TENNESSEE

David A. Draper
LEWIS, THOMASON, KING, KRIEG &WALDROP, P.C.
One Centre Square, Fifth Floor
620 Market Street
Post Office Box 2425
Knoxville, Tennessee 37901
Phone: (865) 546-4646
Fax: (865) 523-6529
Email: ddraper@lewisthomason.com

Bruce Gill
William M. Leech
LEITNER, WILLIAMS, DOOLEY & NAPOLITAN, PLLC
4th & Church Building
201 4th Avenue North, Suite 1100
Nashville, TN 37219
Phone: (615) 324-2730
Fax: (615) 780-2210
Email: bruce.gill@leitnerfirm.com

I. MECHANIC'S AND MATERIALMEN'S LIEN

The purpose of Tennessee Code Annotate § 66-11-101, *et seq*, is to provide prime contractors and remote contractors, who have not been paid for their work, an opportunity to obtain a security interest in the real property for which they have improved. It is important to note that the method for perfecting a lien under this chapter differs depending on whether the claimant is a prime contractor versus a remote contractor.

A. Prime Contractor vs. Remote Contractor

A prime contractor is defined as "a person, including a land surveyor as defined in [Tennessee Code Annotated] § 62-18-102, a person licensed to practice architecture or engineering under title 62, chapter 2, and any person other than a remote contractor who supervises or performs work or labor or who furnishes material, services, equipment, or machinery in furtherance of any improvement; provided, that the person **is in direct privity of contract with an owner, or the owner's agent**, of the improvement. Tenn. Code Ann. § 66-11-101(12) (emphasis added). In contrast, a remote contractor is "a person, including a land surveyor as defined in [Tennessee Code Annotated] § 62-18-102 and a person license to practice architecture or engineering under title 62, chapter 2, 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) (emphasis added).

As you can see, the distinction between the two classes of contractors hinges on whether the contractor is in direct privity of contract of the owner or their agent.

B. Liens by a Prime Contractor

1. Notice of Lien

In order to preserve the priority of a lien where the claimant is a prime contractor, and the claimant has not recorded the applicable contract pursuant to Tennessee Code Annotated § 66-11-111, the claimant must record a Notice of Lien within ninety (90) days after the project is completed or abandoned in the office of the register of deeds of the appropriate county. Tenn. Code Ann. § 66-11-112(a).

2. Statute of Limitations

The prime contractor must file suit within one (1) year of the improvement's completion or abandonment. Tenn. Code Ann. § 66-11-106. But, if the owner submits a written demand requiring the claimant to commence action to enforce their lien, the action shall be commenced within sixty (60) days after service. Tenn. Code Ann. § 66-11-106.

C. Liens by a Remote Contractor

1. Residential Real Property

Before diving into the procedure, please note that remote contractors are prohibited from claiming a lien on residential property. Tenn. Code Ann. § 66-11-146.

2. Notice of Nonpayment

Unlike prime contractors, if their account is unpaid, remote contractors must provide, within ninety (90) days of the last day of the month within the work, services or materials were provided, a notice of nonpayment for such work, services or materials to the owner and the prime contractor upstream from them. The notice shall be served by registered or certified mail, return receipt requested; hand delivery with sworn statement, properly notarized, confirming delivery of written notice; or any other commercial delivery service which can confirm delivery of the notice. It shall contain the information outlined in Tennessee Code Annotated § 66-11-145(a)(1-5).

Failure to provide a notice of nonpayment that complies with Tennessee Code Annotated § 66-11-145 will cause the remote contractor to lose their statutory right to claim a lien under this chapter.

3. Notice of Lien

Within ninety (90) days of the project's completion or abandonment, the remote contractor must first record a notice of lien in the appropriate county as outlined in Tennessee Code Annotated

§ 66-11-112(a) and also serve a notice of lien on the owner of the property improved by the project. Tenn. Code Ann. § 66-11-115(a)(2).

4. Statute of Limitations

The remote contractor must file suit within ninety (90) days from the date notice of lien is served. Tenn. Code Ann. § 66-11-115(b). But, if the owner or prime contractor submits a written demand requiring the claimant to commence action to enforce their lien, the action shall be commenced within sixty (60) days after service. Tenn. Code Ann. § 66-11-106.

C. Enforcement

For the most part, the procedure moving forward is similar regardless of whether the claimant is a prime contractor versus a remote contractor, but differences will be noted.

Pursuant to Tennessee Code Annotated § 66-11-126, "the lien shall be enforce in a court of law or equity by complaint and writ of attachment or in a court of general sessions having jurisdiction by a warrant for the sum claimed and writ of attachment, filed under oath, setting for the facts and describing the real property, with process to be served on the person or persons whose interests the contractor seeks to attach and sell. Tenn. Code Ann. § 66-11-126 (1 & 2). A remote contractor may elect to also serve the complaint or warrant upon the contractor, or subcontractor in any degree, with whom the complainant is in contractual relation. Tenn. Code Ann. § 66-11-126(2). Either way, "the person or persons whose interests the remote contractor seeks to attach and sell shall have the right to make the prime contractor or remote contractor a defendant by third-party complaint or cross-claim . . . ." *Id*.

D. Effect of Filing of Notice of Completion

Fortunately for owners of real property, there is a mechanism available to them to ensure they are protected from lien claims they may not be aware of. Once an improvement to real property is completed, and no sooner, the owner(s) may record a notice of completion in the register of deeds for the appropriate county and shall simultaneously serve a copy of the recorded notice of completion on the prime contractor. Tenn. Code Ann. § 66-11-143(a). The owner(s) only must to serve a copy of the notice of completion on a remote contractor *if* the remote contractor has served a notice of nonpayment, described above and in Tennessee Code Annotated § 66-11-145. Tenn. Code Ann § 66-11-143(d).

