

Department of Legislative Services
Maryland General Assembly
2018 Session

FISCAL AND POLICY NOTE
First Reader

Senate Bill 1155

(Senator Astle)

Judicial Proceedings

Real Property - Construction Contracts - Retention Proceeds

This bill establishes a process and timeline for the payment of retention proceeds in excess of the estimated cost of completing the work remaining on a project after an owner takes possession of a project or otherwise puts a project into use. The bill's provisions do not apply to (1) a contract in an amount less than \$250,000 or (2) a contract or subcontract for a project funded wholly or in part by or through the Department of Housing and Community Development.

Fiscal Summary

State Effect: Expenditures (all funds) increase to provide estimates to contractors due to the aggregate impact on multiple State agencies. Expenditures are mitigated to the extent that an agency has staff who are qualified and available to provide estimates, as discussed below. Revenues are not affected.

Local Effect: Local government expenditures increase to provide estimates to contractors. **This bill may impose a mandate on a unit of local government.**

Small Business Effect: Potential meaningful.

Analysis

Bill Summary: No later than 45 days after an owner takes possession of a project or otherwise puts a project into use, in whole or in part, *the owner* must provide the contractor with (1) an itemized list of any work remaining and (2) a reasonable estimate of the cost of completing the work. If the total cost estimated is less than the amount of retention

proceeds held by the owner, the owner must immediately pay the excess retention proceeds to the contractor.

No later than 10 days after a contractor receives any payment of excess retention proceeds under the bill, the contractor must provide any subcontractor with work remaining with (1) an itemized list of the remaining work and (2) a reasonable estimate of the cost of completing the work. If the total cost estimated is less than the amount of retention proceeds held by the contractor, the contractor must immediately pay the excess retention proceeds to the subcontractor. The same 10-day timeline and process applies to the subcontractor with respect to any subordinate subcontractor.

Current Law:

Prompt Payment

Generally, a contractor or subcontractor who performs work under a construction contract is entitled to prompt payment for services. For contracts between private parties, if the contract does not provide for specific dates or times for payment, an owner must pay a contractor any undisputed amounts under the written terms of the contract within 30 days of either the occupancy permit being granted or the owner taking possession, whichever comes first. If the contract provides for specific dates or times of payment, the owner must pay the contractor within 7 days after the date or time specified in the contract. If the contract is not with the owner, the contractor or subcontractor must pay undisputed amounts owed to its subcontractors within 7 days after receiving each payment for its subcontractor's work or materials.

Remedies for Violations

In addition to any other remedy, a court may award any equitable relief for prompt payment of undisputed amounts that it considers necessary, including enjoining further violations. A court may also award to the prevailing party interest from the date the court determines that the amount owed was due and reasonable costs. The court may award reasonable attorney's fees if it determines that an owner, contractor, or subcontractor has acted in bad faith by failing to pay any undisputed amounts as required.

Retention Proceeds, Generally

State law limits to 5% the percentage of a construction contract that an owner or contractor can retain to guarantee that a contractor or subcontractor completes the work required by the contract if the contractor has provided 100% performance and payment security. If an owner retains less than 5% of a contract from a contractor, the contractor may not retain more than that amount from a subcontractor. However, statute establishes that additional

amounts may be withheld if a contractor's or subcontractor's performance warrants it. Statute exempts contracts of less than \$250,000 and any projects funded wholly or partially by the Department of Housing and Community Development from the 5% cap on retention.

These provisions do not affect the rights of contracting parties under the laws governing statutory liens on property. The provisions also do not apply to a contract for the construction and sale of a single-family residential dwelling, a transaction under the Custom Home Protection Act, or the Maryland Home Improvement Law.

Retention Proceeds for Specified State Agencies

Under *any* State procurement contract for construction, if a contractor has provided 100% performance and payment security, the percentage specified in the contract for retainage may not exceed 5% of the total amount. However, in addition to retainage, a primary procurement unit and the Maryland Transportation Authority (MTA) may withhold, from payments otherwise due a contractor, any amount that the unit reasonably believes necessary to protect the State's interest.

State Expenditures: Expenditures (all funds) increase for multiple State agencies to provide estimates to contractors of the cost of completing any remaining work on various State construction projects. The magnitude of the increase cannot be reliably estimated as it would depend on the aggregate of expenditures across State agencies required to provide the estimates specified in the bill. This analysis assumes that State agencies may need to hire a third party to produce an acceptable estimate. Expenditures are mitigated to the extent that an agency has staff who are qualified and available to provide estimates.

With respect to the release of retention proceeds, the bill is not likely to have a material impact on State finances. Primary procurement units and MTA are subject to different retainage provisions and may withhold other payments by any amount reasonably believed to be necessary to protect State interests.

Small Business Effect: Contractors operating small businesses likely benefit to the extent that additional retained funds are released prior to the completion of work. In addition, the bill's requirements that funds be distributed within a certain amount of time may decrease the length of time small business contractors and subcontractors must wait to receive funds.

Additional Comments: The Department of General Services (DGS) advises that it may not be able to meet the bill's requirement to release excess retention proceeds. DGS notes that its current practice requires a contractor to submit an invoice before retainage is distributed. DGS also notes that the bill's requirement to pay excess retention proceeds when the project is otherwise put "into use" may be impractical, as the majority of DGS

projects are located in existing, *occupied* facilities, which remain in use throughout the project.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): State Board of Contract Appeals; Office of the Attorney General (Consumer Protection Division); Judiciary (Administrative Office of the Courts); Department of General Services; Board of Public Works; Department of Legislative Services

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nb/kdm

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