

WARNING –Extended Liability for Prevailing Wage Enforcement Actions: How to Mitigate the Risk

**By Marion T. Hack, Esq., Barbara R. Gadbois, Esq., and Gary E. Scalabrini, Esq.
of Gibbs Giden Locher Turner Senet & Wittbrodt LLP**

On October 13, 2013, Governor Brown signed several bills amending prevailing wage statutes. The bill that may have the most significant impact on contractors is Assembly Bill 1336, which extends the period for the California Labor Commissioner and joint labor management committees to enforce the prevailing wage statutes from 180 days to **18 months** after either the filing of a notice of completion or acceptance of a public work by the awarding body. Because prevailing wage violations are joint and several obligations of both the subcontractor and the general/direct contractor, this extension of the limitations period means that general contractors may find themselves financially liable for underpayment of prevailing wages and penalties long after projects have been completed.

The general contractor has little recourse against a subcontractor that has been paid in full and is either no longer in business or financially able to satisfy a wage or penalty assessment. General contractors cannot withhold funds from subcontractors in order to wait out the statutory period for enforcement without risking possible exposure to prompt payment penalties and suits to recover unpaid balances unless the direct contractor can document a *bona fide* dispute exists with the subcontractor.

What can a general contractor do to protect itself against the consequences of subcontractors who fail to pay prevailing wages? Since this extension of time for the Labor Commissioner to bring enforcement actions is expected to increase the number of such actions, here are some tips to avoid the repercussions:

1. Request Payment and Performance Bonds from Subcontractors in Bid Solicitation. — Yes, payment and performance bonds may be financially prohibitive on some projects. However, bonds may be worth the cost on a prevailing wage job, especially if you use a subcontractor with whom you do not have a previous positive relationship. If the subcontractor is able to provide bonds, make sure the performance bond language expressly guarantees the subcontractor's compliance with all prevailing wage requirements. Alternatively, the bond should at least contain language that the bond covers all obligations under the subcontract, which should include the requirement for the subcontractor to pay prevailing wages, and the subcontract should be incorporated by reference in the bond. A civil wage and penalty assessment initiated 18 months after completion should be covered by the performance bond since the statute of limitations for a claim on a performance bond is 4 years (breach of contract) although some industry bond forms shorten the period for filing suit to 2 years. If the subcontractor is unable or refuses to provide bonds on a public works project awarded by a public entity, the general contractor is entitled to withhold retention from the subcontractor **exceeding** the amount of retention the public entity withholds from the general contractor pursuant to Public Contract Code section 7201. This should open

the door for the general contractor to withhold disputed amounts if subcontractor prevailing wage violations are discovered by the general contractor's monitoring of subcontractors' prevailing wage compliance.

2. Include Indemnity/Defense Obligations in Subcontract — The general contractor should explicitly include indemnity language that requires the subcontractor to indemnify and defend the general contractor for all prevailing wage and penalty assessments arising from the subcontractor's scope of work.

3. Avoid Penalties by Following the "Safe Harbor" Provisions of Labor Code Section 1775 —Contractors should note that the Labor Commissioner is no longer reliably waiving penalties when negotiating prevailing wage enforcement actions. As such, it is even more important that general contractors comply with the "safe harbor" provisions of Labor Code section 1775. General contractors are not liable for any penalties if they comply with all of the following requirements:

(a) The subcontract includes a copy of the provisions of Labor Code sections 1775, 1771, 1776, 1777.5, 1813, and 1815.

(b) The general contractor monitors the payment of the specified general prevailing rate of per diem wages by the subcontractor to its employees, by periodic review of the certified payroll records of the subcontractor.

(c) Upon becoming aware of any failure of a subcontractor to pay its workers the specified prevailing rate of wages, the general contractor diligently takes corrective action to halt or rectify the failure, including retaining sufficient funds due the subcontractor for work performed on the public works project.

(d) Prior to making final payment to the subcontractor for work performed, the general contractor obtains an affidavit signed under penalty of perjury from the subcontractor that the subcontractor has paid the specified general prevailing rate of per diem wages to its employees on the project and any amounts due for overtime pursuant to Section 1813. **This last obligation, which general contractors tend to forget, should be a required closeout document for every job.**

4. Include Rights to Conduct Labor Compliance Audit and Interviews in the Subcontract — The joint and several liability provisions of California's prevailing wage laws are intended to encourage general contractors to be selective about whom they do business with. Failure to fully investigate a low bid subcontractor can have serious consequences. While the "safe harbor" provisions provide some limited protection from penalty assessments, the greater risk is for unpaid wages. Moreover, periodic review of certified payroll records alone may not uncover subcontractor fraud. General contractors seeking to mitigate the risk of careless or fraudulent underpayment by subcontractors should consider taking a more proactive "watchdog" approach to ensure subcontractor labor compliance by including contractual rights to perform and routinely performing random interviews of subcontractor workers and requesting copies of canceled checks to verify amounts actually paid to workers. If the general contractor becomes aware of a subcontractor's failure to pay specified prevailing wage rates, Labor Code section 1775 directs the general contractor to "diligently take corrective action" to rectify the failure including retaining funds otherwise due the subcontractor. This Labor Code withholding requirement should be sufficient to satisfy the requirement for a *bona fide* dispute under Public Contract Code section 7201 so that the general contractor can withhold 150% of the estimated value of underpaid wages and penalties from payments due the subcontractor.

Please note that these risk mitigation factors may increase the costs of performing public works projects and should to be factored into bid pricing.

For more information about this topic please contact:

[Marion T. Hack, Esq.](mailto:Marion.T.Hack@ggltsw.com), [Barbara R. Gadbois, Esq.](mailto:Barbara.R.Gadbois@ggltsw.com), or [Gary E. Scalabrini, Esq.](mailto:Gary.E.Scalabrini@ggltsw.com)

Gibbs Giden Locher Turner Senet & Wittbrodt LLP

1880 Century Park East, 12th Floor

Los Angeles, California 90067

Phone: (310) 552-3400

email: Mhack@ggltsw.com; Bgadbois@ggltsw.com; or Gscalabrini@ggltsw.com

The content contained herein is published online by Gibbs Giden Locher Turner Senet & Wittbrodt LLP ("Gibbs Giden") for informational purposes only, may not reflect the most current legal developments, verdicts or settlements, and does not constitute legal advice. Do not act on the information contained herein without seeking the advice of licensed counsel. For specific questions about any of the content discussed herein or any of the content posted to the Gibbs Giden website please contact the article attorney author or send an email to info@ggltsw.com. The transmission of information about this article, the Gibbs Giden website, or any transmission or exchange of information over the Internet, or by any of the included links is not intended to create and does not constitute an attorney-client relationship. For a complete description of the terms of use of information over the internet or the website please see the Legal Notices section at www.ggltsw.com/legalnotice. This publication may not be reproduced or used in whole or in part without written consent of the Gibbs Giden.

Copyright 2014 Gibbs Giden Locher Turner Senet & Wittbrodt LLP