments, have credit scores of less than 620, and have serious financial hardships, the documentation previously required to demonstrate need; that is, the Borrower's Response Package, has been all but eliminated. These borrowers are deemed to have qualified for a short sale and are exempt from the requirements to make any cash contribution or sign a promissory note as part of the short sale process. For borrowers that qualify these changes should significantly cut the delays associated with getting a short sale approved. In addition these borrowers will qualify for a "relocation" incentive of up to $3,000 from Fannie Mae to be paid following the successful completion of a short sale.[11]

Military personnel with Permanent Change of Station (PCS) orders

The new guidelines provide special treatment for service members who are being relocated. Now military personnel with PCS orders are automatically eligible for short sales, even if they are current on their existing mortgage obligations. In addition, these personnel will be under "no obligation to contribute funds to cover the shortfall between the outstanding loan balance and the sales price on their homes."[12] Likewise, non-military borrowers who need to relocate more than 50 miles from their current home for a job transfer or new employment opportunity, qualify for a short sale even if the borrower is current on their mortgage payments.[13]

Dealing with second mortgages

In addressing the log jam that has been created by junior lien holders refusing to release their lien claims in deals that have otherwise been approved for a short sale by the servicer, Fannie Mae and Freddie Mac are now requiring subordinate lienholders to accept from the proceeds of the short sale the sum of $6,000 in exchange for a release of their lien claims and a full release of liability for the borrower.[14] (Note: it doesn't matter how many subordinate lien holders there are, the $6,000 amount is an aggregate amount).

Waiving the right to pursue deficiencies

Unless the borrower qualifies for the streamlined documentation short sale process, is active military personnel with PCS orders, or the collection of a deficiency is otherwise exempt by applicable law, the guidelines require the borrower to be evaluated to determine if they will be required to make what FHFA refers to as a "reasonable contribution"[15] or be asked to execute a promissory note as a condition of approving the short sale.

When determining whether or not a borrower who is delinquent on their mortgage payments or in imminent default will have to make a cash contribution, the servicer is required to examine the borrower's financial health; and they do so by examining the disclosures the Borrower made on the Uniform Borrower Assistance Form.[16]

> [I]f the borrower has cash reserves, including assets such as cash, savings, money market funds, marketable stocks or bonds (excluding retirement accounts), . . . are:
>
> - in excess of the greater of $10,000; or
> - six times the contractual monthly mortgage loan payment including principal, interest, and tax and insurance escrows (PITI). (If the servicer does not escrow for taxes and insurance, it must estimate the borrower's monthly tax and insurance premium amounts).
>
> If a borrower has cash reserves of more than $50,000, the servicer must request written approval from Fannie Mae for the contribution amount.
>
> If the servicer determines that the borrower has the capacity to make a cash contribution, the servicer must initially request a contribution of 20% of the borrower's cash reserves, not to exceed the deficiency.[17]

It is of interest to note that the contemplated 20% contribution to the shortage is not written in stone and if a borrower who is more than 30 days delinquent on their payment is either unwilling or unable to pay 20% of their cash reserves, the servicer is given the ability to negotiate a lower cash contribution, "but must provide an explanation in the mortgage loan servicing file of the specific circumstances that limited the borrower's ability to make a full contribution."[18] Likewise, where the borrower

> is offered a short sale under the 'imminent default' standard and is either unwilling or unable to contribute 20% of their cash reserves, the servicer must request approval from Fannie Mae to accept less than the 20% contribution. However, if the borrower's hardship is death of the primary wage earner, the servicer may negotiate a borrower's cash contribution for less than 20% of the cash reserve, but must provide an explanation in the mortgage loan servicing file of the specific circumstances that limited the borrower's ability to make a contribution.[19]

In situations where cash reserves are unavailable the servicer must then evaluate the borrower to see if a contribution can be secured through the use of a promissory note.[20] To determine whether or not a borrower is an appropriate candidate for a promissory note the servicer is required to examine the borrower's future debt-to-income ratio of the borrower (i.e. "back-end-ratio"). If the borrower's total monthly debt is less than 55% then there is an initial determination that the borrower has the capacity to make a promissory note contribution. The borrower's total monthly debt is to include the borrower's future housing expenses,[21] monthly payments on all installment debts with more than 10 months remaining, credit card payments, alimony, child support, separate maintenance payments if more than 10 months remaining, car lease payments, as well as any negative rental income from other investment properties owned.[22]

