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**NULLIFICATION OF ACCEPTANCES, OPEN LIEN PERIODS
AND DEBARRING SURETIES - A LOUISIANA PERSPECTIVE**

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by
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This paper will highlight some issues dealing with the Louisiana Public Works Act,¹ the Louisiana Private Works Act² and the special statute enacted by the Louisiana Legislature which governs contracts issued by the Louisiana Department of Development and Transportation.³

Nullification of Acceptances

The issue of nullification of acceptance arises out of a 1991 amendment to Louisiana Revised Statute, Section 38:2241.1. The section provides, in pertinent part, as follows:

Whenever the public entity enters into a contract for the construction, alteration, or repair of any public works, in accordance with the provisions of R.S. 38:2241, the official representative of the public entity shall have recorded in the office of the recorder of mortgages, in the parish where the work has been done, an acceptance of said work or any specified area thereof upon substantial completion of the work.... **This acceptance shall not be executed except upon the recommendation of the architect or engineer of the public entity whose recommendation may be made upon completion or substantial completion of said public work within thirty days of completion of the project.** 'Substantial completion' is defined for the purposes of this Chapter, as the finishing of construction, in accordance with the contract documents as modified by any change orders agreed to by the parties, to the extent that the public entity can use or occupy the public works or use or occupy the specified area of the public works for the use for which it was intended. The recordation of an acceptance in accordance with the provisions of this Section upon substantial completion shall be effective as an acceptance for all purposes under this Chapter.

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¹ LA. REV. STATS. ANN. §§ 38:2181–38:2226 & 38:2241–38:2249.

² LA. REV. STATS. ANN. §§ 9:4801–9:4842.

³ LA. REV. STATS. ANN. §§ 48:250–48:256.12.

The highlighted portion of the statute is the source of the problem. The argument advanced by claimants who have filed untimely statements of claims is that an acceptance of a public project filed more than 30 days prior to actual completion of the project is a nullity, rendering their late filed claims timely.

The first case to deal with this issue arose in the context of the bankruptcy case of Whitaker Construction Company,⁴ a contractor located in Shreveport, Louisiana. Among the contracts performed by Whitaker, was a contract with the City of Shreveport for the renovation and improvement of Independence Stadium, the site of the annual Independence Bowl. One of the most, if not the most, critical factors involved with the project, was completion of the work so that the 2001 Independence Bowl could take place the end of December 2001. Although not recorded until January 10, 2002, upon the recommendation of the architect for the City of Shreveport, the work was accepted as substantially complete and the owner assumed full possession at noon on December 22, 2001. The 2001 Independence Bowl was played in the stadium as scheduled. Within the lien period, some statements of claims were filed; however, most were not. Four of the liens at issue were filed during the period June through September 2002. The remaining three liens at issue were filed on February 28, 2003.

As the untimely claims would affect the administration of the bankruptcy estate of Whitaker, the debtor made demand for cancellation of the recordation of the late filed statements of claim. When the claimants declined to do so, the debtor filed an adversary proceeding against the claimants.⁵ Ultimately, the issue was presented by way of cross motions for summary judgment. The Bankruptcy Judge found that work had continued until April 2002, that the recordation of the acceptance was a null and void and ruled in favor of the claimants.⁶ On appeal, the District Court affirmed the judgment of the Bankruptcy Judge.⁷ The matter is now on appeal to the United States Court of Appeals for the Fifth Circuit⁸ and is awaiting decision.

“Because of the need to protect those performing labor and furnishing materials for public works, the Legislature in 1918 passed Act 224, the precursor to current public works statutes, La. R.S. 38:2241 *et seq.*, granting rights to laborers and materialmen involved in public works.” *Wilkin v. Dev Con Builders, Inc.*, 561 So. 2d 66, 70 (La. 1990). It is a long-standing principle of statutory interpretation in Louisiana that lien statutes are *stricti juris* and should be strictly construed such that the privileges granted are not extended beyond the statutes. *State v. McInnis Bros. Constr.*, 701 So. 2d 937, 944 (La. 1997) (citing *Guichard*

⁴ In Re Whitaker Constr. Co., 02–BK–12642 (Bankr. W.D.La. involuntary petition filed August 9, 2002).

⁵ Whitaker Constr. Co. v. Oak Cliff Mirror & Glass Co., No. 02–AP–1065 (Bankr. W.D.La. filed December 30, 2002).

