



Michigan Contractors Heading for Greener Pastures: A Checklist for Doing Business in Other States

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It's no secret that the business climate for Michigan contractors is among the worst in the nation. Many local firms have, or are considering, competing for projects in other states, sometimes for the first time. But there are a variety of requirements and pitfalls that need to be considered before a shovel hits the ground. This brief outline covers the most significant of those.

employee located in the state that is qualified to serve as registered agent. Instead of registering, a contractor could form a new corporation or limited liability company in the state in which it wishes to transact business. A



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domestic entity has no obligation to register, but also must have a local registered agent. One significant advantage of forming a local entity is that it provides a separation of liabilities. The only assets at risk are those that are invested in the new entity, and if the project is unsuccessful, or uninsured personal injury or property damage claims arise, only the assets in that new entity will be at risk. However, forming a new entity adds to reporting requirements.

2. CONSTRUCTION LIEN LAWS.

Michigan contractors are tuned into Michigan's requirements of recording liens within 90 days of the last date of work and filing construction lien foreclosure suits within one year of recording the lien. But each state has its own construction lien procedures. In Florida, for example, an owner can file a notice contesting the lien, and a lien claimant must file a suit within 60 days or the lien expires. Any contractor performing construction

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1. QUALIFYING TO DO BUSINESS.

Each state has its own requirements on whether a "foreign" (out-of-state) entity must register to transact business in that state. The sanction for not registering usually means that a contractor has no right to enforce contracts in that state's courts, which could be catastrophic. Other sanctions can include fines, penalties and additional taxes. The tests on what constitutes transacting business at a level that requires registration varies by state, but can turn on whether a company has a physical presence in the state, whether it has employees in the state, whether it enters into and performs contracts in the state, and whether it has a bank account in the state. Registration is typically neither expensive nor difficult, but does add reporting requirements, and a foreign company must maintain a local registered agent to accept lawsuits filed in the state. There are services that will do this for an annual fee, if there is no

Subcontractor Wins Incorporation by Reference Dispute

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Incorporation by reference is a favorite shortcut of general contractors when they draft agreements with their subcontractors. This clause says in effect “rather than go to the trouble of figuring out which parts of my contract with the owner I need you to cover, I’ll just incorporate the whole darn thing and sort it out later.”

In a recent case, that shortcut cost the general contractor significant protection it might otherwise have had. After a contract was signed between the general and its subcontractor, a dispute arose that the parties were unable to resolve. The agreement allowed the subcontractor to sue the general if negotiations to resolve the dispute had failed, so the sub filed suit.

The general contractor claimed that the suit was filed too late. Apparently the prime contract between the owner and contractor had a 180-day deadline for filing suit. In this case the suit had been filed after the 180 days expired. The general contractor claimed that the 180-day deadline was, you guessed it, “incorporated by reference” into the subcontract.

But the general contractor had a problem, since the prime contract had two different “incorporation by reference” clauses. The first was very broad, but the second incorporated only those portions of the prime contract that were “in respect of the work.”

The two clauses were inconsistent. That is all the court needed to rule in favor of the subcontractor. The court found that the

inconsistency prevented the court from finding a “clear intent” of the contractor and the subcontractor to incorporate the 180-day time limit.

LESSONS TO BE LEARNED:

- If you are the general contractor, look at your incorporation by reference clause. Don’t have more than one! Better yet, consider replacing it with a more specific list of portions of the prime contract you wish to incorporate.
- Consider abandoning the phrase “incorporation by reference.” Instead, use more direct language such as:
 - The subcontractor promises to perform the following obligations of the general contractor that are contained in the prime contract, or;
 - The subcontractor agrees that the time limits for bringing claims under the prime contract, which are reproduced below, apply to claims under this contract.
- If you are the subcontractor, press the general contractor to explain which portions of the prime contract should apply to the subcontract. An ounce of prevention may be worth a pound of cure, as the general and the subcontractor found out in this case.

If you would like more information on how to avoid ambiguities with incorporation by reference clauses, or would like a sample clause for your next contract, please contact the author of this article or any other member of Miller Johnson’s Construction Industry Team.

MILLER JOHNSON “AT WORK”

AILEEN M. LEIPPRANDT – presented a “Introduction to Legal Risks and Responsibilities in Green Buildings” seminar at the 2010 Construction & Design Professionals’ Expo at The Pinnacle Center in Hudsonville.

RACHEL J. FOSTER – is a member of the Greater Kalamazoo Association of Realtors (GKAR) Risk Management Committee and was recently appointed to a subcommittee to create a Buyer’s Short Sale Disclosure form.