If the prime contractor or remote contractor has not registered their contract under Tennessee Code Annotated § 66-11-111 or registered a notice of lien pursuant to Tennessee Code Annotated § 66-11-112 and served a copy of the same to the owner, the contractor shall "serve written notice, addressed to the person firm, or organization and at the address designated in the notice of completion for receiving notice of claim, stating the amount of the claim and certifying the claim does not include any amount owed to the claimant on any other job or under any other contract." Tenn. Code Ann. § 66-11-143(e)(1). If the real property is residential, the written notice shall be served not more than ten (10) days from the date the notice of completion is recorded. Tenn. Code Ann. § 66-11-143(e)(2)(a). Otherwise, the written notice shall be served not more

than thirty (30) days from the date the notice of completion is recorded. Tenn. Code Ann. § 66-11-143(e)(2)(b).

E. Contracting Without a License, and Loss of Lien Rights

A contractor shall only claim a lien under Tennessee Code Annotated § 66-11-101, *et seq*. if it has fully complied with title 62, chapter 6. Tenn. Code Ann. § 66-11-102(a). Contracting, including offering to contract, without a license, or doing so above the limit of one's license, bars the contractor from asserting any lien rights. Tenn. Code Ann. § 62-6-103(c). The statute, and Tennessee case law in this regard, is unforgiving. If deemed in violation of the statute, the contractor can recover only actual documented expenses as shown by clear and convincing evidence. Tenn. Code Ann. § 62-6-103(b). Beginning January 1, 2014, the Contractor's Licensing Board has discretion to, in effect, waive a contractor's violation of the licensing limit provision, but contractors would be well-advised not to rely on such discretion. See Tenn. Code Ann. § 62-6-103(a)(1).

II. Public Project Claims

Public project contracting, and the potential for claims arising out of public projects, requires careful consideration of the government owner's specific authority to contract, as well as the administrative and regulatory scheme by which that authority is lawfully exercised. In Tennessee, a contractor may find itself interacting with any of a number government bodies having authority to contract, including the State Building Commission, a local Public Building Authority, the Department of Transportation, or a local school board. Each of these government bodies is bound by unique regulatory constraints on their authority to contract and their particular method of procurement. Project bonding requirements may also differ. In Tennessee, in cases of public improvement there is no lien on the property for material furnished. Neither is there any liability on the part of the public owner to the party who furnishes such material to the contractor. *Tennessee Supply Co. v. Bina Young & Son*, 142 Tenn. 142 (1919).

A. State and Local Public Work

To guard against payment claims arising from contractor insolvency, Tennessee has enacted a "little Miller Act" that requires the posting of a bond on any public work (except TDOT road projects) in Tennessee for all labor and material used by the contractor and any of its subcontractors. This is called a statutory bond and is found in T.CA. § 12-4-201. Because the bond is statutory, all the requirements of the bond must be followed strictly.

Although the statutory bond provides some protection, it does not provide a requirement for a 100% payment bond. The statutory requirement provides for a payment bond for at least 25% of the contract price on contracts in excess of $100,000.00. However, for projects that fall within the jurisdiction of the state building commission, a 100% payment and performance bond must be executed by the contractor on the state bond form.

1. Notice and Enforcement

In order to file a claim under the statutory payment bond, it is essential to give notice properly and file suit within the statutory time. T.C.A. § 12-4-205 and 206 impose the notice timeline, form, and content. A claim must be filed by notice of claim after the subcontractor, supplier or vendor has furnished labor or materials to the public work project and **within 90 days after completion of the project**. What is not clear from the statutory language is whether the ninety days after completion means ninety days after substantial completion or ninety days after final payout. Notice must be given by either return receipt registered mail or personal delivery. Notice must be given either to the contractor who executed the bond or to the public official in charge of awarding the contract. The written notice of claim must set forth the nature of the claim in an itemized account of the material furnished or labor provided, the balance due and a description of the property that was improved. An action to enforce the claim must be filed within six months following the completion of the public work or following the completion of furnishing of labor or materials.

B. State Highway Projects with TDOT

Bonds related to highway projects administered by the Tennessee Department of Transportation are governed by T.C.A. § 54-5-119, and the remedies and requirements for making a claim on a TDOT bond are different than on other public works projects. Basically, on a TDOT project, claimants have two separate remedies: you can file a claim against the bond of the prime contractor, or you can file a claim with the state of Tennessee against the retainage being held on the project. These are not mutually exclusive remedies and both remedies should be sought simultaneously.

T.C.A. § 54-5-119 requires 100% payment bond for all materials purchased and labor employed on the project.

1. Notice and Enforcement (TDOT jobs)

Under § 54-5-119, you must file suit within one year following the date of the first publication of the notice provided in § 54-5-122, which is the statutory notice that final settlement is about to be made between the state and the general contractor. There is no requirement that you give any type of notice prior to filing suit; however, a notice requirement applies if you also plan to file suit against a surety in addition to filing suit against the contractor. To bring an action against the surety on the original payment bond, you must follow the notice requirements in the particular contract bond form used by TDOT.

C. Claims to Public Funds

Tennessee has not enacted a construction trust fund statute.

