

HOUSE OF REPRESENTATIVES STAFF ANALYSIS

BILL #: CS/CS/HB 101 Public Construction

SPONSOR(S): Commerce Committee, Business & Professions Subcommittee, Andrade and others

TIED BILLS: IDEN./SIM. **BILLS:** CS/CS/SB 246

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR or BUDGET/POLICY CHIEF
1) Business & Professions Subcommittee	14 Y, 1 N, As CS	Brackett	Anstead
2) Oversight, Transparency & Public Management Subcommittee	13 Y, 1 N	Moore	Harrington
3) Commerce Committee	18 Y, 1 N, As CS	Brackett	Hamon

SUMMARY ANALYSIS

Retainage is a portion of an agreed upon contract price that is deliberately withheld until the work is substantially complete to assure that a contractor or subcontractor will satisfy its obligations and complete the construction project. Retainage is a common construction practice. When an owner withholds a certain percentage of a progress payment to a contractor, the contractor in turn withholds a certain percentage from a subcontractor. The retained funds are paid to the contractor and subcontractors when the project is completed. Current law sets limits on how much retainage can be withheld on state and local government contracts. For construction contracts with the state or local governments that are for more than \$200,000, the maximum amount that may be retained in a payment is:

- Ten percent of a payment from a government entity to a contractor before half of the work is completed;
- Five percent of a payment from a government entity to a contractor after half of the work is completed;
- Ten percent of a payment from a government entity to a contractor for the entire project if the government entity is a municipality with a population of 25,000 or less or a county with a population of 100,000 or less; and
- Five percent of a payment from a contractor to a subcontractor after half of the work is completed.

For construction contracts with the state that are for \$200,000 or less, the state may withhold up to ten percent of a payment to a contractor.

For contracts more than \$200,000, the bill reduces the maximum amount that may be retained from:

- Ten percent to five percent before half of the work is complete;
- Five percent to two and a half percent after half of the work is complete;
- Ten percent to five percent for the entire project if the government entity is a municipality with a population of 25,000 or less or a county with a population of 100,000 or less; and
- Five percent to two and a half percent of a payment from a contractor to a subcontractor after half of the work is complete.

For contracts less than 200,000, the bill reduces the amount that the state may retain from a progress payment to a contractor from ten percent to five percent.

The provisions of the bill do not apply to FDOT construction projects authorized by ch. 337, F.S., or any contract for construction services entered into, pending approval, or advertised by a government entity, on or before October 1, 2019.

The bill may have a fiscal impact on state government and local governments. See Fiscal Comments.

The bill provides for an effective date of October 1, 2019.

This document does not reflect the intent or official position of the bill sponsor or House of Representatives.

STORAGE NAME: h0101e.COM

DATE: 3/21/2019

FULL ANALYSIS

I. SUBSTANTIVE ANALYSIS

A. EFFECT OF PROPOSED CHANGES:

Current Situation

Construction Contractors

Construction contractors are certified or registered by the Construction Industry Licensing Board (CILB) housed within the Department of Business and Professional Regulation (DBPR). The CILB consists of 18 members who are appointed by the Governor and confirmed by the Senate.¹ Certified construction contractors are licensed and regulated by the CILB and can practice statewide. Registered contractors are those registered with DBPR, but are licensed and regulated by a local jurisdiction and may only practice within that locality.²

Retainage

Payments for construction services are usually made incrementally as progress is made, and retainage is a construction practice whereby a project owner withholds a certain percentage of a payment from the contractor who in turn withholds a certain percentage from the subcontractors until the project is completed. The retained funds are generally paid out when the project is completed.³

The purpose of retainage is provide leverage for the property owner and the contractor to ensure the project is completed in a timely fashion. Retainage also serves as a safeguard against possible overpayment to a contractor or subcontractor when the estimated percentage of project completion, used for periodic progress payments, exceeds the actual percentage completed.⁴

Florida Retainage Rates for Construction Contracts with Government Entities

Section 218.72, F.S., defines a “local government entity” to mean a county or municipal government, school board, school district, authority, special taxing district, other political subdivision, or any office, board, bureau, commission, department, branch, division, or institution thereof.

Section 255.072, F.S., defines a “public entity” to mean the state, or any office, board, bureau, commission, department, branch, division, or institution thereof, but the term does not include a local government entity as defined above.

