STATE OF TENNESSEE
CONSTRUCTION LAW
COMPENDIUM

Prepared by

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This Compendium outline provides a general overview of certain Tennessee construction laws concerning various litigation and legal topics. The Compendium provides a simple synopsis of current law and is not a complete recitation of Tennessee’s construction law. Further, the discussion on any particular topic is not intended to explore lengthy analysis of legal issues. With a few variations, the law applicable to construction disputes in Tennessee is similar to that found in other states. This Compendium is provided for general information and educational purposes only. It does not solicit, establish, or continue an attorney-client relationship with any attorney or law firm identified as an author, editor or contributor. The contents should not be construed as legal advice or opinion. While every effort has been made to be accurate, the contents should not be relied upon in any specific factual situation. These materials are not intended to provide legal advice or to cover all laws or regulations that may be applicable to a specific factual situation. If you have matters or questions to be resolved for which legal advice may be indicated, you are encouraged to contact a lawyer authorized to practice law in the state for which you are investigating and/or seeking legal advice.

I. STATUTE OF LIMITATIONS

In construction cases, there are several statutes of limitation to consider. To determine which statute applies, the claim must first be classified. In Tennessee, courts will look to the gravamen of the complaint or its “substantial point or essence” to determine which period of limitation applies, regardless of whether the claims are designated as an action for breach of contract or sound in tort. *Whaley v. Perkins*, 197 S.W.3d 665, 670 (Tenn. 2006); *Black’s Law Dictionary* 770 (9th ed. 2009). Notably, in analyzing the “gravamen” rule articulated in *Whaley v. Perkins*, the Tennessee Court of Appeals held that courts are not prohibited from applying more than one statute of limitations to a complaint that contains more than one viable claim. *Bluff Springs Apartments, Ltd. v. Peoples Bank of S.*, No. E2009-01435-COA-R3-CV, 2010 WL 2106210, at *7-10 (Tenn. Ct. App. May 26, 2010); see also *French v. Stratford House*, 333 S.W.3d 546, 557 (Tenn. 2011) (stating that courts must ascertain the nature and substance of a claim and not rely on the designation of the claims given by either the plaintiff or defendant).

It is well-settled in Tennessee that if the injury is to the person, the claim must be commenced within one (1) year after the cause of action accrues. Tenn. Code Ann. § 28-3-104 (West 2012). For instance, as related to construction lawsuits, this includes claims related to personal injuries, products liability, wrongful death, and statutory penalties. *Id.* Alternatively, injuries to property must be brought within three (3) years after the cause of action accrues. Tenn. Code Ann. § 28-3-105. This includes actions for injuries to personal or real property and for the detention or conversion of personal property. *Id.* Moreover, breach of contract claims in Tennessee are subject to a six-year statute of limitations. Tenn. Code. Ann. § 28-3-109.

A. The Discovery Rule

As a general rule, the statute of limitation does not begin to run until the action “accrues.” A claim will not “accrue” until it would be reasonable for the plaintiff to “discovery” the existence of a claim. Accordingly, the “discovery rule” is an equitable doctrine that tolls,
i.e., stops, the statute of limitations from running while the plaintiff has no knowledge that a wrong occurred. Cole v. Wyndchase Aspen Grove Acquisition Corp., No. 3:05-0558, 2006 WL 2827452, at *4 (M.D. Tenn. Sept. 28, 2006).

B. Statute of Repose

The statute of repose will bar an action for a certain period of time, regardless of when the plaintiff may have reasonably discovered the injury. The discovery rule, used to determine when a cause of action has accrued under a statute of limitations, does not toll the statute of repose. Watts v. Putnam County, 525 S.W.2d 488, 491 (Tenn. 1975); Tenn. Code Ann. § 28-3-204(a).

In 1967, the Tennessee General Assembly enacted legislation to limit the period in which claims may be brought relating to the improvement of real property (e.g., a claim for defective construction). See Tenn. Code Ann. § 28-3-202. Tennessee’s construction statute of repose provides:

All actions to recover damages for any deficiency in the design, planning, supervision, observation of construction, or construction of an improvement to real property, for injury to property, real or personal, arising out of any such deficiency, or for injury to the person or for wrongful death arising out of any such deficiency, shall be brought against any person performing or furnishing the design, planning, supervision, observation of construction, construction of, or land surveying in connection with, such an improvement within four (4) years after substantial completion of such an improvement.

Id. A cause of action against an architect, builder, developer, or engineer begins to accrue at the time of “substantial completion” of the improvement to the property. Id. The term “substantial completion” is defined as the date on “which the owner can use the [property] for the purpose for which it was intended.” Tenn. Code Ann. § 28-3-201. The contractor and owner may establish the date of substantial completion by written agreement. Id.

Under the statute, the plaintiff has four (4) years from the date of “substantial completion” to bring a claim related to the improvement to real property. Tenn. Code Ann. § 28-3-202. If, however, an injury occurs in the final or fourth year after such substantial completion, the plaintiff gains an additional year in which to file suit. Tenn. Code Ann. § 28-3-203.

The Tennessee Court of Appeals has held that the construction statute of repose does not apply in cases where the plaintiff brings a claim of incomplete performance as opposed to “deficient” performance as referenced in Tenn. Code Ann. § 28-3-202. Pons v. Harrison, No. M2007-01909-COA-R3-CV, 2008 WL 2695665, at *3-4 (Tenn. Ct. App. July 9,
2008) (stating that the chief complaint was nonfeasance or partial performance, as opposed to malfeasance or defective performance, such that the construction statute of repose, Tenn. Code Ann. § 28-3-202, was inapplicable).

1. Exceptions to the Construction Statute of Repose

There are two statutory exceptions in which the construction statute of repose may not be asserted as a defense to a claim for defective improvement of real property. First, if the defendant is in possession or control of the premises (i.e., owner or tenant) of such an improvement, then the defendant is prohibited from using the statute of repose as a defense when the improvement is the proximate cause of injury or death underlying the plaintiff’s cause of action. See Tenn. Code Ann. § 28-3-205(a), -202.

Second, if any defendant is found guilty of wrongfully concealing the plaintiff’s claim or of fraudulently performing or furnishing “the design, planning, supervision, observation of construction, construction of, or land surveying, in connection with such an improvement,” then the defendant shall not be able to assert the construction statute of repose. See Tenn. Code Ann. § 28-3-205(b), -202.

The Tennessee Court of Appeals has stated that the fraudulent misrepresentation necessary under this second exception, Tenn. Code Ann. § 28-3-205(b), to prevent a defendant from invoking the four-year statute of repose “need not be made directly to the plaintiff[.]” such that “remote purchasers of improvements to real property who have had no direct dealings with the contractor who constructed the improvements may pursue a negligence claim against the contractor.” Jenkins v. Brown, 2007 WL 4372166, at *12 (Tenn. Ct. App. Dec. 14, 2007) (affirming trial court’s holding that the defendant contractor was not entitled to assert the four-year statute of repose as a defense because the contractor was found guilty of fraud in connection with the construction of a house); see also Cloud Nine, LLC v. Whaley, 650 F.Supp.2d 789, 797 (E.D. Tenn. 2009) (noting that although Tennessee courts have never held that remote purchasers may pursue claims against contractor based on any theory of liability other than negligence, the Tennessee courts have likewise not rejected such misrepresentation claims against a contractor simply because a plaintiff was a remote purchaser).

