STATE OF CALIFORNIA
GRAY DAVIS, Governor

DEPARTMENT OF INDUSTRIAL RELATIONS
DIVISION OF LABOR STANDARDS ENFORCEMENT
LEGAL SECTION
455 Golden Gate Avenue, 9th Floor
San Francisco, CA 94102
(415) 703-4863

MILES E. LOCKER, Chief Counsel

May 17, 1999

Rich Clark
R.W. Clark Investigators
862 Sir Francis Drake Blvd., Suite 246
San Anselmo, CA 94960-1914

Re: Third Party Beneficiary Claims

Dear Mr. Clark:

This is in response to your April 5, 1999 letter to Labor Commissioner Marcy Saunders, wherein you ask us to reevaluate the issue of whether the Division of Labor Standards Enforcement ("DLSE") will accept unpaid wage claims of employees who are third party beneficiaries to contracts which require the payment of prevailing wages. Such contracts include both public works contracts and private construction contracts under which the contractor and subcontractors are contractually obligated to pay prevailing wages to workers employed in the performance of the project.

Prior DLSE policy in this area was set out in a letter, dated January 5, 1998, from former chief counsel H. Thomas Cadell, Jr., to John J. Davis, Jr. The question posed by that letter was: "must the Division of Labor Standards Enforcement enforce an action for breach of contract based on a third party beneficiary theory?" While acknowledging that DLSE *has the legal authority* and thus, *may* process such wage claims[1], that letter concluded that DLSE has the discretion to decline to process third party beneficiary claims, and that as a general matter, DLSE would not enforce such claims. That conclusion rested upon certain enforcement policy considerations that we now reassess. For the reasons set forth below, we again conclude that there are no legal grounds which would preclude DLSE from accepting and enforcing third party beneficiary prevailing wage claims. We now

[1] Mr. Cadell noted that "the Division does not wish to preclude the filing of third party claims in the future if such an enforcement tool was considered appropriate in the circumstances."

modify our enforcement policy, however, so that henceforth, absent unusual and compelling reasons, DLSE will exercise jurisdiction over such claims.

Third party beneficiary contract claims are, of course, somewhat different than the typical contract claims that are enforced by DLSE. In a typical contract claim, the employee alleges that his or her employer failed to pay certain wages that are owed pursuant to the oral or written agreement between the employee and employer. In contrast, a typical third party beneficiary contract claim against a general contractor is not founded upon the agreement between the employer and employee, but rather, on the agreement between the public or private entity that awarded the job to the general contractor, under which employees working on the job (whether employed by the general contractor or a subcontractor) must be paid a fixed or specified and readily ascertainable wage (such as, for example, the prevailing wage as determined by DLSR for the applicable craft and locality). Alternatively, a third party beneficiary claim against a subcontractor would be founded upon an agreement between the general contractor and the subcontractor, under which the subcontractor agreed to pay its employees a fixed or specified wage.

In *Tippett v. Terich* (1995) 37 Cal.App.4th 1517, the court held that a third party beneficiary claim is a proper means of enforcing an employee's contractual obligation to pay prevailing wages. The court reasoned:

> An employee asserting a third party beneficiary claim for payment of the prevailing wage may never have been promised payment of the prevailing wage by his or her employer, and thus, is unable to bring an direct contract action against his or her employer. But if the contract between the awarding body and the general contractor specifies payment of the prevailing wage for employees performing the contract, these wages can be pursued by means of a third party beneficiary contract claim against the general contractor (whether the employee works for the general or a sub). Likewise, if the employee works for a subcontractor, and that subcontractor entered into an oral or written agreement with the general contractor to pay its employees the prevailing wage, those wages can be pursued by means of a third party beneficiary action against the subcontractor. *Ibid.*, 37 Cal.App.4th at 1533.

A third party beneficiary *contract claim* cannot be maintained in the absence of an oral or written agreement (either between the awarding body and the general contractor, *or* between the general contractor and the subcontractor) to pay a fixed or specified wage.[2] The statute of limitations on a third party beneficiary contract claim is determined by whether the agreement which the claimant seeks to enforce is oral or written. For a written agreement, there is a four year statute of limitations, while for an oral agreement, the limitations period is two years. (Code of Civil Procedure §§ 337, 339) The right to file a claim accrues when the contractual obligation is breached, and thus, a claim is timely if filed within two or four years, respectively under an oral or written contract, from the date the unpaid wages initially became due.[3]

Having set out the legal basis for third party beneficiary claims, we now address the various enforcement policy considerations that were discussed in Mr. Cadell's letter of January 5, 1998. According to that letter, "there is no statutory duty . . . which would require DLSE to accept third party beneficiary claims." In fact, Labor Code §96 provides