Current law provides that for any construction service contract with a local government entity or a public entity (government entities) that is worth more than \$200,000, the maximum amount that a government entity may withhold from a progress payment to a contractor is ten percent, until half of the project is completed. After half of the project is completed, the maximum amount that a government entity may withhold from a progress payment to a contractor is reduced to five percent. However, a municipality with a population of 25,000 or less and a county with a population of 100,000 or less may withhold ten percent until the project is completed.⁵

¹ S. 489.107, F.S.

² See generally s. 489.105, F.S.

³ OPPAGA, *Inflexibility in Contracting and Retainage Practices Could Hurt Construction Industry*, p. 1 (Dec. 2000) <http://www.oppaga.state.fl.us/MonitorDocs/Reports/pdf/0026rpt.pdf> (last visited on Mar. 11, 2019).

⁴ *Id.*; Bausman, Dennis C. *Retainage Practice In The Construction Industry*, Foundation of the American Subcontractors Association, Inc., p. 1 (Nov. 2004) <https://www.asacolorado.com/images/stories/documents/legislation/retainageclemsonstudy.pdf> (last visited on Mar. 11, 2019).

⁵ Ss. 218.735 & 255.078, F.S.

After half of the project is completed, a contractor may request the government entity to release up to half of the retained amount. The government entity must release the requested amount unless the amount is subject to a dispute.⁶

After a contractor completes a project, he or she may submit a request to the government entity for all remaining retained funds. The government entity must release the funds unless there is a good faith dispute that the contractor has not completed an item or items on the government entity's list of items required to complete the project. If there is a good faith dispute, the government entity may withhold an amount not to exceed 150% of the cost to complete the item or items.⁷

After half of a project with a government entity is completed, a contractor may withhold five percent of each progress payment to his or her subcontractors. A contractor may withhold more than five percent based on the contractor's assessment of a subcontractor's past performance, the likelihood that such performance will continue, and the contractor's ability to rely on other safeguards such as a performance bond. If a contractor elects to retain more than five percent, the contractor must notify the subcontractor in writing of his or her determination to withhold more than five percent and the reasons for making that determination, and the contractor may not request the release of such retained funds from the government entity.⁸

For contracts for construction services with the state that are for \$200,000 or less, current law requires the Department of Management Services (DMS) to establish rules that allow the state to retain up to ten percent of each payment made to the contractor. In order to comply, DMS enacted Rule 60D-5.0041, F.A.C., which provides that for public works contracts with the state that are worth more than \$100,000 but not more than \$200,000, a state agency may request DMS to exempt the requirement for a performance and payment bond as long as the state agency retains ten percent of each payment made to the contractor. If the contractor defaults, the agency will use the retained payments to pay any claims of unpaid bills made by laborers, materialmen, and subcontractors.⁹

Chapter 337, F.S., provides that when the Department of Transportation (DOT) uses flexible start and finish times for construction projects, DOT may retain ten percent when a contractor fails to timely commence work or falls behind at any time prior to completion of the contract.¹⁰

Additional Requirements for Construction Contracts with Government Entities

Current law requires a contractor who contracts with the state, a local government, or another public authority to construct a public building or complete some other public works project that is worth more than \$200,000 to obtain a payment bond with an authorized surety insurer equal to the contract price, and a performance bond with an authorized surety insurer. In lieu of a bond, a contractor may file an alternative form of security in the form of cash, a money order, a certified check, a cashier's check, or an irrevocable letter of credit.¹¹

A performance bond issued by a surety guarantees that the contractor or principal will complete the work required under the bonded contract.¹² A payment bond issued by a surety guarantees that the contractor or principal will pay the subcontractors, suppliers, and materialmen associated with the construction project.¹³

⁶ Ss. 218.735 & 255.078, F.S.

⁷ Ss. 218.735 & 255.077, F.S.

⁸ Ss. 218.735 & 255.078, F.S.

⁹ S. 255.05(1)(f), F.S.; Rule. 60D-5.0041, F.A.C.

¹⁰ S. 337.015(5), F.S.

¹¹ S. 255.05(1), (7), F.S.

¹² *American Home Assurance Co. v. Larkin General Hospital, Ltd.*, 593 So. 2d 195, 198 (Fla. 1992).

¹³ *Everett Painting Company, Inc. v. Padula & Wadsworth Construction, Inc.*, 856 So. 2d 1059, 1062 (Fla. 4th DCA 2003).