II. BREACH OF CONTRACT

Breach of contract is a commonly asserted cause of action in construction cases. Unless otherwise provided, Tennessee courts hold that a contract is to be governed by the law of the jurisdiction in which the contract was executed. Vantage Tech., LLC v. Cross, 17 S.W.3d 637, 650 (Tenn. Ct. App. 1999); Ohio Cas. Ins. Co. v. Travelers Indem. Co., 493 S.W.2d 465, 467 (Tenn. 1973). “In a breach of contract action, claimants must prove the existence of a valid and enforceable contract, a deficiency in the performance amounting to a breach, and damages

An enforceable construction contract requires mutual assent of the parties. *Sweeten v. Trade Envelopes, Inc.*, 938 S.W.2d 383, 386 (Tenn. 1996). In interpreting written contracts governed by Tennessee law, courts look not only to the language of the instrument, but must ascertain, if possible, the intent of the parties. *Real Estate Mgmt., Inc. v. Giles*, 293 S.W.2d 596, 599 (Tenn. Ct. App. 1956). It is the duty of the parties to ensure that they understand the provisions of the contract when they give their mutual assent. *Robert J. Denley Co., Inc. v. Neal Smith Const. Co.*, Inc., No. W2006-00629-COA-R3-CV, 2007 WL 1153121, at *4 (Tenn. Ct. App. 2007). In *Robert J. Denley Co., Inc.*, the Tennessee Court of Appeals upheld a contract where one party claimed to have failed to read the entire contract. *Robert J. Denley Co., Inc.*, 2007 WL 1153121, at *4 (stating that a developer who signed, extensively marked and modified the contract was prohibited from disavowing the terms of a contract because the Court presumes that the parties to a contract understand their obligations).

Under Tennessee law, the plaintiff may recover damages to compensate the plaintiff for a loss that are the natural and foreseeable result of the breach of contract. *Bush v. Cathey*, 598 S.W.2d 777, 783 (Tenn. Ct. App. 1979) (finding that purchasers were entitled to award of damages to compensate them for additional moving expenses incurred as result of vendor’s failure to perform contract for sale of home). In construction cases, damages may include the value of the breaching party’s non-performance or partial performance under the contract in addition to the cost of completion or the cost to remedy substantial defects. *See Wilhite v. Brownsville Concrete Co.*, 798 S.W.2d 772, 775 (Tenn. Ct. App. 1990) (holding that contractor defectively built pool and owners were entitled to recover the full cost of repairing the pool from the contractor that installed it); *Allen v. Elliott Reynolds Motor Co.*, 230 S.W.2d 418, 420 (Tenn. Ct. App. 1950) (applying the doctrine of part performance where, in reliance on defendant’s promise of exclusive automobile dealership, plaintiff incurred expenses in converting apartment house to automobile sales room and garage).

In Tennessee, an arbitration provision in a contract for the construction of residential property must be separately signed or initialed by the parties. Tenn. Code Ann. § 29-5-302(a); *see State Farm Fire & Cas. Co. v. Easyheat, Inc.*, No. M2006-02363-COA-R3-CV, 2007 WL 3306765, at *1, 3 (Tenn. Ct. App. 2007) (holding that the parties were required to arbitrate the dispute although the arbitration provision in the contract for the construction of residential property was unsigned because the Federal Arbitration Act was applicable, which requires the enforcement of a written arbitration agreement when the contract evidences a transaction involving interstate commerce).
II. NEGLIGENCE

An injury incurred due to negligent construction may give rise to an action for breach of a contractor’s duty of care based upon, for example, workmanship falling below the standard in the industry, failure to supervise and failure to properly manage the work on a project. Tennessee is a comparative fault state. If the plaintiff is found to be 50% or more at fault, then the plaintiff is barred from recovery. Tennessee abolished joint and several liability when it instituted comparative fault. *McIntyre v. Balentine*, 833 S.W.2d 52, 58 (Tenn. 1992).

To successfully prevail on a claim for negligence, plaintiff must show: (1) a duty of care owed by the defendant to the plaintiff; (2) conduct falling below the applicable standard of care amounting to a breach of that duty; and (3) causation in fact and for a proximate cause of damages or injury. *LDI Design, LLC v. Dukes*, No. M2003-02905-COA-R3-CV, 2005 WL 3555543, at *5 (Tenn. Ct. App. Dec. 28, 2005) (citing *McClenahan v. Cooley*, 806 S.W.2d 767, 774 (Tenn.1991); see also *United American Bank of Memphis v. Gardner*, 706 S.W.2d 639, 642 (Tenn. Ct. App. 1985)).

The Tennessee Supreme Court recently held that contractors have an implied duty to perform services required by their contract with homeowners in a skillful, careful, diligent and workmanlike manner, even in the absence of a written agreement. *Winters*, 354 S.W.3d at293. The Court further held that the delegation of performance of a contract to a subcontractor does not relieve the contractor from the duties implicit in the original contract. *Winters*, 354 S.W.3d at 293-96.

In *Winters*, a contractor entered into an oral contract with homeowners to replace their roof, even though the contractor was not capable of replacing entire roof, and subcontracted the job. *Id.* at 289-90. The unsupervised work of the subcontractor resulted in substantial damage to the home. *Id.* The Court found that because of the implied legal obligation in the oral contract to perform services in a skillful, careful, diligent and workmanlike manner, and because the homeowners never released the contractor from this duty, the contractor was liable for the damages caused by the acts of the subcontractor. *Id.* at 295.

III. BREACH OF WARRANTY

Many plaintiffs assert causes of action for breach of warranty in construction cases. A breach of warranty can be based on express warranty provisions contained in the contract between the plaintiff and the general contractor, the contract between the general contractor and a subcontractor or vendor, and/or warranties implied by law.

Tenn. Code Ann. § 47-2-314 provides for an implied warranty of merchantability with respect to goods. Further, the Court has aligned itself “with those jurisdictions that recognize that the home buying public has a legitimate expectation that the workmanship and materials used by the builder-vendor in the construction of a dwelling will meet the standard of the trade for homes in comparable locations and price range and that such a warranty is implicit in the contract and survives the passing of title to the real estate and the taking of possession, as an exception to the
IV. MISREPRESENTATION AND FRAUD

Under some circumstances, general contractors can be sued by homeowners under the theory of fraud or misrepresentation. Tenn. Code Ann. § 28-3-105 provides that actions for injuries to personal or real property shall be commenced within three (3) years from the accrual of the cause of action. Ne. Knox Util. Dist. v. Stanfort Const. Co., 206 S.W.3d 454, 459 (Tenn. Ct. App. 2006). This statute applies if the plaintiff alleges the builder is “guilty of fraud in performing or furnishing the design, planning, supervision, observation of construction, construction of, or land surveying, in connection with such an improvement,” or if the defendant “shall wrongfully conceal any such cause of action.” Chrisman v. Hill Home Dev., Inc., 978 S.W.2d 535, 541 (Tenn. 1998).