Once this determination is made, the servicer as part of the short sale package must initially request the borrower to execute a five- to 10-year promissory note, at zero interest, with a monthly payment that does not exceed one-half of the difference between the borrower's future monthly housing expenses and 55%. The actual promissory note balance is the final monthly amount negotiated between the borrower and the servicer multiplied by the negotiated term (60 or 120 months) not to exceed the deficiency amount. (NOTE: promissory notes are NOT required if the note balance is less than

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$5,000).

So if we were to assume that a borrower had a future total monthly debt ratio of 49% with a Gross Monthly Income of $4,000 his initial monthly payments under the formula would be $120.[23] Assuming a five year payback, the total amount contributed by the borrower would be $7,200. Again, as we saw with borrowers making cash contributions, if the borrower is unwilling or unable to agree to a monthly promissory note payment based on the prescribed calculation, the servicer is given the authority to negotiate a lower payment, but must provide an explanation in the mortgage loan servicing file of the specific circumstances that limited the borrower's ability to make the payment.

Upon the completion of the short sale, the borrower will be released from any liability for deficiency and will be in a position to qualify for another Fannie Mae / Freddie Mac guaranteed mortgage within two years.

Conclusion

With 4.63 million loans in Fannie's and Freddie's combined portfolios underwater and approximately four out of five of those loans being current,[24] FHFA needed to modify their policies to address the situation faced by homeowners who are upside down on their property and in imminent danger of defaulting on their mortgage obligations. By streamlining the short sale approval process and providing servicers with the ability to make decision without going back to Fannie Mae or Freddie Mac for final approval, FHFA has taken major strides toward providing borrowers with new options for avoiding foreclosure.[25]

Combining these changes with the FHFA announced guidelines earlier in June of this year "that established strict timelines for servicers considering short sales[.]",[26] it appears that the lengthy delays now associated with short sales may actually become a thing of the past.

For transactional attorneys handling short sales these changes should assist in lessening the amount of time we will have to commit to gathering and transmitting financial information to the servicer, especially for delinquent borrowers and military personnel who qualify for the streamlined procedure; but more importantly, they provide us with an additional remedy that we can now offer our ailing clients who are struggling to keep their mortgage current payments. ■

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1. FHFA News Release, August 21, 2012.

2. To determine if you are dealing with a Fannie Mae or Freddie Mac loan you can access the following Web sites: <http://loanlookup.fanniemae.com/loanlookup> and <https://www.FreddieMac.com/corprate>.

3. Fannie Mae Servicing Guide Announcement SVC-2012-19, *Standard Short Sale/HAFA II and Deed-in-Lieu of Foreclosure Requirements,* (page 3) August 22, 2012.

4. Fannie Mae Hardship Affidavit Form 194. Purpose of the Hardship Affidavit was to establish that the borrower was unable to maintain his / her payments; typically due to a reduction in income, or increased monthly obligations caused by the loan resetting (ARMs), the additional of medical expenses, consumer debt, or increased utilities or property taxes.

5. Copies of the Borrower's tax returns, bank statements, W-2's and check stubs are often required by the servicer.

6. FHFA News Release, August 21, 2012. "These new guidelines demonstrate FHFA's and Fannie Mae's and Freddie Mac's commitment to enhancing and streamlining processes to avoid foreclosure and stabilize communities," said FHFA Acting Director Edward J. DeMarco.

7. FHFA News Release, August 21, 2012.

8. Id.

9. Id.

10. Fannie Mae Servicing Guide Announcement SVC-2012-19, *Standard Short Sale/HAFA II and Deed-in-Lieu of Foreclosure Requirements,* (page 4) August 22, 2012.

