CONSTRUCTION RISK MANAGEMENT REPORTER

ERNSTROM & DRESTE LLP

ContrACT

SPRING 2021 ISSUE 28

Total Lack of Direction Not Required to Show Independent Contractor Status

BRIAN M. STREICHER

It can be a significant question for contractors and their workers alike: who is an employee or an independent contractor? The answer has wide-ranging effects on the rights of the worker and the obligations of the hiring party, including vicarious liability for the worker's actions and, as in this case, the worker's rights and benefits under labor and employment laws.

At common law, a fact-specific test was used to answer the employee/independent contractor question:

> "[a]n employer-employee relationship exists when the evidence demonstrates that the employer exercises control over the results produced by [the worker] or the means used to achieve the results."[1]

This inquiry acknowledged that "the relevant indicia of control will necessarily vary depending on the nature of the work."[2]

The 2010 Construction Industry Fair Play Act (Fair Play Act) creates a presumption that a worker is an employee, but permits the rebuttal of the presumption of employment upon meeting certain criteria, including what is known as the "separate business entity test." The first criterion of this test requires that an independent contractor:

> "is performing the service free from the direction or

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"Substantial Completion Bill" Will Impact Punch Lists, Retainage

MATTHEW D. HOLMES

The New York State Legislature, with the support of construction industry groups, recently proposed legislation addressing an issue that too often hangs over heads of contractors: what is the meaning of the term "substantial completion" on a public project? The answer is important, as achieving it signals the final stages of a project (or portion thereof), puts a contractor's retainage within reach, and triggers other legal rights and obligations.

The latest effort provided a standardized definition of substantial completion as part of a bill to speed up the retainage process by triggering the public owner's punch list obligations. S.7664/A.9117, signed into law by Governor Cuomo near the end of 2020, sought to "clarify the meaning of substantial completion," address an ambiguity in existing law relative to the definition of completion and release of retainage, and to avoid "unnecessary" and "needless" disputes and delays. (See S.7664 – Sponsor Memo – Breslin). The bill amends State Finance Law 139-f and General Municipal Law 106-b relating to payment in public construction contracts.

S.7664/A.9117 provides an uncontroversial definition of the important term that conforms to most industry form contracts and documents.[1] The bill states that "substantial completion" is achieved for most public contracts when:

> "the state in the progress of the project when the work required by the contract with the public owner is sufficiently complete in accordance with the contract so that the public owner may occupy or utilize the work for its intended use."

The bill then obligates the owner to issue a complete punch list to a prime contractor after achieving substantial completion (within 45 days), and requires the prime contractor to provide a complete punch list to subcontractors that are owed retainage after receiving a copy of the owner's punch list (within 7 days, changed to 5 business days). So far, so good, right?

But before signing the bill,[2] Governor Cuomo expressed concerns over including any definition of "substantial completion." The accompanying Approval Memorandum stated that while the Governor supported the goals of S.7664/A.9117, "there were technical issues that could hamper public owner construction projects." To address the issues, there was:

> "an agreement with the Legislature to make certain technical changes to the bill, allowing public owner contracts to retain their distinct definition of substantial completion…"

This means that the S.7664/A.9117 definition of "substantial completion" will be eliminated, and soon.

These "technical changes" are currently making their way through legislative channels. Advocacy organizations indicate that the 45-day punch list procedure will likely remain

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intact, and language will be added to clarify "that substantial completion should be defined by public owners in their contracts."[3] The Senate has proposed "technical amendments," including S.880, already unanimously approved.[4] However, not only is the definition of substantial completion for public contracts removed entirely, S.880 provides that "substantial completion" for the purpose of triggering punch list obligations can be determined:

> "as such term is defined in the contract **OR** as it is ***contemplated*** by the terms of the contract." (Emphasis added).

It does not look like public owners will be mandated to define the term in the contract, only encouraged to do so. The law as it is likely to be implemented permits the use of the definition from the contract (if it exists) OR the fuzzy "as contemplated by the terms of the contract" standard that requires contactors to make efforts to clarify and articulate their views of when substantial completion occurs, especially as the project evolves, or as major portions are finished. This inclusion of an alternative standard could lead to confusion for contractors, or even abuse by public owners.

