

## HOUSE OF REPRESENTATIVES STAFF ANALYSIS

**BILL #:** CS/CS/HB 1247 Construction Bonds

**SPONSOR(S):** Civil Justice Subcommittee, Business & Professions Subcommittee, Perez

**TIED BILLS:** IDEN./SIM. **BILLS:** SB 1200

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR or BUDGET/POLICY CHIEF
1) Business & Professions Subcommittee	15 Y, 0 N, As CS	Brackett	Anstead
2) Civil Justice Subcommittee	13 Y, 0 N, As CS	Mawn	Poche
3) Commerce Committee	22 Y, 0 N	Brackett	Hamon

### SUMMARY ANALYSIS

A payment bond guarantees that a contractor will pay subcontractors, laborers, and material suppliers for their work.<sup>1</sup> It forms a three-part contract between the owner, the contractor, and the surety to ensure that liens are not filed on the project. Contractors are required to obtain a payment bond for public projects over \$100,000.<sup>2</sup> In order to receive protection under a bond, subcontractors, laborers, and material suppliers must meet certain requirements, including serving the contractor with a notice of nonpayment.

The bill:

- Provides that a notice of nonpayment must be made under oath and must include:
  - The nature of the labor or services performed;
  - If known, the nature of the labor or services to be performed;
  - The materials furnished;
  - If known, the materials to be furnished;
  - The amount paid on the account; and
  - If known, the amount due and the amount to become due.
- Provides that a subcontractor, laborer, or material supplier who files a fraudulent notice of nonpayment loses his or her rights under the bond but clarifies that a minor mistake in the notice or a good faith dispute as to the amount due is not fraudulent.
- Provides that the negligent inclusion or omission of any information in the notice of nonpayment that has not prejudiced the contractor or surety does not defeat an otherwise valid bond claim.
- Modifies the timeframe for service of a notice of nonpayment with respect to rental equipment.
- Provides that contractors are entitled to attorney's fees for obtaining a judgment against an insurer for failing to make a payment under a bond.

The bill does not have a fiscal impact on state and local governments.

The bill provides an effective date of October 1, 2019.

<sup>1</sup> See Bond, Black's Law Dictionary (10<sup>th</sup> ed. 2014).

<sup>2</sup> S. 255.05, F.S.

## FULL ANALYSIS

### I. SUBSTANTIVE ANALYSIS

#### A. EFFECT OF PROPOSED CHANGES:

##### **Background**

###### *Construction Bonds*

A payment bond is a type of bond that guarantees that a contractor will pay subcontractors, laborers, and material suppliers for their work.<sup>3</sup> It forms a three-part contract between the owner, the contractor, and the surety, and ensures that liens are not filed on the project. A payment bond for a construction project exempts the owner from the construction lien law because the surety insurer providing the bond guarantees the subcontractors, laborers, and material suppliers will receive payment for their work or materials. Current law requires contractors to obtain a payment bond for public projects over \$100,000.<sup>4</sup>

A performance bond guarantees the satisfactory completion of a project by a contractor, and protects the owner from loss should the contractor fail to perform in accordance with a contract's terms and conditions.<sup>5</sup> If the contractor does not complete the project, the surety will either pay for completion or hire a contractor to complete the project. Current law requires a contractor to obtain a performance bond for public projects over \$100,000.<sup>6</sup>

###### *Surety Insurance*

Surety insurance guarantees an obligee that the principal will fulfill an obligation. If the principal fails to do so then the obligee will recover from the surety. In Florida, "surety insurance" is defined to include payment and performance bonds.<sup>7</sup>

Payment and performance bonds involve a surety company that is paid a premium by a principal (i.e. general contractor) and agrees to stand in the place of the principal in the event of default to either the performance or payment of the contract. Unlike customary two-party insurance agreements, which involve the insurer and the insured, a surety agreement is a three-party agreement that consists of:

- The obligee, who may be either the person purchasing the performance from the contractor in the case of a performance bond, or the subcontractor, laborer, or materialman expecting payment from the contractor in the case of a payment bond;
- The principal (i.e. the general contractor); and
- The surety, who provides the bond to protect against the principal's default.

###### *Florida's Construction Lien Law*

Under Florida law, any person who provides services, labor, or materials for improving, repairing, or maintaining real property (except public property) may place a lien on the property, provided the person meets the procedural guidelines set forth in statute.<sup>8</sup> The lien law ensures such persons receive payment for their labor, services, or materials.

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<sup>3</sup> See Bond, Black's Law Dictionary (10<sup>th</sup> ed. 2014).

<sup>4</sup> S. 255.05, F.S.

<sup>5</sup> See Performance Bond, Black's Law Dictionary (10<sup>th</sup> ed. 2014).

<sup>6</sup> S. 255.05, F.S.

<sup>7</sup> S. 624.606(1), F.S.

<sup>8</sup> Ch. 713, F.S.