III. STATUTES OF LIMITATION AND REPOSE

A. Statute of Limitations

Tennessee has a one-year statute of limitation for personal injury actions (T.C.A. §28-3-104(a)(1)) and a three-year statute of limitations for property damage claims (T.C.A. §28-3-105(1)).

Both the personal injury and property damage statutes begin to run when the cause of action accrues. Under Tennessee law, a cause of action accrues when a plaintiff knew or reasonably should have known that a cause of action existed. *Stone v. Hines*, 541 S.W.2d 598 (1976).

Although Tennessee has a general six (6) year statute of limitations for breach of contract actions, it is clear that under Tennessee law an action for defective construction is subject to the three (3) year statute of limitations as opposed to the six (6) year breach of contract statute (T.C.A. §28-3-109(a)(3). In addition, Tennessee courts consistently look to the "gravamen" of the complaint and not to what the plaintiff calls its cause of action (i.e. either "contract" or "tort") in determining the applicable statute of limitations. *Keller v. Colgems-EMI Music, Inc.*, 924 S.W.2d 357 (1996).

B. Statute of Repose

First, lets distinguish between a statute of limitations and a statute of repose. Tennessee Courts have consistently pointed out the distinction between a statute of limitations and a statute of repose. The Court of Appeals discussed these distinctions in the case Wyatt v. A-Best Prods. Co. [1] The Court noted that a statute of limitations has been described as "affecting only a party's remedy for a cause of action," whereas the "running of a statute of repose has been said to 'nullify both the remedy and the right.'"[2] The critical distinction in classifying a statute as one of repose or one of limitations is the "event or occurrence designated as the 'triggering event,' i.e., the event that starts the 'clock' running on the time allowed for the filing of suit."[3] The Court further noted:

> In a traditional statute of limitations, the triggering event is typically the accrual of the action, i.e., when all the elements of the action, including injury or damages, have coalesced, resulting in a legally cognizable claim. A statute of repose, on the other hand, typically describes the triggering event as something other than accrual, prompting courts to note that such statutes are "entirely unrelated to the accrual of any action. . ." Watts v. Putnam Co., 525 S.W.2d 488, 491 (Tenn. 1975), Cronin v. Howe, 906 S.W.2d 910, 913 (Tenn. 1995).[4] Because a statute of repose sets the triggering event as something other than accrual, it can have the effect of barring a plaintiff's claim before it accrues, most typically before the plaintiff becomes aware of his or her injury. See Cronin, 906 S.W.2d at 913; Bruce, 894 S.W.2d at 276 ("A statute of repose is a substantive provision because it expressly qualifies the right which the statute creates by barring a right

[1] Wyatt v. A-Best Prods. Co., 924 S.W.2d 98, 101, 1995 Tenn. App. LEXIS 770, *1, CCH Prod. Liab. Rep. P14,433. Attached as **Exhibit C**.
[2] Wyatt v. A-Best Prods. Co., at, *6-7.
[3] Id. at *6-7.
[4] Id. at *6-7.

> of action even before the injury has occurred if the injury occurs subsequent to the prescribed time period.") This possibility has prompted courts to hold that statutes of repose affect the substantive right of a party to bring suit, as well as the remedy.[5]

Now that we've fleshed out the difference between a statute of limitation and a statute of repose, lets turn to how this state treats a statute of repose. In Tennessee, T.C.A. §28-3-202 specifically provides that:

> 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.

The term "substantial completion" is defined by statute to mean "that degree of completion of a project, improvement or a specified improvement, or a specified area or portion thereof (in accordance with the contract documents, as modified by any change orders agreed to by the parties) upon attainment of which the owner can use the same for the purpose for which it was intended; the date of substantial completion may be established by written agreement between the contractor and the owner." T.C.A. §28-3-201(2).

Notwithstanding the above, T.C.A. §28-3-203 provides that if the injury to property or person occurs during the fourth (4th) year after substantial completion, then the action may be brought within one (1) year after the date on which such injury occurred, but in no event may it be brought more than five (5) years after the substantial completion of any such improvement.

It is clear that under Tennessee law, the above statute of limitation does not extend either the one (1) or three (3) year periods for filing actions based upon personal injuries and property damages. In other words, if a person is injured as the result of a construction deficiency, then that suit must still be brought within one (1) year of the date of injury. If that personal injury occurs outside of the time period set forth in the statute of repose, then the claim is barred. The same result holds for property damage claims.

There are a couple of exceptions to the above statute of repose, however. First, if the alleged negligent party is in actual possession or control of the improvement (as owner, tenant, or otherwise) at the time the deficiency causes the injury in question, then that party cannot rely upon the statute of repose. For example, this would prevent a developer who maintains control and operation of an apartment complex from relying upon the four (4) year statute of repose if a tenant is injured as the result of a construction defect.

---

[5] Id. at *6-7.

In addition, T.C.A. §28-3-205(b) provides that the statute of repose cannot be used as a shield by a person who has "been guilty of fraud in performing or furnishing the design, planning, supervision, observation of construction, construction of, or land surveying, in connection with any such improvement, or to any person who shall wrongfully conceal any such cause of action." This is obviously a public policy exception to the running of the statute of repose.

Not unexpectedly, plaintiffs' attorneys have sought innovative ways to get around the statute of repose. For example, in construction defect cases involving homeowners, claims are often raised under the Tennessee Consumer Protection Act, which like most states' consumer statutes, offers a broad range of remedies for various acts and omissions.

