

2007 Legislature Sets New Rules for Payments on Public Projects

by Wyatt Hoch

The Fairness in Public Construction Contract Act, enacted in the 2007 legislative wrap-up session, contains important new rules for all contracts after July 1, 2007 for public construction in the state of Kansas. The Act generally requires owners to make progress payments within 30 days after receipt of an approved application for payment, requires prime contractors to pay subcontractors within seven business days after receipt of payment from the owner, and requires the owner to release retainage within 30 days after substantial completion of the project. Most notably for the design profession: the architect or engineer of record **must** review, approve, and forward to the owner the contractors' applications for payment within 7 business days after receiving the application from the contractor. Any sub-consultant's review of the application must be accomplished during that 7 day period. [The 2005 prompt pay act for private projects does not contain a parallel provision.]

Scope of coverage

The Act applies to all contracts for construction, renovation, repair or maintenance of essentially any kind of structure, wastewater or water treatment plant, and pipeline in Kansas in which a public entity holds an ownership interest **except** for road, highway, and bridge projects. "Public entity" is defined by the Act to include the State and its agencies, counties, cities, state universities and colleges, school districts, non-profit corporations, and "other organizations operated with public money for the public good." Beware the breadth of this statute. Private projects financed by industrial revenue bonds, where the bond issuer owns the facility and leases it back to a corporation, qualify as public construction. The definition of "public entity" is also broad enough to include churches, charities, and not-for-profit corporations like a country club or homeowners' associations.

Payment turn-around

The owner must pay timely, properly completed, and undisputed (meaning that all parties to the contract agree that payment is owed to the contractor) within 30 days absent "extenuating circumstances" [undefined by the Act], in which case the owner has 45 days to pay. The contractor and its first tier subcontractors must in turn make payment to their subcontractors within 7 days after their receipt of payment. The Act (i) imposes interest at the rate of 18 percent per annum beginning on the first day after payment is due, and (ii) provides the contractor with a statutory right to suspend performance (with provision for recovery of delay and mobilization costs) if payment is not made within 7 days after it is due. The prevailing party in any lawsuit or arbitration over payment is entitled to an award of attorneys' fees and court costs.

Retainage

Retainage may not exceed 10 percent of the contract sum. The owner must release retainage within 30 days after substantial completion of the project. If any subcontractor is continuing to work, the retainage **for that subcontractor** may be held until 30 days after completion of the work. The prime contractor's continuing work, however, does not justify holding retainage. Like with progress payments, the 18 percent penalty applies to late payments of retainage. Unlike progress applications, a timely, undisputed payment application from the contractor is **not** required to trigger the owner's obligation to pay the retainage 30 days after substantial completion. Under a literal reading of the statute, the payment of the retainage is due **even without a pay application**. Thus owner offsets and claims for damages (including delay/liquidated damages) must be asserted within the thirty-day period after substantial completion. Finally, the Act enables, but does not require, the early release of retainage for subcontractors (like earthwork) who complete their work early in the project.

Other restrictions on contract terms

The Act's provisions cannot be varied or waived by contract. Three common construction contract provisions are declared void as against public policy:

- no damage for delay (limiting to an extension of time the contractor's remedy for owner-caused delay);
- waiver of the right to jury trial; and
- waiver of subrogation rights against parties responsible for insured claims, except for builder's risk and wrap-up liability policies.

These new prohibitions, coupled with the anti-indemnity legislation passed in 2004, should trigger a careful review of your supplementary conditions and front-end documents for public projects. The statute is reproduced on the following pages.

For Further Information

Foulston Siefkin regularly counsels clients on issues relating to construction law. If you are interested in additional information regarding this Issue Alert, or if you have questions about how this new legislation may impact you, call Wyatt Hoch at (316) 291-9769 or email him at whoch@foulston.com. For additional information on the Firm, please visit our website at www.foulston.com. Information contained in this bulletin has been prepared for general information purposes only and is not legal advice.

SENATE BILL No. 333

AN ACT concerning contracting; enacting the Kansas fairness in public construction contract act; amending K.S.A. 75-6402 and K.S.A. 2006 Supp. 44-717 and repealing the existing sections.

Be it enacted by the Legislature of the State of Kansas:

New Section 1. (a) Sections 1 through 8, and amendments thereto, shall be known and may be cited as the Kansas fairness in public construction contract act.

(b) The rights and duties prescribed by this act shall not be waivable or varied under the terms of a contract. The terms of any contract waiving the rights and duties prescribed by this act shall be unenforceable.

New Sec. 2. As used in this act:

(a) "Construction" means furnishing labor, equipment, material or supplies used or consumed for the design, construction, alteration, renovation, repair or maintenance of a building, water or waste water treatment facility, oil line, gas line, appurtenance or other improvement to real property, including any moving, demolition or excavation of a building. "Construction" shall not mean the design, construction, alteration, renovation, repair or maintenance of a road, highway or bridge.

(b) "Contract" means a contract or agreement concerning construction made and entered into by and between an owner and a contractor, a contractor and a subcontractor or a subcontractor and another subcontractor.

(c) "Contractor" means a person performing construction and having a contract with an owner of the real property or with a trustee or agent of an owner.

(d) "Owner" means a public entity that holds an ownership interest in real property.

(e) "Public entity" means the state of Kansas, political subdivisions, cities, counties, state universities or colleges, school districts, all special districts, joint agreement entities, public authorities, public trusts, non-profit corporations and other organizations which are operated with public money for the public good.

(f) "Retainage" means money earned by a contractor or subcontractor but withheld to ensure timely performance by the contractor or subcontractor.