Before beginning work, a contractor must execute and record both bonds in the public records of the county where the improvement is located and provide a certified copy of the bonds to the public body commissioning the project. A contractor cannot receive payment until the contractor has provided a certified copy of the bonds.¹⁴

OPPAGA Study of Retainage in December 2000

During the 2000 legislative session, the Legislature directed the Office of Program Policy Analysis and Governmental Accountability (OPPAGA) to conduct a study to evaluate retainage and other construction practices to determine if Florida construction law needed to be revised.¹⁵ At the time, the only contracts that had a statutory cap on retainage were contracts with the state that were worth \$200,000 or less, which was set at ten percent.¹⁶

OPPAGA determined that putting a statutory cap on the amount a property owner could retain could become unfavorable to contractors and subcontractors because property owners and contractors may:

- Seek to protect their property by using alternate forms of leverage that are less favorable than the current system of retainage;
- Be less willing to take the risk associated with working with a new contractor or subcontractor; and
- Not allow an existing contractor or subcontractor to take on a project of an increased size.¹⁷

Proponents for lower retainage rates argue that requiring a performance bond is a reasonable substitute for retainage because a performance bond ensures the contractor will complete the project to the property owner's satisfaction, and will screen out contractors who are unable to perform a project. OPPAGA found that a performance bond was not a reasonable substitute for retainage because retainage served as an incentive for a contractor or subcontractor to complete their work in a timely fashion, and a performance bond only guarantees that a project will eventually be completed if a contractor defaults.¹⁸

OPPAGA also found that a greater portion of risk associated with contracting had shifted from the contractor to the subcontractor. If a subcontractor performed work on a construction project, there could be delays, entirely outside of the subcontractor's control, which prevented the subcontractor from receiving retained money. This could result in the subcontractor waiting for an unreasonable amount of time to receive payment for work the subcontractor completed.¹⁹

OPPAGA indicated that subcontractors could try to mitigate this risk by planning for these funds not being immediately available or requiring that retained funds be placed in an interest bearing account. However, proponents for lower retainage rates argue that this reduces competition because smaller subcontractors cannot compete for projects because even though they might be capable of doing a project, they do not have the funds to plan for a high percentage of their earned money being retained. Proponents also argue that high retainage rates increase the cost of construction projects because contractors and subcontractors are required to charge more in order to ensure they can finance a project.²⁰

After the OPPAGA study was completed, the 2005 Legislature passed and the Governor signed into law the current rate of retainage for government entities. The maximum amount a government entity

¹⁴ S. 255.05(1), F.S.

¹⁵ OPPAGA *supra* note 3, at 1; Ch. 2000-372, Laws of Florida.

¹⁶ *See generally* Ch. 255, F.S. (2000).

¹⁷ OPPAGA *supra* note 3, at 3.

¹⁸ Bausman *supra* note 4 at 9; OPPAGA *supra* note 3, at 4.

¹⁹ OPPAGA *supra* note 3, at 3.

²⁰ *Id.* at 2; Bausman *supra* note 4 at 3.

could retain from a progress payment was set at ten percent because that was the industry norm at that time.²¹

Retainage Rates for Other States

According to the American Subcontractors Association, 44 states specify the maximum retainage percentage that the government may withhold from a payment to a contractor.²² At least ten states, including Florida, Pennsylvania, and Georgia, cap the retainage percentage at ten percent.²³ At least twenty-one states, including California, New York, and Virginia, cap the retainage percentage at five percent.²⁴ South Carolina caps the retainage percentage rate at 3.5 percent.²⁵

Retainage Rate for the Federal Government

Federal law requires the federal government to pay a contractor the full amount of a progress payment. Retainage is not used without cause. However, a contracting officer may withhold a percentage of payment based on the officer's assessment of a contractor's past performance and the likelihood such performance will continue. If the officer determines a contractor has not made satisfactory progress then the officer may retain a maximum of 10 percent of a payment or payments.²⁶

Effect of the Bill

The bill reduces the amount that a government entity may retain from a progress payment to a contractor for contracts worth more than \$200,000 from:

- Ten percent to five percent when less than 50 percent of the project is complete; and
- Five percent to two and a half percent when 50 percent or more of the project is complete.

The bill specifies that the above provision does not apply to DOT construction contracts authorized under ch. 337, F.S.

The bill reduces the amount that a municipality with a population of 25,000 or less and a county with a population of 100,000 or less may retain from a progress payment to a contractor, for contracts worth more than \$200,000, from ten percent to five percent.

The bill reduces the amount that the state may retain from a progress payment to a contractor, for contracts worth \$200,000 or less, from ten percent to five percent.

The bill reduces the amount that a contractor may retain from a progress payment to a subcontractor for contracts with a government entity that are worth more than \$200,000 from five percent to two and a half percent.

The bill specifies that the above provisions do not apply to any contract for construction services entered into, pending approval, or advertised by a government entity, on or before October 1, 2019.

