THE STATE OF NEW HAMPSHIRE
SUPERIOR COURT

CHESHIRE, SS. **SUPERIOR COURT**

Denron Plumbing & HVAC, LLC

v.

MacMillin Company, LLC et al.

No. 213-2019-CV-00221

ORDER ON PLAINTIFF'S MOTION TO STRIKE

The plaintiff, Denron Plumbing & HVAC, LLC ("Denron") filed a complaint against MacMillin Company, LLC ("MacMillin") alleging breach of contract and unjust enrichment. (Court Index #32.) MacMillan answered with several affirmative defenses. (Court Index #35.) Denron now moves to strike MacMillin's eleventh affirmative defense. (Court Index #36.) For the reasons that follow, the Court GRANTS the motion.

BACKGROUND

The following facts are taken from the amended complaint unless otherwise noted. In 2017, Prospect-Woodward Home ("Prospect-Woodward") decided to construct an assisted living facility known as Hillside Village. (Compl. ¶ 3.) Prospect-Woodward contracted with MacMillin to act as the construction manager on the project. (Id. ¶ 4.) MacMillin then subcontracted with Denron to perform plumbing and mechanical work. (Id. ¶ 5.)

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MacMillin and Denron's subcontract ("the Agreement") contained several provisions relating to payment.[1] (Def.'s Answer Ex. A.) First, in sections 9.2A and 9.2B, both under the heading "Progress Payments[,]" the Agreement specified that:

> Subcontractor may apply for a "Progress Payment" for the Subcontract Work performed during the payment period if Contractor has the right to progress payments.
>
> . . .
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> Contractor shall pay Subcontractor 7 days after it receives from Owner a corresponding payment for Subcontractor's Work. Payment terms between the Owner and Contractor including the dates upon which payment is due to the Contractor from the Owner are set forth in Section 12 of the Project Agreement. A condition precedent to its payment obligations is Contractor's actual receipt of the corresponding payment from Owner.

(Id.) Second, in section 9.4 under the heading "Final Payment[,]" the Agreement established that the "[c]ontractor shall make final payment to Subcontractor within 7 days, or as otherwise required by the applicable law in the State of work after it receives final payment from Owner." (Id.) The Agreement also incorporated the prime contract between Prospect-Woodward and MacMillin, which specified that:

> Neither final payment nor any remaining retained percentage shall become due until the Contractor submits to the Architect (1) an affidavit that payrolls, bills for materials and equipment, and other indebtedness connected with the Work for which the Owner or the Owner's property might be responsible or encumbered (less amounts withheld by Owner) have been paid or otherwise satisfied . . .

(Mot. Strike at 7.)

[1] The Court notes that the Agreement was not attached to the complaint but was attached as an exhibit to MacMillin's answer. Even though on a motion to dismiss the Court normally limits its analysis to the complaint and any exhibits attached to it, it can consider documents not in dispute. Beane v. Dana S. Beane & Co., 160 N.H. 708, 711 (2010) ("The trial court may also consider documents attached to the plaintiff's pleadings, or documents the authenticity of which are not disputed by the parties, official public records, or documents sufficiently referred to in the complaint.") (cleaned up). Neither party disputes the Agreement.

After Denron completed its work, MacMillin requested payment from Prospect-Woodward, who refused. (Id. ¶ 9.) MacMillin, then, refused to pay Denron which gave rise to this action. (Id. ¶ 8.)

LEGAL STANDARD

Neither the Superior Court rules nor New Hampshire case law provide guidance for motions to strike. Penney v. Baum Hedlund, Belknap Cnty. Super. Ct., No. 04-C-047, 2008 N.H. Super. LEXIS 17 at *4 (May 17, 2008) (Order, Perkins, J.). Despite the lack of direction, rule 12(f) of the Federal Rules of Civil Procedure ("FRCP") provides insight. Id. Under FRCP 12(f), "the court may strike from a pleading an insufficient defense or any redundant, immaterial, impertinent, or scandalous matter." Motions to strike are "generally disfavored" and "will be allowed only where the Court is convinced that there are no disputed questions of fact, that the questions of law are clear and settled, and that under no circumstances could the defense prevail." Knickerbocker Toy Co., Inc. v. Winterbrook Corp. v. St. James Doll Creations, 554 F. Supp. 1309, 1323–24 (D.N.H. 1982) (cleaned up).

