

Construction Progress Payments and Retainage

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Construction contracts generally embody a unique and complicated system of payment for work completed, consisting of progress payments coupled with retainage. Industry form contracts and general practice call for the general contractor to receive periodic payments (usually monthly) based upon the percentage of work actually completed on the project. Progress payments are sometimes tied to completion of specific phases of work, e.g. first payment upon completion of site grading. This system allows the owner to hold the contractor continuously accountable for the work schedule, permits the contractor to pay for materials and labor as they are consumed, and allocates the risk of breach between the parties.

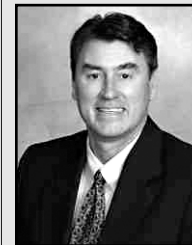
Retainage is used to protect the owner against liens, claims, or defaults. Retainage is merely the withholding of a small percentage of each payment made to the contractor under the contract. Retainage has become the norm rather than the exception in most construction contracts. Retainage

being held in favor of the owner is generally released, in whole or in part, when the project reaches certain pre-specified levels of completion. Retainage is generally released upon substantial completion of the project. Contracts generally provide that retainage must be released to the contractor when the project engineer certifies the project is substantially complete, minus any minor items that need correction. This gives the project engineer wide latitude in determining when retainage should be released. Failure to make timely payments due under a construction contract is a breach on the part of the owner. The contractor is not without recourse for non-payment.

The federal practice was to withhold ten percent of payments to the contractor until the project was fifty percent complete, whereupon the contract officer could then release either part or all of the retainage to the contractor in his discretion. The federal practice now is not to withhold retainage

for those contractors exhibiting good past performance histories in job completion. State agencies, with the exception of the Arkansas Highway and Transportation Department, withhold ten percent of the progress payments as retainage until the project reaches fifty percent completion, and may not withhold any additional retainage after that time.

Retainage may be required by statute, or it may be permissible but capped at a maximum percentage. Specific progress payment dates and retainage amounts may be negotiated in private contracts. The goal of negotiation should be to fairly allocate the risk of default between parties.



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