In a recent decision of the Tennessee Eastern Section Court of Appeals, it was held that the statute of repose did in fact bar a Tennessee Consumer Protection Act claim relating to alleged defective construction. In *Cunha v. Cecil*, 2007 WL 273753 (Tenn. Ct. App.), the plaintiffs claimed that the statute of repose should not apply because the defendant made a series of promises to correct the deficiency but never followed through with those repairs. Plaintiffs argued that as such, their claims were proper under the Tennessee Consumer Protection Act and did not fall within the scope of the statute of repose. The Trial Court had disagreed and granted summary judgment based upon the statute of limitations, and the Court of Appeals affirmed.

This decision is even broader because the defendant was the seller of the home that had partnered with a builder in the housing development. Plaintiffs argued that since the defendant was merely a "vendor", it did not come within the scope of the statute of repose to begin with.

The Court, finding that the seller was involved in a joint venture with the builder, held that it was entitled to protection under the statute of repose.

Plaintiffs further argued that the defendant should be estopped from claiming the benefit of the statute of repose because of its alleged repeated promises to make repairs that were not completed. The Trial Court held that there was insufficient evidence to establish an estoppel, and the Appellate Court did not disturb that finding.

In sum, the Tennessee statute of repose provides a clear outer limit for liability to all parties to the construction process save and except for an owner that maintains control and possession of the property. This is true regardless of whether or not the injury is one for property damage, personal injury or even wrongful death.

IV. PRE-SUIT NOTICE OF CLAIM AND OPPORTUNITY TO CURE

In 2004, Tennessee enacted legislation requiring commercial property owners to give pre-suit notice of a construction defect, and to allow any notified and allegedly responsible parties access to the project to inspect the alleged conditions and an opportunity to cure the defects. The Act applies to all claims for construction defects accruing on or after May 24, 2004. T.C.A. §66-36-101 *et seq*. For the unacquainted, the Act can be easily miscomprehended without careful review of the definitions section, T.C.A. §66-36-101, and the procedural steps for giving notice

and responding set out in T.C.A. §66-36-103. For example, the limitation of the Act to commercial projects arises from the definition of "action":

> "any civil action for damages or indemnity asserting a claim for damage to or loss of commercial property caused by an alleged construction defect, but does not include any civil action or arbitration proceeding asserting a claim for alleged personal injuries arising out of an alleged construction defect."

Under the Act, a "construction defect" is defined as "a deficiency in, or a deficiency arising out of, the design, specifications, surveying, planning, supervision, observation of construction, or construction or remodeling of a structure resulting from:

(A) Defective material, products, or components used in the construction or remodeling;

(B) A violation of the applicable codes in effect at the time of construction or remodeling;

(C) A failure of the design of a structure to meet the applicable professional standards of care at the time of governmental approval, construction or remodeling; or

(D) A failure to construct or remodel a structure in accordance with accepted trade standards for good and workmanlike construction at the time of construction or remodeling; T.C.A. §66-36-101(4).

Another key definition is "contractor", which is defined as any person, firm, partnership, corporation, association, or other organization that is legally engaged in the business of designing, developing, constructing, manufacturing, selling, or remodeling structures or appurtenances to structures. T.C.A. §66-36-101(5).

T.C.A. §66-36-103 sets forth the pre-suit notice procedure, and response duties and timeline for responding to the notice. In brief, the Act generally provides that a commercial property owner must forward written notice of the defect to the last known address of the contractor, subcontractor, supplier or design professional within 15 days of discovery, but failure to give notice within 15 days does not bar the action.

The Act contemplates that all potentially responsible parties will receive notice and have an opportunity to inspect the conditions. By way of example, upon the contractor's receipt of the notice, the contractor must, within 10 days of receipt of the notice, notify all subcontractors, suppliers, or designers that may be responsible for the defects. Those parties are then afforded 10 days from that notice to likewise inspect the defects. Within 30 days of receipt of notice, every notified party must provide the claimant with a written response in which the responding party may: (1) offer to cure the defect at no cost to the claimant, including a timetable for completing the work; (2) settle the claim by monetary payment; or (3), dispute the claim.

Importantly, any offer to cure or settle a claim must be rejected in writing, and must specifically state "rejected" on the rejection. T.C.A. §66-36-103(h). While no Tennessee case has so held, it would seem plausible under this provision of the Act that a contractor's offer to cure or settle, if not properly rejected, constitutes a claimant's acceptance.

Finally, T.C.A. §66-36-103(l) provides that a claimant's written notice tolls the applicable statute of limitations until the later of:

> (1) One hundred eighty (180) days after the contractor, subcontractor, supplier, or design professional receives the notice; or
>
> (2) Ninety (90) days after the end of the correction or repair period stated in the offer, if the claimant has accepted the offer. By stipulation of the parties, the period may be extended and the statute of limitations is tolled during the extension.

Aside from the statutory notice and cure provisions of Tenn. Code Ann. § 66-36-101 *et seq.,* Tennessee common law imposes a general duty to give notice of a construction defect and to allow the defaulting party to repair the defective work, to reduce the damages, to avoid additional defective performance and to promote settlements of disputes. *McClain v. Kimbrough Constr. Co., Inc.*, 806 S.W.2d 194, 198 (Tenn. Ct. App. 1990).