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[2] The California Supreme Court has held that DLSE, under the provisions of the prevailing wage law, can bring a *statutory* claim for unpaid prevailing wages against a contractor notwithstanding the absence of any contract requiring the contractor to pay prevailing wages. *Lusardi Construction Co. v. Aubry* (1992) 1 Cal.4th 976. But to date, no California court decision has given employees the right to bring a similar third party beneficiary statutory claim. In *Aubry v. Tri-City Hospital District* (1992) 2 Cal.4th 962, 969 n.5, the Supreme Court observed that it has not yet had the opportunity to decide that issue. In *Tippett v Terich, supra,* 37 Cal.App.4th at 1539, the court specifically declined to decide whether employees could maintain a statutory cause of action under the prevailing wage law. Since the question now before us is limited to DLSE's enforcement policy with respect to third party beneficiary claims founded upon *contracts* requiring the payment of prevailing wages, we do not herein express any opinion as to the viability of any third party claim for prevailing wages that is not contractually based.

[3] In his January 5, 1998 letter, Mr. Cadell cited *Bogart v. George K. Porter Co.* (1924) 193 Cal. 197, 202, for the proposition that the third party beneficiary claim must be brought within the limitations period for filing an action on a contract "measured from the time the third party beneficiary contract is entered into." This statement is incorrect and is based on a misreading of *Bogart,* which held that "the obligation from the promisor . . . to the third person . . . arises at once upon the making of the agreement," but that the "right of action thereon accrues when the obligation is breached." The statute of limitations starts running upon the breach of a contractual obligation, not upon the execution of the contract that creates the obligation. To hold otherwise would lead to an absurd result, as it would preclude the filing of contract claims where the breach occurs more than two or four years, respectively, after the execution of the oral or written contract.

that the Labor Commissioner "shall, upon the filing of a claim therefor by an employee . . . take assignments" of various types of claims, including "wage claims." The statute does not distinguish between wage claims founded upon a contract between an employee and his or her employer and those founded upon a third party beneficiary theory. Both are wage claims, and both squarely fall within the parameters of section 96.

Another point made in the earlier letter is that DLSE is under no duty to investigate or take action on every complaint filed with the Division. *See Painting & Drywall Work Preservation Fund v. Aubry* (1988) 206 Cal.App.3d 682. This is unquestionably true; as a labor law enforcement agency, DLSE must have the discretion to define its priorities and direct its investigatory and legal resources in the manner it believes most appropriate. This discretion is expressly provided by Labor Code §98:

> The Labor Commissioner shall have the authority to investigate employee complaints. The Labor Commissioner may provide for a hearing in any action to recover wages, penalties, and other demands for compensation properly before the Labor Commissioner . . . . Within 30 days of filing the complaint, the Labor Commissioner shall notify the parties as to whether a hearing will be held, or whether action will be taken in accordance with Section 98.3 or whether no further action will be taken on the complaint.

Thus, under Labor Code §98, DLSE may either 1) proceed with the wage claim through the administrative hearing process, with an adjudicatory hearing in which evidence is presented followed by the issuance of an order, decision or award as provided by Labor Code §98.1, or 2) forward the wage claim to DLSE's legal section for the filing of a civil action pursuant to Labor Code §98.3(b), under which "the Labor Commissioner may prosecute any action for the collection of wages and other moneys payable to employees . . . arising out of an employment relationship," or 3) decline to take any action on the claim, thereby forcing the claimant to either abandon his or her claim or bear the costs of filing a court action to recover the unpaid wages.

DLSE's former non-enforcement policy with respect to third party beneficiary claims was thus founded upon this discretion to decline to adjudicate or enforce claims. But the underlying rationale for this policy is illogical and unsupportable. According to the January 5, 1998 letter, the use of third party

beneficiary claims in enforcing prevailing wages "appears to be inconsistent with the [Division's] enforcement mandate." This purported inconsistency was identified as the conflict between the 90 day limitations period found at Labor Code §1775 (now 180 days under an amended statute) under which DLSE may file a lawsuit on a statutory claim against a contractor to recover unpaid prevailing wages and the significantly longer limitations period for filing a breach of contract action. Of course, there is nothing whatsoever inconsistent about these separate causes of action, and the different limitations periods for each. In the words of the California Supreme Court, ". . . the legislative history of the statutory scheme strongly favors the conclusion that the Legislature intended the contractor's obligation to pay prevailing wages to be both statutory and contractual." *Lusardi Construction Co. v. Aubry, supra,* 1 Cal.4th at 988, n 3.

