Scribbles Squibs #32 (February 12, 2015):*

THIRTEEN THINGS YOU SHOULD KNOW ABOUT THE NEW MASSACHUSETTS RETAINAGE ACT

By Attorney Jonathan Sauer

I. INTRODUCTION.

As those familiar with Massachusetts public construction know, retainage is set by statute in Massachusetts not to exceed five percent as set forth as to public building projects (MGL C. 30, s. 39K) and as to certain public works projects (MGL C. 30, s. 39G). Since these percentages are set forth in statutes, no one has the discretion or authority to establish retainage as to any subcontractor or general contractor at a rate above 5%. However, as to private Massachusetts construction projects, there has not been heretofore any legal limitation as to the amount of retainage that can be retained. That is, until now.

This statute also regulates various issues pertaining to establishing the date of substantial completion, when punch lists are issued and when requisitions can be submitted and be due for payment at both the general contractor and subcontractor levels.

This was enacted by the Massachusetts Legislature in 2014 as Chapter 276 of the Acts of 2014, entitled "AN ACT RELATIVE TO FAIR RETAINAGE PAYMENTS IN PRIVATE CONSTRUCTION". (For anyone wishing to obtain a copy of this fairly lengthy statute, let us know by email and we'll send it right along.) 'Acts' of the Massachusetts legislature do not become enforceable, generally speaking, until they are incorporated into the General Laws. And, this Act has now become MGL C. 149, s.29F.

This statute became effective as of November 6, 2014 for projects for which the 'owner's contract' was entered into on or after this date. The statute specifically references 'deliverables', which are as-built drawings. For ease of reference in the discussion that follows, references to incomplete work may also include this item. References to 'retainage' will also mean 'retention'.

This is a complex statute and in simplifying it for this *Squib*, a number of its provisions have not been referenced or discussed/fully discussed. Unfortunately, there is no substitute for reading any complex statute such as this one. The intent of this *Squib* will be to cover what appear to be the main provisions of this statute.

I will first outline some of the key provisions of this statute – especially those with time requirements - and then discuss certain aspects of this statute.

II. KEY PROVISIONS IN OUTLINE FORM.

1. This applies to private construction contracts subject to mechanics' liens where the general contract is more than three million dollars, excluding projects containing at least 1 but not more than 4 dwelling units.

2. No contract for construction for such projects shall include retainage that exceeds 5 per cent of any progress payment.

3. The general contractor is to submit a notice of substantial completion within 14 days of reaching substantial completion on a form such as that contained within the statute.

4. The owner shall accept or reject this notice within 14 days of its receipt.

5. When the owner rejects the notice of substantial completion, it shall advise the general contractor of this within 14 days of its receipt of the notice.

6. The general contractor has to commence dispute resolution procedures within 7 days of its receipt of the owner's rejection of the notice of substantial completion.

7. A notice of substantial completion not rejected by the owner within 14 days of its receipt of the notice shall be deemed accepted by the owner.

8. Within 14 days of the owner's acceptance of the notice of substantial completion, the owner will provide the general contractor with a punch list.

9. Within 21 days of the owner's acceptance of the notice of substantial completion, the general contractor will provide its subcontractors with punch lists applicable to their work, the scope of which punch lists can exceed that as contained in the owner's punch list to the general contractor.

10. Within 60 days after substantial completion, or earlier if provided by the contract, the general contractor and its subcontractors can submit requisitions for retainage.

11. A requisition for retainage shall be paid by the owner to the general contractor not later than 30 days following its submission, subject to adjustments for incomplete and defective items.

12. Requisitions for retainage shall be paid by the general contractor to the subcontractors not later than 37 days following their submission, subject to adjustments for incomplete and defective items.

13. If the general contractor has not been declared to be in default by the owner, the owner shall not withhold any part of the retainage due a subcontractor against whom there are no outstanding construction issues even where there outstanding issues as to other subcontractors.

III. GENERAL COMMENTS ABOUT THIS STATUTE.

Three things can be said about this act right off the bat.

For one thing, this reads in many regards like the 2010 prompt payment statute, which regulates pay-when-paid clauses for certain projects. (An explanation of this statute can be found in an article at our website, www.sauerconstructionlaw.com.) And, that statute, like this one, is more promise than production.