T.J. ACKERT, JEFFREY S. AMMON, and AILEEN M. LEIPPRANDT – will be presenting “Construction JEOPARDY!” as part of Construction Appreciation Night at the National Association of Women in Construction (NAWIC) Grand Rapids Chapter meeting on April 14.

J. SCOTT TIMMER – gave a presentation on the “Home Affordable Foreclosure Alternatives Program” (HAFA)

to Keller Williams Realty in Grand Rapids on March 25.

JEFFREY S. AMMON and **RACHEL J. FOSTER** – recently assisted a client in completing the acquisition of a warehousing facility in Florida comprising a total of 1,010,786 square feet for \$34.5 million dollars. The acquisition also involved the seller leasing back the facility.

work in a state must be completely familiar with that state’s lien laws.

3. BONDING REQUIREMENTS.

Each state has its own specific statutes regarding bonding requirements on public works projects. Texas, for example, requires public works contractors to post both a performance bond and a payment bond, each in the amount of the contract, for all projects above \$25,000.00. However, lower tier subcontractors and suppliers, which don’t have contracts with the prime contractor or a subcontractor of the prime contractor, may not have bond protection in that state. This highlights the importance of familiarity with local requirements before a project begins.

4. INSURANCE COVERAGE.

Insurance coverage can be divided into statutory requirements and contractual requirements. Each state has statutory workers’ compensation insurance requirements, as well as for automobile coverage. But both private developers and state and local governments will certainly impose contractual insurance requirements for automobile liability, commercial general liability, workers’ compensation and builder’s risk that comply with local law.

5. LICENSING AND CERTIFICATIONS.

Local licensing and certifications vary widely. Michigan’s own statutes illustrate this. Michigan requires a residential builder’s license for residential excavation, carpentry, roofing and a variety of other tasks. However, this license doesn’t allow residential plumbing, electrical or mechanical work. Indiana requires public works contractors to be certified by the state for any public work project in Indiana costing more than \$100,000.00. Certification requires answering Board inquiries as to the organization, and its personnel, equipment and experience. The Board has over 100 different categories for certification, but a contractor can only select four, based on its experience. By contrast, Nevada has six classifications for contractors, and requires four notarized references verifying at least four years of work experience in the classification that is sought. These huge variations by state mandate careful review of the requirements of the state for which a particular license or certification is sought.

6. TAXATION.

Most states have a state income tax, and a few, such as Texas and Florida, don’t. States that do have an income tax typically provide a credit to avoid double taxation in the state where the work was done and the state of residence of an employee. Different states emphasize different ways of obtaining tax revenue. California has a graduated income tax that reaches 10.55%. Sales tax in Chicago is 10.25%! But there is no sales tax in Alaska, Delaware, Montana, New Hampshire and Oregon. State business taxes provide even greater variation. A handy site for accessing state tax information can be found at www.business.gov/finance/taxes/state.html, which has, on a state-by-state basis, information on business tax registration, general tax information and forms, workers’ compensation insurance and unemployment insurance tax. It also has links to each state’s taxation department website.

7. RIGHT TO WORK AND PREVAILING WAGE LAWS.

All of the Sunbelt and most western states are “right to work” states, without forced union membership. Prevailing wage laws require workers on certain public construction contracts to be paid a specified minimum wage, often calculated from collective bargaining agreements. A total of 33 states have adopted such laws. These are sometimes referred to as “little Davis-Bacon Acts,” since they track the federal prevailing wage statute. As with “right to work” laws, the states without prevailing wage statutes are located in the Sunbelt and the West.

CONCLUSION

Ready to look for contracting opportunities in other states? Be prepared, and be successful. For additional information and detailed counseling as it relates to any specific state, please contact the author or your Miller Johnson attorney before taking action.

“AT WORK” *continued from page 2*

T.J. ACKERT and AILEEN M. LEIPPRANDT recently assisted a Michigan contractor in establishing, incorporating, and licensing a construction company in Florida.

“OPERATING EFFECTIVELY IN AN UNCERTAIN ECONOMY”

Join us at the **Miller Johnson Construction Industry seminar: “Operating Effectively In An Uncertain Economy.”** The seminar will be held in Grand Rapids on May 12. You can register at www.millerjohnson.com in the Events section.

Not All Prevailing Wage Laws Are Created Equal

by Keith E. Eastland; eastlandk@millerjohnson.com; 616.831.1749



Keith E. Eastland

For years, construction employers in Michigan have associated prevailing wage projects with Michigan's Prevailing Wage Act, and for good reason. Most of the available publicly funded construction work has not been funded with federal funds.

