

Waivers and Releases in Construction Contracts: Drafting Guidance

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Contractors and subcontractors are typically required to provide lien and claim waivers and releases as part of the payment process on a construction project. Often these releases are not properly drafted and disputes arise concerning whether claims have been waived. This Practice Note provides guidance to all construction project participants for drafting unambiguous waiver and release forms and using these documents to ensure that they are enforced as intended if disputes arise.

Contractors and subcontractors are typically required to provide lien and claim waivers and releases in connection with their receipt of progress payments and final payment. However, significant and costly disputes concerning the scope, application, and enforcement of claim waivers and releases provided by contractors and subcontractors in return for progress or final payments are a common occurrence in the construction industry. Rarely is there a claim for additional compensation where the party from which payment is sought does not attempt to avoid payment by contending that the claim or some portion of it was forfeited by a release or waiver executed by the claimant during construction of the project.

While well-drafted construction agreements require contractors and subcontractors to execute lien and claim waivers or releases in return for progress payments and final payment, too often these forms are:

- Poorly drafted.
- Incorrectly or arbitrarily used.
- Executed by project personnel that do not understand the potential consequences of signing these documents.

This Practice Note provides guidance for all construction participants on how to properly draft and use a waiver and release form that achieves the desired result of bringing finality to a payment or claim. It also provides guidance to contractors and subcontractors on how to properly preserve claim rights they did not intend to waive or release when executing these forms.

REASONS TO OBTAIN WAIVERS AND RELEASES

As a project is constructed and contract funds are disbursed, project owners rely on executed waivers or releases to:

- Manage financial risk.
- Reduce potential claims exposure.

However, when forms are poorly drafted or improperly used, there is no certainty that claims believed to have been resolved may not resurface later in the project. At that point, it is more difficult, if not impossible, to mitigate or plan for extra costs.

Contractors and subcontractors frequently do not understand or choose to ignore the import of waivers and releases, often believing they are merely acknowledging receipt of payment. Depending on the form's specific language, however, erroneous execution of a release or waiver can result in devastating consequences, including forfeiture of valid claims, even where contractually compliant notices of claim were previously issued.

Contractors and subcontractors must never rely on unwritten "understandings" or verbal "side agreements" that purport to reserve the right to pursue claims not specifically identified as reserved in these forms. Otherwise they run the risk that:

- Representatives of owners or upper-tier contractors later forget or simply ignore the undocumented agreements years later.
- Owners or upper-tier contractors argue that claims are barred by contract language that requires preservation of claim rights be memorialized in writing to be excluded from broadly drafted claim waivers.
- Owners or upper-tier contractors contend that their project representatives lacked the authority to vary the terms of a written agreement.
- Witnesses needed to corroborate verbal agreements are no longer available.
- A court or arbitrator summarily rejects the undocumented claims because the contract language requires written notice for a claim to be reserved.

Understanding the issues and implementing proactive measures can make the use of claim waivers more effective and reduce disputes. Parties required to execute claim waivers may also benefit by using the process to update claim details and provide supplemental claim notices (see A Tool to Update Claim Reporting).



WAIVERS AND RELEASES UNDER STATE LAW

There are generally three types of waivers or releases that can be issued during the progress of a project:

- A general waiver and release of any and all claims related to the project.
- A waiver of the statutory right to file a mechanic's lien or other construction lien.
- A waiver of the right to seek compensation for unpaid claims from the surety if a payment bond was issued for the project.

CONTRACTUAL WAIVERS

General claim waivers are typically enforced according to their express terms. Courts and arbitrators customarily consider a release to be a negotiated agreement, voluntarily entered into between sophisticated, commercial parties. As a result, courts and arbitrators routinely enforce the unambiguous terms of a claim release.

In most states, courts treat with disfavor any contractual provision that attempts to create a forfeiture of valid claims and strictly construe ambiguous language in a waiver or release in a manner that preserves claims. Accordingly, the party attempting to enforce a release or waiver must ensure that the language in the form is clear and unequivocal (see *Use Clear and Unambiguous Language*).