DISCUSSION

Denron moves to strike MacMillin's eleventh affirmative defense, namely, that "MacMillin is not obligated to pay Denron until MacMillin is paid by Prospect-Woodward under the terms of the Subcontract." (Def.'s Answer at 5.) Denron supplies two arguments. (See generally Mot. Strike.) First, it argues that the relevant contract provision to this dispute should be section 9.4, an alleged pay-when-paid clause, because this suit is for final payment. (Id. at 6.) Second, it argues that incorporation of the prime contract between Prospect-Woodward and MacMillin creates an ambiguity

which negates the alleged pay-if-paid clause in section 9.2B. (Id. at 7–8.) MacMillin responds with three arguments. (See generally Obj. Mot. Dismiss.) First, it argues that section 9.2B, the alleged pay-if-paid clause, should apply because, even though Denron finished its work, the outstanding amounts owed by Prospect-Woodward to MacMillin are for progress payments. (Obj. Mot. Strike at 7.) Second, it disagrees that incorporation of the prime contract creates an ambiguity. (Id. at 7–8.) Third, it contends that the Court should respect the parties' freedom of contract. (Id. at 8.)

The Court will analyze the parties' arguments regarding pay-if-paid and pay-when-paid clauses in turn. But because the topic has never been discussed by the New Hampshire Supreme Court nor any Superior Courts, the Court will first survey other jurisdictions to glean the proper approach.

I. Legal Background

"Construction projects of any significance generally require a myriad of people and organizations, interlocked in a complex set of contractual relationships." Walter N. Vernon IV, "Show Me The Money!": A Comment On The Enforceability Of "Pay-If-Paid" Clauses In Contracts For Professional Services, 33 U.S.F.L. L. Rev. 99 (1998) (cleaned up). As a result of that complexity, a common problem arises: owner non-payment. Id. In response, the construction industry in the 1980s began using contract language to shift risk from the general contractor, who typically is paid directly from the project owner, to the subcontractors, who are paid by the general contractor. 8 Williston on Contracts § 19:59 (4th ed.). These clauses are known as "pay-if-paid" or "pay-when-paid" clauses and have been succinctly described by the Tenth Circuit:

> A typical "pay-when-paid" clause might read: "Contractor shall pay subcontractor within seven days of contractor's receipt of payment from the

> owner." Under such a provision in a construction subcontract, a contractor's obligation to pay the subcontractor is triggered upon receipt of payment from the owner. Most courts hold that this type of clause at least means that the contractor's obligation to make payment is suspended for a reasonable amount of time for the contractor to receive payment from the owner. The theory is that a "pay-when-paid" clause creates a timing mechanism only. Such a clause does not create a condition precedent to the obligation to ever make payment, and it does not expressly shift the risk of the owner's nonpayment to the subcontractor.
>
> . . .
>
> A typical "pay-if-paid" clause might read: "Contractor's receipt of payment from the owner is a condition precedent to contractor's obligation to make payment to the subcontractor; the subcontractor expressly assumes the risk of the owner's nonpayment and the subcontract price includes this risk." Under a "pay-if-paid" provision in a construction contract, receipt of payment by the contractor from the owner is an express condition precedent to the contractor's obligation to pay the subcontractor. A "pay-if-paid" provision in a construction subcontract is meant to shift the risk of the owner's nonpayment under the subcontract from the contractor to the subcontractor.

MidAmerica Constr. Mgmt., Inc. v. MasTec North America, Inc., 436 F.3d 1257, 1261–62 (10th Cir. 2006); see also BMD Contractors, Inc. v. Fid. & Deposit Co. of Maryland, 679 F.3d 643, 649 (7th Cir. 2012).[2]

These clauses have been "in vogue" ever since the 1980s. American Bar Association, Fundamentals of Construction Law 131 (Carina Y. Enhada et al. eds., 2001). Despite the trend, many consider them as some of the most divisive issues in the construction industry. Gerald B. Kirksey, "Minimum Decencies"--A Proposed Resolution of the "Pay-When-Paid" /"Pay-If-Paid" Dichotomy, 12 The Constr. Lawyer 1, (1992). Courts and legislatures have responded to the controversy in a variety of ways. Some void them; others require explicit language for their use; and still others enforce

[2] Some courts and commentators only use the term "pay-when-paid" clause but find that there are two types: ones that are conditions precedent and others that are timing mechanisms only.

them strictly like any other contract provision. As will be discussed below, this Court will take the middle approach.