11. There are exceptions to this policy. Borrowers required to contribute funds or execute a promissory note; a military borrower who receives a Dislocation Allowance (DLA) or other governmental relocation assistance, or a borrower receiving relocation assistance from any other source is prohibited from receiving the $3,000 incentive. Fannie Mae Servicing Guide Announcement SVC-2012-19, *Standard Short Sale/HAFA II and Deed-in-Lieu of Foreclosure Requirements,* (page 14) August 22, 2012.

12. FHFA News Release, August 21, 2012.

13. Id.

14. Fannie Mae Servicing Guide Announcement SVC-2012-19, *Standard Short Sale/HAFA II and Deed-in-Lieu of Foreclosure Requirements,* (page 11) August 22, 2012.

15. FHFA News Release, (attached fact sheet). August 21, 2012.

16. Fannie Mae/Freddie Mac Form 710.

17. Fannie Mae Servicing Guide Announcement SVC-2012-19, *Standard Short Sale/HAFA II and Deed-in-Lieu of Foreclosure Requirements,* (page 6) August 22, 2012.

18. Id.

19. Id.

20. Fannie Mae provides a Promissory Note template (Form 190) at eFannieMae.com. Use of this note is not mandatory.

21. If the actual future housing expenses of the borrower is not known, the servicer is to use 75% of the borrowers current monthly mortgage payment (PITI, including sums for assessment fees) to determine eligibility.

22. Fannie Mae Servicing Guide Announcement SVC-2012-19, *Standard Short Sale/HAFA II and Deed-in-Lieu of Foreclosure Requirements,* (page 8) August 22, 2012.

23. Initial Monthly Promissor Note Payment = (55% - future total monthly debt ratio) ÷ 2 x Gross Monthly Income.

24. Statement made by acting FHFA director, Edward J. DeMarco.

25. Fannie and Freddie Short Sale Guidelines – Positive for Housing, Michael Terry, Rubicon Associates, LLC, August 27th, 2012: "One of the potential outcomes of this program is pulling forward what would be distressed sales at short sale prices. While some owners continue to make payments even though they are upside down and in distress, these borrowers will now be able to engage in a short sale instead of adding to the REO inventory and at typically higher realized prices." <http://seekingalpha.com/article/829021-fannie-and-freddie-short-sale-guidelines-positive-for-housing>.

26. FHFA News Release, August 21, 2012. Servicers are required to review and respond to short sales within 30 days of receipt of a short sale offer; they must provide weekly status updates to the borrower if the offer is still under review after 30 days, and they must make and communicate final decisions to the borrower within 60 days of receipt of the offer and complete borrower response package.

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The leaky "pay-if-paid" clause: A fluid story of the "if's" and "when's" of contingent payments

Continued from page 1

mentation of "pay-if-paid" clauses results in a subcontractor being squeezed from both sides, with no recourse against the upstream contractor, and no defense to its downstream suppliers' demand for payment.

In such instances, subcontractors are left scrambling to find any means of securing payment in an effort to satisfy their own creditors. Fortunately for subcontractors, and to the chagrin of contractors, the seemingly impenetrable protection afforded by a "pay-if-paid" clause is not always so resolute. Accordingly, subcontractors and contractors would both be well served in making themselves aware of the proper means of creating a "pay-if-paid" clause, and the various ways it might be circumvented.

I. Condition Precedent ("Pay-if-Paid") or Payment Schedule ("Pay-when-Paid")

In Illinois, as in most states, conditions precedent that result in a forfeiture of payment are disfavored.[1] Accordingly, while a provision that makes payment by a general contractor contingent upon its receipt of funds from the owner is valid and enforceable,[2] the intent to create such a condition precedent must be established through clear, unambiguous language, otherwise it will not be enforced.[3] Based on this standard, courts throughout the country have interpreted provisions expressing a clear, unambiguous intent to create a contingent payment, and those that lack such a clear expression, as creating two distinct types of protection.[4] These two distinct provisions are commonly referred to as "pay-if-paid" and "pay-when-paid" clauses, respectively.[5]

a. Payment Schedule ("Pay-When-Paid")

A "pay-when-paid" clause establishes that a contractor will make payment to its subcontractors after funds are received from the owner. A typical example of such a provision is set forth as forth in 7th Circuit's decision BMD Contractors, as follows: "'Contractor shall pay subcontractor within seven days of contractor's receipt of payment from the owner.'"[6]

Because these provisions do not include language conveying an express and unambiguous intent to create a condition precedent, courts interpret such clauses as creating merely a timing mechanism aimed at protecting against minor delays in payment.[7] Such a provision provides a contractor with a "reasonable" amount of time to collect payment, but it does not allow the contractor to avoid its payment obligations to subcontractors in the event it fails to collect payment for itself. If a general contractor fails to make payment to its subcontractors within a "reasonable" time, regardless of whether funds are ever received from the owner, the subcontractor can freely pursue a breach of contract claim against the general contractor.

