

HB 4006 (2024) Clarification

Q1: What is “Retainage”?

A: Retainage, also known as “retention,” is money that a construction contractor earns for work that it performs, but that an owner withholds from paying until the end of a construction project. Prime contractors likewise withhold retainage from subcontractors. In Oregon, parties who withhold retainage are limited to five percent of the amount earned with each progress payment. However, on large projects, retainage can end up being hundreds of thousands, or even millions, of dollars, withheld from payment even though it has been earned.

Q2: How does this bill affect the interest-bearing escrow requirements from HB 2415 (2019)?

A: HB 2415 imposed a new requirement that any cash retainage withheld from a progress payment under a construction contract of more than \$500,000 must be kept in an interest-bearing escrow account. The concept behind that bill was to ensure that withheld funds were secure and were not losing value over time via inflation. The problem is that, in practice, there is no commercially available escrow marketplace for this function. Therefore, owners and contractors alike, including public owners, regularly ignore the law or write waivers of the requirement into their contract documents. HB 4006 repeals the escrow account requirement, but gives contractors the option of requesting that cash retainage carry interest at market rates.

Q3: What is a “bond in lieu of retainage”?

A: A “bond-in-lieu-of-retainage” or “retainage bond” is a tool that has been in Oregon law for many years. In current law, when a contractor submits a bond from a qualified surety, an owner is required to accept the bond in place of holding the cash retainage. The surety bond provides the owner with security to ensure the completion of the project (in addition to all of its other rights, including payment and performance bonds), and the contractor receives all of the funds that it has earned for its work contemporaneously with its progress billings.

Q4: What if the owner does not want to accept a retainage bond and release the cash retainage?

A: In current law as well as in HB 4006, an owner's discretion to refuse to accept a retainage bond is limited. Under current law, a public owner must make written findings that the bond "poses an extraordinary risk that is not typically associated with the bond." In HB 4006, the owner may reject a qualifying bond "only if the contracting agency first finds in writing good cause for the rejection that is based on unique project circumstances." This language results from negotiations among involved stakeholders. Under both current and prospective law, an agency may not use rejection of a retainage bond as a tool to disqualify, disfavor, or dismiss a contractor, for example, based on reputation or past dealings.

Q5: Do retainage bonds preserve the underlying purpose of retainage?

A: First, it is important to remember that the withholding of cash payments that have been earned by one party to a contract is unique to construction. And that cash is often the difference between profitability and unprofitability for contractors, in particular for small or disadvantaged businesses that make up a significant portion of the subcontracting community.

In this context, to answer the question, a retainage bond will likely provide more security and more leverage for an owner than withholding cash retainage. This is because when a party makes a claim – or even threatens a claim – on a surety bond, that surety has substantial leverage with the contractor that an owner may not have. Surety bonds, and the relationship between surety and contractor, are the lifeblood of public construction. If a prime contractor runs afoul of its surety, its ability to continue to perform public work is in jeopardy.

Additionally, retainage is but one of many tools that an owner has to ensure completion of a project. The owner has contract rights, including the right to contractual offset, the right to withhold progress payments, and the right to make claims on the contractor's performance bond – a separate surety bond that covers the entire scope of the project, not simply the retainage dollars. When a project is in distress, there are usually signs many months prior to

completion, and a prudent project owner will have taken steps to ensure that it is well protected beyond the limited possible remedies that cash retainage would provide.

Finally, nothing in HB 4006 substantively or substantially changes the state of the law regarding retainage bonds as between public and private owners and prime contractors. As noted above, contractors already have the right to submit bonds in lieu of retainage, and owners already have the obligation to accept those bonds except in very rare circumstances. HB 4006 will not change that relationship.

Q.6 Will subcontractors have any direct rights against owners with the new legislation?

A: No. Current law provides that when a prime contractor submits a bond in lieu of retainage, a subcontractor may then submit its own retainage bond to the contractor, so that it may also receive its full progress payments without retainage being withheld. HB 4006 will change current law only to allow subcontractors to initiate the process by requesting that the prime contractor submit a retainage bond to the owner for at least the amount of that subcontractor's retainage. However, subcontractors will not have the ability to submit retainage bonds directly to owners. There will be no changes to contractual privity as the result of HB 4006.

Q.7: Who supports HB 4006?

A: A broad coalition that includes prime contractors, subcontractors, unions, and state and local public agencies, have all worked together since 2022 to draft the legislation, which is the product of significant time, effort, and compromise. Supporters include Associated General Contractors, Plumbing and Mechanical Contractors Association, NECA, IEC, Iron Workers Local 29, Associated Wall & Ceiling Contractors, National Association of Minority Contractors Oregon, Oregon State Association of Electrical Workers, SMACNA Oregon & SW Washington, and Operating Engineers Local 701. The legislation committee guiding this effort included representatives from, and attorneys that represent, owners, local governments, subcontractors, general contractors, sureties, and others in the construction industry.