Fraudulent misrepresentation requires proof that: (1) the defendants made false representation; (2) the plaintiff relied on the misrepresentation; and (3) the plaintiff suffered injury as a result of relying on the misrepresentation. Also, a party to a contract has a duty to disclose to the other party any material fact affecting the essence of the subject matter of the contract, unless ordinary diligence would have revealed the undisclosed fact. Lonning v. Jim Walter Homes, Inc., 725 S.W.2d 682, 685 (Tenn. App. Ct. 1986).

V. INDEMNITY CLAIMS

A. Express Indemnity

Express indemnity claims derive from contract provisions in which one party to the contract agrees to pay costs incurred by the other party to the contract as a result of the other party being held liable to a third party or having to defend against a claim filed by a third party. See Winter v. Smith, 914 S.W.2d 527, 541-42 (Tenn. Ct. App. 1995). If one is to be indemnified for his own negligence, the indemnifying agreement must clearly and unequivocally so state. Summers Hardware and Supply Co., Inc. v. Steele, 794 S.W.2d 358, 363 (Tenn. App. Ct. 1990); see also Kroger Co. v. Giem, 387 S.W.2d 620, 626 (Tenn. 1965) (holding that in Tennessee it is nearly a “universal rule that there can be no recovery where there was concurrent negligence of both indemnitor and indemnitee unless the indemnity contract provides for indemnification in such case by ‘clear and unequivocal terms;’ and general words will not be read as expressing such an intent”).

Tennessee has consistently recognized that the right of parties to allocate liability for future damages through indemnity clauses, under most circumstances, is not contrary to public policy. Planters Gin Co. v. Fed. Compress & Warehouse Co., Inc., 78 S.W.3d 885, 892 (Tenn. 2002). Tennessee courts have found, however, that indemnity clauses are invalid as to damages caused by gross negligence or willful conduct on the part of the indemnified. Id.
The Tennessee General Assembly has barred indemnity in certain cases involving construction as against public policy. When a covenant, promise, agreement or understanding in connection with a contract relating to the construction, alteration, repair or maintenance of a building purporting to indemnify or hold harmless the promisee against liability for damages arising out of bodily injury to persons or damage to property resulting from the sole negligence of the promisee, the promisee’s agents or employees, or indemnitee, is against public policy and is void and unenforceable. Tenn. Code Ann. § 62-6-123.

B. Contribution or Implied Indemnity:

The Tennessee Supreme Court, in McIntyre v. Balentine, 833 S.W.2d 52 (Tenn. 1992), adopted the principles of comparative fault and, thus, limited the availability of contribution or implied indemnity. McIntyre, 833 S.W.2d at 58.

In regards to contribution, the Pittway Court first noted that the remedy of contribution was no longer available except in limited circumstances as a result of McIntyre. Time & Security Mgmt, Inc. v. Pittway Corp. 422 F. Supp. 2d 907, 916 (W.D. Tenn. 2006). The Court stated that while McIntyre did not completely abolish contribution, it could only be had in (1) cases in which the cause of action arose prior to McIntyre, (2) cases in which joint and several liability continued to apply under doctrines such as the family purpose doctrine or respondeat superior, or (3) appropriate cases in which fairness demanded contribution. Pittway Corp., 422 F. Supp. 2d at 910-11. The Court noted that the third category applied only when the failure to prevent contribution would impose an injustice. Id.

As for the claim of implied indemnity, following McIntyre which adopted the principles of comparative fault, the Supreme Court has held that “there can be no claim for indemnification based on active-passive negligence because that distinction is subsumed into the doctrine of comparative fault . . . . However, where implied indemnity is based on the legal relationship between the parties the traditional principles of indemnity continue to apply.” Id. at 914 (dismissing Pittway’s claims for indemnity because Pittway was defending against allegations of its own wrongdoing, for which the third-party was neither contractually nor legally responsible) (quoting Owens v. Truckstops of Am., 915 S.W.2d 420, 434 (Tenn. 1996)).

C. Third-Party Beneficiary:

Tennessee has clearly established its rule on third-party beneficiaries: “[u]nder the modern rule, third parties may enforce a contract if they are intended beneficiaries of the contract . . . . If, on the other hand, the benefit flowing to the third party is not intended, but is merely incidental, the third party acquires no right to enforce the contract . . . . In order to maintain an action as an intended beneficiary, a third party must show: (1) a valid contract made upon sufficient consideration between the principal parties and (2) the clear intent to have the contract operate for the benefit of a third party . . . . The
evidence must be clear and direct.” *Owner-Operator Indep. Drivers Assoc., Inc. v. Concord EFS, Inc.*, 59 S.W.3d 63, 68-69 (Tenn. 2001). The Court further stated a test to determine whether a third-party beneficiary of a contract was “entitled to enforce the contract’s terms, if: (1) the parties to the contract have not otherwise agreed; (2) recognition of a right to performance in the beneficiary is appropriate to effectuate the intention of the parties; and (3) the terms of the contract or the circumstances surrounding performance indicate that either: (a) the performance of the promise will satisfy an obligation or discharge a duty owed by the promise to the beneficiary; or (b) the promise intends to give the beneficiary the benefit of the promised performance.” *Id.* at 70.

Courts have also ruled that “unless the construction contracts involved clearly provide otherwise, prime contractors on construction projects involving multiple prime contractors will be considered to be intended or third party beneficiaries of the contracts between the project’s owner and all the other prime contractors.” *Moore Constr. Co., Inc. v. Clarksville Dep’t of Elec.*, 707 S.W.2d 1, 10 (Tenn. Ct. App. 1985). The court laid out the factors for prime contractor’s claims as third-party beneficiaries to be: “(1) the construction contracts contain substantially the same language; (2) all contracts provide that time is of the essence; (3) all contracts provide for prompt performance and completion; (4) each contract recognizes other contractors’ rights to performance; (5) each contract contains a non-interference provision; and (6) each contract obligates the prime contractor to pay for the damage it may cause to the work, materials, or equipment working on the project.” *Id.*

1. Providing that No Third-Party Beneficiaries Exist

Tennessee courts have held that if an agreement explicitly provides that there shall be no third party beneficiary, then that provision should be enforced as a matter of law. *AmSouth Erectors, LLC v. Skaggs Iron Works, Inc.*, No. W2002-01944-COA-R3-CV, 2003 WL 21878540, at *3 (Tenn. Ct. App. Aug. 5, 2003); *see Owner-Operator Indep. Drivers Assoc., Inc.*, 59 S.W.3d at 72. The *AmSouth Erectors* court stated that an “‘explicit statement . . . that the parties intended to reserve to themselves the benefits of their agreement’ shall be dispositive of the parties’ intent to exclude third-party beneficiaries. *AmSouth Erectors, LLC*, 2003 WL 21878540, at *4 (citing *Owner-Operator Indep. Drivers Assoc., Inc.*, 59 S.W.3d at 72). In *AmSouth Erectors*, the contract between the owner of the construction project and the prime contractor provided that nothing contained in the contract documents or otherwise shall create any contractual relationship between the owner and any subcontractor or sub-subcontractor. *Id.* at *3.