WAIVERS OF STATUTORY RIGHTS

Applicable law concerning waiver of statutory lien rights and payment bond claims varies significantly from state to state. Some states have strict guidelines and even specify forms, language, or font requirements that must be used to make waivers enforceable. In states that regulate waiver of potential claims, failure to strictly comply with the requirements of those laws usually renders the waiver or release unenforceable.

Most states outright prohibit waiving lien rights in advance of performing the work, usually finding such waivers to be void as against public policy.

There are valid reasons for increased scrutiny of waivers on construction projects. The public purpose for statutory liens and statutorily-required payment bonds is to provide contractors and subcontractors with additional security for payment. Any attempt by contract to restrict a party's ability to file a lien or make a claim against a mandated payment bond negates that purpose and encroaches on legislative authority.

IDENTIFY ALL REQUIREMENTS

If claim waivers or releases are used on a project, the construction contract should include specific language concerning the requirement for and consequences of executing the forms without reserving rights to claims, even if previously noticed. The contract should provide all details regarding the parties required to execute the waivers and when the waivers must be submitted. The waiver and release forms should also be attached as exhibits to the contract.

Waiver and release forms are often required as part of a complete payment application entitling a contractor or subcontractor to be paid. They are commonly executed and submitted before payment is issued. If so, the form should include language that states that the claim waiver being provided does not become effective unless and until the related payment is actually received.

Progress payments are typically issued based on the percentage completion of contractually compliant work, not for executing claim waivers (see Practice Note, *Payment Provisions in Construction Contracts: Drafting Guidance, Payment Application Process* (<http://us.practicallaw.com/1-568-1506>)). If the contract does not specifically require the contractor or subcontractor to execute a claim waiver or release as a condition of payment, arguably no legal "consideration" has been provided to the releasing party for executing the waiver. Unless the contract provides otherwise, the payment is due based solely on the completion of the work.

When the contract dictates that payment is to be made only on completion of the related work and submission of a contract-compliant payment application that includes the claim waiver or release, execution of the waiver becomes part of the scope of work. In other words, payment of the contract funds then serves as consideration for requiring the contractor or subcontractor to execute the claim release.

Including well-drafted, detailed claim waiver requirements in the construction contract also helps to reduce later allegations of ambiguities concerning the purpose, use or scope of the required waivers or releases. When tasked with interpreting these documents, courts and arbitrators often must decide whether the document was intended as one or more of the following:

- A simple acknowledgement of receipt of a specific payment amount.
- A waiver of statutory lien rights.
- A waiver of the right to make a claim against a payment bond.
- A complete waiver and release of all claims through the date of the release (or alternatively, only for the work for which payment is being made).

Like all contract documents, if there is an ambiguity, it is typically construed against the party that drafted the waiver or release form. Therefore, the party that drafts the form and seeks to limit claims through its use should ensure that the form is drafted as clearly as possible.

More sophisticated construction agreements link the waiver and release forms to contractual notice of claim requirements. For example, in addition to independent claims notice provisions, the contract may provide that all claims that are not specifically reserved or noted as exceptions in the progress payment releases, including those for which notice has been provided, are automatically waived. This reinforces the intended consequences of a party failing to reserve claims in the waiver or release forms.

USE CLEAR AND UNAMBIGUOUS LANGUAGE

If the language in a proposed release or waiver form is not perfectly clear, it should not be used. This is another reason for attaching copies of the forms to the contract documents. For the benefit of all parties, any issues concerning the forms' language should be resolved before contract execution. In practice, these forms are not commonly reviewed until the first payment becomes due.

From the owner's perspective, the forms should do more than just acknowledge that the releasing party (contractor or subcontractor) has received a specific progress payment and waives any right to file a mechanic's or construction lien for the amount received or to be received.

The form should instead unequivocally state that the party executing the release waives any and all claims related to or arising out of the project in any way **except** for those claims specifically identified. The release or waiver should specifically apply to either:

- All claims up to the date the release is executed.
- All claims associated with the work for which a related payment is being issued.

Where the releasor is also waiving or releasing the right to file a claim against the payment bond or the right to file a statutory lien, the form should clearly and conspicuously say so, both in the title and in the body of the document. Again, counsel should confirm that the form's language strictly complies with any state-specific requirements in the state where the project is located, regardless of any contrary choice of law provisions.

