

Why You Should Have Your Contracts Reviewed Periodically – More Money In Your Pocket, by Michael D. Ganz, Esq. featured in "The Light," Suffolk County Electrical Engineers Newsletter, 2-2024

Contractors and subcontractors are often reluctant to have their own contract documents reviewed by an attorney, presumably to avoid the legal fees. Often their construction contracts and subcontracts are left unchanged for many years, and even decades, despite changes in the law which should be addressed in those agreements. More to the point, often the few hours an attorney will spend to review these agreements including identifying critical language before the construction project commences can prevent the contractor and subcontractor from hidden surprises down the road that will cost the contractor and subcontractor many times more than those initial attorney's fees. Notably, New York State's law on the withholding of retainage recently changed and those construction agreements should be edited accordingly.

Retainage is an amount of money withheld by an owner from a contractor, or a contractor from a subcontract (typically 10%) from each payment requisition until generally substantial or final completion is achieved. So, if your company earned five thousand dollars in the past month, the owner (or contractor) was allowed to withhold five hundred dollars (10%) from each payment to your company until you reached substantial completion – that is the punch list phase of the project. Obviously, the reason to do so was for the owner (or contractor) to hold money back to ensure that your company would complete the project including the punch list. Ultimately the money is yours but to the extent your company receives more of it on a monthly basis rather than at the end of the project – so much the better for your cashflow. Using the above example, the contractor will have \$250 per month extra in its pocket or \$3,000 per year instead of waiting until completion of the project.

However, on November 17, 2023, Senate Bill S3539/Assembly Bill 4167 was signed by the governor into law to reduce the amount of retainage that can be held on private construction projects in the state and accelerate the time in which contractors can bill for final payment on those projects.

The new bill amends N.Y. General Business Law Section 756-c so that no more than 5% of the contract sum can be withheld as retainage from a contractor or subcontractor on a construction project equal to or greater than \$150,000. Again, this law only applies to private construction projects where the total value of the entire project (not just your portion) is or exceeds \$150,000.

In addition to the 5% cap, the lower-tier subcontracts are limited to "the actual percentage retained by the owner" where the prime contract is lower than 5%. Previously, project owners, contractors, and subcontractors could agree to withhold "a reasonable amount" of retainage on downstream parties. So, if the owner only withholds 3% retainage (unlikely), then the 3% retainage would in effect become the maximum retainage cap.

The new bill also amends N.Y. General Business Law Section 756-a to allow contractors to submit invoices for final payment once the contractor reaches substantial completion (as substantial completion is defined in the contract or contemplated by the terms of the contract – generally when the project can be utilized and occupied as intended with only punch list work remaining). Previously, contractors and subcontractors often had to wait until they completed all contract obligations (including final completion of the project) before a final invoice could be submitted.

Owners and contractors may argue that the new law will affect their ability to ensure a contractor or subcontractor will complete the project since they will be holding less money. However, a better argument is that the new law appears to benefit contractors and owners alike. The 5% retainage limit should provide increased cash flow to contractors and subcontractors on projects. Importantly, the opportunity to submit final invoices at substantial completion instead of final completion, should reduce the time in which contractors and subcontractors are paid. Because this obligation may now be triggered at substantial completion rather than the end of the project a result may be the earlier resolution of punch-list and warranty work and other disputes. As a result of these changes, an owner may receive its completed project sooner, and contractors and subcontractors may receive final payments earlier.

Note that this law is very new and there are some wrinkles that will have to be sorted out. Firstly, it is unclear how the new law affects ongoing construction projects where the contract was executed under the old retainage law. Presumably, only new contracts executed

on or after November 17, 2023 would be subject to the new law. Moreover, some project owners may be impacted in their ability to comply with their existing lending requirements which fund the project, including minimum retainage requirements which exceed the 5% retainage maximum withholding. Time will tell.

Contractors or subcontractors are advised to review their contracts carefully and consult their attorneys to ensure compliance with the new retainage law, and other laws and contract requirements that may be in effect and not included in their current agreements.

Author bio: *Michael D. Ganz is a partner in the Woodbury, New York office of Kaufman Dolowich LLP. He focuses his practice on Construction Law and has more than 20 years of experience in construction transactional matters and litigation. He can be reached at Michael.Ganz@kaufmandolowich.com or (516) 283-8761.*

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