Further, the contract between the owner and project manager included similar language in addition to specifically stating that nothing in the contract shall be deemed to give any such party or any third party any claim or right of action against the owner or project manager. *Id.* Accordingly, the court held that AmSouth Erectors, LLC, a subcontractor on the project, was not a third-party beneficiary entitled to enforce either contract. *Id.* at *4.
VII. ECONOMIC LOSS DOCTRINE

In general, the economic loss doctrine “prohibits the recovery of purely economic damages for negligence when the plaintiff lacks privity of contract with the defendant.” *John Martin Co., Inc. v. Morse/Diesel, Inc.*, 819 S.W.2d 428, 430 (Tenn. 1991). The rationale behind the economic loss doctrine stems from the idea that a party should not be able to obtain relief under tort law for a dispute that should be settled under contract law. *Trinity Indus., Inc. v. McKinnon Bridge Co., Inc.*, 77 S.W.3d 159, 171-72, (Tenn. Ct. App. 2001).

Tennessee law provides that “economic loss” does not include damages for personal injury or property damage, as follows:

> In all causes of action for personal injury or property damage brought on account of negligence, strict liability or breach of warranty, including actions brought under the provisions of the Uniform Commercial Code, privity [of contract] shall not be a requirement to maintain such action.

Tenn. Code Ann. § 29-34-104. While the doctrine is easily stated, Tennessee does not have a definitive body of law in reported cases, making the application of the principle more difficult. *Trinity Indus., Inc.*, 77 S.W.3d at 173.

Distinguishing between personal injuries and economic loss is much clearer than determining whether there is property damage or economic loss. In *Messer Griesheim Indus., Inc.*, the court explained the difference between property damage and economic loss:

> [W]e use the terms “property damage” on the one hand and “economic loss” on the other to describe different kinds of damage a plaintiff may suffer. An action brought to recover damages for inadequate value, cost of repair, and replacement of defective goods or consequent[ial] loss of profits is one for “economic loss.” Property damage, on the other hand, is the *Restatement’s* physical harm . . . to [user’s] property.

131 S.W.3d at 465 (quoting Restatement (Second) of Torts § 402A (1965)).

In addressing the economic loss doctrine to products liabilities claims, the Tennessee Court of Appeals embraced the principle that the decreased value of an end product caused by a defective component is economic loss unless the component causes physical damage to the end product, in which case the loss is property damage. *See McCrary v. Kelly Technical Coatings, Inc.*, 1985 WL 75663, at *3 (Tenn. Ct. App. Aug. 28, 1985). In *McCrary*, the contractor painted a pool and had to repaint the pool because of defective paint. *McCrary*, 1985 WL 75663, at *1, 3. The contractor filed suit against the paint manufacturer for the cost of repainting the pool. *Id.* The Tennessee Court of Appeals determined that there was no evidence that the paint (the component) caused damage to the pool (the end product) and that the cost of repainting was a cost of repair or cost of defective goods and, therefore, an economic loss not property damage.
Accordingly, the contractor was precluded from recovering from the paint manufacturer because there was no privity between the two parties. *Id.*

In Tennessee, plaintiffs may recover on negligent misrepresentation or supervision claims from parties for which there is no privity of contract, thus circumventing the economic loss doctrine. *John Martin Co., Inc.*, 819 S.W.2d at 431 (finding that a subcontractor could recover increased labor and material costs when the construction manager provided subcontractor with incorrect measurements for a concrete structure).

VIII. RECOVERY FOR INVESTIGATIVE COSTS

Tennessee may allow recovery of investigative costs, but these types of damages are rarely awarded. *Chastain v. Tenn. Water Quality Control Bd.*, 555 S.W.2d 113, 115 (Tenn. 1977).

IX. EMOTIONAL DISTRESS CLAIMS

In Tennessee, the general rule is that damages for emotional distress claims are not recoverable in contract causes of action. *Johnson v. Woman’s Hosp.*, 527 S.W.2d 133, 137 (Tenn. Ct. App. 1975). However, the *Johnson* Court noted limited exceptions where damages are recoverable, such as breach of contract where there is physical injury or any conduct (i.e., mishandling of a corpse) which the parties would naturally expect to result in emotional distress. *See also Rice v. Van Wagoner Cos., Inc.*, 738 F.Supp., 252 (M.D. Tenn. 1990) (dismissing plaintiffs’ claim for mental anguish damages as part of breach of contract damages).

The Tennessee Supreme Court follows the modern trend to “allow damages for mental anguish where it is clearly [foreseeable] within the terms of the contract or transaction and was negligently or wantonly caused by the defendant.” *Se. Greyhound Lines v. Freels*, 144 S.W.2d 743, 745 (Tenn. 1940); *see also Whaley v. Perkins*, 197 S.W.3d at 670. (“Where the act occasioning the injury to the property is inspired by fraud, malice, or like natures, mental suffering is a proper element of damage”).

A homeowner may be able to recover compensatory damages for emotional distress because of injury to real property. For example, the Tennessee Supreme Court has indicated that the recovery of emotional injury damages that stemmed from injury to real property when misrepresentations had been made may be recoverable. *See Whaley*, 197 S.W.3d at 670. The Courts have not decided a case of this nature in the context of construction defect litigation. The elements of a cause of action for emotional distress in Tennessee are:

A. Intentional Infliction

In Tennessee, there are three essential elements to a claim for intentional infliction of emotional distress: the defendant’s conduct must be intentional or reckless; the conduct must be so outrageous as not to be tolerable by civilized society; the conduct must result in serious mental injury. *Arnett v. Domino’s Pizza I, LLC*, 124 S.W.3d 529, 539 (Tenn. Ct. App. 2003).
B. Negligent Infliction

“To resolve this issue, we begin the analysis by reviewing the elements of a claim for negligent infliction of emotional distress. In Tennessee, such a claim requires that the plaintiff establish the elements of a general negligence claim: (1) duty, (2) breach of duty, (3) injury or loss, (4) causation in fact, and (5) proximate causation. In addition, the plaintiff must establish the existence of a serious or severe emotional injury that is supported by expert medical or scientific evidence.” Lourcey v. Estate of Scarlett, 146 S.W.3d 48, 52 (Tenn. 2004) (internal citations omitted).

X. STIGMA DAMAGES/DIMINUTION IN VALUE

In cases where the diminution in value is greatly exceeded by the cost of repair or completion, the courts have held that the appropriate damages should equal the diminution in value. Tennessee courts have “uniformly held that the measure of damages for injury to real estate is the difference between the reasonable market value of the premises immediately prior to and immediately after injury but if the reasonable cost of repairing the injury is less than the depreciation in value, the cost of repair is the lawful measure of damages.” Redbud Coop. Corp. v. Clayton, 700 S.W.2d 551, 560 (Tenn. Ct. App. 1985).

XI. ECONOMIC WASTE

As a general rule, the measure of damages is the cost of correcting the defects or completing the omissions. GSB Contractors, Inc. v. Hess, 179 S.W.3d 535, 542 (Tenn. Ct. App. 2005). However, in a case where this measure of damages would result in economic waste, “the courts generally adhere to the view that if a builder or contractor has not fully performed the terms of the construction agreement, but to repair the defects or omissions would require a substantial tearing down and rebuilding of the structure, the measure of damages is the difference in value between the work if it had been performed in accordance with the contract and that which was actually done, or (as it is sometimes said) the difference between the value of the defective structure and that of the structure if properly completed.” GSB Contractors, Inc., 179 S.W. 3d. at 542.

