

SUBJECT: Prompt pay of vendors and subcontractors by governmental entities

COMMITTEE: State Affairs — committee substitute recommended

VOTE: 6 ayes — Marchant, Madden, B. Cook, J. Davis, Gattis, Goodman

0 nays

3 absent — Elkins, Lewis, Villarreal

WITNESSES: For — Jason Moore. (*Registered, but did not testify:*) Jack Baxley, Quoin Chapter Associated General Contractors; Jonathan Betcher, Austin Chapter Associated General Contractors; Travis Blair, Texas Construction Association; Mackie Bounds, Texas Construction Association and the Texas Masonry Council; Mike Boyle, Texas Building Branch - Associated General Contractors; John Braun, Austin Associated General Contractors and Braun Butler Construction; Travis Byrd; Yvonne Castillo, Texas Society of Architects; C.D. Henderson; Nancy Jones, Associated Plumbing-Heating-Cooling Contractors of Texas; Virginia Lee, Texas Glass Association; Doug McMurry, The San Antonio Chapter of Associated General Contractors of America; Shannon Noble, Texas Air Conditioning Contractors Association; Doug Nunnally, San Antonio Chapter of the Associated General Contractors; Evelyn Page; Nick Page, Texas Construction Association and the Central Texas Masonry Contractors Association; Doris Reid, Texas Contractors Association and Texas Masonry Council; Raymond Risk, Texas Construction Association; Raleigh Roussell, Quoin Chapter Associated General Contractors; Jason Schnurr; Jim Sewell, Associated General Contractors - Building; Linda Sickels, Trinity Industries, Inc.; Michael Smith; Joe Vogel; Richard White

Against — None

On — (*Registered, but did not testify:*) Thomas Bohuslav, Texas Department of Transportation

BACKGROUND: Government Code, ch. 2251, subch. B stipulates that payment by a government entity to a vendor is overdue on the 31st day after the later of the date the performance of the service under the contract is completed or the date the governmental entity receives an invoice, unless the governmental entity notifies the vendor of a bona fide dispute regarding payment.

Property Code, ch. 28 is the prompt payment statute for private construction work. Sec. 28.009 permits contractors and subcontractors to suspend work for nonpayment in private construction contracts, under certain circumstances. There is not a provision that allows contractors and subcontractors to suspend work for nonpayment in contracts with governmental entities.

Demobilization and remobilization costs are those incurred by companies in preparation for working on a job and cleaning up after a job; for example, the expense of transporting equipment, such as bulldozers, to or from the job site.

DIGEST: **Vendor remedy for nonpayment.** Government Code, ch. 2251, subch. D would allow a vendor (general contractor) to suspend performance of a contract with a governmental entity if the entity did not pay the vendor an undisputed amount within the time limits established by subchapter B of this section. The vendor would have to provide written notice to this effect and wait 10 days after giving notice before suspending work, unless the dispute involved a highway contract under sec. 2251.053.

A vendor who suspended performance would not be required to supply further labor, services, or materials until the vendor received full payment, including costs for demobilization and remobilization. The vendor would not be responsible for damages that resulted from suspending work if the governmental entity had not notified the vendor in writing before suspension of work that payment had been made or that a bona fide dispute for payment existed. Notice of a dispute would have to include a list of the specific reasons for nonpayment, and the vendor would be entitled to a reasonable opportunity to address any noncompliance.

Subcontractor remedy for nonpayment. A subcontractor of a vendor under contract with a governmental entity would have the same rights in regard to the vendor as this bill would grant the vendor in regard to the governmental entity.

Remedy for nonpayment regarding highway contracts. For highway construction contracts entered into with the Texas Department of Transportation (TXDOT), a vendor would have to provide written notice of nonpayment and intent to suspend work and wait 20 days after giving notice before suspending work. Notice would have to be sent by certified mail or personally delivered to the director of TXDOT, TXDOT director of construction, or the person designated in the contract to receive notice.

Notices. Notice or other written communication would have to be delivered to the person designated in the contract, or if the contract did not designate a person, the executive director or chief administrative officer of the governmental entity. If notice or other written communication was sent by certified mail, it would be effective on the day it was deposited in the U.S. mail. If notice was sent by electronic means, it would be effective on the date the designated recipient received it.

Miscellaneous provisions. The bill would allow the collection of attorneys' fees by the prevailing party in any arbitration, formal administrative or judicial action to collect an invoice payment or interest due under this chapter.

CSHB 2397 would stipulate that the rights and remedies provided by this bill would be in addition to those in other law and that no person could waive any right or remedy granted by this chapter.

The bill would take effect September 1, 2003.

**SUPPORTERS
SAY:**

CSHB 2397 would give vendors, and their subcontractors, the same rights in their dealings with governmental entities as they have in dealings with private parties. If a vendor is not paid promptly for work properly performed, and no valid dispute exists regarding payment, the vendor should be able to cease work until it receives payment. It is not appropriate that the government can compel a vendor to work without payment when a private party cannot. This bill would allow the vendor to suspend performance until payment was made, thereby encouraging the government to pay for services rendered.

CSHB 2397 would have built in safeguards to protect governmental entities from vendors and subcontractors wrongfully walking off a job. Prior to ceasing work, a vendor would have to give adequate notice of nonpayment

and the intent to suspend performance until payment was received. If there was a valid dispute over payment, performance could not be suspended until that dispute was resolved. If there was a claim of nonpayment, but the entity had paid the vendor or subcontractor, the entity would have at least 10 days to prove that payment had indeed been made before the vendor could suspend performance. TXDOT would receive even more notice — 20 days — to remedy any problems before the suspension of a highway construction project.

It is necessary to encourage governmental entities to promptly pay vendors because subcontractors are not bound to vendors under existing law the way vendors are bound to governmental entities. Currently, if an entity does not pay a vendor, who in turn does not pay a subcontractor, the subcontractor can legally leave the job for nonpayment. The vendor still would have the obligation to complete the contract, despite nonpayment, and would have to hire another subcontractor to complete the work.

Although this bill would not directly address what sort of condition the job site would have to be in before a vendor could suspend work, other areas of the law provide penalties for leaving the site in an unsafe state.

Requiring entities to pay demobilization and remobilization costs would both encourage prompt pay by governmental entities and reimburse subcontractors and vendors for their costs associated with suspending performance.

**OPPONENTS
SAY:**

This bill could endanger the public because it contains no protections to prevent a vendor from leaving a highway construction project, or any other project, in an unsafe condition.

CSHB 2397 would require governmental entities to pay demobilization and remobilization costs, which could be very expensive. Entities should not have to pay these additional costs when vendors or subcontractors walk off the job.

This bill would not offer subcontractors the same protection as vendors. If a vendor contracted with the governmental entity and the vendor hired a subcontractor to help in performing the contract, the subcontractor could not act against the entity itself to secure payment; it could seek redress only from

the vendor. Subcontractors should have the same rights regarding governmental entities as they would regarding vendors.

The bill would require more notice of a possible work suspension on a highway construction contract than it would for a highway maintenance contract. Both types of contracts would be with TXDOT, and it would not make sense to have two different lengths of notice.

NOTES:

The committee substitute differs from the bill as introduced by moving the sections regarding vendor remedy for nonpayment of a contract from subchapter B to subchapter D. It would add special notice provisions for highway contracts and would permit the prevailing party to recover attorneys' fees in arbitration or formal administrative or judicial actions to collect invoice payments or interest under this chapter.

The companion bill, SB 1720 by Williams, was considered in a public hearing in the Senate State Affairs Committee on May 8.