⁶ Whitaker Constr. Co. v. Oak Cliff Mirror & Glass Co., No. 02–AP–1065 (Bankr. W.D.La. judgment issued October 6, 2003).

⁷ Whitaker Constr. Co. v. Oak Cliff Mirror & Glass Co., No. 03–AP–1959 (Bankr. W.D.La. judgment issued February 27, 2004).

⁸ Whitaker Construction Co. v. Benton & Brown, Inc. (In re Whitaker Constr. Co.), No. 04-30344 (5th Cir. appeal docketed on April 14, 2004).

Drilling Co. v. Alpine Energy Svcs, Inc., 657 So. 2d 1307, 1313 (La. 1995)); *Wilkin v. Dev Con Builders, Inc.*, 561 So. 2d at 71; *United Rentals Highway Tech., Inc. v. St. Paul Surety*, 852 So. 2d 1200, 1203 (La. App. 2d Cir. 2003). The reason for strict construction is that the statutes grant special rights to claimants who have no privity of contract with the public body. The argument being advanced by the untimely lien claimants, if successful, would turn the Louisiana Public Works Act on its ear.

The rights and privileges granted subcontractors and materialmen by the Legislature must be preserved by recordation of their statements of claim within the time delays established by the statutes. *Pratt v. Damon Castle Hall Co.*, 2 Pelt. 67, 1918 WL 1371 (La. App. Orleans 1918). Pursuant to Louisiana Revised Statute Section 38:2242 (B), a claimant must file his claim within forty-five days after recordation of the acceptance of the work or of notice of default of the contractor. If a claimant fails to preserve its statutory privilege by timely filing a sworn statement of its claim within the statutory time delay, the claimant has no right of action on the bonds. LA. REV. STAT. ANN. § 38:2247.

Acceptance is based upon substantial completion. Substantial Completion is a term of art defined in the statute⁹ and well recognized in the jurisprudence. It occurs when a project has reached the stage of completion at which it can be used for the purpose for which it was intended.

In the cases the cases which have dealt with this issue thus far, there has been no suggestion that the public owner acted fraudulently when it accepted the projects in question as substantially complete nor has there been any suggestion that the projects, in fact, were not substantially complete, at least, as defined by the statute.

The practical reality is that very rarely, if ever, is actual completion of a public works project achieved within 30 days of the filing of notice of the acceptance of the project as substantially complete.

The argument made by the lien claimants is that because the projects in question were not finally complete, which the claimants equate with completion of the punch list, the recordation of the acceptance of the projects as substantially complete is somehow invalidated, *i.e.*, treated as if never filed, resulting in a lien period which remains open indefinitely. Such an interpretation does not comport with the reading of the statutory section at issue, nor does it comport with the well thought out scheme established by the Louisiana Public Works Act. Also, such an interpretation would take the certainty provided by the Louisiana Public Works Act and replace it with uncertainty, basically, making the acceptance of any public contract as to which statement of claims are not filed timely, potentially the subject of litigation.

The sole change Louisiana Act 947 of 1991 made to Louisiana Revised Statute, Section 2241.1 was to add the phrase “within thirty days of completion of the project” to the third sentence. Prior to the 1991 amendment, the third sentence of Section 2241.1 simply required that the architect’s recommendation had to be made “upon completion or substantial completion of said public works.” The phrase added by Act 947 modifies the clause “whose

⁹ LA. REV. STAT. ANN. § 38:2241.1.

recommendation may be made.” The reading of the statute urged by the claimants would not only effect the deadline for filing claims on a project, but would also affect other rights and responsibilities under the Public Works Act. Among other things, acceptance triggers the commencement of the preemptive period for claims against the contractor and for claims by the contractor and the surety. LA. REV. STAT. ANN. § 38:2189; LA. REV. STAT. ANN. § 38:2189.1.

The first sentence of Louisiana Revised Statute Section 38:2241.1, by use of the word “shall,” requires a public entity to file an acceptance of the work upon substantial completion of the work. The Public Works Act does not provide for filing an acceptance upon substantial completion and then filing another acceptance upon final completion. There is also no provision in the Public Works Act for the automatic nullification or invalidity of the recordation of an acceptance, even if one were improperly filed. Acceptance is one of the central elements of the Public Works Act. Indeed, the public records doctrine charges all persons with the knowledge of the filing and puts them on notice of the necessity of protecting the special rights granted to them by the Public Works Act. *United Rentals Highway Tech.*, 852 So. 2d at 1200; *McConnico v. Red Oak Timber Co.*, 847 So. 2d 191 (La. App. 2d Cir. 2003).

