AMENDED IN ASSEMBLY APRIL 13, 2009

california legislature—2009–10 regular session

ASSEMBLY BILL No. 396

Introduced by Assembly Member Fuentes

February 23, 2009

An act to amend Sections 3186, 3252, 3260, 3260.1, and 3262.5 of, and to add Section 3260.5 to, the Civil Code, and to amend Sections 7107, 10261, and 10261.5 of, and to add Section 7201 to, the Public Contract Code, relating to works of improvement.

legislative counsel's digest

AB 396, as amended, Fuentes. Works of improvement: liens.

(1) Existing law provides that all persons and laborers of every class, except for an original contractor, performing labor upon, bestowing skill or other necessary services on, furnishing materials or leasing equipment to be used or consumed in, or furnishing appliances, teams, or power contributing to, a public work of improvement may serve a stop notice upon the public entity responsible for the public work, as specified. Existing law imposes a duty on a public entity to withhold money or bonds due or to become due to the original contractor in an amount sufficient to answer the claim stated in the stop notice and to provide for the public entity's reasonable cost of any litigation on the matter, as specified.

This bill would qualify the requirement that the public entity withhold money or bonds sufficient to provide for reasonable litigation costs to make it applicable only if the original contractor fails to promptly accept a tender of defense of the public entity in the litigation.

(2) Existing law requires that a 20-day public work preliminary bond notice be given under specified circumstances. If the notice is not given,

a claimant may enforce a claim by giving written notice to the surety and the bond principal within 15 days after recordation of a notice of completion. If no notice of completion has been recorded, the time for giving written notice to the surety and the bond principal is extended to 75 days after completion of the work of improvement.

This bill would provide, instead, if no notice is given, a claimant may enforce a claim by giving written notice to the surety and the bond principal prior to the completion of the project or recordation of a notice of completion.

(3) Existing law imposes a penalty of 2% per month on funds that are improperly withheld in a contract dispute relating to public and private works of improvement, as specified. Existing law requires any person or corporation that has contracted to do business with a public utility to pay any subcontractor within 15 working days of receipt of each progress payment from the public utility, except as specified. Existing law also requires a state agency *or an owner* that fails to make any progress payment within 30 days after receipt of the payment request to pay interest at the rate of 10% per year.

This bill would revise, recast, and consolidate these and various other provisions governing the timely payment of progress payments, retention proceeds, and final payments under a contract for a public or private work of improvement with respect to contracts entered into on or after January 1, 2010. The bill would *eliminate the requirement that a state agency or an owner make a progress payment within 30 days after receipt of the payment request. The bill would* make the 2% penalty described above, in lieu of any interest otherwise due, applicable to an owner, including a public utility or a state agency, a contractor, or a subcontractor that fails to make timely progress, retention, or final payments, as specified. *The bill would require an owner or original contractor to make specified payments to subcontractors within 7 days of receiving final payment or accepting disputed work.* The bill would revise and recast notice and withholding requirements in the case of a dispute, as specified.

(4) Existing law provides that in a contract between the original contractor and a subcontractor, and in a contract between a subcontractor and any subcontractor thereunder, the percentage of retention proceeds withheld cannot exceed the percentage specified in the contract between the public entity and the original contractor.

This bill would instead require that retention proceeds not exceed 5% of the payment, as specified, for all contracts entered into on or after

January 1, 2010, between a public entity, as defined, and an original contractor, between an original contractor and a subcontractor, and between all subcontractors thereunder.

(5) Existing law requires the Department of General Services to withhold not less than 5% of the contract price for a public work of improvement until final completion and acceptance of the project.

This bill would require the Department of General Services to withhold not more than 5% of the contract price until final completion and acceptance of the project.

Vote: majority. Appropriation: no. Fiscal committee: yes. State-mandated local program: no.

The people of the State of California do enact as follows:

SECTION 1. Section 3186 of the Civil Code is amended to read:

3186. It shall be the duty of the public entity, upon receipt of a stop notice pursuant to this chapter, to withhold from the original contractor, or from any person acting under his or her authority, money or bonds, if bonds are to be issued in payment for the work of improvement, that are due or to become due to that contractor in an amount sufficient to (a) answer the claim stated in the stop notice and (b) provide for the public entity's reasonable cost of any litigation thereunder, if the original contractor fails to promptly accept a tender of defense of the public entity in the litigation. The public entity may satisfy this duty by refusing to release money held in escrow pursuant to Section 10263 or 22300 of the Public Contract Code.