“Despite this latter rule, however, there is some authority to the effect that damages for a contractor's breach of a contract to construct a dwelling, where it is not constructed in accordance with the plans and specifications, are the amount required to reconstruct it to make it conform to such plans and specifications, rather than the difference in loan or market value on the finished dwelling, since unlike a commercial structure, a dwelling has an aesthetic value and must be constructed as the owner wants it, even though the finished dwelling may be just as good.” Id.
XII. DELAY DAMAGES

Damages for delay and an extension of time for performance are two types of relief available to a contractor when its performance is delayed through no fault of its own. Moore Const. Co., Inc. 707 S.W.2d at 13 (ruling “that a contractor whose performance is delayed through no fault of its own has two types of relief available under the standard contract prepared by the American Institute of Architects. It first has the right to an extension of the time available for performance. In addition to a time extension, a contractor may have the right to be compensated for the increased costs it has incurred as a result of this delay.”).

“No damages for delay” clauses are commonly used in the construction industry. The clauses are meant to further the protection of the public interest and are “aimed generally against the contractor . . . with a view of limiting the cost of an improvement to the sum agreed upon and such additional sums as are specially provided for . . . Courts normally interpret such clauses according to their plain and ordinary meaning.” Thomas & Assocs., Inc. v. Metro. Gov’t of Nashville, No. M2001-00757-COA-R3-CV, 2003 WL 21302974, at *13 (Tenn. Ct. App. June 6, 2003).

XIII. RECOVERABLE DAMAGES

A. Direct Damages

Tennessee has held that “as a general rule, the measure of damages for defects and omissions in the performance of a construction contract is the reasonable cost of the required repairs. This is especially true when the structure involved is the owner's home. However, in the event that the cost of repairs is disproportionate when compared with the difference in value of the structure actually constructed and the one contracted for, the diminution value may be used instead as the measure of damages.” GSB Contractors, Inc. v. Hess, 179 S.W.3d at 543.

In some situations, however, reconstruction value may be the correct measure of damages:

It seems to us that when an owner contracts to have a dwelling constructed he wants a particular structure, not just any structure that could be built for the same price. We, therefore, think that the trial court was correct in awarding damages equal to the amount required to reconstruct the dwelling so as to make it conform to the specifications, rather than adopting the difference in loan value on the dwelling as the measure of damages, as contended by appellant.

Id. at 542.
B. **Punitive Damages**

Punitive damages are to be awarded only in the most egregious of cases. A plaintiff must prove the defendant's intentional, fraudulent, malicious, or reckless conduct by clear and convincing evidence. This higher standard of proof is appropriate given the twin purposes of punishment and deterrence: fairness requires that a defendant's wrong be clearly established before punishment, as such, is imposed; awarding punitive damages only in clearly appropriate cases better effects deterrence. *Hodges v. S.C. Toof & Co.*, 833 S.W.2d 896, 901 (Tenn. 1992).

Cases in which punitive damages are sought are bifurcated into the compensatory damages phase and, if compensatory damages are awarded, a punitive damages phase.

To determine the amount of punitive damages the court will weigh the following elements: (1) the defendant’s financial affairs, financial condition, and net worth; (2) the nature and reprehensibility of defendant's wrongdoing; (3) the defendant’s awareness of the amount of harm being caused and defendant's motivation in causing the harm; (4) the duration of defendant’s misconduct and whether defendant attempted to conceal the conduct; (5) the expense plaintiff has borne in the attempt to recover the losses; (6) whether defendant profited from the activity, and if defendant did profit, whether the punitive award should be in excess of the profit in order to deter similar future behavior; (7) whether, and the extent to which, defendant has been subjected to previous punitive damage awards based upon the same wrongful act; (8) whether, once the misconduct became known to defendant, defendant took remedial action or attempted to make amends by offering a prompt and fair settlement for actual harm caused; and (9) any other circumstances shown by the evidence that bear on determining the proper amount of the punitive award. *Hodges*, 833 S.W. 2d at 901-02.

C. **Attorneys’ Fees**

Tennessee follows the “American Rule” providing that attorneys’ fees are generally not recoverable. *See Whitelaw v. Brooks*, 138 S.W.3d 890, 893 (Tenn. Ct. App. 2003) (holding that “in the absence of a contract, statute, or recognized ground of equity so providing there is no right to have attorneys’ fees paid by an opposing party in civil litigation” (citations omitted)).

Attorneys’ fees are recoverable when they are provided for either by contract or statute. One of the most commonly used statutes to recover attorneys’ fees is the Prompt Pay Act Tenn. Code Ann. §§ 66-34-101 *et seq*. The Prompt Pay Act allows attorneys’ fees to be awarded to an unpaid contractor if that contractor is the “prevailing party” and that the non-prevailing party acted in “bad faith.” Tenn. Code Ann. § 66-34-602(b). The Tennessee Supreme Court has held “bad faith” to include “actions in knowing or reckless disregard of . . . contractual rights.” *Trinity Indus., Inc. v. McKinnon Bridge Co., Inc.*, 77 S.W.3d 159, 181 (Tenn. Ct. App. 2001) (quoting *Glazer v. First Am. Nat. Bank*, 930 S.W.2d 546, 549 (Tenn. 1996) (holding an award of attorney’s fees was inappropriate...
because the general contractor appeared to honestly believe that it did not owe money to the plaintiff).

In addition, a plaintiff may recover attorney’s fees in cases of malicious harassment or frivolous appeals. See Tenn. Code. Ann. §§ 4-21-701, 27-1-122.

Tennessee courts have discretion to determine whether an award of attorney’s fees is proper or reasonable. See Tenn. Sup. Ct. R. 8, RPC 1.5(a) (“A lawyer’s fee and charges for expenses shall be reasonable.”).

D. Expert Fees and Costs:

Under Tenn. R. Civ.P. 54.04(2), “costs not included in the bill of costs prepared by the clerk are allowable only in the court’s discretion. Discretionary costs allowable are reasonable and necessary court reporter expenses for depositions or trials, reasonable and necessary expert witness fees for depositions (or stipulated reports) and for trials, reasonable and necessary interpreter fees for depositions or trials, and guardian ad litem fees; travel expenses are not allowable discretionary costs.” See also Mass. Mut. Life Inc. Co. v. Jefferson, 104 S.W.3d 13, 38 (Tenn. Ct. App. 2002) (stating that “prevailing parties cannot recover expert witness fees for preparing for depositions or trial, no matter how reasonable and necessary these fees are”).

IV. INSURANCE COVERAGE FOR CONSTRUCTION CLAIMS

A. Interpretation of the Insurance Policy

It is well established that the duty to defend an insured is more extensive than the duty to indemnify the insured. Travelers Indem. Co. of Am. v. Moore & Assocs., Inc., 216 S.W.3d 302, 305 (Tenn. 2007). Tennessee courts have held that:

[W]hether a duty to defend arises depends solely on the allegations contained in the underlying complaint. Accordingly, the insurer has a duty to defend when the underlying complaint alleges damages that are within the risk covered by the insurance contract and for which there is a potential basis for recovery. The duty to defend arises if even one of the allegations is covered by the policy. The duty to defend is broader than the duty to indemnify because the duty to defend is based on the facts alleged, while the duty to indemnify is based upon the facts found by the trier of fact. Any doubt as to whether the claimant has stated a cause of action within the coverage of the policy is resolved in favor of the insured.