A question arises as to how a lien claimants can protect its rights. The answer is that it could have filed a timely statement of claim. Also, rather than making a collateral attack long after the filing of the acceptance, if a lien claimant believes that it has the grounds to do so, it could take legal action, such as a mandamus proceeding, within the lien period, to have stricken from the public records the recordation of the notice of acceptance. It also does not take a great deal of imagination to determine who will bear the brunt of the loss in these situations. If the owner, at the end of the lien period, is furnished with a clear lien and privilege certificate, the public owner will pay the contractor its retainage. If, at a later date, it is determined that the acceptance was not timely filed, thus, reopening the lien period, any remaining contract balances will likely have been disbursed and the surety will be left holding the bag.

While the language of the provision at issue is not the most artfully drafted, the provision should be interpreted in a manner that is in harmony with, rather than in a manner that does violence to the statutory scheme established by the Louisiana Public Works Act. At this time, a state trial court has ruled that the filing of the acceptance is not nullified and the rights of the claimants have preempted. What the United States Court of Appeal, Fifth Circuit, will decide remains to be seen.

Open Lien Periods

This issue arises in connection with the interpretation and application of the provision of the Louisiana Private Works Act which establishes the periods during which claimants may file statements of claim and privilege. In the typical situation, notice of the contract will be filed and either a notice of termination of the work or an acceptance of the work. The time period for filing statements of claim and privilege under those circumstances is clear cut. The claimant has 30 days from the filing of either notice of termination of the work or an acceptance of the work as substantially complete within which to file. LA. REV. STAT. ANN. § 9:4822(A). The time period when notice of the contract is not filed is also clear cut. A claimant has sixty days from the filing of the notice of termination of the work or substantial completion or abandonment of the work, if a notice of termination of the work is not filed. LA. REV. STAT. ANN. § 9:4822 (C).

The problem arises when notice the contract is recorded and neither a notice of termination of the work nor an acceptance of the work as substantially complete is filed. That was precisely the situation in another case arising out of the Whitaker bankruptcy case.¹⁰

While the Bankruptcy Court decided the case on another issue, the District Court focused on LA. REV. STAT. ANN. § 9:4822 (C) in finding that the statement of claim and privilege at issue was timely.¹¹ LA. REV. STAT. ANN. § 9:4822(C) provides as follows:

Those persons granted a claim and privilege by R.S. 9:4802 for work arising out of a general contract, notice of which is not filed, and other persons granted a privilege under R.S. 9:4801 or a claim and privilege under R.S. 9:4802 shall file a statement of their respective claims and privileges within sixty days after:

- (1) The filing of a notice of termination of the work; or
- (2) The substantial completion or abandonment of the work, if a notice of termination is not filed.

The contract at issue was dated July 24, 2000. It was recorded in the mortgage records of Caddo Parish, Louisiana on July 27, 2000. Payment and performance bonds were furnished as required by the Louisiana Private Works Act. The City of Shreveport issue a Certificate of Occupancy on July 25, 2001. No certificate of substantial completion was ever filed, although the work was completed and the owner occupied the premises for the purpose for which the construction was intended.

The subcontractor who had not been paid in full for the work performed on the project was one of three petitioning creditors who filed an involuntary bankruptcy petition against Whitaker on August 9, 2002. Ultimately, the bankruptcy case was converted from a Chapter

¹⁰ Fitzgerald Contractors, Inc. v. Fidelity & Deposit Company of Maryland, No. 03AP-01034 (Bankr.

W.D.La. judgment issued March 26, 2004).

¹¹ Fitzgerald Contractors, Inc. v. Fidelity & Deposit Company of Maryland, No. 03-1757 c/w 04-0913 (W.D.La. judgment issued December 10, 2004).

7 to a Chapter 11 proceeding. On July 16, 2003, in the Whitaker bankruptcy case, the subcontractor filed an adversary complaint against the surety seeking recovery of the amounts due and owing the subcontractor by Whitaker. The Bankruptcy Court ruled in favor of the subcontractor on the basis that the subcontractor's filing of the involuntary bankruptcy petition constituted a timely assertion of its rights within the meaning of the Louisiana Private Works Act, *i.e.*, within the one year and sixty day preemptive period established by LA REV. STATS. ANN. §§ 9:4822(C) & 9:4813(E).

