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Lien Waivers – Critical to Processing Payment but a Word of Caution

Client Alert

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When we give training sessions to contractors about implementing construction lien systems, one critical component we address is the importance of lien waivers. Contractors and suppliers deliver labor and materials to projects on credit understanding they will be paid shortly thereafter. The Construction Lien Act provides security against that credit risk should the contractor or supplier not be paid timely for the full value which they contributed to the project.

When owners and contractors make progress payments, they want to ensure the payments flow downstream to lower-tier subcontractors and suppliers without having to pay twice for the same labor or materials. Sworn statements and lien waivers are typically utilized to track these downstream payments and to minimize or to eliminate the risk of double payment.

Normally, an owner or general contractor will require a conditional waiver of lien before payment followed by an unconditional waiver of lien after receipt of payment. We are often confronted with situations where an owner or general contractor demand an unconditional waiver of lien as a precondition to payment. A subcontractor or supplier that signs an unconditional waiver of lien before payment risks not being paid and losing its lien rights because the waiver is effective immediately. These problems also arise when a contractor uses a payment software like Oracle's Textura Payment Management. While intended to enhance payment efficiency, subcontractors may find overly broad lien waivers online as a condition to receiving the electronic payment. Such overly broad lien waivers can result in subcontractors unintentionally waiving or releasing remedies otherwise available to them.

We have also recently seen owners and general contractors attempting to use forms that go beyond simply waiving lien rights through a particular date or pay request in exchange for

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payment, and contain broader waiver language that release, for example, outstanding change orders, potential claims, or future payment, in exchange for the requested payment.

For this reason, we counsel subcontractors and suppliers to exercise caution and carefully review lien waivers, particularly those containing broad or lengthy legal language. You can easily distinguish these broad forms from "traditional" lien waivers. The Michigan Construction Lien Act, in particular Section 115 (MCL 570.1115), contains form waivers which are straightforward and short. If there is overly broad language, the subcontractor or supplier should try to carve out the disputed unpaid items with "reservation of rights" language modifying the lien waiver form. However, it is better to discuss and agree upon a mutually acceptable lien waiver process well before the first pay request.

If you encounter a recalcitrant owner or contractor who stubbornly insists upon an executed unconditional waiver of lien before receipt of payment or the subcontractor or supplier inadvertently signs such a form and then the owner or contractor does not make the requested payment, all is not lost. The subcontractor or supplier should send the owner and the contractor a letter stating, "the consideration for the waiver has failed and is hereby rescinded." The waiver will thereafter be ineffective.

Please contact the author of this Alert or your Butzel attorney for more information.

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