The clearer the language, the more difficult it is for:

- The releasing party to argue that it did not understand:
 - what it was executing or the resulting legal consequences; or
 - in the alternative, that its execution did not legally cause a waiver of the disputed claims.
- The party being released to argue that the document waived claims that were not expressly included in the release.

The form should also identify all individuals or entities that are being released from potential liability for claims, including all lenders and owner-related parties. A court or arbitrator likely assumes that the parties did not intend for the release to benefit anyone not specifically identified in the claim release.

Claim waivers and releases are generally judicially interpreted based solely on their plain language. In most jurisdictions, a court or arbitrator is not permitted to rewrite, ignore or add additional terms to an unambiguous document. Where terms are ambiguous, the language may be interpreted, at least in part, based on the hindsight arguments advanced by legal counsel, as opposed to the parties' original intentions.

SPECIFY CLAIMS NOT RELEASED OR WAIVED

Claim release or waiver forms often do not provide a space for the releasing party to identify claims that are not being released. Some forms do not even reference the releasing party's right to reserve claims. This should not, however, deter a contractor or subcontractor from reserving its claim rights. If there is little or no space provided, the releasing party should add a statement to the form incorporating an attached schedule that expressly identifies all claims the releasing party does not intend to release or waive.

An example of such language can be:

The claims identified on the attached schedule are not being released or waived by the undersigned's execution of this release. All rights to the claims identified in the attached schedule are specifically reserved notwithstanding the undersigned's receipt of payment or anything stated to the contrary in this release.

Contractors and subcontractors must take full advantage of their right to reserve unresolved claims despite the use of an overly-broad waiver or release form. They should not be deterred by concerns of antagonizing an upper-tier party. The failure to reserve claim rights can result in outright forfeiture of potentially valid claims and have significant financial implications.

A TOOL TO UPDATE CLAIM REPORTING

No one voluntarily waives claims rights, especially on a construction project where participants are often uncertain at any specific point in time whether viable claims exist. Even when claim waivers or releases are required, the process should be proactively managed and carefully supervised by designated project personnel. If properly used, required waiver and release forms can actually benefit the releasing party by:

- Providing an opportunity for the contractor or subcontractor to update its claim notices.
- Helping to ensure that the contractor or subcontractor complies with any contractual supplemental claim notice requirements.

Often claims are not properly reserved in these forms or timely noticed simply because no one at the project level wants to address them. Claims interrupt productivity and create conflict. Required periodic claim waivers, however, absolutely mandate aggressive management of the claims process or the contractor or subcontractor risk a forfeiture of its claims.

Therefore, it is crucial that the party required to provide the release or claim waiver identify a specific member of the project team authorized to execute the document. That individual should be fully informed of all potential and noticed claims as well as all contractual claim notice requirements. Preferably, the designated individual is also involved in:

- Initially noticing and documenting all claims.
- Ongoing negotiation and resolution of claims.

Mistakes are frequently made because these forms are hastily executed to meet a progress payment submission deadline or to collect an overdue payment. If the individual designated to execute the release form is also actively involved in the overall claim process, mistakes are less likely to occur.

Many contracts also require that claims be periodically updated through supplemental claim notices as:

- Additional information is obtained.
- The scope of work or anticipated costs change.
- Preliminary estimates are replaced by final scope of work or costs.

Unless the contract requires separate claims notices and updates be submitted in a particularized format, there is no reason why the schedule of claims excluded from a waiver or release form cannot also serve as an updated notice of all outstanding claims, including any changes to the claims as initially filed.

If the contract contains specific requirements for supplemental claim notices, such as a certification by the submitting party, the schedule of reserved claims should be modified accordingly to match those requirements. A reservation of rights to amend claims "as additional information becomes available" should always be included in the description of each claim unless the claimant is certain that all costs or impacts have been finalized and quantified.

From the owner's prospective, parties requiring timely claims notices and the execution of claim waivers or releases should carefully examine updated claims information to ensure changes relate only to the original claim, as opposed to creating an independent claim that should have previously been noticed or has already been waived.