SEC. 2. Section 3252 of the Civil Code is amended to read:

3252. (a) With regard to a contract entered into on or after January 1, 1995, in order to enforce a claim upon any payment bond given in connection with a public work, a claimant shall give the 20-day public works preliminary bond notice as provided in Section 3098.

(b) If the 20-day public work preliminary bond notice was not given as provided in Section 3098, a claimant may enforce a claim by giving written notice to the surety and the bond principal as provided in Section 3227 prior to the completion of the project, as defined in Section 3086, or recordation of a notice of completion.

SEC. 3. Section 3260 of the Civil Code is amended to read:

3260. (a) This section is applicable with respect to all contracts entered into on or after July 1, 1991, relating to the construction of any private work of improvement. However, the amendments made to this section during the 1992 portion of the 1991–92 Regular Session of the Legislature are applicable only with respect to contracts entered into on or after January 1, 1993, relating to the construction of any private work of improvement. Moreover, the amendments made to this section during the 1993 portion of the 1993–94 Regular Session of the Legislature are applicable only with respect to contracts entered into on or after January 1, 1994, relating to the construction of any private work of improvement.

~~(b) This section shall apply only to contracts entered into prior to January 1, 2010.~~

~~(c)~~

(b) The retention proceeds withheld from any payment by the owner from the original contractor, or by the original contractor from any subcontractor, shall be subject to this section.

~~(d)~~

(c) Within 45 days after the date of completion, the retention withheld by the owner shall be released. “Date of completion,” for purposes of this section, means any of the following:

(1) The date of issuance of any certificate of occupancy covering the work by the public agency issuing the building permit.

(2) The date of completion indicated on a valid notice of completion recorded pursuant to Section 3093.

(3) The date of completion as defined in Section 3086.

However, release of retentions withheld for any portion of the work of improvement which ultimately will become the property of a public agency, may be conditioned upon the acceptance of the work by the public agency. In the event of a dispute between the owner and the original contractor, the owner may withhold from the final payment an amount not to exceed 150 percent of the disputed amount.

~~(e)~~

(d) Subject to subdivision ~~(f)~~ *(e)*, within 10 days from the time that all or any portion of the retention proceeds are received by the original contractor, the original contractor shall pay each of its subcontractors from whom retention has been withheld, each subcontractor’s share of the retention received. However, if a

retention payment received by the original contractor is specifically designated for a particular subcontractor, payment of the retention shall be made to the designated subcontractor, if the payment is consistent with the terms of the subcontract.

~~(f)~~

(e) If a bona fide dispute exists between a subcontractor and the original contractor, the original contractor may withhold from that subcontractor with whom the dispute exists its portion of the retention proceeds. The amount withheld from the retention payment shall not exceed 150 percent of the estimated value of the disputed amount.

~~(g)~~

(f) Within 10 days of receipt of written notice by the owner from the original contractor or by the original contractor from the subcontractor, as the case may be, that any work in dispute has been completed in accordance with the terms of the contract, the owner or original contractor shall advise the notifying party of the acceptance or rejection of the disputed work. Within 10 days of acceptance of the disputed work, the owner or original contractor, as the case may be, shall release the retained portion of the retention proceeds.

~~(h)~~

(g) In the event that retention payments are not made within the time periods required by this section, the owner or original contractor withholding the unpaid amounts shall be subject to a charge of 2 percent per month on the improperly withheld amount, in lieu of any interest otherwise due. Additionally, in any action for the collection of funds wrongfully withheld, the prevailing party shall be entitled to his or her attorney's fees and costs.

~~(i)~~

(h) It shall be against public policy for any party to require any other party to waive any provision of this section.

~~(j)~~

(i) This section shall not be construed to apply to retentions withheld by a lender in accordance with the construction loan agreement.

(j) This section shall apply only to contracts entered into prior to January 1, 2010.

SEC. 4. Section 3260.1 of the Civil Code is amended to read:

3260.1. (a) This section is applicable with respect to all contracts entered into on or after January 1, 1992, relating to the construction of any private work of improvement.