Although the so-called "substantial completion bill" and proposed amendments represent a missed opportunity to clarify and standardize an important term in public construction, there could be laudable benefits for contractors and subcontractors related to punch lists and retainage. Receipt of a punch list should now confirm substantial completion was reached, which also means a reduction of retainage from 5% to two times the value of the punch list items. The requirement that punch lists itemize "all remaining items to be completed by the contractor" will (hopefully) curtail the common "rolling" punch lists received after the building is occupied and being used for its intended purpose. (*See* S.7664/A.9117 and S.880). The timing mechanism for the issuance of punch lists could ultimately serve to bring projects to their successful conclusions by giving contractors and subcontractors all of the information they need to promptly obtain their final payment of retainage. But if the owner and contractor do not agree as to whether substantial completion has been reached, a snag in retainage will exist regardless of the new law. E&D

1 For example, the definition is little different than the one included in the New York Office of General Services – Design and Construction Group Document 007213 General Conditions: 2.21 The term "substantial completion" means that the Work or major milestones thereof as contemplated by the terms of this contract are sufficiently complete so that the Work can be used for the purpose for which it is intended.

2 The bill became Chapter 341 Laws of 2020.

3 http://www.nesca.org/images/newsletters/January%202021.pdf

4 Assembly bill A.967 proposes the same terms as S.880.

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> control over the means and manner of providing the service, subject only to the right of the contractor for whom the service is provided to specify the desired result."

This poses the question: what degree of control must the employer exercise in order to create an employer-employee relationship? The Appellate Division, Third Department recently clarified the answer in the case of *Matter of Tuerk (Adelchi Inc.-Commissioner of Labor)*.[3] In *Tuerk*, a construction management company (CM), hired an individual (the Claimant) through his business entity to perform residential renovation and remodeling work. Claimant later filed for unemployment insurance benefits against CM. The Department of Labor (DOL) found that Claimant was CM's employee. CM was thus liable for additional unemployment insurance contributions. CM appealed to an Administrative Law Judge (ALJ), who upheld the DOL's decision, determining that CM failed to provide any proof that "[Claimant] was ***free from any direction or control over the means and manner*** of providing the service." (Emphasis added). The Unemployment Insurance Appeal Board (the Board) then adopted the ALJ's factual findings and legal analysis, holding CM liable.

On appeal to the Third Department, CM argued that the Board misconstrued the first criterion of the separate business entity test under the Fair Play Act by requiring proof of a lack of any direction or control over Claimant. CM maintained that the first criterion was merely a codification of the common-law rule in which the relevant indicia of control will necessarily vary depending on the nature of the work.

The court agreed with CM, expressly rejecting the Board's requirement of a "total lack of direction or control over a business entity." The Fair Play Act was enacted to enforce long-standing employment laws rather than to create new standards, the court said, and CM need only prove that the:

> "relationship as a whole did not show sufficient control over the results produced or the means used to achieve the results by the contractor to reflect an employer-employee relationship."

The court found that "incidental control over the results produced" does not, without more, reflect an employer-employee relationship. The matter was remitted to the Board to determine whether CM met the first criterion under the proper standard.

The result in *Tuerk* is a favorable one for contractors facing scrutiny under the Fair Play Act and represents a reasonable restraint on the trend toward broad application of the Act at administrative levels. While contractors do not have to show complete absence of any control, there is no bright-line guidance as to the degree of control that a contractor can exercise and still successfully rebut the presumption of the employment. At a minimum, contractors should ensure that contracts and work orders avoid language that appears to specify the means and methods of the worker. E&D

1 *Matter of Hertz Corp. (Commissioner of Labor)*, 2 N.Y.3d 733, 735 (2004).

2 *Matter of Vega (Postmates Inc.-Commissioner of Labor)*, 35 N.Y.3d 131 (2020).

3 184 A.D.3d 295 (3d Dep't 2020).

Open-Shop Contractors' Court Challenge to PLA on Thruway Project Fails

NELL M. HURLEY

New York courts ended an effort by non-union, "open-shop" contractors to annul the decision of the New York State Thruway Authority (NYSTA) to include a Project Labor Agreement (PLA) in the bid specifications of a 2017 project.[1] The Appellate Division, Fourth Department, ruled that the contractors lacked standing to commence the proceeding and failed to exhaust available administrative remedies prior to doing so. The New York State Court of Appeals then denied a motion to allow an appeal.

The matter stems from a NYSTA project for the replacement of eight highway bridges in central New York that required the successful bidder to adhere to a PLA mandating the use of union trade labor, among other things. The contractors did not submit bids for the work because of the PLA, but instead brought a legal proceeding to annul the NYSTA's inclusion of the PLA arguing that it effectively excluded open-shop construction firms, such as themselves, from bidding on the project in violation of the New York State Constitution, the Labor Law, the State Finance Law, and the Legislative Law.