## *Payment Bonds for Public Projects*

Under current law, contractors, subcontractors, laborers, and material suppliers cannot place a lien on publicly-owned lands or buildings. Because of this limitation, and to protect those who work on public projects, the Legislature enacted s. 255.05, F.S.,<sup>9</sup> which requires a contractor who enters into a formal contract over \$100,000 with the state or with a county, city, political subdivision, private entity, or other public authority for the construction, completion, or repair of a public building, to deliver to the public owner a payment and performance bond issued by a state-authorized surety insurer. This requirement guarantees that subcontractors, laborers, and material suppliers will be paid for their labor, services, or materials, despite their inability to place a lien on the subject property.

In order to receive protection under a payment bond, a subcontractor, laborer, or material supplier must meet certain requirements:

- If the subcontractor, laborer, or material supplier is not in privity<sup>10</sup> with the contractor, he or she must provide written notice to the contractor that the lienor intends to look to the bond for protection within 45 days after commencing work or furnishing materials;
- All subcontractors, laborers, and material suppliers, regardless of whether they are in privity with the contractor, must provide written notice of nonpayment to the contractor. The notice may not be served within 45 days after commencing work or the first furnishing of materials or after 90 days of finishing work or the last furnishings of materials. With regards to rental equipment, notice may not be served after 90 after the date the rental equipment was on the jobsite and available for use; and
- All such persons must file an action against the contractor or the surety on the payment bond within one year after the performance of labor or furnishing of the materials.<sup>11</sup>

If a contractor has furnished a payment bond, and the state, county, municipality, or other public authority makes any payment to the contractor or directly to a subcontractor, laborer, or material supplier, the contractor may serve a written demand upon the subcontractor, laborer, or material supplier not in privity with the contractor for a written statement under oath setting out:

- The nature of the labor or services performed and to be performed, if any;
- The materials furnished and to be furnished, if known;
- The amount paid on the account to date; and
- The amount due on the account or to become due, if known.<sup>12</sup>

If the subcontractor, laborer, or material supplier fails to provide the written statement within 30 days after the contractor's demand or provides a false or fraudulent statement, her or she loses his or her rights under the bond. A subcontractor, laborer, or material supplier will also lose his or her rights under the bond for the negligent inclusion or omission of any information in the written statement if the contractor demonstrates prejudice from the negligent inclusion or omission.<sup>13</sup>

## *Payment Bonds for Private Projects*

Current law provides that an owner of private real property may exempt his or her property from the construction lien law when the contractor obtains a payment bond.<sup>14</sup>

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<sup>9</sup> Ss. 713.01(26) and 713.06(1), F.S.; *Aqua Plant Management, Inc. v. Paramount Engineering, Inc.*, 977 So. 2d 600, 603 (Fla. 4th DCA 2007).

<sup>10</sup> Privity is a legal relationship between two parties based on contract, estate, or other lawful status that confers rights or remedies. Cornell Law School, Legal Information Institute, <https://www.law.cornell.edu/wex/privity> (last visited Mar. 25, 2019).

<sup>11</sup> S. 225.05(2)(a), F.S.

<sup>12</sup> S. 255.05(8), F.S.

<sup>13</sup> *Id.*

<sup>14</sup> S. 713.23(1), F.S.

Specifically, s. 713.23, F.S., provides that an owner's property is exempt from construction lien law if the contractor:

- Obtains a bond in at least the amount of the original contract price before commencing construction;
- Attaches a copy of the bond to the notice of commencement (NOC) when the NOC is recorded;
- Uses a surety insurer authorized to do business in this state; and
- Conditions the bond to require the contractor to promptly make payments for labor, services, and material to all obligees under the contractor's direct contract with the owner.

In order to receive protection from the bond, a subcontractor, laborer, or material supplier must meet certain requirements:

- If the subcontractor, laborer, or material supplier is not in privity with the contractor, he or she must provide written notice to the contractor that he or she intends to look to the bond for protection within 45 days after commencing work or furnishing materials;
  - However, if the bond is not recorded with the NOC, the subcontractor, laborer, or material supplier may elect to serve the contractor with the written notice within 45 days of receiving a copy of the bond.
- All subcontractors, laborers, and material suppliers, regardless of whether they are in privity with the contractor, must provide written notice of nonpayment to the contractor and the surety no later than 90 days after the final furnishing of labor, services, or materials. The written notice of nonpayment may be substantially in a form which includes the following:
  - The name and address of the notice provider;
  - The name and address of the surety;
  - A description of the services provided or materials furnished;
  - A description of the real property improved;
  - The amount due and unpaid; and
  - The notice provider's signature.
- All such persons must file an action against the contractor or surety within one year of the final furnishing of labor, services, or materials.<sup>15</sup>

### *Attorney Fees*

Pursuant to s. 627.48, F.S., parties that prevail against insurers in court are entitled to an award of reasonable attorney fees. The purpose of this section is to place the insured in the place he or she would have been had the insurer paid the insured's claim without causing the insured to hire counsel and incur fees.<sup>16</sup>

Section 627.756, F.S., provides that owners, subcontractors, laborers, and material suppliers that bring lawsuits against surety insurers for failing to make a payment under a payment or performance bond are also entitled to an award of attorney fees under s. 627.48, F.S.