(b) This section shall apply only to contracts entered into prior to January 1, 2010.

(c) Except as otherwise agreed in writing, the owner shall pay to the contractor, within 30 days following receipt of a demand for payment in accordance with the contract, any progress payment due thereunder as to which there is no good faith dispute between the parties. In the event of a dispute between the owner and the contractor, the owner may withhold from the progress payment an amount not to exceed 150 percent of the disputed amount. If any amount is wrongfully withheld in violation of this subdivision, the contractor shall be entitled to the penalty specified in subdivision (h) of Section 3260.

(d) Nothing in this section shall be deemed to supersede any requirement of Section 3260 respecting the withholding of retention proceeds.

SEC. 5. Section 3260.5 is added to the Civil Code, to read:

3260.5. (a) Notwithstanding any other law, this section applies to all contracts entered into on or after January 1, 2010, relating to the construction of any private or public work of improvement.

(b) This section applies to contractual obligations between all of the following entities:

(1) Owners and original contractors.

(2) Original contractors and subcontractors.

(3) Subcontractors and subcontractors.

~~(c) The owner shall pay to the contractor, within 30 days following receipt of a demand for payment, any progress payment due if there is no good faith dispute between the parties.~~

~~(d)~~

(c) (1) Within 45 days after the date of completion, or 100 days after cessation of labor, the retention proceeds or final payment withheld by the owner shall be released. “Date of completion,” for purposes of this section, means any of the following:

(A) The date of issuance of any certificate of occupancy covering the work by the public agency issuing the building permit.

(B) The date of completion indicated on a valid notice of completion recorded pursuant to Section 3093.

(C) The date of completion as defined in Section 3086.

(2) Notwithstanding paragraph (1), the release of retention proceeds or final payments~~,~~ withheld for any portion of a work of improvement which ultimately will become the property of a public agency~~,~~ may be conditioned upon the acceptance of the work by the public agency.

~~(e) Subject to subdivision (h), within 10 days from the time that~~

(d) Subject to subdivision (g), within seven days from the time that all or any portion of the progress payment, retention proceeds, or final payment is received by the original contractor, the original contractor shall pay each of its subcontractors from which the progress payment, retention proceeds, or final payment has been withheld, each subcontractor's share of the progress payment, retention proceeds, or final payment received. However, if the progress payment, retention proceeds, or final payment received by the original contractor is specifically designated for a particular subcontractor, payment of the progress payment, retention proceeds, or final payment shall be made to the designated subcontractor.

~~(f)~~

(e) If a bona fide dispute exists between an owner and original contractor or between the original contractor and a subcontractor, the owner or original contractor may withhold from the party with which the dispute exists an amount not to exceed 150 percent of the disputed amount. The amount withheld shall not exceed 150 percent of the estimated value of the disputed amount.

~~(g)~~

(f) Within 10 days of receipt of written notice by the owner ~~form~~ *from* the original contractor, or by the original contractor from the subcontractor, that any work in dispute has been completed in accordance with the terms of the contract, the owner or original contractor shall advise the notifying party of the acceptance or rejection of the disputed work. Within ~~10~~ *seven* days of acceptance of the disputed work, the owner or original contractor shall release the retained portion of the disputed payment.

~~(h)~~

(g) If any payment is not made within the time periods required by this section, the owner or original contractor withholding the unpaid amount shall be subject to a charge of 2 percent per month on the improperly withheld amount, in lieu of any interest otherwise due. Additionally, in any action for the collection of

funds wrongfully withheld, the prevailing party shall be entitled to attorney's fees and costs.

~~(i)~~

(h) It is against public policy for any party to require any other party to waive any provision of this section.

~~(j)~~

(i) The remedies authorized pursuant to this section are separate from, and in addition to, any other remedy authorized by law.

SEC. 6. Section 3262.5 of the Civil Code is amended to read:

3262.5. (a) This section shall apply only to contracts entered into prior to January 1, 2010.