Travelers Indem. Co. of Am., 216 S.W.3d at 305 (internal citations omitted).
In interpreting an insurance policy, the opinion of the Tennessee Supreme Court in *Travelers Indem. Co. of Am. v. Moore & Assoc.*, Inc., is instructive. *Travelers Indem. Co. of Am.*, 216 S.W.3d at 305-07. The Court in *Travelers Indem. Co. of Am.* held that when an insurance contract at issue is a CGL, the “insuring agreement” should be construed before the “exclusions” to avoid confusion or error. *Id.* at 306. Generally, the interpretation of insurance contracts is governed by the same rules of interpretation used in other contracts. *Id.* at 306-07. Further, an insurance contract must be interpreted fairly and reasonably, affording the language its usual and ordinary meaning. *Id.* at 306. Insurance policies should also be construed as a whole in a reasonable and logical manner. *Id.*

**B. Occurrences that Trigger Coverage**

The starting point for an analysis of whether there is an “occurrence” under a policy is the policy language and any applicable exclusions.

Interpreting one “occurrence” policy, the Tennessee Supreme Court has stated that “[a]n ‘occurrence policy’ is a policy in which the coverage is effective if the negligent act or omitted act occurs within the policy period, regardless of the date of discovery.” *See State of Tenn. ex rel. McReynolds v. United Phys. Ins. Risk Retention Group*, 921 S.W.2d 176, 177 n.1 (Tenn. 1996).

If a policy is ambiguous as to when an injury must occur to be covered, then “Tennessee law requires that ambiguities of this nature must be resolved in favor of the insured.” *Am. Justice Ins. Reciprocal v. Hutchison*, 15 S.W.3d 811, 815 (Tenn. 2000).

In a case involving a tree which fell onto an apartment building killing a girl, the Sixth Circuit held that even though the tree fell three months after the owner had cancelled the insurance contract and sold the apartment building, the occurrence of negligence, not the injury, occurred during the coverage period. This decision was based on ambiguous language of the contract which covered “bodily injury … caused by an occurrence which takes place… during the policy period.” *State Farm Fire and Cas. Co. v. McGowan*, 421 F.3d 433, 438 (6th Cir. 2005) (applying Tennessee law). The Court went on to say that “even though an injury must manifest itself in order to trigger [the insuror’s] obligation to defend [the insured], the policy requires only that the occurrence must take place during the policy period, not the resulting injury.” *Id.*

**C. Bodily Injury**

The extent to which bodily injury will be covered by a CGL policies will be governed by the language of the policy.

In interpreting one CGL policy, the court found that the word “disease”, unrestricted by anything in the policy, included diseases of the mind as well as the body. *Am. Indem. Co.*
D. Property Damage:

The extent to which property damage is covered will also be determined by the language of the policy.

E. Defective Workmanship

Defective workmanship by the insured is usually excluded from coverage under the “Your Work” exclusion of a CGL policy. See, e.g., Vernon Williams & Son Const., Inc. v. Cont’l Ins. Co., 591 S.W.2d 760, 765 (Tenn. 1979) (stating that “the standard comprehensive general liability policy does not provide coverage to an insured-contractor for a breach of contract action grounded upon faulty workmanship or materials, where the damages claimed are the cost of correcting the work itself”). Some policies include the work performed by a subcontractor under the “Your Work” exclusion, while others do not. It is important to read the policy and exclusions carefully to determine the parameters of the “Your Work” exclusion.

If an insured’s work causes damage to existing construction or the work of another, the “Your Work” exclusion generally does not apply.

XV. MECHANICS’ AND MATERIALMEN’S LIENS

A. Introduction and Threshold Requirements

The statutory requirements for obtaining mechanics’ and materialmen’s liens (collectively, “mechanics’ liens”) are set forth under Tenn. Code Ann. §§ 66-11-101 et seq. As a threshold matter, the statute states that mechanics’ liens are available “on any lot or tract of real property upon which an improvement has been made by a prime contractor and any remote contractor. The lien shall secure the contract price.” Tenn. Code Ann. § 66-11-102(a).

The statute defines “real property” broadly to include “real estate, lands, tenements and hereditaments, corporeal and incorporeal, and fixtures and improvements thereon.” Tenn. Code Ann. § 66-11-101(13).

The statute also provides a detailed definition of the term “improvement” under Tenn. Code Ann. § 66-11-101(5). To make an “improvement,” the statute requires the claimant to furnish materials or labor and make a permanent change to the real property. See generally id.

B. Attachment of the Mechanics’ Lien
Under the statute, mechanics’ liens “shall attach and take effect from the time of the visible commencement of operations, excluding, however, demolition, surveying, excavating, clearing, filling or grading, placement of sewer or drainage lines, or other underground utility lines or work preparatory therefor, erection of temporary security fencing and the delivery of materials therefor.” Tenn. Code Ann. § 66-11-104(a).

If, however, “there is a cessation of all operations at the site of the improvement for more than ninety (90) days and a subsequent visible resumption of operations, any lien for labor performed or for materials furnished after the visible resumption of operations shall attach and take effect only from the visible resumption of operations.” Tenn. Code Ann. § 66-11-104(b).

C. Prime Contractor vs. Remote Contractor

After determining whether an “improvement” has been made to “real property” and that a lien has “attached,” the next factor to consider is whether the individual and/or entity claiming the lien is a prime contractor or a remote contractor. The distinction is important not only because remote contractors have to undertake additional steps to perfect the mechanics’ lien, but also because the statute limits the type of property subject to a remote contractor’s lien.

Under the statute, a prime contractor is a “person . . . in direct privity of contract with an owner” and can include “any person . . . who supervises or performs work or labor or who furnishes material, services, equipment, or machinery in furtherance of an improvement.”

In contrast, a remote contractor is a “person . . . who provides work or labor or who furnishes material services, equipment or machinery in furtherance of any improvement under a contract with a person other than an owner.” Tenn. Code Ann. § 66-11-101(14). A remote contractor cannot obtain a lien on “contracts to improve residential property.” Tenn. Code Ann. § 66-11-146(a)(2). Residential property is defined under the statute as being property “consisting of one (1) dwelling unit intended as the principal place of residence of a person or family.” Tenn. Code Ann. § 66-11-146(b)(1)(A). If, however, a prime contractor is the owner of the residential property, the subcontractors and suppliers who contract with the prime contractor are entitled to obtain mechanics’ liens on the property. Tenn. Code Ann. § 66-11-146(a)(2).

D. Priority and Enforcement – Prime Contractors

1. Perfection of a Prime Contractor’s Lien

A prime contractor does not have to serve or record any notice regarding the lien under the statute. A prime contractor should, however, record the lien to place subsequent purchasers and/or encumbrancers for value on notice of the lien. See Tenn. Code Ann. § 66-11-111.
A prime contractor has two methods available to record the lien, thus ensuring priority. First, the statute provides that “[w]here the lienor’s contract is in writing, and has been acknowledged, or in lieu of acknowledgement is sworn to by the prime contractor as to its execution by the owner, it may be recorded in the lien book in the register of deeds of the county where the real property, or any part of the affected real property, lies.” Id. Second, the lienor who has not recorded the contract under Tenn. Code Ann. § 66-11-111 “is required to record in the office of the register of deeds of the county where the real property, or any part affected lies, a sworn statement of the amount for, and a reasonably certain description of the real property on, which the lien is claimed.” Tenn. Code Ann. § 66-11-112(a). The lienor opting to record under Tenn. Code Ann. §66-11-112(a) must record “no later than ninety (90) days after the date the improvement is complete or is abandoned.”

