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GETTING PAID: STRATEGIES TO SECURE PAYMENT FOR SERVICES DELIVERED

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While money isn't everything, it is the measure and fuel of any business, including a design firm. Without payment for services firms suffer, starve, and even die. Payment issues are also often the single greatest indicator of a project in trouble. Accordingly, prompt payment for services should always receive the highest attention.

CLIENT SELECTION

As the old saying goes, you cannot get blood from a turnip. Accordingly, appropriate client selection is one of the most important steps in assuring payment for services. Client selection is also one of the first and most important steps in any appropriate risk management plan for a design professional. Nevertheless, it is amazing how many design professionals will become involved with a new client on projects valued at millions of dollars without any real effort to investigate or evaluate that client. It is equally amazing how many firms will return to do business with an existing client who has burned them in the past. Obviously, such an approach is shortsighted, particularly as it relates to the subject of getting paid and making a profit. The most important considerations for client selection should be the following:

1. **Client Expertise/Expectations.** The most important factor in evaluating any prospective client is to establish the client's relative expertise and corresponding expectations. The key is communication. Making certain that the client and design professional share common expectations and that those expectations are realistic **before** beginning work on the project is the

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greatest key to avoiding later problems on the project. Differing and unrealistic expectations are among the most frequent bases for a client's refusal to pay.

2. **Client Track Record.** Whether it is a new client or an existing client, any design firm should investigate the client's track record for payment and litigation. For a subconsultant, this analysis should obviously include both the prime consultant and the owner.

For new clients, as part of getting to know them, their expectations and expertise, ask them about past projects and their experience on those projects. Ask them about both their positive and negative experiences. Such experiences will necessarily impact upon their new relationships on a new project and just as necessarily impact upon how the design professional should proceed. Armed with this information, the design professional can also conduct its own recognizance. Appropriately diligent firms will contact past project participants to check out their experiences. Similarly, with the locating of the past projects, a quick electronic search of court and county records will often reveal if there was litigation on the past projects and if there were problems getting paid.

For existing clients, design firms should review past projects before agreeing to another retention. Was the client fair and did they make timely and complete payments? If not, why not and what steps can be taken to avoid similar issues? These issues should be resolved before the project gets underway. Similarly, design professionals should not automatically assume that because one project went well, others have as well. Design professionals should revisit the original due diligence and make any appropriate updates.

3. **Financial Stability.** Unfortunately, many design professionals somehow feel it is unprofessional to ask a client how a project will be funded and for verification of that funding. On the contrary, the failure to investigate such issues is actually the unprofessional conduct. It is both unwise and unprofessional to get into a project which lacks solid funding to see the project through to completion.

In evaluating such financial stability, design professionals should be wary of unfunded development companies where the contracts are with one company, but the funds reside with another. The design professionals should also investigate the actual ownership of the property. Failure to do so may hamper lien rights and make ultimate collection of payment more difficult. Where multiple entities are involved, the design professional may wish to have those other parties added to the agreement, at least for payment purposes, or seek guarantees from such parties.

CONTRACTUAL PROVISIONS.

The starting point to protect and secure payment of fees is obviously the service agreement. First and foremost, if you do not have a written agreement signed by both sides, you will often have an almost impossible task to secure payment. Assuming that a written agreement is in place, several key provisions have proven critical to securing prompt and appropriate payment:

Early Identification of Disputed Issues. The agreement should provide that the client has a very short time period after receipt of an invoice to identify any disputed portion. For example, the agreement could provide that the client must identify any disputes with the invoice within ten days of receipt or shall be presumed to be in agreement with all portions of the invoice.

Payment of Undisputed Portions. In the event the client does dispute a portion of an invoice, the agreement should provide that they will make prompt payment of all undisputed portions.

Short Payment Durations. Keep the period between receipt of invoice and the date for payment as short as possible. Ideally, payment should be due before the next scheduled invoice to avoid a mounting series of unpaid invoices.

Right to Suspend. Include a provision which provides that, in the event payment of an invoice is not received within the prescribed time period, the professional may suspend services at their option until payment is received and shall be compensated for the expenses of the disruption. However, such a provision is only useful if the professional is willing use it, or at least threaten to use it. Often, design professionals do not use such provisions because they are fearful of liability from the project impacts. Accordingly, the professional should protect against these risks by providing that the client shall defend, indemnify, and hold harmless the design professional from any and all claims, damages, or losses arising out of such a suspension. In this way, the professional is protected not just from the client, but from third parties (such as contractors) as well.

No Setoff. Provide that the client may not back-charge the professional or reduce payments as a setoff to perceived damages arising out of the professional's services. Such setoffs frequently subject the professional to the double impact of lost fees **and** liability payments. Provide that the client may only withhold fees for that portion of the services improperly performed.

Non-Payment Precludes Right to Use Documents. Finally, and often most effectively, the agreement should make the client's right to use the design professional's work product contingent upon full payment of all fees and costs payable under the agreement. In the final analysis, such provisions are often the last and best means to compel an otherwise recalcitrant owner to live up to their obligations and make payment to the design professional.

STATUTORY LIEN PROTECTIONS.

In addition to the contractual provisions, any design professional working on a construction project also has statutory lien protections. Such provisions may often be the most useful tools to securing payment in that it can invoke pressure from third parties such as lenders, investors, and buyers who may demand a "clean title" on the project. Such provisions will vary from state to state. However, the procedures in California are somewhat typical.

In California, design professionals have two possible sources for such liens: the design professional specific lien laws set forth in Civil Code §§ 3081, *et seq.*, and the more generic Mechanic's Lien laws set forth in Civil Code §§ 3082, *et seq.* Which scheme applies and provides the greater tools will vary depending on the project and the circumstances (*i.e.*, what type of project is it and who is the professional's immediate client). Accordingly, each set of statutes should be analyzed within the context of a particular project. However, this analysis **should always be performed at the outset of a project** since some rights may be foreclosed if certain steps and notices are not accomplished at the very outset.

NON-CONTRACTED ADDITIONAL SERVICES.

The best contract, and the most strict adherence to lien laws, often cannot protect the professional against the self-inflicted damage of providing non-contractual additional services. Most often, such services arise in one of two ways: the professional falls victim to "scope creep" and unilaterally provides services beyond the contracted scope, or the professional provides what he or she perceives to be "additional" services, often even at the client's request, without reducing the agreement to provide those additional services and the related payment obligation to writing. When such events occur, the professional and its attorney are often left with few arguments but equity and mercy in order to secure payment. Accordingly, any professional must strive for two standards during the course of a project:

1. Strict adherence to the contractual scope of work.
2. Consistent and thorough written documentation of requests for **and agreements to** additional services. Often, this effort is aided by self-executing provisions which put the onus on the client to say that such additional services are not requested or to be provided.

In general, those statutes provide the following remedies and timelines:

Design Professional Lien

- Unlike Mechanics' Liens, design professional liens may be filed before physical work begins on the project site.
- Requirements:
 1. Direct written contract with landowner.
 2. Building permit or "other governmental approval in furtherance of the work".
 3. Physical work has not commenced.
- Exclusion: Owner occupied residential projects under \$100,000.
- Timing: Lien must be filed no later than ninety (90) days after the design professional knows or has reason to know the owner is not going to build the project.
- Notice: Must give ten (10) days' notice before filing. Notice by registered or certified mail. Therefore, notice is due within eighty days of knowledge that project not to be built.
- Enforcement: Action to enforce must be filed within ninety (90) days of recording of lien.
- Expiration: Earlier of ninety days from recording or start of physical work on project.