



## CONDITIONS ON PAYMENTS TO SUB-CONTRACTORS & NOTICE OF DEFAULT

2010 White Paper for MN Senate File  
SF 2163 (SCHEID) / HF 2393 (NELSON)

---

- **Conditions on Payments to Sub-Contractors, § 1, Subd. 2a**
  - **“Paid if Paid” clauses are unenforceable.**
    - Payment by the owner to a contractor IS NOT REQUIRED before payment to a subcontractor.
    - Payment by a contractor to a sub-contractor IS NOT REQUIRED before payment to any other sub-contractor.
  
- **Notice of Loan Default, § 2, Subd. 4a**
  - A **Lender must give written notice** to all known prime and sub-contractors of a **default** on a financing agreement by Owner.
  - Upon receipt of the notice, prime and sub-contractors may suspend work until:
    - Default is cured; or
    - Owner makes adequate assurances of payment
  - If Lender does not give notice following a default, then the Lender's mortgage is subordinate to mechanic's liens for the value of work performed by contractors after the date the notice of default should have been given.



## RETAINAGE

2010 White Paper for MN Senate File  
SF 3057 – MURPHY, SCHEID, GIMSE, CARLSON, SPARKS

---

### ➤ Construction Contracts Allow for **Progress Payments & Retainage.**

- A progress payment is a monthly payment made to a contractor/sub-contractor by the owner based upon estimates of work completed.

### ➤ What is **Retainage?**

- Retainage is a sum withheld from progress payments to the contractor/sub-contractor.
- The retainage is money earned by a contractor/sub-contractor but not paid to the contractor/subcontractor until the completion of construction.
- Currently, up to 5% of the progress payment may be retained.
  - \* For example, Contractor enters into a 5 month building project with Owner. In month #1, Contractor earns \$10,000 upon pouring a foundation. Owner pays Contractor \$9,500 and retains (“keeps”) \$500.
- **When is the Retainage Released and Paid to the Contractor/Sub-Contractor?**
  - \* The current statute does not answer this question.
- **Where is the Retainage Held?**
  - \* The current statute does not answer this question.

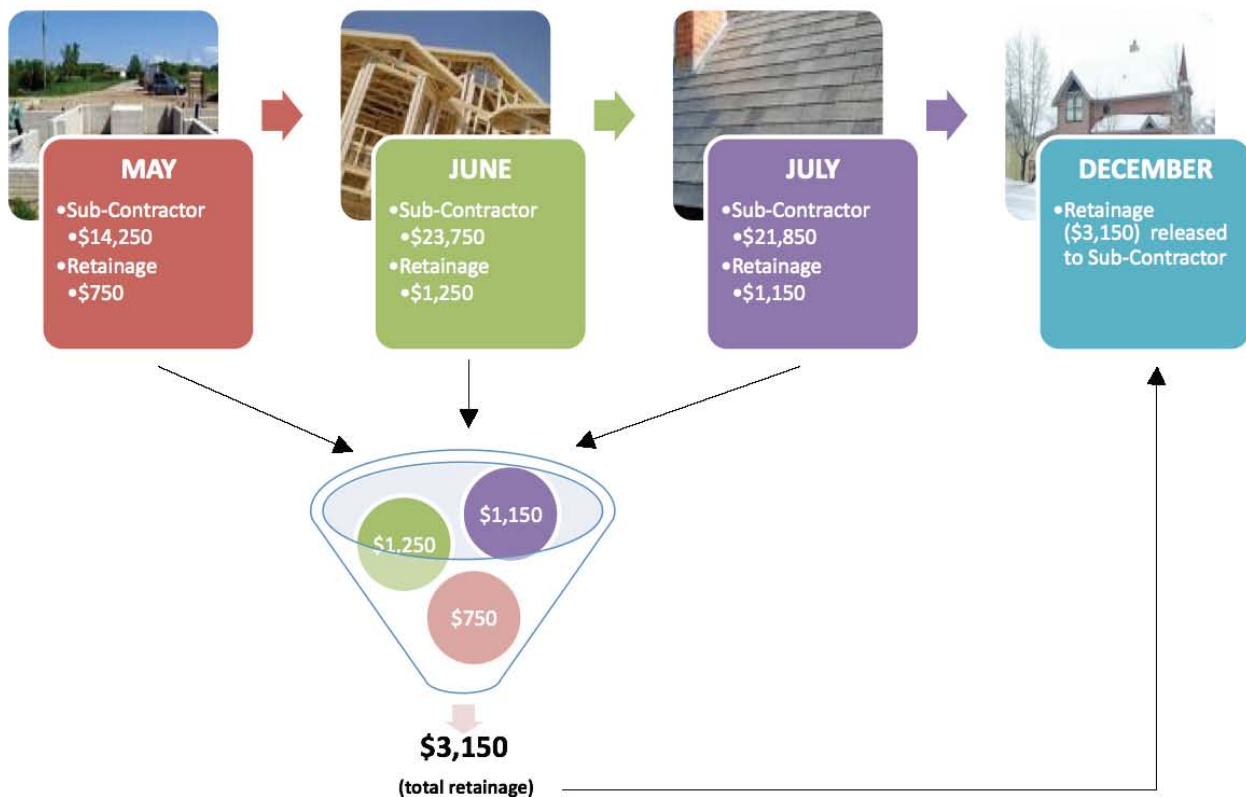
### ➤ **What Does This Bill Do?**

- Requires retainage to be held in an interest bearing escrow or trust account
- Requires retainage and interest to be released and paid to the Contractor within 30 days after substantial completion of the project

# CONTRACTOR *Bill of Rights*

## RETAINAGE

Imagine how your auto-mechanic would react if you told him, prior to a brake pad replacement, that you were not planning on paying the full amount of the bill until you were convinced the work was defect-free. Now, imagine what his reaction would be when you told him it could take you 12-18 months to decide whether you are convinced the new brakes are satisfactory. *This unusual practice is widespread in the construction industry and is known as retainage.*



For example, Sub-Contractor earns \$15,000 for work completed in May. In June, Sub-Contractor earns an additional \$25,000 for other work completed. In July, Sub-Contractor earns \$23,000 for additional work completed. By December, the 8<sup>th</sup> month, the project is substantially complete. At each monthly payment, 5% is held back (“retained”) by the Owner and released upon substantial completion of the entire projects.

A sub-contractor with 100 employees may be working on up to 50 projects at any given time. If these 50 projects are similar to the example above, this particular sub-contractor could have just under **\$160,000** of earned money (**retained**) held until December for work completed during the months of May, June, and July.