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Colorado's Statutory Cap on Construction Project Retainage

January 2022 • [David Plantz](#)

In the fall of 2021, as the leaves started to change colors and the days were getting noticeably shorter, a law regulating the amount of retainage on private construction contracts quietly went into effect. Colorado's Legislature passed HB21-1167, codified at Colo. Rev. Stat. § 38-46-101 et seq. (the "**Act**"), which took effect on September 7, 2021. Under the Act, retainage on private projects is now capped at 5% of the price of the work completed, subject to certain exceptions.

Background

Generally, "retainage" means the withholding of a certain sum of money - usually a percentage of the contract price - from a contractor as assurance that the work will be satisfactorily completed and that all subcontractors will be paid (thereby limiting the potential for mechanics liens).

In 2011, Colorado placed a 5% statutory cap on retainage for public works projects, but there was no such limit on retainage for private projects. Industry standard retainage for private projects is between 5-10%, oftentimes reducing with the attainment of certain milestones (e.g., completion of 50% of the project). However, prior to the Act private parties were free to negotiate retainage.

Five Percent Cap Now Applies to Private Projects

The Act applies to contracts to “construct, alter or repair” a structure or improvements upon privately-owned real property where the value of work under the contract meets or exceeds \$150,000 (with some exceptions, noted below). The Act generally prohibits any property owner, contractor or subcontractor from withholding as retainage on a private project more than 5% of the price of the work completed under the applicable contract, subcontract or supply agreement (e.g., purchase order). If a prime contract is subject to the Act, subcontracts and supply agreements related to the prime contract automatically fall under the provisions of the Act, regardless of the value of the work under such subcontracts or supply agreements.

Property owners may be concerned that the Act predominantly benefits contractors and material suppliers to the detriment of owners, but the Legislature was careful to clarify that this reduction in retainage does not “change, override or invalidate” other provisions in contracts which may provide protections similar to retainage for the property owner (with respect to contractors) or contractors (with respect to subcontractors or material-providers).

To that end, the Act provides a non-exclusive list of contractual provisions which are not affected by the Act, including: satisfactory performance of the work before payment is due; deduction from payments for back-charges or other amounts authorized under the agreement; or conditions which must be satisfied before payment is due (including “pay-if-paid” or “pay-when-paid” clauses). Further, the Act requires that lien waivers be provided by payees for amounts actually received (if required by the agreement). The Act also clarifies that making partial payments does not act as an acceptance or approval of any portion of the work, nor a waiver of defects in the work. Thus, even with retainage significantly reduced, several protections can be put in place with respect to issues retainage is intended to address.

Exceptions

The Act provides for the following exceptions from the 5% retainage cap, and does not apply when:

(i) the price of the work completed under a prime contract is less than \$150,000; provided, as mentioned above, if the Act applies to the prime contract it also automatically applies to subcontracts and supply agreements to such prime contract regardless of the price of the work under such subcontracts or supply agreements;

(ii) the contract pertains to a public works project (i.e., the construction contract is entered into with the State, a County, City, City and County, Town, District or any political subdivision thereof); or

(iii) a single contract governs the building of either (a) one single-family dwelling, or (b) one multi-family dwelling of less than five dwelling units.

Practical Considerations

On its face, the Act appears to be a windfall for contractors, subcontractors and material-suppliers by essentially reducing by half the amount of funds which can be withheld as retainage, thereby allowing contractors to be paid more of their fees sooner, and subject to fewer conditions (often retainage is withheld until completion of the overall project, as touched upon below). That may be the case in many instances. However, a large proportion of private projects are financed, and construction lender issues may undercut this apparent windfall – particularly as the amount financed increases.

Construction lenders typically require specific conditions be met prior to a borrower releasing retainage to contractors, so as to ensure sufficient retainage remains in place to incentivize timely completion, quality workmanship and the payment of subcontractors and material-providers. Such conditions often include the issuance of a Certificate of Occupancy, executed final lien waivers from payees and reports from architects and/or inspectors. However, often a construction lender will agree to release a portion of the retainage prior to completion of the project (e.g., to subcontractors whose work is completed relatively early in the construction schedule). As a consequence of the Act, construction lenders have less retainage to underwrite and may be less willing to agree to the early release of retainage. As a result, some contractors who could have been paid prior to completion of the project may find themselves waiting longer to be paid in full.

Prudent developers should consult with counsel, the construction lender and the general contractor prior to executing a construction contract, so as to ensure the developer does not commit to release retainage in violation of the provisions of the construction loan documents.

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