### **Effect of Proposed Changes**

#### *Payment Bonds for Public and Private Projects*

The bill provides that a subcontractor, laborer, and material supplier's written notice of nonpayment must be made under oath and include the following:

- The name of the contractor and the contractor's address;
- The name of the surety and the surety's address;
- The nature of the labor or services performed;
- The nature of labor or services to be performed, if known;

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<sup>15</sup> S. 713.23(1)(c)-(e), F.S.

<sup>16</sup> *Johnson v. Omega Ins. Co.*, 200 So. 3d 1207, 1215-16 (Fla. 2016).

- The materials furnished;
- The materials to be furnished, if known;
- The amount paid on the account;
- The amount due and the amount to become due, if known; and
- The notice provider' signature and address.

The bill provides that with respect to rental equipment for private construction projects, the notice of nonpayment may not be served later than 90 days after the date the rental equipment was on the job site and available for use.

The bill also provides that a subcontractor, laborer, or material supplier who files a fraudulent notice of nonpayment loses his or her rights under the bond. This is a complete defense to his or her claim against the bond. A notice of nonpayment is fraudulent if the subcontractor, laborer, or material supplier:

- Willfully exaggerated the amount due;
- Willfully included a claim for work not performed or materials not furnished; or
- Prepared the notice with willful and gross negligence, which resulted in a willful exaggeration.

However, a minor mistake in the notice or a good faith dispute as to the amount due does not amount to a willful exaggeration that defeats an otherwise valid claim against the bond. Further, the negligent inclusion or omission of any information in the notice of nonpayment that has not prejudiced the contractor or surety does not defeat an otherwise valid bond claim.

#### *Attorney Fees*

The bill adds contractors to the list of people entitled to attorney fees under s. 627.48, F.S., for obtaining a judgment against an insurer for failing to make a payment under a payment or performance bond. The bill also declares that this provision does not apply to payment or performance bonds issued before October 1, 2019.

#### B. SECTION DIRECTORY:

- Section 1: Amending s. 255.05, F.S., relating to bond of contractor constructing public buildings; form; action by claimants.
- Section 2: Amending s. 627.756, F.S., relating to bonds for construction contracts; attorney fees in case of suit.
- Section 3: Amending s. 627.428, F.S., relating to attorney's fee.
- Section 4: Amending s. 713.23, F.S., relating to payment bond.
- Section 5: Creates an unnumbered section of law providing applicability.
- Section 6: Provides an effective date of October 1, 2019.

## II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

#### A. FISCAL IMPACT ON STATE GOVERNMENT:

##### 1. Revenues:

None.

##### 2. Expenditures:

None.

**B. FISCAL IMPACT ON LOCAL GOVERNMENTS:**

1. Revenues:

None.

2. Expenditures:

None.

**C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:**

Unknown. It is unclear if the additional provisions required in order to serve a notice of nonpayment will have an effect on the private sector. The new provisions may make it more difficult for a subcontractor to file a notice of non-payment. Other provisions may make it easier for a prevailing contractor to collect attorney fees in a claim against the surety insurer.

**D. FISCAL COMMENTS:**

None.

**III. COMMENTS**

**A. CONSTITUTIONAL ISSUES:**

1. Applicability of Municipality/County Mandates Provision:

None.

2. Other:

None.

**B. RULE-MAKING AUTHORITY:**

None.

**C. DRAFTING ISSUES OR OTHER COMMENTS:**

None.

**IV. AMENDMENTS/ COMMITTEE SUBSTITUTE CHANGES**

On March 19, 2019, the Business & Professions Subcommittee adopted a strike-all amendment and reported the bill favorably as a committee substitute. The committee substitute:

- Deleted a requirement that a notice of nonpayment include copies of certain documents, such as:
  - The lienor's contract or purchase order and any amendments thereto;
  - Invoices, pay requests, bills of lading, delivery receipts, or similar documents; and
  - A statement of account reflecting all payments requested and received for the labor, services, or materials.
- Deleted the requirement that a notice of nonpayment include written verification under penalties of perjury. Instead, it requires that a notice of nonpayment be made under oath.
- Changed the timing for sending a notice of nonpayment for a private construction project from not earlier than 45 days after commencing work to not earlier than when payment of the amount claimed to be owed is considered past due.

On March 25, 2019, the Civil Justice Subcommittee adopted a strike-all amendment and reported the bill favorably as a committee substitute. The amendment:

- Replaced “labor, materials, or supplies” with “labor, services, or materials” for consistency;
- Provided that the negligent inclusion or omission of any information in the notice of nonpayment that has not prejudiced the contractor or surety does not defeat an otherwise valid bond claim;
- Declared that a notice of nonpayment is fraudulent if the claimant willfully included a claim for unperformed work or unfurnished materials;
- Removed superfluous prevailing party attorney fee language;
- Deleted a provision prohibiting the service of a notice of nonpayment before payment is considered past due; and
- Deleted all provisions relating to conditional payment bonds.

This analysis is drafted to the committee substitute to the committee substitute as adopted by the Civil Justice Subcommittee.