A second thing that can be said about this statute is that whoever wrote it is either unfamiliar with C.93A legal principles or, on the other hand, is *very* familiar with those principles. (C. 93A is Massachusetts' unfair and deceptive trade practices act which awards successful plaintiffs with an award of double or triple damages plus actual attorneys' fees.)

I say this is as this new statute uses the word 'shall' frequently throughout it. The word 'shall' in statutory construction is deemed to be a mandatory word. In other words, where there is a 'shall' requirement, there is no discretion for the person to whom this applies. The use of the word 'may', on the other hand, merely expresses a preference rather than an absolute requirement. The word 'shall' is like a posted speed limit of 55 mph while the word 'may' only requires one to drive safely. 'Shall' expresses a rule while 'may' expresses a standard, the two being as different as night from day, one being rigid and inflexible and the other less so.

Why is the use of this one word so critical? It's critical for a number of reasons. For one thing, the statute is reasonably complex with a variety of new requirements and concepts. But, principally, a question arises as to what happens when a party subject to a 'shall' requirement doesn't do what that requirement mandates? Is an intentional disregard of such a requirement an automatic C. 93A violation, under which statute the offending party may have to pay double or triple damages plus actual attorneys' fees? Is a mere negligent disregard of such a requirement also a C. 93A violation? Is ignorance of this statute a C. 93A violation? (Massachusetts courts have frequently ruled that ignorance of the law is no excuse to complying with its requirements.) And, a statute such as this one will probably be interpreted as being a 'public policy' statute, the requirements of such to be considered as more important and worthy of enforcement as compared with a more garden variety type of statute. And, what would be the purpose of having all of these 'shall' requirements if there are no consequences for those who ignore or violate them?

Thirdly, this statute seems to be in love with the idea of people being able or required to commence dispute resolution procedures under various circumstances. Dispute resolution involving litigation by arbitration or by court is not inexpensive and it is not quick, as anyone familiar with these processes knows.

Many of the problems involved with civil litigation are made worse by the fact that, typically, each side to litigation has to bear its own attorneys' fees and court costs irrespective of who wins the case. (*Squib* number 26, available at our website, discusses this in detail.) This is the so-called 'American Rule' on attorneys' fees.

Actually, the previous statement has a rather small misstatement. The General Laws *do* provide for the payment of attorneys' fees to successful plaintiffs. M.G.L.A. 261 § 23 provides that as to superior court litigation, an item of 'costs' is attorneys' fees. This as follows: "For an attorney's fee, if an issue in law or fact is joined, two dollars and fifty cents; if not, one dollar and twenty-five cents." The 'joining of an issue' typically means that an answer has been filed to the complaint. So, the award of an attorney's fee is either $1.25 or $2.50. Whoever receives this shouldn't spend it all in one place!

Are they *serious*? The answer is 'yes'. Now, that is not to say that an actual attorney's fee won't be awarded if the underlying contract provides for one or if the recovery is under a statute which provides for an award of an attorney's fee if the plaintiff wins. But, otherwise, you are looking at $1.25 or $2.50 for an attorneys' fee for the *whole* case. It is no wonder that the statue of Lady Justice wears a blindfold. Looking at many of our laws that make so little or no sense is hard to look at!

Folks, for those readers who have already been to the litigation rodeo, they know that litigation favors those who can best/better afford it. In many instances, a general contractor will have an advantage in this regard over subcontractors. And, in many instances, an owner will have an advantage in this regard over a general contractor.

Statutes like this one which provide for any number of opportunities – even, *requirements* – for a party to commence dispute resolution procedures make little sense unless the party which unfairly or wrongfully made that dispute resolution procedure necessary has to pay the freight. Common sense suggests that if a potential party to a litigation understands at the outset that it may be forced not only to pay for its own attorney but, also, to pay for the other side's attorney if the other side wins the case will likely mean that low merit and baseless litigation would significantly reduce. This is what the 'English Rule' of attorneys' fees provides for. Perhaps, only one further circumstance evidencing that the colonists are not, well, quite civilized!

Ultimately, the law is what the courts say it is. Questions concerning this statute will most likely be answered as court cases are decided. Realistically, we won't know how courts will interpret this statute until court cases are tried and appealed, the greatest source of decisional (judge-made) law in Massachusetts being opinions of the Appeals Court and of the Supreme Judicial Court. The law can and often does move very slowly, like a glacier on a lazy day.

This statute applies only to private construction projects that are subject to mechanics' liens, the general contract being $3,000,000 or more but not including a project which contains between one and four housing units. For applicable projects, retainage from progress payments 'shall' not exceed 5%.