(b) Any person or corporation which has contracted to do business with a public utility, hereafter referred to in this section as a contractor, shall pay any subcontractors within 15 working days of receipt of each progress payment from the public utility, unless otherwise agreed in writing by the parties, the respective amounts allowed the contractor on account of the work performed by the subcontractors, to the extent of each of the subcontractors' interest in that work. In the event that there is a good faith dispute over all or any portion of the amount due on a progress payment from a contractor to a subcontractor, then the contractor may withhold no more than 150 percent of the disputed amount.

(c) Any contractor who violates this section shall pay to the subcontractor a penalty of 2 percent of the disputed amount due per month for every month that payment is not made. In any action for the collection of funds wrongfully withheld, the prevailing party shall be entitled to his or her attorney's fees and costs.

(d) This section shall not be construed to limit or impair any contractual, administrative, or judicial remedies otherwise available to a contractor or a subcontractor in the event of a dispute involving late payment or nonpayment by a contractor, or deficient performance or nonperformance by a subcontractor.

SEC. 7. Section 7107 of the Public Contract Code is amended to read:

7107. (a) This section is applicable with respect to all contracts entered into on or after January 1, 1993, relating to the construction of any public work of improvement.

(b) This section shall apply only to contracts entered into prior to January 1, 2010.

(c) The retention proceeds withheld from any payment by the public entity from the original contractor, or by the original contractor from any subcontractor, shall be subject to this section.

(d) Within 60 days after the date of completion of the work of improvement, the retention withheld by the public entity shall be released. In the event of a dispute between the public entity and the original contractor, the public entity may withhold from the final payment an amount not to exceed 150 percent of the disputed amount. For purposes of this subdivision, “completion” means any of the following:

(1) The occupation, beneficial use, and enjoyment of a work of improvement, excluding any operation only for testing, startup, or commissioning, by the public agency, or its agent, accompanied by cessation of labor on the work of improvement.

(2) The acceptance by the public agency, or its agent, of the work of improvement.

(3) After the commencement of a work of improvement, a cessation of labor on the work of improvement for a continuous period of 100 days or more, due to factors beyond the control of the contractor.

(4) After the commencement of a work of improvement, a cessation of labor on the work of improvement for a continuous period of 30 days or more, if the public agency files for record a notice of cessation or a notice of completion.

(e) Subject to subdivision (f), within seven days from the time that all or any portion of the retention proceeds are received by the original contractor, the original contractor shall pay each of its subcontractors from whom retention has been withheld, each subcontractor’s share of the retention received. However, if a retention payment received by the original contractor is specifically designated for a particular subcontractor, payment of the retention shall be made to the designated subcontractor, if the payment is consistent with the terms of the subcontract.

(f) The original contractor may withhold from a subcontractor its portion of the retention proceeds if a bona fide dispute exists between the subcontractor and the original contractor. The amount withheld from the retention payment shall not exceed 150 percent of the estimated value of the disputed amount.

(g) In the event that retention payments are not made within the time periods required by this section, the public entity or original contractor withholding the unpaid amounts shall be subject to a charge of 2 percent per month on the improperly withheld amount, in lieu of any interest otherwise due. Additionally, in any action for the collection of funds wrongfully withheld, the prevailing party shall be entitled to attorney's fees and costs.

(h) If a state agency retains an amount greater than 125 percent of the estimated value of the work yet to be completed pursuant to Section 10261, the state agency shall distribute undisputed retention proceeds in accordance with subdivision (d). However, notwithstanding subdivision (d), if a state agency retains an amount equal to or less than 125 percent of the estimated value of the work yet to be completed, the state agency shall have 90 days in which to release undisputed retentions.

(i) Any attempted waiver of the provisions of this section shall be void as against the public policy of this state.

SEC. 8. Section 7201 is added to the Public Contract Code, to read:

7201. (a) (1) This section shall apply with respect to all contracts entered into on or after January 1, 2010, between a public entity and an original contractor, between an original contractor and a subcontractor, and between all subcontractors thereunder, relating to the construction of any public work of improvement.

(2) Under no circumstances shall any provision of this section be construed to limit the ability of any public entity to withhold 150 percent of the value of any disputed amount of work from the final payment, as provided for in subdivision (c) of Section 7107. In the event of a good faith dispute, nothing in this section shall be construed to require a public entity to pay for work that is not approved or accepted in accordance with the proper plans or specifications.