As such, some construction employers may have little, stale, or no experience dealing with the federal prevailing wage requirements. With the recent influx of billions of dollars in federal funding for construction, however, much of the available construction work is now subject to the Davis-Bacon Act.

You might be thinking "what's the big deal—a prevailing wage project is a prevailing wage project, right?" But that line of thinking can land you in a significant legal and financial pinch. Indeed, there are important differences between what is required under the state and federal acts. Don't overlook them. This article highlights a few of those differences.

- First, contractors on Davis-Bacon projects must pay their workers at least weekly and must submit a certified copy of weekly payrolls to the contracting agency in charge. This is most often done using the Department of Labor's Form WH 347. The same is not true under the state Act. The Michigan Act requires contractors to "keep an accurate record showing the name and occupation of, and the actual wages and benefits paid to, each construction mechanic," but it does not require weekly payments or certified payrolls.
- Second, employers on Davis-Bacon projects must examine all of their fringe benefits closely to determine whether credit will be permitted under federal law. There are generally two types of *bona fide* fringe benefits allowed on Davis-Bacon projects: funded and unfunded benefit plans. To receive credit toward the prevailing wage rate for "funded" benefits, the contractor must make *irrevocable payments to a trustee or third party pursuant to a fund, plan or program at least quarterly*. On the other hand, a contractor may receive credit for "unfunded" benefits such as vacation or sick leave *only* if the plan: (1) can reasonably be anticipated to provide benefits; (2) represents a commitment that can be legally enforced; (3) is carried out under a financially responsible plan or program; and (4) has

been communicated in writing to the affected employees. These federal requirements are much more exacting than those under Michigan's Act. Contractors simply cannot assume that their fringe credits will be the same for federal and state projects, and do so at their own risk.

- Third, the calculation of fringe credits is different. For instance, Michigan requires contractors to divide the yearly cost or contributions for an employee's fringe benefit by 2,080 hours. This holds true no matter how many hours the employee actually works. The same is not true for Davis-Bacon projects. On federal projects, contractors may divide the total cost of a *bona fide* fringe benefit by the actual hours an employee works. Further, when the total annual actual hours are unknown, contractors may use the actual hours worked by the employee in the previous month or in the same month from the previous year to determine the hourly credit.
- A fourth difference involves apprenticeship ratios. On Davis-Bacon projects, these ratios are derived from an employer's U.S. Department of Labor, B.A.T.-approved program and must be followed. The same is not true on state prevailing wage projects. But contractors should keep in mind that there may be other Michigan statutes that impose ratio requirements such as the Electrical Administrative Act.
- Finally, the available remedies are markedly different, and the penalties for violations are much more severe on federal projects. Contractors must keep in mind that the U.S. Department of Labor has specific legal authority to withhold contract funds as well as to seek debarment based on violations. The same is not true on state projects.

These are just a few of the important differences between state and federal prevailing wage law. There are others that you don't want to discover when it's too late. You can help prevent potential violations by contacting your Miller Johnson attorney to discuss specific differences that will apply *before* bidding or starting work on federally funded projects.

Should the Owner Give the Design-Builder a Chance to Fix Its Work?

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Jeffrey S. Ammon

An owner learned a painful lesson recently: it should have given its design-builder a chance to fix defective work. In this case the owner had hired the design-builder to design and install a new HVAC system for an auto dealership. Several months after the job was done, the owner experienced HVAC problems. Instead of contacting the design-builder, the owner hired a different engineering firm to examine the problem. That new company suggested that the entire system be removed and replaced. The owner agreed, the system was replaced, and the owner sued the original design-builder for the cost of replacement.

The owner lost because the owner breached a significant term in its contract with the design-builder. That contract required the owner to notify the design-builder of any problems with the system. It also required the owner to give the design-builder an opportunity to fix the problem. Only after those steps were completed would the owner be able to terminate the contract.

By ignoring the contract requirements of notice and opportunity to cure, the owner committed a substantial breach of its agreement with the design-builder. That breach excused the design-builder from responsibility for defective design.

Lessons to be learned from this decision:

- If you believe the other side is in breach, review carefully the contract provisions that describe your rights and obligations. Ignoring them could destroy your rights, which is exactly what happened to the owner in this case.
- Look at the AIA and other standard form agreements, which generally allow a contractor the right to cure defective work.

For more information, contact the author of this article or any other member of Miller Johnson's Construction Industry Team.



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