
**WHEN CONTRACTORS ROB PETER TO PAY PAUL:
CONSTRUCTION CONTRACTORS BOARD (CCB)
ENFORCEMENT ON DISPLAY IN RECENT CASE**

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Innovative Design & Construction LLC v. Construction Contractors Board, 278 Or App 448 (May 25, 2016) illustrates the potential reach of the CCB's enforcement power against contractors who use funds received for subcontractor or supplier bills incurred on new construction projects to pay off older debts incurred on earlier unrelated construction projects (termed by some to be the practice of "robbing Peter to pay Paul"). Although the CCB only sought a monetary penalty against Innovative, when reviewed in the light of other statutory enforcement tools at the CCB's disposal, the case suggests the CCB may seek to further extend its enforcement reach in the future to address contractors who "rob Peter to pay Paul."

In the appeals case, the contractor Innovative entered into various contracts with homeowners in 2006, 2007 and 2008. On each project mentioned in the opinion, the contractor failed to pay various subcontractors despite receiving more than enough funds to pay all subcontractors from the owners of the particular projects. After an investigation of the underlying transactions, the CCB issued a notice that proposed to assess a \$12,000 penalty against Innovative based on twelve different statutory violations. Innovative requested a hearing. *Innovative*, 278 Or App 451-452.

The basis of the CCB's enforcement action was ORS 701.098(1)(L)(as renumbered in 2009), which generally requires two elements: That a contractor has "*engaged in conduct as a contractor that is dishonest or fraudulent...that the board finds injurious to the welfare of the public.*" To effectuate the statute, the CCB promulgated OAR 812-002-0260, which provides "*dishonest or fraudulent conduct*" includes failing to pay subcontractors and suppliers that performed or supplied a particular project when the contractor has received sufficient funds to pay those bills from the particular project.¹ *Id.* at 453. The administrative law judge made various factual findings after a formal hearing and the CCB issued its final administrative order assessing a \$12,000 penalty. *Id.* at 451 n.1.

On appeal, Innovative argued the CCB exceeded its statutory authority by promulgating the portion of OAR 812-002-0260 that provides non-payment of subcontractors when payment has been received is "*dishonest or fraudulent.*" *Id.* at 453. The contractor, who represented itself at the administrative hearing without legal counsel, argued that "he" was honest and simply had cash flow problems. The court held the assertion of honesty at the hearing was insufficient to preserve the error it now raised on appeal. *Innovative*, 278 Or App at 455. The contractor also appealed on the basis that the CCB's interpretation of "*injurious to the welfare of the public*" under its regulation was erroneous. Again, the court held the contractor failed to preserve the error.

While *Innovative* does not create much law insofar as the appellant's arguments against similar CCB enforcement actions remain undecided, some remarkable insights about the reach of the CCB's enforcement authority can be drawn from the opinion. For example:

¹ See OAR 812-002-0260: "Dishonest or fraudulent conduct," as used in ORS 701.098(1)(L) and (4)(a)(D) includes, but is not limited to, the following: * * * (2) Failing to pay monies when due for materials or services rendered in connection with the applicant's or licensee's operations as a contractor when the applicant or licensee has received sufficient funds as payment for the particular construction work project or operation for which the services or materials were rendered or purchased; * * *

No Fraudulent or Dishonest Intent Required? Innovative argued in its brief on appeal that the CCB's regulation OAR 812-002-0260 exceeded the legislature's grant of authority. Specifically, Innovative argued that because the statute uses the terms "*dishonest*" or "*fraud*," the legislature only delegated rule making authority for a regulation that included a "*mens rea*" or intent element. Brief for Appellant at 11-14 (June 14, 2013). Again, the court held Innovative failed to preserve this argument for appeal. However, the CCB's appellate brief defended the lack of a *mens rea* requirement by arguing that fraudulent intent could be inferred from a failure to disburse funds in a different manner than was intended by the payor. Brief for Respondent at 9-11 (Oct. 11, 2013).

No Present Harm Required? Notwithstanding facts in the record that some subcontractors filed liens against some of the projects, the court's opinion suggests the CCB's interpretation of "*injurious to the welfare of the public*" does not require actual, present harm. Although dicta, the court opinion includes a quote from the administrative law judge's findings that Innovative's business practices pose a risk to "*any potential clients that their payments will be diverted from their own construction projects*" and to "*any subcontractor that it will not be paid for its work on a future project.*" *Innovative*, 278 Or App 456 (*Emphasis added*).

No Final Adjudication on Debt Required? Apparently none of the subcontractor debt described in *Innovative* had been adjudicated (rather, Innovative simply admitted a certain sum was owed). *Id.* at 452. Under ORS 701.102, the CCB may revoke, suspend or refuse to issue a license if a contractor incurs a "*construction debt*," which is generally defined as a debt related to construction activities in Oregon that has been reduced to final judgment, award or CCB order (with the possible exception of non-payment of wages). See ORS 701.102 and 701.005(4) (definition). The CCB's definition of "*dishonest or fraudulent*" effectively permits the CCB to assert its authority includes imposition of penalties involving debts that are not "*construction debts*"

under ORS 701.005(4). The CCB likely would argue this interpretation is permissible due to the focus on conduct involving the diversion of funds rather than simple non-payment of debt. *See e.g.* Respondent Brief at 9.

Financial Penalty for Non-Payment of Debts? In *Innovative*, the appellant argued the CCB sought a penalty of \$12,000 for twelve violations of ORS 701.102(1)(L), essentially for non-payment of debts. This author found no statute or regulation purporting to impose financial penalties for non-payment of “construction debts” under ORS 701.102. *See* OAR 812-005-0800 (titled “Schedule of Penalties”). To the contrary, a violation of ORS 701.102 (involving non-payment of “*construction debt*”) provides three penalties: License suspension, revocation or refusal (ORS 701.102(1)); probation with classes (ORS 701.102(3)); or the requirement of an enhanced licensure bond (OAR 812-003-0175 - Increased Bond, Letter of Credit or Cash Deposit Requirement, Past Unresolved Activity).

Emergency Suspension of License Without Prior Hearing. ORS 701.098(4) provides that upon certain criterion, the CCB administrator may, after making specific findings, “*suspend or refuse to renew a license without hearing in any case where the administrator finds a serious danger to the public welfare.*” (*Emphasis added*). The criterion includes the failure to maintain a bond, the failure to maintain insurance, incurring a “*construction debt*,” or “*dishonest or fraudulent conduct.*” As noted above, a “*construction debt*” is generally (except possibly in the case of wages) a debt owed pursuant to a final adjudication. ORS 701.005(4). *Innovative* demonstrates that a logical extension of the CCB’s OAR 812-002-0260(2) definition of “dishonest or fraudulent conduct” is that the CCB can suspend contractors for non-payment of *alleged* subcontractor debts that have not been proved to be owed. If robbing Peter to pay Paul is dishonest or fraudulent conduct that is a danger to public welfare without actual proof of present harm, what more is needed to be deemed a

“*serious*” danger to enable the CCB to issue an emergency license suspension?

In sum, while the *Innovative* case does not create much new law as the key arguments of appellant were not preserved, the case demonstrates the CCB’s breadth of enforcement powers and its willingness to push the margins of the statutes in particular instances.