(3) For purposes of this section, "public entity" means the state, including every state agency, office, department, division, bureau, board, or commission, the California State University, the University of California, a city, county, city and county, including chartered cities and chartered counties, district, special district, public authority, political subdivision, public corporation, or nonprofit transit corporation wholly owned by a public agency and formed to carry out the purposes of the public agency.

(b) (1) The retention proceeds withheld from any payment by a public entity from the original contractor, by the original contractor from any subcontractor, and by a subcontractor from any subcontractor thereunder shall not exceed 5 percent of the payment. In no event shall the total retention proceeds withheld exceed 5 percent of the contract price. In a contract between the original contractor and a subcontractor, and in a contract between a subcontractor and any subcontractor thereunder, the percentage of the retention proceeds withheld may not exceed the percentage specified in the contract between the public entity and the original contractor.

(2) This subdivision shall not apply if the contractor provides written notice to the subcontractor, *pursuant to Section 4108 of the Public Contract Code,* prior to or at the time that the bid is requested, that ~~a bond~~ *bonds* may be required and the subcontractor subsequently is unable or refuses to furnish to the contractor a performance ~~or~~ *and* payment bond issued by an admitted surety insurer.

~~(c) No party identified in subdivision (a) may require any other~~

(c) A party identified in subdivision (a) shall not require any other party to waive any provision of this section.

SEC. 9. Section 10261 of the Public Contract Code is amended to read:

10261. Payments upon contracts shall be made as the department prescribes upon estimates made and approved by the department, but progress payments shall not be made in excess of 95 percent of the percentage of actual work completed plus a like percentage of the value of material delivered on the ground or stored subject to or under the control of the state, and unused, except as otherwise provided in this section. The department shall withhold not more than 5 percent of the contract price until final completion and acceptance of the project. However, at any time after 95 percent of the work has been completed, the department may reduce the funds withheld to an amount not less than 125 percent of the estimated value of the work yet to be completed, as determined by the department, if the reduction has been approved, in writing, by the surety on the performance bond and by the surety on the payment bond. The Controller shall draw his or her warrants upon estimates so made and approved by the department and the Treasurer shall pay them. The funds may be released by electronic transfer if that procedure is requested by the contractor, in writing, and if the public entity has, in place at the time of the request, the mechanism for the transfer.

SEC. 10. Section 10261.5 of the Public Contract Code is amended to read:

10261.5. (a) This section shall apply only to contracts entered into prior to January 1, 2010.

(b) Any state agency which fails to make any progress payment within 30 days after receipt of the payment request from a contractor on a construction contract for an undisputed payment request, which was properly submitted by the contractor to the agency, shall pay interest to the contractor equivalent to the legal rate set forth in subdivision (a) of Section 685.010 of the Code of Civil Procedure. Any state agency which independently calculates the amount due on a progress payment and which fails to make a progress payment within 30 days of the first submittal of the estimate for each contract by the engineer, shall pay interest to the contractor equivalent to the legal rate set forth in subdivision (a) of Section 685.010 of the Code of Civil Procedure. In the event that the payment is not made within 30 days of receipt of the contractor's request or the first submittal by the engineer, and the Controller has processed the payment within 14 days of receipt of the request or submittal, the contracting state agency shall pay interest to the contractor equivalent to the legal rate set forth in subdivision (a) of Section 685.010 of the Code of Civil Procedure. In the event that the payment is not made within 30 days of receipt of the contractor's request or the first submittal by the engineer, and the contracting state agency has processed the payment within 16 days after receipt of the request or submittal, the Controller shall pay interest as provided in Section 685.010 of the Code of Civil Procedure.

For purposes of this section, a payment request shall be considered properly executed if funds are available for payment of the payment request, and payment is not delayed due to an audit inquiry by the Controller.

(c) Upon receipt of a payment request, each agency shall require:

(1) That each payment request be reviewed as soon as practicable after receipt for the purpose of determining that a payment request is a proper payment request.

(2) Any payment request determined not to be a proper payment request suitable for payment shall be returned as soon as

practicable, but not later than seven days, after receipt, specifying the reasons that the payment request is not a proper payment request.

(3) The number of days available to a state agency to make a timely payment of payment request without incurring interest shall be reduced by the number of days by which an agency exceeds the requirements of paragraph (2).

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