

Department of Planning and Budget

2019 Fiscal Impact Statement

1. Bill Number: SB1369

House of Origin ☒ Introduced ☐ Substitute ☐ Engrossed
 Second House ☐ In Committee ☐ Substitute ☐ Enrolled

2. Patron: Norment

3. Committee: Courts of Justice

4. Title: Virginia Public Procurement Act; statute of limitations on actions on construction contracts; statute of limitations on actions on performance bonds

5. Summary: Provides that no action may be brought by a public body on any construction contract, including construction management and design-build contracts, unless such action is brought within five years after substantial completion of the work on the project and that no action may be brought by a public body on a warranty or guarantee in such construction contract more than one year from the breach of that warranty, but in no event more than one year after the expiration of such warranty or guarantee. The bill also limits the time frame during which a public body, other than the Department of Transportation, may bring an action against a surety on a performance bond to within one year after substantial completion of the work on the project. Current law allows a public body, other than the Department of Transportation, to bring such an action within one year after (i) completion of the contract, including the expiration of all warranties and guarantees, or (ii) discovery of the defect or breach of warranty that gave rise to the action.

6. Budget Amendment Necessary: No

7. Fiscal Impact Estimates: Indeterminate, see Item 8.

8. Fiscal Implications: The fiscal impact of this bill is indeterminate.

Department of General Services (DGS): The bill is changing the current code section on performance bonds. Currently, public bodies can take action on a performance bond for any contract (goods, services, technology, and construction):

- (i) within one year after completion of the contract,
- (ii) within one year of the expiration of all warranties and guarantees, and;
- (iii) within in one year of the discovery of a defect or breach of warranty that gave rise to the action.

The proposed change will only permit the public bodies to take action on a performance bond for any contract (goods, services, technology, and construction):

- (i) within one year after *substantial* completion of work on the project.

This change may create an increased risk for the Commonwealth when establishing the contract. Additionally the change to “substantial” completion is a term that is used only for construction related contracts and may prohibit the public bodies from being able to require a performance bond on other types of contracts, further creating risk with non-construction contracts.

The bill is also adding a statute of limitations provision to the VPPA for construction contracts. Currently, the Commonwealth of Virginia is sovereign in the code and therefore not subject to the statute of limitations, unless expressly stated.

This will now limit public bodies to take action within:

- (i) five years after *substantial* completion of the work on the project.
- (ii) within one year from the breach of warranty and guarantee, but in no event no more than one year after expiration of such warranty and guarantee.

Defects in construction can appear after five years, and when identified can cost hundreds of thousands, or even millions, of dollars to correct, and this bill may prevent public bodies from holding the contractor responsible to the requirements set forth in the solicitation and contract. With this new language, when a defect is the result of the non-compliance to contract requirements it may result in the public body having the financial responsibility to correct.

One way to mitigate the increased risk that is expected from the addition of the statute of limitations on construction contracts is to increase the number of inspections performed during the construction process by DGS. DGS estimates that additional funds for 5 FTE positions, plus related non-personal costs, to perform project management responsibilities for construction contracts may be needed, and is estimated at \$1,000,000 annually. Additionally, in order to mitigate the financial risk DGS will evaluate all contracts for goods, services, technology and construction, to determine if more warranties and guarantees are necessary.

There is no provision that limits this bill to future solicitation/contract awards only, so this applies to all contracts previously made prior to this bill becoming law. DGS currently has identified a construction defect on project completed in 2013 and are seeking remedy with the contractor. This legislation may not allow DGS to pursue legal action against the contractor if they refuse to remedy the defect. The potential financial burden will be on the Commonwealth for the repair and it is estimated at \$3,100,000.

Virginia Department of Transportation (VDOT): The fiscal impact of the bill is indeterminate. Currently, the Commonwealth has sovereign immunity and is not subject to statutes that limit the time frame in which it must bring a legal action against a construction contractor who contracted with the Commonwealth. Many defects in construction work are latent and may take more than five years to be discovered. This bill would limit or eliminate the Department's legal remedies against construction contractors and their sureties for deficient or defective construction work or materials, shifting the risk of hidden defects to the VDOT. The result would be that VDOT and the Commonwealth may be left to bear the cost

of defective work or materials without recourse against the contractor or its surety, as is currently the case under existing law. At this time, the estimated impacts are still being determined.

Virginia Community College System (VCCS): As a public body, the VCCS relies on several parties to ensure completion of a construction project in accordance with the construction documents incorporated within construction contracts (i.e. architect-engineer of record, DGS/DEB professional staff, special material design inspectors, agency project inspectors). However, it remains the responsibility of the contractor to deliver a finished project with a warranty free of material and construction related defects. The statute of limitation created by this legislation may shift some responsibility for construction quality assurance to public bodies of the Commonwealth.

In order to mitigate the risk associated with this legislation, VCCS may need to increase front-end inspections of contractor's work in accordance with the required contract documents. The VCCS estimates that adding two additional full time inspectors to each of its six major capital projects; providing additional special inspections; requiring the AE to come to the site every week on active capital projects; and providing an elevated level of inspections and oversight on maintenance reserve projects at 23 community colleges may cost millions annually, however, the total cost is indeterminate at this time.

Other Higher Education Institutions: It is presently unknown how these provisions might impact the balance of Virginia's higher education institutions, all of which have active capital project.

9. **Specific Agency or Political Subdivisions Affected:** This bill as written applies to all state and local public bodies subject to the Virginia Public Procurement Act (VPPA), higher education institutions operating under Management Agreements and Memoranda of Understanding in the operational area of procurement (currently eleven Level III and Level II institutions), and local governments.

10. Technical Amendment Necessary: No

11. **Other Comments:** Companion to HB1667. This FIS has been revised to reflect additional information provided by DGS, VDOT, VCCS, Higher Education Institutions.