Citing two Louisiana cases, *Bernard Lumber Co. v. Lake Forest Constr. Co.*, 572 So. 2d 178, 181 (La App 1st Cir. 1990) and *Rowley Co. v. Southbend Contractors, Inc.*, 517 So. 2d 1260, 1261 (La. App. 4th Cir. 1987), *writ not considered*, 519 So. 2d 139 (La. 1988), the District Court ruled that because a notice of termination was not filed, the time period during which a claimant had to file its statement of claim and privilege never began to run.

Bernard Lumber did rule as the District Court ruled in the case at issue; however, the ruling in *Rowley* produced the same result but because the notice of termination was found to be deficient. The rulings in *Bernard Lumber* and *Rowley*, as well as in the case at issue are based upon the assumption that the fundamental aim of the Louisiana Private Works Act was to protect materialmen, laborers and subcontractors who contributed to the construction project. While protection of claimants were certainly an important purpose of the Louisiana Private Works Act, as discussed, *supra*, with respect to the Louisiana Public Works Act, the jurisprudence has long recognized that the Act is in derogation of common property rights and that the Act is *stricti juris*. The legislature, in adopting the Louisiana Private Works Act, established a scheme which was intended to cover the realm of possibilities, create certainty and not to leave a gaping hole in that scheme. It must be presumed that the language in LA. REV. STAT. ANN. § 9:4822 (C) which reads "and other persons granted a privilege under R.S. 9:4801 or a claim and privilege under R.S. 9:4802...." is in the statute for a purpose. LA. REV. STAT. ANN. § 9:4801 grants a privilege, among others, to contractors and laborers or employees of the owner. LA. REV. STAT. ANN. § 9:4802 similarly grants a privilege, among others, to subcontractors, laborers or employees of the contractor or a subcontractor and sellers of goods to the contractor or contractor. The clear purpose of that language is to establish a scheme which covers all claimants and establishes a time certain with which for such claimants to file their statements of claim.

The District Court decision is on appeal to the United States Court of Appeal, Fifth Circuit. Both the open lien period issue and the question of whether the filing of the involuntary petition constituted a timely assertion of the claimant's rights under the Louisiana Private Works Act will be before the Fifth Circuit.

Debarring Sureties

Louisiana has a special statute which governs contracts issued by the Department of Transportation and Development (“DOTD”) on its own behalf, as well as those it lets on behalf of other public entities.

For purposes of this paper, the primary focus will be on LA. REV. STAT. ANN. § 48:255.2, which deals with the liability of the surety in case of default of the contractor. LA. REV. STAT. ANN. § 48:255.2 provides as follows:

Within thirty days after default by a contractor on a public works project, the department shall notify the surety company with whom the contractor acquired a performance bond. Such notification shall be in writing by certified mail or overnight delivery. Within thirty days of receipt of such notification, the surety company shall present to the department either a plan assuming performance on the contract and procuring, or tendering completion of the project, the bond penal sum, or provide the public entity in writing with a reasonable response for the contractor's alleged default. If no plan is presented by the surety company and the public entity completes the project, the surety company shall then be responsible for payment to the public entity of the costs of completion of the project and stipulated damages assessed by the public entity up to the total amount of the bond purchased by the contractor. In addition, if the surety company has not timely completed the project and a court of competent jurisdiction has determined that the surety company has in bad faith refused to take over the project as provided in this Section, the surety company shall be responsible for the payment of any stipulated damages for any delay in the completion of the project as specified in the original contract and any reasonable attorney fees and court costs incurred by the public entity in collection of the payments required by this Section.

Although the response time provided in the statute is short and there have been attempts to reduce it further, at first reading, the statute appears to be fairly even handed. While a negative inference, the statute could be read to provide that if the surety presents a plan to the Department, within thirty days of receipt of written notification of its principal's default, the surety will not be responsible for the payment of stipulated damages. Think again!

Those sureties who have dealt with a default on a DOTD contract know that is a pipe dream. Regardless of whether the statute can be read in that manner, the Department of Transportation and Development does not do so. At the outset, the surety is working within an abbreviated time period. Performing the analysis of the project that sureties typically do will be difficult, if not impossible, within the time period allowed by the statute. Understanding, much less vetting the contractor's defenses, may be another casualty of the time period within which the surety must respond.

