

# New York State Legislation Limiting Withholding of Retainage on Private Construction Projects: What Does It Mean for Your Contracts?

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**O**n Nov. 17, 2023, Governor Kathy Hochul signed legislation amending New York's General Business Law Sections 756-a and 756-c, known as the Prompt Payment Act, to limit the withholding of retainage on private improvement construction projects.

The amended Prompt Payment Act sets the maximum amount of retainage that can legally be withheld on a private improvement project at 5%, a reduction by half of the usual and customary 10% of progress payments that were typically withheld under most construction contracts and subcontracts. However, the amendments to the Prompt Payment Act lack clarity as to when retainage and/or final payment must be released or paid, bringing into question whether the amendments accomplish their intended purpose and, more importantly, how it effects an existing form of construction contract.

As a result of these amendments, close attention must be paid to contract terms and conditions during contract preparation, review or negotiation.

The amended Prompt Payment Act is applicable to construction contracts entered into on or after Nov. 17, 2023, and applies only to private improvement projects in excess of \$150,000.00. The amended Prompt Payment Act does not apply to contracts for public works or public improvement projects, and excludes residential construction projects for "the construction,



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**Close-up of construction contract and blueprint.**

reconstruction, alteration, repair, maintenance, moving or demolition of an individual one, two or three family residential dwelling..." or to residential tract developments of one hundred or less one- or two-family dwellings, or any residential construction project of forty-five hundred square feet or less. (GBL §756 (1)).

The amendment's sponsors pointed to severe financial burden to contractors and subcontractors resulting from the withholding of retainage for completed work that goes unpaid for months or years after the completion of a project as the reason for the amendment.

Specifically, the legislation's sponsor stated, "[t]he lack of clarity in existing law results in avoidable disputes, which in turn prolongs the release of retainage payments. This ambiguity creates economic burdens

for contractors and subcontractors...This bill would revise the procedures for contract payment of retainage for owners, contractors, and subcontractors..."

However, does the amendment limit the amount and duration of withholding of retainage, resolve the ambiguity in the old version of the Prompt Payment Act and avoid the long delays in project closeout and payment? In part it does, and in part it does not.

The amendment to the Prompt Payment Act, at GBL §756-c, provides that owners, general contractors and subcontractors may not withhold retainage of more than 5% of the contract sum (and in no case may any contractor's retainage of subcontractor's contract proceeds exceed the percentage retained by the owner against the general contractor).

The prior version of the Prompt Payment Act allowed an owner to retain a "reasonable amount" as retainage (typically 10%) and allowed the retainage to be held until all of the contractor's contractual obligations had been satisfied, which engendered disputes and delays in payment. So, the amended Prompt Payment Act clearly and expressly limits the amount of retainage to no more than 5% of the contract.

As to when retainage must be released or paid, the amendment to the Prompt Payment Act, at GBL §756-a, now provides that a contractor is entitled to "submit a final invoice for payment in full *upon reaching substantial completion*, as such term is defined in the contract or as it is contemplated by the terms of the contract," (emphasis added) rather than the prior version's "upon the performance of all the contractor's obligation [sic] under the contract."

However, the existing language of GBL §756-c remains unchanged: "[r]etainage shall be released by the owner to the contractor no later than thirty days *after the final approval of the work under a construction contract*." (emphasis added). Thus the question remains, when is the contractor entitled to have the retainage released/paid, upon reaching substantial completion or only after all obligations/conditions of its contract have been satisfied? [An owner's or upstream contractor's failure to release retainage as

required would subject the owner or contractor to liability for interest of 1% per month from the date the retention became due and owing.]

While not directly conflicting, the amendments to the Prompt Payment Act, at GBL §§756-a and 756-c, and the existing language of GBL §756-c, make clear the need to carefully draft or review and negotiate a private construction contract or subcontract, particularly as to the definition of substantial completion and the conditions to be satisfied before final approval of the work and final payment.

Importantly, from an owner's perspective, substantial completion should be drafted so as to include, among other things, provision of final certificates of occupancy, inspections, approvals and sign-offs of such governmental authorities with jurisdiction over the project so as to give greatest effect to GBL §756-c's "final approval of work" under the contract.

From a contractor's perspective, care should be taken to, among other things, avoid conflict between the provisions so as to secure timely release of retainage from the owner or an upstream contractor, and for careful adherence to the limitations of proper pay when paid conditions of a subcontract (e.g., so that a contractor is not obligated to release or pay retainage to its subcontractor before the owner releases or pays retainage to the contractor).

While the new amendment to the private Prompt Payment Act does effectuate limitation of retainage to 5%, it does not, however, arguably change or clarify when retainage must be paid, thus careful attention to contract provisions governing substantial completion, completion of the work, final approval, satisfaction of conditions precedent and final payment, among others, is crucial. Careful review, negotiation and drafting of construction contracts and subcontracts in consultation with experienced construction counsel is well-advised.

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