The statute ties many of its provisions to a project's reaching substantial completion.

Within 14 days after reaching substantial completion, the general contractor 'shall' submit to the owner a notice of substantial completion in the form provided in this statute, which notice will state the date on which the project became substantially complete.

Those familiar with Massachusetts mechanics' lien law know that that statute in MGL C. 254, s. 2A also contains a provision for notices of substantial completion. The notice required by this new law is something different from that required under the mechanics' lien law, the purpose of which is largely to establish a deadline for the filing of mechanics' liens for first and second tier material suppliers and subcontractors. This lien law provision also has a 'shall' component to it, requiring such documents to be filed at the registry of deeds. Yet, in the real world, I very rarely see them. Off the top of my head, I can't recall a single court decision punishing either the general contractor or the owner for not filing this mechanics' lien document.

The owner "shall" accept or reject the notice of substantial completion within 14 days of receipt of the notice. Acceptance is indicated by the owner's signing the notice provided. A failure to deliver the notice to the general contractor within this 14-day period means that the notice will be deemed as accepted.

This will probably be one of the most important provisions of this law. I can foresee many owners who when they receive such a notice won't understand why they are receiving it, what its significance is, what they are supposed to do with it and will simply ignore it. Architects prepare project manuals and we know how much 'cut and paste' is involved with that. One cannot cut and paste this provision from a previous project manual, as this provision didn't exist when that previous project manual was prepared. Also, architects are not generally attorneys and I suspect it will be awhile until these requirements become familiar to many attorneys not working in this area on a frequent basis.

If the project owner rejects the notice of substantial completion, the project owner shall, within 14 days of receipt of the notice, notify the general contractor in writing of the rejection. A rejection of the notice shall be subject to the dispute resolution provisions of the contract for construction, which, notwithstanding any provision in the contract to the contrary, shall be commenced by the general contractor within 7 days of receipt of the rejection of the project owner.

This seems almost silly. At such time as many projects are at the near substantial completion level, there are any variety of issues and disputes pending, the majority of which will not reach the dispute resolution phase or go very deep into it. The actual date of substantial completion may only be one of these issues.

What happens if the 'dispute resolution' provision requires the general contractor to commence litigation immediately? This provision could have general contractors and owners in litigation over this *one* issue. Thirty-nine years of doing this work have taught me that once parties are in litigation, negotiation towards the resolution of a dispute is frequently some period of time down the road, often, a period of years. And an adversarial attitude between the general contractor and the owner is a great deal different from a 'cooperative' or 'partnering' attitude, which is often required to resolve disputes. And, by forcing 'dispute resolution' to be quickly filed on this *one* issue, this could cause other issues to not be negotiated in the ordinary course of business. This can deprive general contractors and subcontractors of monies they might otherwise be rightfully entitled to as change orders, which may not get resolved in the ordinary course of business due to the fact that the general contractor and owner are in litigation. And,

requiring this lightning fast pursuit of dispute resolution procedures can only have the tendency of putting more issues into litigation with the delay and expense attached to that. The court system presently can't promptly provide trials for construction disputes with the number of them it currently has. This procedure will/could only increase that number, potentially slowing down the resolution of other construction cases, most of which cases will address *all* of the disputes between the parties. Superior court cases don't often come to trial for five years. Does anyone think that this time period should be made even *longer*?

Not later than 14 days after the express or deemed acceptance of the notice of substantial completion or, in the case of a dispute, after final and binding resolution of the dispute, the project owner shall submit to the general contractor a punch list.

A punch list within 14 days of the date of substantial completion? At first glance, that sounds pretty good. But, the potential problem with this provision is that the punch list is not due until a 'final and binding resolution of the dispute'. So, in cases requiring arbitration, presumably the matter has to go through the arbitration process. And, an arbitration award does not become a judgment until the prevailing party files an action in court to confirm the arbitration award. That can be two pieces of litigation. And, as discussed above, for civil superior court cases to achieve a final judgment can often take five years or more.