The statute provides a form “Notice of Lien” that a lienor can use under Tenn. Code Ann. § 66-11-112(d). A copy of the statutory form “Notice of Lien” is also attached as Appendix A.

2. Enforcement of a Prime Contractor’s Lien

In order to enforce the lien, a prime contractor must file a verified complaint in a court of law or equity or in a court of general sessions setting seeking issuance of an attachment. Tenn. Code Ann. § 66-11-126. The clerk of the court will require the “plaintiff or the plaintiff’s attorney to execute a bond with a sufficient surety payable to the defendant or defendants in the amount of one thousand dollars ($1,000) or the amount of the lien claimed, whichever is less.” Id.

A prime contractor must enforce the lien in a court of competent jurisdiction within the applicable period of time, which is one (1) year of the completion of the work. The statute, however, does not require attachment to be issued by a Court within the one (1) year time period. See Tenn. Code Ann. § 66-11-126(3) (stating that “an action . . . is timely filed if a suit seeking the issuance of an attachment is filed within the applicable period of time, even if the attachment is not issued or served within the applicable period.”); see also Tenn. Code Ann. § 66-11-106 (stating that the applicable period of time to enforce a prime contractor’s lien is “one (1) year after the date the improvement is complete or is abandoned.”)

E. Priority and Enforcement – Remote Contractors

1. Perfection of a Remote Contractor’s Lien – Notice of Non-Payment

To perfect a lien, “[e]very remote contractor with respect to an improvement, except one-family, two-family, three-family and four-family residential units,
shall serve, within ninety (90) days of the last day of each month in which work or labor was provided or materials, services, equipment or machinery furnished and for which the remote contractor intends to claim a lien . . . a notice of nonpayment . . . to the owner and prime contractor in contractual privity with the remote contractor if its account is, in fact, unpaid.” Tenn. Code Ann. § 66-11-145(a). The statute outlines the necessary information required in the notice and also provides a form “Notice of Non-Payment” under Tenn. Code Ann. § 66-11-145(d). A copy of the statutory “Notice of Non-Payment” form is also attached as Appendix B. A remote contractor who fails to provide notice under 66-11-145(a) loses the right to claim a lien for the month in question. Tenn. Code Ann. § 66-11-145(b).

2. Perfection of a Remote Contractor’s Lien – Notice of Lien and Recording of Notice of Lien

In addition, the remote contractor must serve a Notice of Lien in writing on the owner of the property on which the remote contractor made improvements within ninety (90) days after the days after the date of improvement is complete or is abandoned. Tenn. Code Ann. § 66-11-115(a)(2) (citing Tenn. Code Ann. § 66-11-112(a)). The notice of the lien can be in substantially the same form as set forth in Tenn. Code Ann. § 66-11-112(d), a copy of which is attached as Appendix A.

Like the prime contractor, the remote contractor must also record the Notice of Lien pursuant to the requirements set forth under Tenn. Code Ann. § 66-11-112(a) to preserve priority:

[T]he lienor . . . is required to record in the office of the register of deeds of the county where the real property, or any part affected, lies, a sworn statement of the amount for, and a reasonably certain description of the real property on, which the lien is claimed . . . . Recordation is required to be done no later than ninety (90) days after the date of improvement is complete or is abandoned.


3. Enforcement of Remote Contractor Lien

Like prime contractors, remote contractors must file a verified complaint in a court of law or equity or in a court of general sessions setting seeking issuance of an attachment to enforce the lien. Tenn. Code Ann. § 66-11-126. The clerk of the court will require the “plaintiff or the plaintiff’s attorney to execute a bond with a sufficient surety payable to the defendant or defendants in the amount of one
thousand dollars ($1,000) or the amount of the lien claimed, whichever is less.”

A remote contractor must enforce the lien in a court of competent jurisdiction within the applicable period of time, which is ninety (90) days from the date of service of notice in favor of the remote contractor. The statute, however, does not require attachment to be issued by a court within the ninety (90) day time period. See Tenn. Code Ann. § 66-11-126(3) (stating that “an action . . . is timely filed if a suit seeking the issuance of an attachment is filed within the applicable period of time, even if the attachment is not issued or served within the applicable period”); see also Tenn. Code Ann. § 66-11-115(b) (stating that “the lien shall continue for the period of ninety (90) days from the date of service of notice in favor of the remote contractor, and until the final termination of any suit for its enforcement properly brought . . . within that period”)

F. Other Considerations

1. Bond to Discharge the Lien


If the owner records a payment bond totaling one hundred percent (100%) of the prime contractor’s contract price, attachment of the real property is unnecessary and the lien is enforced by acting on the bond. Tenn. Code Ann. §§ 66-11-124, 126(5).

2. Notice of Completion

In order to protect the owner or purchaser of improved real property against unrecorded liens, the statute allows the owner to record a Notice of Completion in the office of the register of deeds in the county where the real property or any affected part of the real property is located. Tenn. Code Ann. § 66-11-143. The statute provides a form “Notice of Completion” under Tenn. Code Ann. § 66-11-143(g). A copy of the form “Notice of Completion” provided under the statute is also attached as Appendix C.

The owner is required to serve a copy of the Notice of Completion on the prime contractor, except such notice is not required when the owner acts as general contractor. Tenn. Code Ann. § 66-11-143(a). The owner is also required to serve a copy of the Notice of Completion on any remote contractor that has served a Notice of Non-Payment. Tenn. Code Ann. § 66-11-143(d).
3. Release of Lien

“If a lienor whose lien has been forfeited, expired, satisfied or adjudged against the lienor in an action on the lien, fails to cause the lien provided by this chapter to be released within thirty (30) days after service of written notice demanding release, the lienor shall be liable to the owner for all damages arising therefrom, and costs, including reasonable attorneys’ fees, incurred by the owner.” Tenn. Code Ann. § 66-11-135(a).

XVI. RETAINAGE UNDER THE PROMPT PAY ACT

A. Introduction and Amount of Retainage Required

The Prompt Pay Act of 1991 (“Prompt Pay Act” or the “Act”) was created to allow contractors, subcontractors, laborers, and materialmen a mechanism to sure that they are paid for their services and/or materials within a reasonable time. Tenn. Code Ann. §§ 66-34-101 et seq. Under the Prompt Pay Act, all construction contracts on any project in Tennessee both public and private, allow the owner to withhold up to five percent (5%) of the gross amount of the contract, which is typically released once the project is complete or after substantial completion of the project. Tenn. Code Ann. § 66-34-103.

B. Releasing the Retainage

“The owner, whether public or private, shall release and pay all retainages for work completed pursuant to the terms of any contract to the prime contractor within ninety (90) days after completion of the work or within ninety (90) days after substantial completion of the project for work completed, whichever occurs first.” Tenn. Code Ann. § 66-34-103(b). The work is completed when the scope of the work and all terms and conditions of the contract are provided. Id. The prime contractor is required to pay all retainage due any subcontractor within ten (10) days after receipt of the retainage from the owner. Id. Further, “any subcontractor receiving the retainage from the prime contractor shall pay to any subsubcontractor or material supplier all retainages due the subsubcontractor or material supplier within ten (10) days after receipt of the retainages.” Tenn. Code Ann. § 66-34-103(b).