II. Jurisdictions Voiding Pay-If-Paid Clauses

North Carolina, Wisconsin, and South Carolina have voided pay-if-paid clauses by statute. See N.C. Gen. Stat. § 22C-2 (2012) (North Carolina); Wis. Stat. 779.135 (3) (2006) (Wisconsin); S.C. Code Ann. § 29-6-230 (2000) (South Carolina). North Carolina's statute, for example, reads:

> Performance by a subcontractor in accordance with the provisions of its contract shall entitle it to payment from the party with whom it contracts. Payment by the owner to a contractor is not a condition precedent for payment to a subcontractor and payment by a contractor to a subcontractor is not a condition precedent for payment to any other subcontractor, and an agreement to the contrary is unenforceable.

N.C. Gen. Stat. § 22C-2.

New York and California have similarly held such clauses unenforceable through court action. See West-Fair Elec. Contractors v. Aetna Cas. & Sur. Co., 661 N.E. 2d 967, 971 (N.Y. 1995); Wm. R. Clarke Corp. v. Safeco Ins. Co., 928 P.2d 372, 374 (Cal. 1997) (same). The Court of Appeals of New York, for example, based its reasoning on the availability of mechanic's liens. West-Fair, 661 N.E. 2d at 970–71. The court referenced a recent enactment of New York's lien law which voided "any contract . . . whereby the right to file or enforce any lien created under article two is waived . . . ." Id. at 970. The court also noted that "in the event the general contractor fails to pay a subcontractor with the sums the owner has already paid, the Lien Law protects owners from paying more than the value of the improvements, or the contract price." Id. at 971. With that in mind, the court held that "a pay-when-paid provision which forces the

subcontractor to assume the risk that the owner will fail to pay the general contractor is void and unenforceable as contrary to public policy set forth in the Lien Law § 34." Id.

Illinois, Missouri, and Maryland have not voided pay-if-paid clauses, but each has passed laws noting that parties cannot use such clauses as a defense against mechanic's liens. See 770 Ill. Comp. Stat. 60/21(e) (2014) (Illinois); Mo. Rev. Stat. § 431.183 (1995) (Missouri); MD. Code Ann., Real Property, § 9-113 (1995) (Maryland). Additionally, Delaware law prohibits and renders void any contract provisions stating "that a contactor assumes the risk of nonpayment of the owner." De. Code Ann. tit. 6, § 3507 (e)(1) (2012). Delaware's law, though, does not appear to void pay-if-paid provisions, and there are no cases interpreting it.

III. The Majority Approach: Clear and Unambiguous Intent

Rather than voiding pay-if-paid clauses, most jurisdictions take a middle approach: pay-if-paid clauses are only enforced if the language is clear and unambiguous. See Koch v. Construction Technology, Inc., 924 S.W.2d 68, 71 n. 1 (Tenn. 1996) (compiling cases); 8 Williston on Contracts § 19:59 n.3–4 (4th ed.) (same); David Hendrick et al., Battling For The Bucks: The Great Contingency Payment Clause Debate, 16-JUL Constr. Law. 12 (1996) (same). An early case blazing the trail for this rule was Thos. J. Dyer Co. v. Bishop Intern. Eng'g Co., 303 F.2d 655 (6th Cir. 1962). See BMD Contactors, 679 F.3d at 650 ("Dyer is the leading case in this group . . . ."); Koch, 924 S.W.2d at 72 (citing Dyer as a "seminal" case).