In any discussions with DOTD, the surety will be reminded of the provisions of the Louisiana Standard Specifications For Roads and Bridges. See STATE OF LOUISIANA DEPARTMENT OF TRANSPORTATION AND DEVELOPMENT, LOUISIANA STANDARD SPECIFICATIONS FOR

ROADS AND BRIDGES (2000 ed.) (cited as LaDOTD Standard Specifications). LaDOTD Standard Specifications, Section 108.08 deals with the failure of the contractor to complete the work within the contract time. Stipulated damages are established by that section and are based upon the amount of the contract and whether the contract time is expressed in calendar days or a fixed date, on the one hand, or working days, on the other hand. LaDOTD Standard Specifications, Section 108.08 provides that the contractor will “automatically be subject to stipulated damages by the expiration of the contract time on the project and the contractor hereby waives any requirement of written notice of default for failure to attain completion of the project within the contract time.” Default and termination are dealt with by Section 108.09. In addition to the typical provision one would expect to see, it is also provided that a contractor will be in default if it allows any final judgment to stand unsatisfied for a period of fourteen calendar days or is a party to fraud. LaDOTD Standard Specifications, Sections 108.09 (a)(3) & (a)(12).

The real source of the problem is to be found in LaDOTD Standard Specifications, Section 108.09 (c), which reiterates, but also elaborates upon LA. REV. STAT. ANN. § 48:255.2. LaDOTD Standard Specifications, Section 108.09 (c) provides, in part:

If no plan is presented by the surety, **or at any time if immediate action must be taken to protect the public interest** or the safety of the public or workers, the Department will take the prosecution of the work out of the hands of the contractor or surety, may appropriate or used the materials and/or equipment on the project, or may enter into an agreement for completion of the contract or use other methods as required for completion of the contract in an acceptable manner.

In the eyes of DOTD, this provides the Department with the sword of Damocles. The surety must either respond as the DOTD wishes or face the threat that prosecution of the work will be taken out of the hands of the contractor or surety and the word debarment is not far behind.

However, there is no provision that permits the DOTD to bar a bonding company that has the statutory requirements set forth in LA. REV. STAT. ANN. § 48:255(D) from writing bonds for projects with the DOTD. In fact, the sole remedies against the surety on the performance bond are set forth in LA. REV. STAT. ANN. § 48:255.2, which makes no mention of barring the surety from writing bonds for DOTD projects. Instead, it is the Louisiana Insurance Commissioner, not the DOTD, who is vested with the authority to regulate insurers who transact business in the state. See LA. REV. STAT. ANN. § 22:1457 & 22:1458.

Louisiana Revised Statute Sections 49:295.1 *et seq.* sets forth the procedures for the DOTD to disqualify a contractor. However, this statute makes no reference at all to sureties. The procedures outlined in the statutes requires the DOTD to institute a hearing procedure **before** debarring a contractor from future DOTD projects, and the hearing must afford the contractor an opportunity to be heard **before** debarment. Previously with sureties, the DOTD has not followed any of these procedures, and thus has denied sureties' their due process rights.

Another argument against debarment is that a Surety has a protected property interest in its license to sell bonds in the State of Louisiana. Procedural due process requires adequate and timely notice and a meaningful opportunity to be heard. If the DOTD follows the statutory debarment procedures for contractors, it then satisfies due process safeguards (although the debarment would nonetheless be *ultra vires* and subject to challenge). But summary debarment with only a subsequent offer of a hearing does not satisfy due process.

If faced with this situation, what is a Surety's remedy? The Supreme Court has made clear that a state actor may not use the Eleventh Amendment as a shield from injunctive and declaratory relief in the federal courts when a constitutional violation or *ultra vires* act is alleged. See *Ex Parte Young*, 209 U.S. 123, 28 S.Ct. 441 (1908); *Florida Dept. of State v. Treasure Salvors, Inc.*, 458 U.S. 670, 697, 102 S.Ct. 3304, 3321 (1982). Thus, filing suit in federal court to enjoin the DOTD prospectively from enforcing a debarment notice would be the first step. Consideration should also be given to requesting a preliminary injunction inasmuch as a debarment impacts not only a Surety's rights and business, but the ability of its client contractors to bid on DOTD projects. Further, the damages incurred by the surety and its clients could be staggering, making injunctive relief in the best interest of the taxpayers of the State.