C. Funding the Retainage:

If any prime construction contract is valued at $500,000 or greater, compliance with the requirements of Tenn. Code Ann. § 66-34-104 may not be waived by contract. Tenn. Code Ann. § 66-34-104(g)-(h). Under that section of the Prompt Pay Act, retainage must be deposited in a third-party interest-bearing escrow account, which, upon deposit, becomes the sole property of the contractor to whom the funds are owed. Tenn. Code Ann. § 66-34-104(b). At the time of the deposit of the retained funds, the funds become by law the sole and separate property of the prime contractor or remote contractor to
whom they are owed. *Id.* If the contractor fails to fulfill its duties under the contract, the party depositing the funds may divest the contractor of his right to the funds and use the funds to cure any breach. *Id.*

As amended in 2009, failure to abide by the provisions of the Prompt Pay Act may subject violators to daily fines of up to $3,000, claims for attorney’s fees, and even criminal penalties, including, a Class A misdemeanor. Tenn. Code Ann. § 66-34-103(e).

D. Relief under the Prompt Pay Act:

For a party, such as an unpaid contractor, to seek relief under the Prompt Pay Act, it must comply with the statutory notice requirements. Tenn. Code Ann. §§ 66-34-601 et seq. An unpaid contractor must serve notice upon the party failing to make payment of the provisions of the Prompt Pay Act and of its intent to seek relief under the statute. Tenn. Code Ann. § 66-34-602(a)(1). This notification must be submitted by registered or certified mail, with return receipt requested. Tenn. Code Ann. § 66-34-602(a)(2). If the notified party fails to make payment or give legal justification for its non-payment within ten (10) calendar days after receipt of such notice, then the unpaid contractor may file suit in chancery court in which the real property is located for the sum due as well as equitable relief. Tenn. Code Ann. § 66-34-602(a)(3).

Notably, if a plaintiff contractor files suit before the ten (10) calendar day waiting period expires, the right to seek remedies under the Prompt Pay Act will be lost. *Id.* The notified party can foreclose the contractor’s right to remedies under the Act by either: 1) submitting payment for the disputed amount within ten (10) days, or 2) sending notice setting forth “adequate legal reasons” for failing to make payment under the contract. Tenn. Code Ann. § 66-34-602(a). A copy of the statutory form “Prompt Pay Act Notice” is also attached as Appendix D.

If a construction contract does not provide for the remedies of interest and attorney’s fees, the Act may be the sole basis for the contractor to recover these expenses. Tenn. Code Ann. §§ 66-34-601, -602.

E. Limitations to the Prompt Pay Act

There are limitations on the applicability of the Prompt Pay Act. For example, the Act does not apply to residential construction contracts, including improvements to property containing one to four single-family dwellings. Tenn. Code Ann. § 66-34-702. Further, an owner or third party holding the funds dedicated for construction must hold these sums in trust for the benefit and use of the contractor. Tenn. Code Ann. § 66-34-205. This requirement does not apply to the State of Tennessee, including its departments, boards or commissions, or to any institution of higher education, oral contracts or “any bank, savings bank, savings and loan association, industrial loan and thrift company, other regulated financial institution or insurance company.” Tenn. Code Ann. §§ 66-34-201, -301, -401, -501, 703.
APPENDIX A

NOTICE OF LIEN

State of __________
County of __________

______ being first duly sworn, says that ________, the Lien Claimant, furnished certain material or performed certain work or labor in furtherance of improvements to the real property hereinafter described, in pursuance of a certain contract, with ________, [the owner, prime contractor, remote contractor, or other person, as the case may be]. The first of the work or labor was performed or the first of the material, services, equipment, or machinery was furnished on the __________ day of __________, ___ (year). The last of the work or labor was performed or the last of the material, services, equipment, or machinery was furnished on the __________ day of ___, __________ (year), and there is justly and truly due Lien Claimant therefor from ________, [the owner, prime contractor, remote contractor, or other person, as the case may be] over and above all legal setoffs, the sum of _________ dollars, for which amount Lien Claimant claims a lien under Tenn. Code Ann. §§ 66-11-101 et seq. on the real property, of which ________ is or was the owner, which is described as follows:

____________________________________________
____________________________________________
____________________________________________
____________________________________________

_____________________
Lienor

[Notary Acknowledgment]

Tenn. Code Ann. § 66-11-112(d)
APPENDIX B

NOTICE OF NON-PAYMENT

TO: ___________________ [Contractor] ___________________ [Owner]

________________ Contracting ___________________

________________ w/ Owner] ___________________

______________ ___________________

Pursuant to Tenn. Code Ann., § 66-11-145, notice is hereby given that __________ [Lienor] has not been paid for certain labor, materials, services, equipment, or machinery it supplied in the __________ [description of work] of the __________ [description of project], located at __________ [description of property].

The amount presently due and owing is $__________. The last date labor, materials, services, equipment, or machinery were provided in connection with the improvements was __________[date].

You may send any communications regarding this matter to the following name and address:______________________________________________.

_________________

Lienor
Dated: ___________________

This Instrument prepared by:

Name _____________________
Address ___________________
_________________________

NOTICE OF COMPLETION

Legal name of owner or owners of the real property:
______________________________________________________________________________

Names of all applicable prime contractors:
______________________________________________________________________________

The location and description of the real property:
______________________________________________________________________________
______________________________________________________________________________
______________________________________________________________________________

Date of completion of the entire improvement:
______________________________________________________________________________

A transfer of ownership of all or part of the real property or an interest therein and encumbrance thereon or a settlement of the claims of parties entitled to the benefits of Title 66, Chapter 11 of the Tennessee Code Annotated will take place not less than ten (10) days after the date of the recording of this Notice of Completion; provided, that the ten-day expiration for lien claimants shall only apply to contracts for improvements to or on real property for one-family, two-family, three-family, and four-family residential units. On all other contracts for improvement to or on real property, the expiration time for lien claimants shall be thirty (30) days after the date of the recording of this Notice of Completion. The name and address of the person, firm, or organization on which parties entitled to the benefits of Title 66, Chapter 11, may serve notice is as follows:
Name:

_____________________________________________________________________________

Street Address:

_____________________________________________________________________________

City:

______________________________________________________________________________

State: Zip Code:

________________________________________ _________________________

Dated this the _____ day of ______________________________, 20___

Signature

________________________________________________________

(Check One)

___________________________________, Owner

___________________________________, Purchaser

___________________________________, Prime Contractor

Tenn. Code Ann. § 66-11-143(g)
APPENDIX D

NOTICE OF PROMPT PAY ACT

You have failed or refused to pay the sums owing of $_______ to [Contractor]. Your failure to promptly pay [Contractor] is a violation of the provisions of the Prompt Pay Act of 1991, Tenn. Code Ann. §§ 66-34-101 et seq. This letter will serve as demand pursuant to the Prompt Pay Act of 1991 that you remit payment in the amount of $_______.

If payment is not received within 10 days from the date of this letter, [Contractor] will consider the lack of payment to be in bad faith, and will seek all remedies available at law or equity, including those found in the Prompt Pay Act of 1991.

Tenn. Code Ann. § 66-34-602