In *McClain*, the Court imposed upon a contractor a duty to give its subcontractor notice and an opportunity to cure alleged defects prior to terminating a contract for a commercial construction project. *Id*. at 198-99. The rule requiring giving notice and an opportunity to cure has also been extended to cases involving residential construction. *E.g., Greeter Const. Co. v. Tice*, 11 S.W.3d 907, 910-11 (Tenn. Ct. App. 1999); *Lavy v. Carroll*, No. M2006-00805-COAR3-CV, 2007 Tenn. App. LEXIS 809, at **9-10 (Tenn. Ct. App. Dec. 26, 2007), *Rule 11 appl. perm. appeal denied May 27, 2008*; and *Custom Built Homes by Ed Harris v. McNamara*, No. M2004-02703-COA-R3-CV, 2006 Tenn. App. LEXIS 781, at **14-15 (Tenn. Ct. App. Dec. 11, 2006), *no appl. perm. appeal filed.*

V. INSURANCE COVERAGE AND ALLOCATION ISSUES

A. Coverage Issues

Under Tennessee law, a liability insurer's duty to defend is determined by comparing the allegations of the complaint filed against the insured with the terms of the insurance policy. *Drexel Chem Co. v. Bituminous Ins. Co.*, 933 S.W.2d 471, 480 (Tenn. App. 1996). If the allegations of the complaint against the insured are potentially within the coverage of the insurance policy, the insurer has a duty to defend. *Id.* An insurer's duty to indemnify its insured, by contrast, is based upon the "actual facts", rather than the complaint allegations. *St. Paul Fire & Marine Ins. Co. v. Torpoco*, 879 S.W.2d 831, 834-35 (Tenn. 1994). Where the allegations in the complaint against the insured are ambiguous and there is doubt whether they trigger

coverage, the doubt should be resolved in favor of the insured. *Dempster Bros., Inc. v. U.S. Fidelity & Guar. Co.*, 388 S.W.2d 153, 156 (Tenn. 1964).

Under Tennessee law, an unambiguous exclusionary clause precludes coverage and the courts should give the words and exclusionary clauses their ordinary meaning. *Blaine Const. Corp. v. Insurance Co. of North America*, 171 F.3d 343, 349 (6th Cir. 1999). Tennessee follows the general insurance law rule that "exceptions, exclusions and limitations in policies of insurance are to be most strongly construed against the insurer." *Travelers Ins. Co. v. Aetna Cas. & Surety Co.,* 491 S.W.2d 363, 366-67 (Tenn. 1973).

In a typical "all risk" policy, coverage extends to risks not usually contemplated, and recovery under the policy will generally be allowed at least for all losses of a fortuitous nature in the absence of fraud or other intentional misconduct of the insured unless the policy contains a specific provision expressly excluding the loss from coverage. *HCA, Inc. v. American Protection Ins. Co.*, 174 S.W.3d 184, 187-88 (Tenn. App. 2005).

Generally, damage to the insured's property caused by faulty workmanship is an insured risk under a general liability policy unless expressly eliminated by an exclusion provision. The defective work itself, however, is not covered. In 2007, with its decision in *Travelers Indem. Co. of America v. Moore & Associates, Inc*., 216 S.W.3d 302 (Tenn. 2007), the Tennessee Supreme Court joined with a growing minority of states in finding that defective workmanship may constitute an "occurrence" and that damage caused by faulty workmanship is "property damage."

Commercial general liability (CGL) insurance policies cover risks that the insured's product or work will cause bodily injury or damage to property other than the work itself for which the insured may be found liable. *Standard Fire Ins. Co. v. Chester O'Donley & Associates, Inc.*, 972 S.W.2d 1, 6-7 (Tenn. App. 1998).

B. Allocation Issues

The allocation of a loss depends initially whether or not the policy is a "claims-made" or "occurrence" policy. An "occurrence" policy protects the insured against incidents that occur while the policy is in force, even if the claim that arises from that incident is not filed until after the policy expires or is terminated. *Pope v. Leut & Heath, PLLC*, 87 S.W.3d 89, 93 (Tenn. App. 2002). On the other hand, a "claims-made" policy protects an insured against claims that are filed while the policy is in force, even if the incident giving rise to the claim occurred before the policy was executed. *Id.*

C. Trigger of Coverage

Although there is a scarcity of case law in Tennessee on the issue, it appears that Tennessee follows the continuous trigger theory, i.e. where a progressive injury existed over multiple policy periods. In *State Farm Fire & Cas. Co. v. McGowan*, 421 F.3d 433, (6th Cir. 2005), a claim was made relating to a rotting tree that was left standing adjacent to an insured apartment building. The insured (on whose property the rotten tree was situated) made a claim against its insurer for the time period that the tree was rotting. The tree later fell and killed

someone after the subject policy had expired. Nonetheless, the court held that because the language of the applicable coverage period and definitions were ambiguous, there was potentially an "accident" and thus an "occurrence" under the policy.

In another unreported case, *State Auto Mutual Ins. Co. v. Shelby Mut. Ins. Co.*, 1988 WL 67155 (Tenn. Ct. App.1988), the Tennessee Court of Appeals held that an insured cannot "enjoy completed operations coverage indefinitely" after the coverage period. If a complaint alleges injury from a continuous exposure over a specific time, however, there will probably be coverage even though the continuous exposure extends past the policy period. The expiration of the policy should not bar pro rata responsibility on a prior carrier in a continuous exposure situation. The prior carrier would receive an undue windfall if the subsequent carrier were charged with the entire loss.

Under a continuous trigger situation, it is likely that the Tennessee courts would apply a pro rata approach in allocating the loss among the various carriers that afforded coverage to the insured during the applicable time periods. This is the general rule from other jurisdictions, specifically including most states within the Sixth Circuit of which Tennessee is a part.