Most courts and arbitrators enforce unambiguous contract requirements. Therefore, all parties should carefully review the contract documents to ensure that:

- All specified notice requirements have been timely issued.
- The required notices have been issued to the correct parties.
- Any and all required claim details are provided in the exact format required including good faith estimates of the claim, even if difficult to ascertain or subject to change.

The same guidelines apply to final payment applications. The contractor or subcontractor must ensure that it has submitted all contractually-required close-out documents and information (see Practice Note, Payment Provisions in Construction Contracts: Drafting Strategies, Final Payment (<http://us.practicallaw.com/1-568-1506>)). Inadvertent waiver of claims can and often do result from a party's failure to meet all close-out requirements, especially where the contract is with a governmental entity.

If the document submitted is intended to serve dual or multiple purposes, that intent should be clearly indicated in the title or heading of the document or in the reference line if provided in letter form. For example, if the document is being used to supplement a previously served notice of claim and to identify additional claims for which rights are reserved, it should be labeled "New and Supplemental Notice of Claims for Which All Claim Rights are Reserved."

Contractual notice of claim requirements are often (perhaps intentionally) complicated and compliance can be difficult. This is particularly true where the contract provides short deadlines for providing notice after learning of the cause or resulting impact of the claim (see Practice Note, Changes in the Work: Drafting Strategies for Construction Contracts, Notice of the Change in Work (<http://us.practicallaw.com/5-573-5705>)). Even if the initial notice of claim failed in some way to comply with the contract requirements or deadline, if claim details are regularly updated and repeatedly re-noticed, it is less likely that a court or other tribunal may later bar the entire claim for failing to strictly comply with the contract's initial notice of claim provisions.

CHECKLIST OF REQUIREMENTS

For a claim waiver or release to be clear and unequivocal, the following items should be confirmed:

- **All statutory requirements for waiver have been met.** Counsel should check statutes for any specific language or font requirements for the waiver or release to be effective. Include a review of the law of the state in which the project is located even if a different choice of state law is specified in the contract.
- **Both the party releasing the claims (releasor) and all parties being released (releasees) have been clearly identified.** The releasor's name should match the contract or subcontract and include a release by the releasor's parents, subsidiaries and affiliates. Identification of the releasees should include:
 - all owners of the real property on which the construction is being performed;
 - any party developing the property or contracting with the builder, if not the same as the owner;
 - any lender that may be responsible by statute for paying for the construction work; and

- all officers, directors, shareholders, members, employees, agents, affiliates, successors and assigns of each named releasee.
- **The releasor owns the lien rights and has not transferred or assigned them to any other party.**
- **The real property being improved by the work of the contractor or subcontractor has been fully described.** This should include:
 - the property address;
 - recording information, such as block and lot numbers;
 - project name; and
 - any name and number assigned to the contract between the owner and contractor.
- **The work that was performed is fully described, including specific contract reference.** This can consist of a general description of the scope of work and refer to a specification section or contract document to describe the work performed during that payment period.
- **The dollar amount paid that is covered by the release.** This should identify both the amount covered by that partial waiver and release of lien and the total amount paid for all work performed to that date.
- **The form describes in broad language the scope of the release of lien rights and waivers of all claims to the date of the release.** The language should expressly confirm that the waiver and release are unconditional, except for any claims that may be reserved.
- **The waiver and release are acknowledged and notarized.** While not required in every jurisdiction, a notarized statement provides additional confirmation of the releasor's intention to release its claims and the consideration for that release. Where the release is being provided on behalf of a business entity, the acknowledgement should identify the name and title of the individual and confirm their authority to bind the entity.

In addition to the clear and unambiguous language meeting these requirements, a contractor or a subcontractor should also confirm that the waiver or release provides an opportunity to exclude open claims from the waiver or release.

If the release form is addressed during contract negotiations and attached as an exhibit, the contractor or subcontractor can confirm that space is provided for claims that are being reserved during each payment cycle (see Specify Claims Not Released or Waived). Even if the intended releasee argues that the form cannot be changed, the contractor or subcontractor has still put the upper-tier party on notice that it intends to reserve open or unresolved claims if they arise during the project.

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