

Protecting Yourself and Your District in the Use of “Piggyback” Contracts

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Three Basic Ways to Protect Your District

- Obtain performance and payment bonds
- Execute front-end documents
- Follow California case law guidance



Aurora Modular: A Case for Obtaining Bonds

- Aurora Modular, one of largest suppliers of modular classrooms unexpectedly went out of business in August 2004.
- School districts with Aurora Contracts were split into two classes: the Haves and the Have-Nots.



The Purpose of Bonds:

- The purpose of a Performance Bond is a guarantee to the district the performance of the terms of the contract.
- The purpose of a Payment Bond is to provide recourse to those unpaid by the principal for their services or materials.



Aftermath of Aurora

- Districts that had bonds were protected financially. They compelled sureties to honor their bonds and complete performance.
- Districts that did not have bonds were left with the following problems:
 - Incomplete work and materials
 - Liability for unpaid subcontractor claims
 - Need for revenue where contracts had been pre-paid



Code of Civil Procedure Section 3247

- (a) Every original contractor to whom is awarded a contract by a public entity, . . . in excess of twenty-five thousand dollars (\$25,000) for any public work shall, before entering upon performance of the work, file a payment bond with and approved by the officer or public entity by whom the contract is awarded.

A public entity shall state in its call for bids for any such contract that a payment bond is required in the case of such expenditure.



Payment Bonds

- *A subcontractor may hold a public entity liable for failing to discharge its duty under Civil Code section 3247. N.V. Heathorn Inc. v. County of San Mateo (2005) 126 Cal.App.4th 1526.*
- *A public entity must make certain that the payment bond is sufficient and issued by an admitted surety. Electrical Electronic Control, Inc. v. Los Angeles Unified School District (2005) 126 Cal.App.4th 601.*
- *School Districts may only approve the bond if it complies with Civil Code Section 3248 with respect to the language and sufficient amount.*



Performance Bonds

- Required by Title 2, Section 1863.20 of the *California Code of Regulations*.
- As a matter of prudent practice, should be obtained because they benefit the public entity owner.
- In the event of contractor default, public entity can compel surety to assume and discharge performance.



Follow Up: Front-End Documents

- Good Practice to follow-up a purchase order with a complete set of front-end documents.
- Per an approved Purchase Order, parties are bound to certain contractual obligations as set forth in the Purchase Order and original contract.
- However, there are no restrictions on creating more stringent terms.



Follow Up: Front End Documents

- There is no restriction on creating more stringent terms to a “piggyback” contract.
- Must only make sure that said terms are not less stringent than the terms of the purchase order.



Front-End Documents

- Front- End documents formalize treatment of “Piggyback” Contract
 - Provide vehicle for procurement of bonds and insurance
 - Opportunity to add further terms and add standard protections



California Case Law Guidance

- *California Public Contract Code* § 20118 permits school districts to pay for “the reasonable costs . . . for furnishing the services incidental to the lease or purchase of the personal property.”



California Case Law Guidance

- There are no cases construing the meaning of “incidental” under *California Public Contract Code* § 20118.
- However, courts have construed the meaning of “incidental” in similar circumstances



California Case Law Guidance

- *Steelguard, Inc. v. Jannsen* (1985) 171 Cal.App.3d 79
 - *Steelguard* court based their definition of “incidental” on the State Office of Procurement and what they consider “incidental” with respect to the purchase of relocatable classrooms.



California Case Law Guidance

- The *Steelguard* court noted that where such installation comprises less than 10% of the total contract price, the Office of Procurement considers the work “incidental” and therefore, not subject to the State Contract Act. Where the installation work comprises more than 10, but less than 50%, of the contract price, the Office of Procurement then evaluates the contract on an individual basis to determine the most appropriate procurement method.



California Case Law Guidance

- On this basis, the *Steelguard* court held that “portable classrooms are within the definition of materials or supplies which involve only incidental onsite installation and that they are therefore not within the purview of the State Contract Act.”



California Case Law Guidance

- If the value of the construction services related to the delivery of modular classroom is less than 10% of the value of the modular components purchased or leased, then the construction services are likely to fall within the meaning of the word “incidental” as used in *California Public Contract Code* § 20118.
- If the value of those construction services is more than 10, but less than 50%, then the school district should determine on a case-by-case basis whether those services are incidental to the purchase or lease of the modular classrooms and should record and formalize any findings and their rationales.



California Case Law Guidance

- However, it is imperative to keep in mind that this issue has never been addressed with respect to *California Public Contract Code* §§ 20118 or 20652.
- The pending opinion of the Attorney General will be persuasive authority on the issue, but no position will be binding until it is presented in a California Court.