The frequently cited rationale behind such rulings is the universal disfavor of conditions precedent that result in the forfeiture of payment. Hence, a "pay-when-paid" provision only offers protection against minor delays in payment, but it will not protect a contractor against an upstream party's insolvency or failure to pay.[8]

b. Condition Precedent ("Pay-if-Paid")

In stark contrast, a "pay-if-paid" clause reflects a clear and unambiguous intent to create a condition precedent, whereby a contractor's obligation to pay its subcontractors will not arise unless and until it receives payment itself. There are two frequently cited cases in Illinois that discuss what language is sufficient to create a condition precedent. The first case is a First District decision in *A.A. Conte*, which holds that the following language is sufficient to create a condition precedent:

> ...invoices submitted before the 25th of the current month will be paid by the 28th of the following month, provided the material so delivered is acceptable, and if payment for invoiced materials has been received by [the general contractor] under its general contract. [Emphasis added by Court].[9]

In its decision, the Court in *A.A. Conte* reiterated that conditions precedent are disfavored, and that they will not be construed as allowing a contractor to avoid its payment obligations unless such intent is supported by clear and unambiguous language. In a majority opinion, the Court in *A.A. Conte* went on to rule that the language in the above quoted provision clearly established that payment to the subcontractors was contingent upon the general contractor first being paid. The Court provides little analysis or insight into its finding, but based upon the emphasis that it placed on the phrase starting with the term "if", it can only be presumed that the word "if" was essential to the Court's decision that the language was clear and unambiguous.[10]

In addition to a lack of a detailed analysis, the decision in *A.A. Conte* also failed to address, or even acknowledge, the apparent conflict between its ruling and the current rule in the vast majority of jurisdictions as well as the guidance of the Restatement (Second) of Contracts.[11] The failure of the majority's opinion to offer an in-depth analysis or address the apparent conflict with other jurisdictions was identified in the dissenting response, which made a point to cite a series of jurisdictions and various other authority, all of which held that language similar to that at issue was insufficient to create a condition precedent.[12] The rationale of the dissenting opinion in *A.A. Conte* was subsequently adopted by the Northern District of Illinois in its decision of *Brown & Kerr, Inc. v. St. Paul Fire and Marine Insurance Co*.

In *Brown & Kerr*, the Court found the following language failed to create a condition precedent:

> . . . the entire unpaid balance of the Subcontract Sum, shall be made by the Contractor to the Subcontractor when . . . the Contractor has received final payment from the [owner]. . . [Emphasis added].[13]

In support of its decision, the Court cited to the dissent's analysis in *A.A. Conte*, and further acknowledged that since the ruling in *A.A. Conte*, the Illinois Legislature had codified the universal dislike of such conditions precedent by making such clauses unenforceable with respect to relief sought under the Illinois Mechanics Lien Act.[14] While the Court acknowledged that the statutory prohibition against "pay-if-paid" clauses did not apply to contract claims, it construed the Legislature's enactment of this prohibition as additional support for the strict interpretation promoted by the dissent in *A.A. Conte* and adopted by a majority of other jurisdictions.

Absent the Northern District's apparent inclination to follow the more strict approach followed by other jurisdictions, the only difference between the clauses in *Brown & Kerr* and *A.A. Conte* is the use of the term "when" instead of "if". Because the First District's decision in *A.A. Conte* remains uncontroverted in Illinois State Court, it would appear that beyond the venue of the case, the difference between whether a clause will be construed as either a "pay-when-paid" or "pay-if-paid" provision may turn on as little as the words if or when.