Another reason for the non-enforcement policy articulated in the January 5, 1998 letter was that "the determination of the rights of parties in third party beneficiary situations requires application of unique rules of contract law and discovery which are not usually utilized by the Division." In fact, the issues posed by a third party beneficiary claim are no more complex than the issues posed by any breach of contract wage claim. The focus of inquiry simply shifts from the contractual agreement between the employee and his or her employer to the contractual agreement between the awarding body and the general contractor, or between the general contractor and the subcontractor. Evidence needed to support a third party beneficiary claim would include copies of the contract or contracts which establish the obligation to pay a fixed or specified wage to the employees (or, if no written contract is involved, testimony concerning the oral agreement), and if the promised wage rates are not fixed as a set dollar amount in the contract(s), copies of other documents (such as relevant prevailing wage determinations issued by DLSR) or testimony concerning the methodology used in determining the dollar amount of the specified wage rate.[4]

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[4] If the claim is processed as an administrative hearing under Labor Code §98, the claimants can obtain any necessary documents through the subpoena process provided at Govt. Code §11450.10-.50, under which a subpoena duces tecum is issued by the DLSE hearing officer at the request of the claimant, or by the claimant's attorney. The deputy labor commissioner handling the claim may provide assistance to an unrepresented claimant in drafting a subpoena *duces tecum* for issuance by the hearing officer. Such subpoena may require the production of documents at any reasonable time and place or at a hearing. (Govt. Code §11450.10) Alternatively, if the claim is being investigated by BOFE for possible referral to the DLSE Legal Section for the filing of a civil action under Labor Code §98.3, documents that are needed to determine the validity of

Finally, according to the January 5, 1998 letter, enforcement of third party beneficiary claims "would severely strain the limited resources available to the Division," and would thereby "impact on our mandated enforcement of minimum labor standards." There are three points that we now raise in response to this contention. First, with respect to employees employed on public works projects, we disavow any distinction between the enforcement of prevailing wage claims (including those brought under a third party beneficiary theory) and the enforcement of minimum labor standards.[5] Second, with respect to employees employed on private construction projects, minimum standards are implicated by minimum wage claims and overtime claims. Moreover, under Labor Code §1195.5, any claims for wages *which exceed* the minimum wage *shall* be investigated and enforced by the Division. Thus, the Division's duties extend to wage claims which exceed minimum labor standards. And third, however limited DLSE's resources may be, an across the board non-enforcement policy engenders employer non-compliance with the very minimum labor standards and other labor laws that we are mandated to enforce. Compliance, and the resulting reduction in unpaid wage claims, is best fostered by a policy that promotes enforcement. In short, our responsibilities as a labor law enforcement agency do not permit us to maintain a policy that denies enforcement of an entire category of unpaid wage claims.

Thus, absent unusual and compelling circumstances which may be unique to a specific case, DLSE will henceforth process all third party beneficiary claims alleging a breach of contract to pay prevailing wages (or some other fixed or specified wage) on public and private construction projects. DLSE will exercise discretion on a case by case basis in determining whether any

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a claim can be obtained through the issuance of an investigative subpoena. (see *Millan v. Restaurant Enterprises Group, Inc.* (1993) 14 Cal.App.4th 477.)

[5] Labor Code §90.5 provides for the maintenance of DLSE's field enforcement unit, BOFE, "[i]n order to ensure minimum labor standards are adequately enforced." Under this statute, BOFE is charged with enforcement of those minimum labor standards that are "most effectively enforced through field investigations," including Labor Code §1771, which requires the payment of prevailing wages on public works projects. Clearly, the Legislature did not view prevailing wage enforcement as anything other than minimum labor standards enforcement. The courts have similarly characterized the prevailing wage law as a "minimum wage law," and thus, a minimum labor standard. *Metropolitan Water District v. Whitsett* (1932) 215 Cal. 400, 417; *WSB Electric v. Curry* (9th Cir. 1996) 88 F.3d 788, 790 (California's "prevailing wage law requires that public works contractors pay their employees a minimum wage, called the prevailing rate of per diem wages.")

such claim should proceed through the administrative hearing process set out at Labor Code §98, or through the mechanism for filing a civil action set out at Labor Code §98.3. Employee claims concerning non-payment of the prevailing wage on public works projects should not be processed through the administrative hearing process if DLSE has already issued a notice to withhold or has filed a timely lawsuit in connection with that project, so that all claims may be resolved in a consistent manner in one proceeding through DLSE's enforcement action.

Thank you for your ongoing interest in California wage and hour law and DLSE enforcement policies. Feel free to contact us if you have any other questions.

Sincerely,

Miles E. Locker
Chief Counsel

Marcy V. Saunders
State Labor Commissioner

cc: Jose Millan, Chief Deputy Labor Commissioner
Tom Grogan, Assistant Labor Commissioner
Greg Rupp, Assistant Labor Commissioner
Nance Steffen, Assistant Labor Commissioner
John Chiolero, Senior Deputy Labor Commissioner
Roger Miller, Senior Deputy Labor Commissioner
All DLSE Professional Staff