VI. CONTRACTUAL INDEMNIFICATION

Tennessee law does not permit contractual provisions, in connection with or collateral to an agreement to improve a structure or real estate, which indemnify the promisee for negligence caused solely by such promisee. T.C.A. § 62-6-123 states that:

> A covenant promise, agreement or understanding in or in connection with or collateral to a contract or agreement relative to the construction, alteration, repair or maintenance of a building, structure, appurtenance and appliance, including moving, demolition and excavating connected therewith, purporting to indemnify or hold harmless the promisee against liability for damages arising out of bodily injury to persons or damage to property caused by or 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.

The scope of this statute, however, is not limited to construction contracts *per se*. T.C.A. § 62-6-123 broadly covers agreements and contracts between all parties regarding the construction or improvement to real property. *Elliot Crane Servs., Inc. v. H.G. Hill Stores, Inc.*, 840 S.W.2d 376, 379 (Tenn. Ct. App. 1992). In *Elliot Crane*, the plaintiff insisted that Elliot Crane Service was not a "contractor" under the language of § 62-6-123 because it was merely in the business of furnishing cranes to further construction. This argument did not persuade the Tennessee Court of Appeals which held that a company operating a crane designed to be used in constructing a building cannot logically claim that the company was unaware of the construction use of the crane. *Elliot Crane*, 840 S.W.2d at 379-80 (*citing Am. Pecco Corp. v. Concrete Building Sys[s].*, Co., 392 F.Supp. 789, 793 (N.D. Ill. 1975). The Court of Appeals of Tennessee also dealt with the scope of § 62-6-123 in *Corroum v. Dover Elevator Co.*, when it stated that "there is no language limiting [T.C.A. § 62-6-123]'s applicability solely to construction contracts." *Corroum v. Dover Elevator Co.*, 806 S.W.2d 777, 779 (Tenn. Ct. App. 1990). The

Corroum court interpreted the statute to "include any agreement relative to the construction of a building." *Id.* at 780. Thus, the Court of Appeals held, "a contract to provide certain services relative to a building under construction under a separate contract would be included under [the statute] and any provision purporting to indemnify . . . the promisee . . . is void and unenforceable." *Id.* at 780.

In 2017, the United States District Court for the Eastern District of Tennessee in the case of American Guaranty & Liability Insurance Company v. Norfolk Southern Railway Company, 278 F.Supp.3d 1025, 1045-1047 (E.D. Tenn. 2017), reiterated that T.C.A. § 62-6-123 predominantly applies to construction or construction-related contracts and specifically held that it does not apply to contracts for insurance in which a party carries insurance to indemnify itself from its own negligence. The court held that T.C.A. § 62-6-123, and the cases interpreting the same, does not void an insurance contract. See AIG at 1047. In reaching its conclusion, the court observed that Trinity Industries, Inc. v. McKinnon Bridge Company, 77 S.W.3d 159, 174 (Tenn. Ct. App. 2001) abrogated on other grounds by Bowen ex rel Doe v. Arnold, 502 S.W.3d 102 (Tenn. 2016), holds that the cases applying T.C.A. § 62-6-123 involved some aspect of a construction project. The court repeated the holdings from Posey v. Union Carbide, 507 F.Supp. 39, 41 (N.D. Tenn. 1980), Carroun v. Dover Elevator Company, 806 S.W.2d 777, 780 (Tenn. Ct. App. 1990) and the Elliott Crane cases (see Elliott Crane Serv., Inc. v. HG Hill Stores, Inc., 840 S.W.2d 376, 379 (Tenn. 1992) and Armoneit v. Elliot Crance Serv., Inc., 65 S.W.2d 623 (Tenn. Ct. App. 2001), which all stand for the proposition that T.C.A. § 62-6-123 applies to all construction and construction- related contracts, but noted that there are limits to the statute's application.. The court reasoned that "if the statute applied to insurance contracts, such as the AIG policy here, it would result in outlawing the insurance industry in sectors covered by the T.C.A. § 62-6-123." Thus, an insurance policy may indemnify a party from its own negligence.

VII. CONTINGENT PAYMENT AGREEMENTS

A. Enforceability

Contingent payment agreements are not favored in Tennessee, but are likely enforceable if the contract clearly conveys that the general contractor's receipt of payment is an express condition precedent to its obligation to pay lower tier contractors. There are two cases addressing these contract payment terms. The first, and more prominent, is *Koch v. Construction Technology, Inc.* 924 S.W.2d 68, 71 (Tenn. 1996). In *Koch*, the Tennessee Supreme Court held that conditions precedent are not favored in contract law, and will not be upheld unless there is clear language to support them; doubtful language will be construed to impose a duty rather than create a condition precedent.

Koch involved a painting subcontractor's claim for payment against the general contractor and its surety. The contract contained a payment term which provided: "[p]artial payments subject to all applicable provisions of the Contract shall be made when and as payments are received by the Contractor." The Court held that this term did not condition the obligation of payment upon the general contractor's receipt of payment, but instead merely

established the timing of payment. The Court further noted that the contract impliedly obligated the general contractor to make payment within a reasonable time of the subcontractor's application for payment.