The astute practitioner, however, will be justified in treating any payment clause that relies solely on the term "if" as suspect. The lack of analysis contained in the court's decision in *A.A. Conte*, the Illinois Legislature's subsequent codification of the policy disfavoring conditions precedent, the First District's subsequent reaffirmation of the universal dislike for conditions precedent,[15] and the recent 7th Circuit decision adopting the majority view,[16] all suggest that simply including the term "if" may no longer be enough. Accordingly, any attempt to create a "pay-if-paid" clause should include one or more of the following phrases: "condition," "unless and until," "if and only if," or other similar language.[17]

II. Prevention Doctrine

The mere existence of a "pay-if-paid" clause does not protect a contractor from all instances of non-payment. As with all conditions precedent, a Court will construe the condition as being satisfied or waived if the party to whose benefit the condition runs contributes to its non-occurrence.[18] Stated more plainly, if the contractor was a contributing cause to the owner's non-payment, the "pay-if-paid" clause will not be enforced to protect the contractor from his own wrong.

This doctrine is commonly referred to as the "prevention doctrine" or "wrongful prevention doctrine."[19] As applied in Illinois, it has been used to prevent contractors from relying on a "pay-if-paid" clause in instances in which the contractor failed to properly submit payment applications,[20] or when the contractor improperly agreed to accept a lesser amount from the owner without the subcontractors' authority.[21] Other jurisdictions have applied the doctrine to instances in which a contractor convinced the owner not to pay a subcontractor,[22] when a contractor contributed to the owner's decision not to secure additional financing to pay subcontractors,[23] or when a contractor failed to timely submit change order requests.[24] A more common application of the "prevention doctrine" is likely to occur when the owner withholds payment due to deficiencies in the contractor's work, or because of deficiencies in the work of the contractor's other subcontractors.[25]

Importantly, it is not necessary that a subcontractor demonstrate that the upstream contractor acted willfully or intentionally in causing the condition precedent not to occur.[26] Rather, the subcontractor need only show that the contractor acted unreasonably or unjustly.[27] Based upon the view of jurisdictions with more extensive case law on the topic, a "pay-if-paid" clause might be waived even though the contractor was not the sole cause of the non-payment. Rather, it may be enough to avoid a "pay-if-paid" clause if the contractor "materially contributed or hindered" the owner's ability or decision to pay.[28]

III. Mechanics Lien and Bond Claims

Lastly, if a conditional payment clause is found to create an enforceable condition precedent, and the condition was not rendered unenforceable by the conduct of the contractor, the subcontractor still has recourse under the Illinois Mechanics Lien Act, and may also have a claim against any applicable payment bond.

The Mechanics Lien Act expressly states that liability under the act cannot be avoided by a contractual clause that conditions payment on the receipt of funds from a third party.[29] Thus, the importance of properly protecting and securing a subcontractor's mechanics lien claim cannot be overstated.

In addition, the judiciary has ruled that a surety on a payment bond cannot rely upon a "pay-if-paid" clause in the construction contract as a defense to a bond claim.[30] This is an exception to the common law rule that a surety is entitled to assert any defense that its principal would be able to claim, but the exception may not apply if the bond itself expressly incorporates the "pay-if-paid" clause.[31]

The application of "pay-if-paid" versus a "pay-when-paid" clause can have drastic and far reaching implications. It is thus essential that these disparate clauses are fully understood, because the impact of such clauses might be the difference between a contractor floating to safety or drowning in debt. ■

