

SUBCONTRACTOR REMEDIES UNDER THE THEFT BY CONTRACTOR STATUTE

In the May/June 2003 edition of this publication I discussed the Wisconsin Supreme Court Case of Tri-Tech Corporation of America v. Americomp Services, Inc., where the court held that a subcontractor was entitled to treble damages against a prime contractor who failed to pay the subcontractor for installation of computer cabling, provided that the subcontractor adequately prove the elements of the criminal offense of theft by contractor which are: (1) the defendant acted as a prime contractor, (2) the defendant received money for the improvement of land from the owner or mortgagee, (3) the defendant intentionally used the money for purposes other than the payment of bona fide claims for labor and materials prior to the payment of such claims, (4) the use was without the owner or mortgagee's consent and contrary to the contractor's authority, (5) the contractor defendant knew the use was without consent and contrary to his authority, and (6) the defendant contractor used the money with the intent to convert it to his own use or the use of another.

In State v. Keyes, decided on June 3, 2008, the Wisconsin Supreme Court went further and clarified that even where a prime contractor was acting as a subcontractor, if that contractor received construction loan monies and failed to distribute proportionally those loan monies to all other unpaid subcontractors, a theft by contractor has been *prima facie* established. In State v. Keyes, the owner ultimately lost trust in and terminated the prime contractor and the State brought a criminal complaint against the prime contractor alleging that it had violated § 779.02(5), Stats., by failing to distribute proportionally the construction loan monies to all unpaid subcontractors. The prime contractor filed a motion to dismiss the criminal charge arguing that it was simply keeping the money for materials purchased and work performed as a subcontractor.

The thrust of the decision was to clearly place upon all prime contractors and subcontractors in Wisconsin the full burden of the theft by contractor statute which includes the obligation of a prime contractor or subcontractor to distribute construction monies

proportionately if the amount available is not sufficient to pay all subcontractors.

In State v. Keyes, the owner may have been acting as its own general contractor and the prime contractor may have been acting as a subcontractor, which lessened the clarity and value of the court's decision. However, the Supreme Court chose not to decide whether the defendant was acting as a prime contractor or a subcontractor, and did not comment on whether the owner was acting as its own general contractor and simply focused upon the obligation of any prime contractor *or* subcontractor to use construction monies received for improvements to real estate only as a trust fund until all subcontractor claims have been paid. The court held that the use of any such monies by a prime contractor or a subcontractor for any other purpose until all claims, except those which are the subject of a bona fide dispute and then only to the extent of the amount of the dispute have been fully paid or proportionally paid in cases of a deficiency, constitutes theft by contractor a criminal act, subjecting not only the contractor but its officers, directors, members, partners, or agents to criminal prosecution. Under the Tri-Tech decision the prime contractor or subcontractor breaching the trust may also be pursued by the unpaid subcontractor for the recovery of treble damages.

A portion of the Supreme Court's decision in State v. Keyes discussed whether a prime contractor or subcontractor receiving construction monies must pay all their subcontractors in full or proportionally in cases of a deficiency, before paying themselves a profit. The court in essence held that while profits may be part of a contractor's pay application, construction monies paid to that contractor were still trust fund monies until the unpaid subcontractors were either paid in full or proportionately in the event of a deficiency.

Professional engineers are often officers, directors, members, partners or agents of prime contractors and subcontractors. They are vitally and directly involved in understanding and adhering to the provisions of § 779.02(5) of the Wisconsin Statutes, known as the theft by

contractors statute. However, professional engineers who are engaged in the practice of engineering relating to real estate improvements should also be aware of and concerned about the distribution of construction monies. Unpaid subcontractors have lien rights which the Wisconsin legislature has protected from erosion. Section 779.135 of the Wisconsin Statutes provides:

779.135 Construction contracts, form of contract. The following provisions in contracts for the improvement of land in this state are void:

(1) Provisions requiring any person entitled to a construction lien to waive his or her right to a construction lien or to a claim against a payment bond before he or she has been paid for the labor, services, materials, plans, or specifications that he or she performed, furnished, or procured.

(2) Provisions making the contract subject to the laws of another state or requiring that any litigation, arbitration or other dispute resolution process on the contract occur in another state.

(3) Provisions making a payment to a prime contractor from any person who does not have a contractual agreement with the subcontractor, supplier, or service provider a condition precedent to a prime contractor's payment to a subcontractor, supplier, or service provider. This subsection does not prohibit contract provisions that may delay a payment to a subcontractor until the prime contractor receives payment from any person who does not have a contractual agreement with the subcontractor, supplier, or service provider.

Since professional engineers in private practice often draft construction contracts in addition to project specifications, careful attention must be paid to the legislative provisions voiding certain contract terms requiring a waiver of lien rights, making the provisions of the contract subject to the laws of some other state and making payments to a prime contractor a condition precedent to the prime contractor's obligation to pay a subcontractor.

During the 50 years that this writer has practiced law in the area of design and construction, the legislature has made substantial changes in Wisconsin's construction lien law, giving it more muscle and emphasis. The cases of Tri-Tech Corporation v. Americomp Services and State v. Keyes represent examples of our Wisconsin Supreme Court giving full force and effect to what the legislature has provided in Chapter 779 of the Wisconsin Statutes.