In Dyer, the general contractor and subcontractor executed an agreement for the subcontractor to perform work on a job. Id. at 656. Their agreement noted that "[t]he total price to be paid to Subcontractor shall be $109 Dollars ($115,000.00) lawful money

of the United States, no part of which shall be due until five (5) days after Owner shall have paid Contractor therefor." Id. When the owner of the project went into bankruptcy and failed to pay the general contractor, the subcontractor sued the general contractor to obtain payment. Id. In addressing whether the contract provision prevented the subcontractor from obtaining payment, the Court reasoned that:

> Th[e] expectation and intention of being paid is even more pronounced in the case of a subcontractor whose contract is with the general contractor, not with owner. In addition to his mechanic's lien, he is primarily interested in the solvency of the general contractor with whom he has contracted. He looks to him for payment. Normally and legally, the insolvency of the owner will not defeat the claim of the subcontractor against the general contractor. Accordingly, in order to transfer this normal credit risk incurred by the general contractor from the general contractor to the subcontractor, the contract between the general contractor and subcontractor should contain an express condition clearly showing that to be the intention of the parties.

Id. at 660–61. The Restatement (Second) of Contracts has suggested a similar approach:

> § 227. Standards of Preference with Regard to Conditions:
>
> (1) In resolving doubts as to whether an event is made a condition of an obligor's duty, and as to the nature of such an event, an interpretation is preferred that will reduce the obligee's risk of forfeiture, unless the event is within the obligee's control or the circumstances indicate that he has assumed the risk.

Restatement (Second) of Contracts § 227.

Insolvency of the owner is not the only risk to subcontractors. The U.S. District Court for the Northern District of Indiana, for example, explained another risk:

> The facts of the case at bar inspire a hypothetical fact situation which underscores the wisdom of the Dyer rule. Under the terms of a general contract such as that between Schools and Hall, in which the owner retainage for the second half of the work is five percent, and subcontracts such as we find here, in which the general contractor retains ten percent from the subcontractors throughout the job, it is a virtual certainty that the prime contractor will find himself owing the subcontractors more than is

> owed to him by the owner. Under the rule for which Hall argues, it would not be inconceivable that a malefic general contractor might intentionally maintain a dispute with the owner which would cause the owner to refuse to make payment; the general contractor could thereby avail himself for several years of funds to which he has no right. The Dyer rule precludes such an intolerable state of affairs.

Midland Eng'g Co. v. John A. Hall Constr. Co., 398 F.Supp. 981, 994 (N.D. Ind. 1975); see also Koch, 924 S.W.2d at 72 (describing same).

IV. The Strict Approach

Georgia falls on the other end of the spectrum: it reads contract provisions relating to payment strictly and will often find conditions precedent even in the face of minor language. See Peacock Construction Co. v. A. M. West, 142 S.E.2d 332 (Ga. Ct. App. 1965), superseded by statute as recognized in Olympic Const., Inc. v. Drywall Interiors, Inc., 348 S.E.2d 688, 690 (Ga. Ct. App. 1986); see also Statesville Roofing & Heating Co., Inc. v. Duncan, 702 F.Supp. 118, 120–21 (W.D.N.C. 1988) ("Georgia has a long line of cases holding that pay-when-paid clauses in written contracts must be taken literally[.]")

For example, in Peacock, the parties' contract specified that "Final payment shall be made within 30 days after the completion of the work included in this subcontract, written acceptance by the Architect, and full payment therefor by the Owner." 142 S.E.2d at 333. The Court held that "as we construe the plain and unambiguous language of the agreement, there are clearly expressed conditions precedent to defendants' liability for the final payment of the contract price." Id.

V. The Agreement

With that legal backdrop in mind, the Court adopts the Dyer/Restatement (Second) approach, and will require MacMillin to show a clear and unambiguous intent

for the condition precedent it asserts. This approach is most consistent with New Hampshire law, which generally disfavors conditions precedent and requires clear language to enforce them. See Greenwald v. Keating, 172 N.H. 292, 298 (2019) ("Conditions precedent are not favored in the law, and we will not construe contracts to include them unless required by the plain language of the agreement in question.") There are also several policy reasons supporting the rule. First, the Court acknowledges the concern in several jurisdictions that such clauses violate subcontractors' rights under Mechanic's Lien laws. See supra 6–7. New Hampshire has such a law. See N.H. RSA 447:5. Second, subcontractors are often at the mercy of the general contractor during negotiations. With that in mind, the burden should be on the general contractor to display a clear intent. Third, the general contractor is in a better position to avoid risk because it has a direct relationship with the owner; the subcontractor, though, is further down the chain.

