

New York's 5 Percent Retainage Law Underscores Construction Contract Drafting

*By Gina A. Fonte, Robert S. Bernstein and Jeanne Harrison**

In this article, the authors discuss a new law in New York that restricts the amount of retainage that may be withheld on private construction contracts of \$150,000 or more to no more than 5 percent.

New York Governor Kathy Hochul has signed Senate Bill S3539 (Retainage Amendment),¹ which amended Sections 756-a² and 756-c³ of the New York General Business Law,⁴ commonly referred to as the Prompt Payment Act. The Retainage Amendment restricts the amount of retainage that may be withheld on private construction contracts of \$150,000 or more to no more than 5 percent. The amendment took effect immediately and applies to contracts entered into on or after the effective date of November 17, 2023.

The Retainage Amendment presents opportunities and challenges for all parties in the construction industry doing business in New York. Importantly, it presents an opportunity for parties to review and revise their standard contract forms to comply with and adopt new administrative policies, procedures and provisions for carrying out the requirements of the Retainage Amendment where the statute is silent and does not address key concepts.

New York joins a growing number of other jurisdictions regulating retainage on private construction projects, including Massachusetts, Connecticut, Minnesota, Montana and Nevada, among others.

RETAINAGE CHANGES UNDER THE NEW YORK PROMPT PAYMENT ACT

The new Retainage Amendment will create greater certainty and consistency around the issue of retainage withholding on private construction contracts in excess of \$150,000. Previously, the New York Prompt Payment Act provided for retainage withholding in any amount the parties deemed, by agreement, to be "reasonable." Often, this resulted in a wide range of retainage withholding, from 5 percent on the low end to as high as 15 percent of the contract sum.

The Retainage Amendment provides that by mutual agreement of the parties, an owner may retain no more than 5 percent of the

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contract sum as retainage. In turn, the contractor or subcontractor cannot retain more than 5 percent in retainage. Notably, the Retainage Amendment permits an owner and contractor, by agreement, to withhold a retainage amount of less than 5 percent. In such circumstances, however, the Retainage Amendment requires that the corresponding retainage held by the contractor or subcontractor not exceed “the actual percentage retained by the owner.”

With respect to the timing of retainage release, the Retainage Amendment provides that retainage must be released by the owner to the general contractor “no later than 30 days after the final approval of the work.” The term “final approval of the work” is not defined by the statute or under New York law. Rather, what constitutes final approval of the work is as determined by the parties under their construction contract. Other provisions of the New York Prompt Payment Law continue to apply. For example, a contractor shall be entitled to submit a final invoice for payment in full upon reaching substantial completion (Section 756-a of the New York General Business Law). The issue of when the contractor reaches substantial or final completion is left open and to be determined by how such term is defined under the construction contract.

PENALTIES FOR FAILING TO PROPERLY RELEASE RETAINAGE

As was previously the case, in the event that an owner fails to release retainage as required by the New York Retainage Law or the contractor or a subcontractor fails to release a proportionate amount of retainage to the applicable parties after receipt of retainage from the owner, then the owner, contractor or subcontractor, as the case may be, shall be subject

to paying interest at the rate of 1 percent per month on the date retention was due and owing.

CLEAR CONTRACTUAL PROVISIONS ARE ESSENTIAL TO MANAGING EXPECTATIONS, RISK AND LIABILITY

Both New York’s retainage law and its Prompt Payment Law leave material terms undefined, such as: “When has substantial completion has been achieved?” and “What constitutes ‘final approval of the work?’ ” It is imperative that project stakeholders carefully review their construction contracts that are subject to these laws. Ensuring construction agreements clearly define these triggering events is key to managing the parties’ expectations, risk and liability. Careful consideration should be given to identifying project closeout items required by the project’s owner, lender and/or surety, as relevant. Provisions surrounding treatment of mechanic’s liens, lien waivers, lender approvals, surety releases and closeout documentation - as well as how to deal with claims or unperformed, defective or deficient work - are also important. Proactively managing these risks contractually will avoid delays and conflicts at the critical phase of project closeout.

IN SUMMARY

- New York Gov. Kathy Hochul recently signed Senate Bill S3539, which amended Sections 756-a and 756-c of the New York General Business Law to restrict the amount of retainage that can be withheld on construction contracts of at least \$150,000 to no more than 5 percent. The retainage amendment adds New York to a growing list of jurisdictions

that regulate retainage on private construction projects.

- Owners, contractors and subcontractors failing to release the correct retainage amount to applicable parties after receipt of retainage from the owner are subject to an interest penalty.
- Key terms that are not defined in the retainage amendment are left to the parties to negotiate contractually, emphasizing the importance of clear contract drafting to manage stakeholders' expectations, risk and liability.

CONCLUSION

The recent amendments to Section 756-a and 756-c of the New York Prompt Payment Act impact retainage withholding and release on all private construction projects of \$150,000 or more. This article only paraphrases and

summarizes the amendment; the actual language of the bill should be reviewed carefully in developing new practices and contract language.

Construction project stakeholders doing business in New York would be well served to conduct a thorough review of their construction contracts to ensure compliance, manage rights and responsibilities, and mitigate the effects of the recent amendments to the New York Prompt Payment Act.

NOTES:

¹ <https://www.nysenate.gov/legislation/bills/2023/S3539>.

² https://newyork.public.law/laws/n.y._general_business_law_section_756-a.

³ https://newyork.public.law/laws/n.y._general_business_law_section_756-c.

⁴ https://newyork.public.law/laws/n.y._general_business_law.