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1. *A.A. Conte, Inc. v. Campbell-Lowrie-Lautermilch Corp.,* 132 Ill.App.3d 325 (1st Dist. 1985).
2. *Standard Asbestos Mfg. Co. v. Kaiser, et al,* (abstract) 316 Ill.App. 441 (1st Dist. 1942).
3. *Brown & Kerr Incorporated v. St. Paul Fire and Marine Insurance Co.,* 940 F.Supp. 1245, 1250 (N.D.Ill. 1996).
4. *BMD Contractors, Inc. v. Fidelity and Deposit Company of Maryland,* 679 F.3d 643 (7th Cir. 2012) (citing numerous other jurisdictions and authority in establishing the difference between "pay-if-paid" and "paid-when-paid" provisions).
5. While the distinction amongst these two distinct provisions has been acknowledged for several decades, it is only recently that Courts have made a clear attempt to distinguish the provisions by labeling them "pay-if-paid" and "pay-when-paid". To avoid potential confusion, be aware that earlier federal decisions, and all Illinois State Court decisions, fail to differentiate between the two distinct clauses by title, and will refer to both types of provisions interchangeably by the names "pay-if-paid" or "pay-when-paid".
6. *Id.* at 648.
7. *Brown & Kerr, supra.*
8. *Id.* at 648-49.
9. *A.A. Conte, supra* at 327-28.
10. *Id.*
11. *Id.* at 331 (dissenting opinion) (citations omitted).
12. *Id.*
13. *Brown & Kerr, supra* at 1249.
14. 770 ILCS 60/21
15. *Premier Electrical Construction Co. v. American National Bank of Chicago,* 276 Ill.App.3d 816, 824 (1st Dist. 1995) (found "pay-if-paid" clauses containing language clearly establishing a condition precedent as being preempted by other language in the contract).
16. *See, BMD Contractors, supra.*
17. *Evans, Mechwart, Hambleton & Tilton, Inc. v. Triad Architects, Ltd.,* 196 Ohio App.3d 784, 791-92 (10th Dist. 2011) (citing a series of cases from various jurisdictions, articles, books and journals. Citations omitted).
18. *See, Standard Asbestos, supra, See also, Preload, Inc. v. Marino Construction Co., Inc.,* 1991 WL 202651 (N.D.Ill 1991), *citing Standard Asbestos.*
19. *See, Cummings v. Beaton & Associates, Inc.,* 249 Ill.App.3d 287 (1st Dist. 1992), *See also, Moore Brothers Co. v. Brown & Root, Inc.* 207 F.2d 717 (4th Cir. 2000).
20. *Preload, supra* at 4 (holding that motion to dismiss filed by general contractor on "pay-if-paid" clause was properly denied where general contractor may have contributed to non-payment through its failure to timely and properly submit payment applications).
21. *Standard Asbestos, supra.*
22. *Jay-Ton Construction Co., Inc. v. Bowen Construction Services, Inc.,* 2003 WL 22656912, at 14-15 (Va.Cir.Ct. 2003).

23. *Moore Brothers, supra* at 725.

24. *Northeast Drilling, Inc. v. Inner Space Services, Inc.,* 243 F.3d 25, 40-41 (1st Cir. 2001).

25. While such an application of the "prevention doctrine" is consistent with the reasoning in the cited case, no case law has been found where the doctrine was applied to prevent a contractor from asserting a "pay-if-paid" clause based upon deficiencies in its work.

26. *Preload, supra* at 2-4 (denying motion to dismiss based on "pay-if-paid" clause pursuant to prevention doctrine, holding that complaint sufficiently pled general contractor failed to "use reasonable efforts" to have condition occur, and pleading of malicious, willful, or bad faith conduct was not necessary).

27. *Id., See also, Capuano v. Consolidated Graphics, Inc.,* 2007 WL 2688421 (N.D.Ill. 2007) (holding plaintiff was not required to prove that failure of condition precedent by defendant was intentional, especially when condition precedent was outside of plaintiff's control and within defendant's), *citing. Barrows v. Marco,* 94 Ill.App.3d 959 (1st Dist. 1981).

28. *Moore Brothers, supra.*

29. 770 ILCS 60/21.

30. *Brown & Kerr, supra* at 1249 (holding that surety could not rely on "pay-when-paid" clause in contract because it was against the very purpose of securing a payment bond, the provision was not expressly incorporated into the bond, and the provision itself was insufficient to even create a condition precedent).

31. *Id.*

Upcoming CLE programs

To register, go to www.isba.org/cle or call the ISBA registrar at 800-252-8908 or 217-525-1760.

February

Friday, 2/1/13 - Bloomington, Holiday Inn and Suites—Hot Topics in Agriculture Law- 2013. Presented by the ISBA Agricultural Law Committee. All Day.