The second case, *Eagle Supply & Mfg., L.P. v. Bechtel Jacobs Co., LLC*, 868 F.3d 423 (6th Cir. 2017), addresses a second but similar type of condition: "pay-when-paid." Categorizing *Koch* as a "pay-**if**-paid" condition, which does not require the contractor to pay *unless* it is paid, a pay-when-paid clause delays payment *until* the contractor is paid. The court anticipated that Tennessee would treat the clauses identically: the contractor only pays the subcontractor when and if it receives payment. Because Tennessee strongly disfavors pay-when-paid clauses, enforcing such conditions only when there is clear language to support them, and because the risk of nonpayment normally lies with the prime contractor, the court held that these types of conditions "require absolute precision of language." *Id*. at 436.

B. Requirements

There is no reported decision in Tennessee in which the terminology of an enforceable contingent payment agreement has been upheld. However, the *Koch* case establishes (and *Eagle Supply* reinforces) that to be enforceable, contingent payment terms must plainly and unambiguously state that the general contractor's obligation of payment is *expressly conditioned* upon its own receipt of payment from the owner, and that the general contractor's receipt of payment from the owner is an express condition precedent to its obligation of payment to a subcontractor.

VIII. MEASURE AND TYPES OF DAMAGES

Under Tennessee law, the awarding of damages for a breach of contract action is both a question of law and fact. *GSB Contractors, Inc. v. Hess*, 179 S.W.3d 535, 541 (Tenn. Ct. App. 2005). However, there are different standards for the award of each type of damages.

A. Personal Injury Damages vs. Construction Defect Damages

A party sustaining personal injuries as a result of a construction defect can recover for past and future pain and suffering, past and future medical expenses, loss of earning capacity and loss of enjoyment of life; provided, however, that any future damages are established by competent medical testimony within a reasonable degree of medical certainty.

Tennessee has two (2) methods of recovery for damage to real property. The first method concerns permanent damage. For permanent damage, the court will award the difference between the property's value before the damage and the value after the damage. *Cathcart v. Malone*, 229 S.W.2d 157 (Tenn. Ct. App. 1950). One common example is the cutting of a tree on someone else's property. Such was the case in *Cathcart*, where the court deemed the loss of a tree permanent and thus awarded the difference in value of the property before and after the cutting of the tree. *Id.* at 159.

The second method concerns damage that is only temporary in nature. For temporary damage a court will award either the reasonable cost of repair or the diminution in value of the property. *Jones v. Johnson*, 2003 WL 21278282 *1 (Tenn. Ct. App. 2003). The court determines which to award based on which is amount is less. *Id.*

B. Attorney's Fees Shifting and Limitations of Recovery

Tennessee does not permit the collection of attorneys' fees unless there is a statute or the parties have contracted for attorneys' fees in the event of litigation. *Elec. Controls v. Ponderosa Fibres of Am.*, 19 S.W.3d 222 (Tenn. Ct. App. 1999). However, the Tennessee Supreme Court has found attorneys' fees recoverable without statute when the dispute involves indemnity. *Pullman Standard, Inc. v. Abex Corp.*, 693 S.W.2d 336 (Tenn. 1985). Resultantly, the indemnitee may recover attorneys' fees in an indemnity relationship.

C. Consequential Damages

Consequential damages are damages a court awards to put the injured party in the position they would have been had a breached contract been performed fully. However, such damages must be reasonable and necessary for a court to award. In *Custom Built Homes by Ed Harris v. McNamara*, 2006 WL 3613583 *7 (Tenn. Ct. App. 2006), the court would not award the plaintiff's entire damage request as the plaintiff could not show that the repairs they made on their home were needed. Even though a homeowner may make repairs, repairs that are beyond the scope of the original contract, such as upgrades, are not consequential as they are not foreseeable. *Id.*

D. Delay & Disruption Damages

To recover delay damages, the items for which a party is attempting to recover must have been part of the contract. *White's Elec. v Lewis Constr.*, 1999 WL 605654 *14 (Tenn. Ct. App. 1999). These damages can be in the form of increased operating expenses, late service charges, and miscellaneous costs. *Id.* at *4. It naturally follows from these examples that a court may consider increased labor costs as well. *McClain v. Kimbrough Constr. Co., Inc.*, 806 S.W.2d 194, 201 (Tenn. Ct. App. 1990).

E. Economic Loss Doctrine

The "economic loss doctrine" mandates that when there is only an economic loss underlying an action the proper action is not one for negligence. *Ritter v. Custom Chemicides, Inc.*, 912 S.W.2d 128, 133 (Tenn. 1995). Moreover, when dealing only with economic loss, the rights of the parties are governed exclusively by the contract. *Messer Griesheim v. Eastman Chem.*, 194 S.W.3d 466 (Tenn. Ct. App. 2005). As a side note, be sure to see the section below that addresses the Collateral Source Rule and the recent *Dedmon* ruling.

F. Interest

From the entry of judgment in a breach of contract action, the maximum interest rate is defined in T.C.A. § 47-14-103:

> Except as otherwise expressly provided by this chapter or by other statutes, the maximum effective rates of interest are as follows:
>
> (1) For all transactions in which other statutes fix a maximum effective rate of interest for particular categories of creditors, lenders, or transactions, the rate so fixed;
>
> (2) For all written contracts, including obligations issued by or on behalf of the state of Tennessee, any county, municipality, or district in the state, or any agency, authority, branch, bureau, commission, corporation, department, or instrumentality thereof, signed by the party to be charged, and not subject to subdivision (1), the applicable formula rate; and
>
> (3) For all other transactions, ten percent (10%) per annum.

Also, according to T.C.A. § 47-14-109, pre-judgment interest begins accumulation from the time the contract is due.