The contractors amended the petition to include the firm ultimately selected for the project via the bid solicitation process. The winning bidder asserted affirmative defenses and objections that the contractors lacked standing and failed to exhaust their administrative remedies, and the trial court dismissed the petition. The contractors appealed.

The Appellate Division held that the contractors failed to establish the requisite injury to entitle them to common law standing and the right to bring suit because:

> "…the alleged harm occurred, not by their failure to secure the winning bid, but via their voluntary decision to entirely forego the bid solicitation process."

You cannot complain that you were fouled if you are not in the game, so to speak.

Further, the court found, even if the contractors were injured, any economic injury or lost business opportunity suffered does not fall within the zone of interests protected by the state's competitive bidding statutes. A disinclination by non-union contractors to submit bids where a PLA is applicable to the project does not preclude competition such that the competitive bidding mandate [of the statutes] is offended, opined the court.

The court found the contractors' claims of citizen taxpayer standing under the State Finance Law were precluded because of NYSTA's status as a public authority, which "enjoys an existence separate and apart from the State, even though it exercises a governmental function." In addition, such standing is precluded because the contractors challenged the contract's PLA requirement, noted the court, not the unlawful expenditure of State funds. Common law taxpayer standing is also unavailable, the court found, because the contractors are not seeking review of legislative action and are unable to show that an "impenetrable barrier to judicial review" of the PLA requirement is created by failure to grant standing.

Finally, the court held that dismissal was warranted because the contractors failed to exhaust their administrative remedies before commencing the proceeding. The formal protest process contained in the bid specifications is a condition precedent to commencing litigation, the court ruled, and the contractors failed to perform it. The court further rejected the contractors' assertion that pursuit of the administrative remedies would have been futile, finding instead that there was merely "some reason to doubt" that such remedies would have succeeded.

The decision in this case confirms that a direct legal challenge to a particular project PLA is unlikely to be successful, at least by a non-bidder. With Governor Cuomo's $306 billion infrastructure plan, and the influence of the unions in New York State, the inclusion of PLAs will be increasingly common. Of course, PLAs have always been controversial, particularly when mandated for public works projects. Many construction industry groups oppose them, saying PLAs actually increase a project's cost by decreasing competition. They seek to keep the government's thumb off the scale on the issue of union versus non-union labor by supporting legal, legislative and executive efforts to allow all contractors to fairly complete for public construction projects. For now, at least, those efforts will continue to be profoundly tested, as will open-shop contractors who must navigate an increasingly PLA-friendly construction landscape. E&D

1 *Matter of Barrett Paving Materials, Inc. v. New York State Thruway Auth.*, 184 A.D. 3d 1173 (4th Dep't 2020), *lv. denied*, 35 N.Y. 3d 916 (Oct. 22, 2020).

John Dreste, right, and Tim Boldt, in background, presented The Salvation Army of Greater Rochester a check for $2,500 on behalf of Ernstrom & Dreste, LLP as a donation to the 2020 Red Kettle Campaign. The event took place on-air during the televised *Salvation Army Red Kettle Telethon* on November 18, 2020 in Rochester, New York.

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Ernstrom & Dreste, LLP also publishes the Fidelity and Surety Reporter. If you would like to receive that publication as well, please contact Clara Onderdonk at conderdonk@ed-llp.com. Copies of ContrACT Construction Risk Management Reporter and The Fidelity and Surety Reporter can also be obtained at Ernstrom & Dreste, LLP's website (ernstromdreste.com).

FIRM NEWS

John W. Dreste was named the *Best Lawyers® 2021 Litigation – Construction "Lawyer of the Year"* in Rochester, New York.

John Dreste co-presented the program entitled *A Practical Guide to Construction Litigation from Experienced Practitioners* put on by the Monroe County Bar Association in Rochester, New York on March 3, 2021.

John Dreste and Kevin Peartree presented together on the topic of design delegation at the AGC NYS Virtual Construction Industry Conference on December 10, 2020.

Kevin Peartree was the featured speaker on the ConsensusDocs Master Subcontract Agreement at the AGC Joint Contractors Virtual Conference on November 12, 2020.

Todd Braggins attended the Philadelphia Surety Claims Association annual golf outing at Bala Golf Club in Philadelphia on October 26, 2020.

Matt Holmes presented on the topic of "Bid Errors" at the ABA TIPS *Fidelity and Surety Law 2021 Virtual Midwinter Conference: Construction Lawyer as Disaster Artist* held on Feb. 3-4, 2021.

Todd Braggins is authoring an article on the topic of the bond producer's role in financing the principal to be published in the National Association of Surety Bond Producers upcoming *Surety Bond Quarterly*.