Friday, 2/1/13 - Chicago, ISBA Chicago Regional Office—Illinois Sentencing- Statutory and Case Law. Presented by the ISBA Criminal Justice Section. All day.

Friday, 2/1/13 - Teleseminar—Independent Contractor Agreements. Presented by the Illinois State Bar Association. 12-1.

Tuesday, 2/5/13 – Live Studio Webcast—After the Fiscal Cliff: Roller Coaster or Merry Go Round -- Income and Transfer Tax Issues. Presented by the Trust & Estates Section. 12 – 1 pm.

Tuesday, 2/5/13 – Webinar—Intro to Legal Research on Fastcase. Presented by the Illinois State Bar Association – Complimentary to ISBA Members Only. 1:30 – 2:30 p.m. CST.

Thursday, 2/7/13 – Webinar—Advanced Tips for Enhanced Legal Research on Fastcase. Presented by the Illinois State Bar Association – Complimentary to ISBA Members Only. 1:30 – 2:30 p.m. CST.

Friday, 2/8/13 - Teleseminar—Liquidity Planning in Estates and Trusts. Presented by the Illinois State Bar Association. 12-1.

Monday, 2/11/13 – Live Studio Webcast—The Illinois Legislative Process – What Every Attorney Should Know. Presented by the ISBA Standing Committee on Government Lawyers. 1:30 – 3:00 pm.

Monday, 2/11/13 Teleseminar—Asset Purchase Deals- Securing Value & Limiting Liability, Part 1. Presented by the Illinois State Bar Association. 12-1.

Tuesday, 2/12/13 - Teleseminar—Asset Purchase Deals- Securing Value & Limiting Liability, Part 2. Presented by the Illinois State Bar Association. 12-1.

Tuesday, 2/12/13 - Chicago, ISBA Chicago Regional Office—Fred Lane's ISBA Trial Technique Institute- Spring 2013 (18 sessions). Presented by the ISBA. Tuesdays 5:15-6:45pm.

Wednesday, 2/13/13 - Live Studio Webcast—Settling FSLA and Wage Claim Cases: What You Need to Know. Presented by the ISBA Labor and Employment Section Council. 10:00 – 11:30 am.

Wednesday, 2/13/13 - Live Studio Webcast—Changes to the Employment Eligibility Verification Form I-9: Is Your Business Client in Compliance? Presented by the ISBA International & Immigration Law Section Council. 12:30 PM – 2:30 PM.

Friday, 2/15/13 - Bloomington, Holiday Inn and Suites—Guardianship Boot Camp. Presented by the ISBA Trust and Estates Section. All Day.

Monday, 2/18-Friday, 2/22/13 - Grafton, Pere Marquette Lodge—40 Hour Mediation/Arbitration Training. Presented by the Illinois State Bar Association. 8:30-5:45 daily.

Monday, 2/18/13 - Chicago, James R. Thompson Center- Auditorium—Advanced Workers' Compensation 2013. Presented by the Workers' Compensation Law Section. 9-4.

Monday, 2/18/13 - Fairview Heights, Four Points Sheraton—Advanced Workers' Compensation 2013. Presented by the Workers' Compensation Law Section. 9-4.

Tuesday, 2/19/13 - Teleseminar—S Corp Business Planning & Stockholder Agreements, Part 1. Presented by the Illinois State Bar Association. 12-1.

Wednesday, 2/20/13 - Teleseminar—S Corp Business Planning & Stockholder Agreements, Part 2. Presented by the Illinois State Bar Association. 12-1.

Wednesday, 2/20/13 - Webinar—Introduction to Boolean (Keyword) Search. Presented by the Illinois State Bar Association – Complimentary to ISBA Members Only. 1:30 – 2:30 p.m. CST.

Thursday, 2/21/13 – Chicago, Chicago Regional Office—Recent Developments in State and Local Tax. Presented by the ISBA State and Local Tax Section. 9:00 am – 12:30 pm.

Thursday, 2/21/13 – Live Studio Webcast—Recent Developments in State and Local Tax. Presented by the ISBA State and Local Tax Section. 9:00 am – 12:30 pm. ■

Commercial Banking, Collections & Bankruptcy Law

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