



Lovein Ribman PC



Texas Board Certified Construction Attorneys

(888) 368-2483

www.loveinribman.com

The Trust Fund Statute (Personal Liability and Civil/Criminal Penalties)

A Builder/Contractor who diverts construction funds from the Project can be both civilly and criminally liable. Pursuant to Texas Property Code, Chapter 162, referred to as the “Trust Fund Statute” Contractors, Subcontractors, Suppliers and their respective officers, employees and agents who receive Project funds become a “trustee” of those funds for the Homeowners’ benefit and for those of whom are owed money for their labor or material provided to the Project. A trustee who intentionally, knowingly or with the “**intent to defraud**” directly or indirectly retains, uses, disburses, or otherwise diverts trust funds from the Project without first fully paying all current or past due obligations, is considered to have misapplied trust funds. A trustee acts with an “**intent to defraud**” when the trustee: (1) retains, uses, disburses, or diverts trust funds with the “**intent to deprive the beneficiaries of the trust funds**”; or (2) uses, disburses, or diverts trust funds that were paid to the trustee in exchange for a Lien Waiver & Release wherein the express representation was made that the funds would be used to pay current or past due obligations. A trustee who misapplies trust funds amounting to \$500 or more commits a Class A misdemeanor. A trustee who misapplies trust funds amounting to \$500 or more with the “**intent to defraud**”, commits a third-degree felony. The individual trustee who had control over the misapplied funds is personally liable, both civilly and criminally.

Example: If the Homeowners pay \$100,000.00 to a Builder/Contractor and \$40,000.00 of which is owed to its Subcontractors or Suppliers, then the Builder/Contractor becomes a trustee of the \$40,000.00 until the money is paid to the Subcontractors/Suppliers. If the Builder/Contractor diverts the \$40,000.00 from the Project by using the money to pay non-Project related debts, then the Builder/Contractor could be personally liable and criminally prosecuted for violating the Trust Fund Act.

A trustee can potentially defeat an alleged Trust Fund violation if the trustee can prove that: (1) the funds were used to pay other Project related expenses; (2) the funds were retained in accordance with the Prompt Payment Act “Good Faith Dispute” exception (explained above); or (3) if the trustee pays the beneficiaries the funds owed within no later than 30 days following the filing of a criminal complaint or notice of a pending criminal investigation.

Additionally, on residential Projects wherein the work is performed under a written Contract in an amount over \$5,000.00, the Builder/Contractor is required to maintain a construction account and deposit the Project funds into that account. The periodic statements from the bank must specifically identify the account as a “construction account”. A Builder/Contractor who is required to maintain a construction account shall maintain records for the account that provides information relating to: (1) the source and amount of the funds in the account and the date the funds were

deposited; (2) the date and amount of each disbursement from the account and the person to whom the funds were disbursed; and (3) the current balance of the account. The Builder/Contractor shall maintain an account record for each Project that specifies the direct and indirect costs charged to the Homeowners. The Builder/Contractor is required to retain all invoices and other supporting documentation received relating to the funds disbursed from the construction account. The Contractor shall ensure that all deposit and disbursement documentation includes the construction account number or information that provides a direct connection between the documentation and the account. The Contractor must maintain and not destroy the above information for one year from completion of the Project. Failure to maintain a construction account is a misdemeanor.