B. SECTION DIRECTORY:

Section 1. Amends s. 218.735, F.S., relating to public construction retainage.

²¹ See House Analysis of 2005 House Bill 509 (April 22, 2005).

²² American Subcontractors Association, Inc., *Retainage Law in the 50 States*, <https://olis.leg.state.or.us/liz/2013R1/Downloads/CommitteeMeetingDocument/21969> (last visited Mar. 11, 2019).

²³ *Id.*; 62 Pa. Cons. Stat. § 3921(a); Ga. Code Ann. § 13-10-80(b)(2)(A).

²⁴ *Id.*; Cal. Pub. Cont. Code § 10261 & 20146; N.Y. State. Fin. Law § 9-139(f) (New York caps the retainage rate at 5% if the contractor obtains a performance bond); Va. Code Ann. § 2.2-4301 & 4333.

²⁵ *Id.*; S.C. Code Ann. § 11-35-3030(4).

²⁶ 48 U.S.C. § 32.103.

- Section 2. Amends s. 255.05, F.S., relating to public construction retainage.
- Section 3. Amends s. 255.078, F.S., relating to public construction retainage.
- Section 4. Provides that the bill does not apply to certain public construction contracts.
- Section 5. Provides an effective date of October 1, 2019.

II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

None.

2. Expenditures:

See Fiscal Comments.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

None.

2. Expenditures:

See Fiscal Comments.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

See Fiscal Comments.

D. FISCAL COMMENTS:

The bill may result in contractors and subcontractors who provide services in the construction of public projects for the state and local governments receiving more money in progress payments, which could result in more competition for public works projects and lower costs for the state and local governments.

According to DMS, for state construction projects of \$200,000 or less, the state may incur costs if a contractor does not complete a project and the state must use the remaining funds to rehabilitate the project and hire a new contractor to complete the project.²⁷ For construction projects of \$200,000 or less, the state does not require a contractor to obtain a performance or payment bond if the state agency withholds ten percent of each payment to the contractor. If the contractor defaults, the state agency uses the withheld amount to pay any claims of unpaid bills by subcontractors, materialmen, and laborers. Reducing the amount the state can retain for projects of \$200,000 or less could require the state to use additional funds to pay any claims of unpaid bills made by subcontractors, laborers, and materialmen if the amount retained is not enough to cover their claims.²⁸

²⁷ Department of Management Services, Agency Analysis of 2019 House Bill 101, p. 2 (Jan. 18, 2019).

²⁸ Email from Joseph Valley, Legislative Analyst, Department of Management Services, DMS Bill Analysis Request – HB 101 Retainage (Feb. 7, 2019).

III. COMMENTS

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision:

Not applicable. This bill does not appear to require counties or municipalities to spend funds or take action requiring the expenditures of funds; reduce the authority that counties or municipalities have to raise revenues in the aggregate; or reduce the percentage of state tax shared with counties or municipalities.

2. Other:

None.

B. RULE-MAKING AUTHORITY:

None.

C. DRAFTING ISSUES OR OTHER COMMENTS:

None.

IV. AMENDMENTS/ COMMITTEE SUBSTITUTE CHANGES

On February 13, 2019, the Business & Professions Subcommittee adopted a strike-all amendment and reported the bill favorably as a committee substitute. The committee substitute:

- Reduces the amount that a local government entity may retain from a progress payment to a contractor for construction contracts worth more than \$200,000 from:
 - Ten percent to five percent when less than 50 percent of the project is complete; and
 - Five percent to two and a half percent when 50 percent or more of the project is complete.
- Reduces the amount that a municipality with a population of 25,000 or less and a county with a population of 100,000 or less may retain from a progress payment to a contractor for contracts worth more than \$200,000 from ten percent to five percent.
- Reduces the amount that a contractor may retain from a progress payment to a subcontractor for contracts with a local government entity that are worth more than \$200,000 from five percent to two and a half percent.
- Provides that the bill does not apply to any contract for construction services entered into, pending approval, or advertised by a local government entity or a public entity, on or before July 1, 2019.

On March 21, 2019, the Commerce Committee adopted one amendment and reported the bill favorably as a committee substitute. The amendment:

- Changes the date used to determine when the exemption applies:
 - From July 1, 2019, to October 1, 2019.
- Provides that the bill does not apply to FDOT construction projects authorized by ch. 337, F.S.
- Changes the bill's effective date from July 1, 2019 to October 1, 2019.

This analysis is drafted to the committee substitute as approved by the Commerce Committee.