G. Punitive Damages

Tennessee does not normally allow punitive damages when there is a breach of contract. *Hodges v. S.C. Toof & Co.*, 833 S.W.2d 896 (Tenn. 1992). However, this is not always true; and thus, there is a two-step process for awarding punitive damages. In the first step, the fact finder must determine whether punitive damages should even be awarded. *Id.* at 901. The fact finder must find by "clear and convincing evidence" that a party acted (1) intentionally,(2) fraudulently, (3) maliciously, or (4) in a reckless manner. *Id.* at 900-01.

If there is a determination that punitive damages are proper, then there is a second step where the fact finder determines the necessary amount to award. *Id.* at 901. In reaching a determination, the fact finder considers many factors which essentially amount to a standard of "totality of the circumstances". *Id.* at 901-02. Use of such a standard allows the consideration of all factors and the assignment of a value to each factor or consideration.

IX. CASE LAW AND LEGISLATION UPDATE

A. Legislation

During 2018 and 2019, real property owners in the state of Tennessee wielded a mighty weapon against liens on their property. On May 21, 2018, the Tennessee Legislature passed Tennessee Code Annotated Section 66-21-108 addressing remedies for owners challenging real property liens. The statute created a cause of action in which an owner that successfully challenges the validity of a lien on their property could not only get the lien removed, but would be entitled to significant remedies. Under this law, the owner may recover as follows:

> [A] real property owner who prevails in an action challenging the validity of a lien, including in a slander of title proceeding, shall recover:
> (1) The owner's reasonable attorney's fees;
> (2) Reasonable costs incurred by the owner to challenge the validity of the lien:
> (3) Liquidated damages in an amount equal to ten percent (10%) of the fair market value of the property not to exceed one hundred thousand dollars ($100,000); and
> (4) Any actual damages incurred by the owner.

First, the law included the term "shall recover," meaning it was not left to the court's discretion. Rather, if the prevailing party sought them, the court was required to award them even if the lien was filed in good faith. Secondly, it entitled the prevailing owner to *all* of the remedies listed in the statute. Courts are hesitant to provide liquidated damages, and are only to award attorneys' fees if a statute or agreement specifically provides them. Moreover, the use of "reasonable costs" and "any actual damages" could serve as a catch-all for just about any other arguable amount incurred by the owner in challenging the lien.

In 2019, the Legislature considered an amendment to the statute requiring a showing of malice in order to award the statute's significant penalties. Additionally, it was proposed that the use of "shall recover" be replaced with "may recover." However, instead of adopting this amended version of the statute, the Legislature simply repealed it in its entirety effective April 5, 2019. Owners could still attempt to seek and argue for equitable relief for the costs they have incurred in removing an invalid lien, as well as remedies available to them under mechanic's lien laws. However, they are no longer equipped with the right to receive liquidated damages, attorneys' fees, reasonable costs, and actual damages upon request after the removal of an invalid lien.

B. Case Law

The Tennessee Court of Appeals issued two opinions in 2019 regarding the applicability of the retainage statute. In Tennessee, the Prompt Pay Act, codified at Tennessee Code Annotated § 66-34-101, *et seq*. requires that all retainage withheld on construction projects be deposited into a separate interest-bearing escrow account with a third party. If a contractor fails to deposit retainage as required, the contractor must pay the subcontractor an additional $300 penalty per day for each and every day that such retained funds are not deposited. On March 20, 2019, the Tennessee Court of Appeals ruled in the matter of *Vic Davis Construction v. Lauren Engineers & Constructors, Inc.*, No. E2017-00844-COA-R3-CV, 2019 WL 1300935 (Tenn. Ct. App. Mar. 20, 2019), which involved a subcontractor's allegations that the general contractor failed to comply with the Prompt Pay Act requirements. Specifically, the subcontractor alleged that the contract called for a final payment of 5% for "Turn-over, As-Builts, Final Clean Up, Demobolize." The subcontractor argued that this holdback payment constituted retainage that should have been escrowed and relied upon the fact that Tennessee law limits retainage on construction projects to 5% of the contract amount. The Court disagreed, finding that the contractor paid the subcontractor's first 12 payment applications in full and the contract explicitly stated that "invoices are not subject to retention." Although the amount of the final payment likely exceeded the value of the as-built portion of the project, final clean-up and other items, the Court held that the holdback did not constitute retainage.

In *E Sols for Buildings, LLC v. Knestrick Contractor, Inc.*, No. 2018-02028-COA-R3-CV, 2019 WL 5607473 (Tenn. Ct. App. Oct. 30, 2019), the Tennessee Court of Appeals considered the Prompt Pay Act in the context of a dispute regarding the Nashville Centennial Sportsplex Indoor Fitness expansion. In this case, the project's HVAC material supplier brought suit for nonpayment against the HVAC subcontractor, general contractor and owner. On appeal, the Court found that the general contractor had violated the Prompt Pay Act by withholding more in liquidated damages from the HVAC subcontractor's retainage than its claim to setoff and that such action constituted bad faith subjecting the contractor to attorney's fees under the Prompt Pay Act. The Court noted that, although a finding of bad faith is a prerequisite to an award of attorney's fees under the statute, what constitutes bad faith is not statutorily defined. Previous courts have determined that "acts taken in bad faith involve knowing or reckless disregard for contractual rights or duties." The Court noted that, even though liquidated damages were assessed in this case, the general contractor failed to pay for completed work under the subcontract for an amount that it acknowledged was higher than the amount of liquidated damages. The Court found that, at a minimum, the general contractor acted in reckless disregard with regard to its withholding of the difference between the balance of the unpaid work and the assessed damages.