Did/do the authors of this legislation intend for a punch list not to be issued for a period of five years or more? I have to assume that they didn't. But, that is what the words could likely require. So, if, for example, an HVAC system needs to be balanced, does the owner (and tenants) really want to have some people very hot at the time some people are very cold, this for a period of *years*? Do these authors intend that owners/tenants won't be receiving as-built drawings and spare parts that they need to maintain and operate the building until five years after the job is done? As premiums for payment and performance bonds are usually only for a limited term, extending the length of the job this much might cause sureties to demand an additional bond premium. This could also needlessly increase a bond principal's work in progress statement, needlessly reducing the amount of available credit to support the issuance of additional bonds. And, if everyone has to wait for a resolution of disputes to determine when the project is substantially complete, who is going to pay for any necessary demobilizations and remobilizations the general contractor and subcontractors might incur? What will be the date a warranty would start for a project where the date of actual substantial completion is litigated for a matter of years?

Again, with the benefit of thirty-nine years of experience, it is my opinion that good legal writing should be as *short* as possible. The more words that are used to say something, the greater the chance is for contradictions and for pure errors and confusion. This statute just has far too many words in it to express its provisions and requirements.

An example. One section of the statute provides as follows:

"Not later than 14 days after the express or deemed acceptance of the notice of substantial completion or, in the case of a dispute, final and binding resolution of the dispute, the project owner shall submit to the prime contractor a written list describing all incomplete or

defective work items and deliverables required of the prime contractor under the prime contractor's contract for construction. The list shall be certified by the project owner as made in good faith."

Doesn't this mean: "The owner will provide the general contractor with a punch list within 14 days of substantial completion"? If so, then why so many words.

Not later than 21 days after the express or deemed acceptance of the notice of substantial completion or, in the case of a dispute, final and binding resolution of the dispute, the general contractor will provide its subcontractors subject to withheld retention a written punch list of items necessary to complete a subcontractor's work, which list can include additional items above and beyond those contained in the owner's punch list.

Unless the general contract (and, presumably, subcontract) otherwise provides, after the expiration of 60 days after substantial completion or, in the case of a dispute under subsection (d), final and binding resolution of the dispute, the general contractor (and, presumably, subcontractors) can submit requisitions for retainage accompanied by a written list identifying what items of its punch lists have been completed.

General contractors 'shall' have their requisitions for retainage paid in thirty days after submission. Subcontractors shall have their requisitions paid in thirty-seven days. Both of these are subject to various potential adjustments: for incomplete items, either the value of mutually agreed upon items in writing or, failing agreement, not more than 2.5% of the adjusted contract price of the party seeking payment; or 150% of the reasonable cost to complete/correct incomplete or defective work; and the reasonable value of claims and the costs and attorneys' fees incurred as the result of claims, providing this is permitted by the language of the contract at issue. Monies can't be withheld for these items unless the party seeking payment receives a list of incomplete or defective work before the date that payment is due.

That's quite a list. Does this list suggest retainage will be payable *more* quickly than it would be paid presently without this statute? It doesn't appear so, particularly where a party is able to withhold the value of claims and, potentially, attorneys' fees related to those claims. I don't recall seeing generally contracts which allow a party to deduct its attorneys' fees from retention as to claims *in advance*. But, not to worry: it's there now.

Retainage held by the owner on account of work performed by the general contractor itself shall be eligible for payment to the same extent as if the work was performed by a subcontractor. If the general contractor has not been declared to be in default of its contract, the owner 'shall' not withhold retainage ultimately due to subcontractors who are not involved in a claim between the general contractor and owner not related to that specific subcontractor(s) work. In other words, this language seems to say that if there is a dispute between the general contractor and owner as to HVAC work, the painter cannot have his retainage withheld. The rejection of an application for retainage and a dispute regarding incomplete or defective work items shall be subject to the applicable dispute resolution procedure. (As Ronald Reagan once said to Walter Mondale during a campaign debate: 'there you go again'.)

A contractual provision requiring a party to wait for more than 30 days after the rejection of a retainage requisition or the receipt of written notice of a dispute before commencing dispute resolution shall be unenforceable. The payment of retainage shall be subject to subsection (e) of section 29E which can include contractual provisions relating to pay-when-paid and other related items. (MGL C. 149, section 29E is as complex as this particular statute or even more so.)

Writings required under this section can be made electronically (presumably referencing emails).

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* A *'squib'* is defined as 'a short humorous or satiric writing or speech'. Wiktionary defines a '*squib'* as: "a short article, often published in journals, that introduces empirical data problematic to linguistic theory or discusses an overlooked theoretical problem. In contrast to a typical linguistic article, a squib need not answer the questions that it poses."

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