Thus, although the Court will not wholesale void pay-if-paid clauses, it sees the Dyer/Restatement (Second) approach as the fairest way to balance freedom of contract and subcontractors' rights. Therefore, the Court will now apply that approach to the Agreement here to test if it clearly and unambiguously expressed an intent for Prospect-Woodward's payment to MacMillin to serve as a condition precedent to Denron's pay from MacMillin.

When interpreting a contract, the Court "give[s] the language used by the parties its reasonable meaning, considering the circumstances and the context in which the agreement was negotiated, and reading the document as a whole." Birch Broad. v. Capitol Broad. Corp., 161 N.H. 192, 196 (2010). Absent an ambiguity, "the parties'

intent will be determined from the plain meaning of the language used in the contract." Id. Contract language is ambiguous, though, "if the parties to the contract could reasonably disagree as to the meaning of that language." Id.

As an initial matter, the Court reads section 9.2B as a pay-if-paid clause. It clearly uses express condition precedent language. Section 9.4, on the other hand, is clearly a pay-when-paid clause, which only triggers a timing mechanism. With that in mind, the Court finds the Agreement's provisions regarding payment ambiguous.

First, sections 9.2B and 9.4 are ambiguous when read together. For example, it does not specify which clause applies to a situation where Denron applies to MacMillin for final payment, but MacMillin still has not received progress payments from Prospect-Woodward. In that situation, would the pay-if-paid clause in section 9.2B or the pay-when-paid clause in section 9.4 apply?

Another ambiguity arises from the incorporation of the prime contract between Prospect-Woodward and MacMillin. The prime contract requires MacMillin to show that it has paid its payrolls before Prospect-Woodward will pay MacMillin. That creates an ambiguity when reading the condition precedent language in section 9.2B (even though the Court already found that section ambiguous in itself). Other courts have agreed. See OBS Co. v. Pace Construction Corp., 558 So.2d 404, 406 (Fla. 1990); IES v. Scherer, 74 S0.3d 531, 534 (Fla. Ct. App. 2011). For example, in OBS, the Supreme Court of Florida explained why such a provision creates ambiguity:

> The general contract between Pace [the general] and the owner was a "cost plus" or reimbursement type contract which required Pace to pay its subcontractors before the owner reimbursed Pace. The concomitant general conditions required Pace to submit an affidavit certifying that its subcontractors had been paid before final payment from the owner became due. In contrast, provision 6.3 of the subcontract clearly required payment

> from the owner to Pace as a condition precedent to final payment becoming due to OBS [the subcontractor]. The direct conflict between the subcontract and the general contract and conditions, at the very least, creates some ambiguity as to who should bear the risk of the owner's nonpayment.

OBS, 558 So.2d at 406. Likewise, this Court finds the Agreement ambiguous due to the prime contract's language regarding duties between Prospect-Woodward and MacMillin. For those two reasons, the Court finds the Agreement ambiguous as to payment; as such, MacMillin cannot use the pay-if-paid defense asserted in its answer.

In conclusion, the Court wishes to emphasize that these facts present peculiar problems when the owner has paid neither the general nor the subcontractor. But, as the Supreme Court of Florida noted:

> Our decision to require judicial interpretation of ambiguous provisions for final payment in subcontracts in favor of subcontractors should not be regarded as anti-general contractor. It is simply a recognition that this is the fairest way to deal with the problem. There is nothing in this opinion, however, to prevent parties to these contracts from shifting the risk of payment failure by the owner to the subcontractor. But in order to make such a shift the contract must unambiguously express that intention. And the burden of clear expression is on the general contractor.

Peacock Const. Co., Inc. v. Modern Air Conditioning, Inc., 353 So. 2d 840, 843–42 (Fla. 1977). MacMillin has simply failed to show such a clear expression.

CONCLUSION

For the reasons outlined above, the Court GRANTS Denron's motion to strike. MacMillin's eleventh affirmative defense will be stricken.

Date: April 26, 2021

Hon. David W. Ruoff

Clerk's Notice of Decision
Document Sent to Parties
on 04/29/2021