(g) "Subcontractor" means any person performing construction covered by a contract between an owner and a contractor but not having a contract with the owner.

(h) "Substantial completion" means the stage of a construction project where the project, or a designated portion thereof, is sufficiently complete in accordance with the contract, so that the owner can occupy or utilize the constructed project for its intended use.

(i) "Undisputed payment" means payments which all parties to the contract agree are owed to the contractor.

New Sec. 3. (a) Subject to the provisions of subsections (b), (c), (d), (e), (f), (g), (h) and sections 4 and 5, and amendments thereto, all owners, contractors and subcontractors, who enter into a contract for public construction after the effective date of this act, shall make all payments pursuant to the terms of the contract.

(b) The following provisions in a contract for public construction shall be against public policy and shall be void and unenforceable:

(1) A provision that purports to waive, release or extinguish the right to resolve disputes through litigation in court or substantive or procedural rights in connection with such litigation except that a contract may require nonbinding alternative dispute resolution as a prerequisite to litigation;

(2) a provision that purports to waive, release or extinguish rights to file a claim against a payment or performance bond, except that a contract may require a contractor or subcontractor to provide a waiver or release of such rights as a condition for payment, but only to the extent of the amount of payment received; and

(3) a provision that purports to waive, release or extinguish rights of subrogation for losses or claims covered or paid by liability or workers compensation insurance except that a contract may require waiver of subrogation for losses or claims paid by a consolidated or wrap-up insurance program, owners and contractors protective liability insurance, or project management protective liability insurance or a builder's risk policy.

(c) All contracts for public construction shall provide that payment of

amounts due a contractor from an owner, except retainage, shall be made within 30 days after the owner receives a timely, properly completed, undisputed request for payment according to terms of the contract, unless extenuating circumstances exist which would preclude approval of payment within 30 days. If such extenuating circumstances exist, then payment shall be made within 45 days after the owner receives such payment request.

(d) The architect or engineer of record or agent of the owner shall review, approve and forward undisputed requests for payment to the owner within seven business days of receipt from the contractor.

(e) If the owner fails to pay a contractor within the time period set forth in subsection (c), the owner shall pay interest computed at the rate of 18% per annum on the undisputed amount to the contractor beginning on the day following the end of the time period set forth in subsection (d).

(f) A contractor shall pay its subcontractors any amounts due within seven business days of receipt of payment from the owner, including payment of retainage, if retainage is released by the owner, if the subcontractor has provided a timely, properly completed and undisputed request for payment to the contractor.

(g) If the contractor fails to pay a subcontractor within seven business days, the contractor shall pay interest to the subcontractor beginning on the eighth business day after receipt of payment by the contractor, computed at the rate of 18% per annum on the undisputed amount.

(h) The provisions of subsection (g) shall also apply to all payments from subcontractors to their subcontractors.

New Sec. 4. (a) An owner, contractor or subcontractor may withhold no more than 10% retainage from the amount of any undisputed payment due.

(b) An owner must release the retainage on any undisputed payment due on a construction project within 30 days after substantial completion of the project; however, if any subcontractor is still performing work on the project under its subcontract, an owner may withhold that portion of the retainage attributable to such subcontract until 30 days after such work is completed.

(c) If an owner, contractor or subcontractor fails to pay retainage, if any, pursuant to the terms of a contract for public construction or as required by this act, the owner, contractor or subcontractor shall pay interest to the contractor or subcontractor to whom payment was due, beginning on the first business day after the payment was due, at a rate of 18% per annum.

(d) Nothing in this section shall prevent early release of retainage if it is determined by the owner, the contractor and the project architect or engineer, that a subcontractor has completed performance satisfactorily and that the subcontractor can be released prior to substantial completion of the entire project without risk or additional cost to the owner or contractor. Once so determined, the contractor shall request such adjustment in retainage, if any, from the owner as necessary to enable the contractor to pay the subcontractor in full, and the owner shall, as part of the next contractual payment cycle, release the subcontractor's retainage to the contractor, who shall, as part of the next contractual payment cycle, release such retainage as is due to the subcontractor.

New Sec. 5. If any undisputed payment is not made within seven business days after the payment date established in a contract for public construction or in this act, the contractor and any subcontractors, regardless of tier, upon seven additional business days' written notice to the owner and, in the case of a subcontractor, written notice to the contractor, shall, without prejudice to any other available remedy, be entitled to suspend further performance until payment, including applicable interest, is made. The contract time for each contract affected by the suspension shall be extended appropriately and the contract sum for each affected contract shall be increased by the suspending party's reasonable costs of demobilization, delay and remobilization.

New Sec. 6. In any action to enforce sections 3, 4 or 5 and amendments thereto, including arbitration, between a contractor and subcontractors or subcontractors and subcontractors, the court or arbitrator shall award costs and reasonable attorney fees to the prevailing party. Venue

of such an action shall be in the county where the real property is located and under Kansas law. The hearing in such an arbitration shall be held in the county where the real property is located.

New Sec. 7. Any provision in a contract that purports to waive the rights of a party to the contract to collect damages for delays caused by another party to the contract shall be void, unenforceable and against public policy. This provision is not intended to create a contract between parties where a contract did not otherwise exist.

New Sec. 8. The provisions of the Kansas fairness in public construction contract act shall not apply to construction projects which are required to comply with section 109 of the Kansas department of transportation special provisions to the standard specifications, 1990 edition (90P-205-R6) or any subsequent editions.

Sec. 9. K.S.A. 2006 Supp. 44-717 is hereby amended to read as follows: 44-717. (a) (1) *Penalties on past-due reports, interest on past-due contributions, payments in lieu of contributions and benefit cost payments.* Any employer or any officer or agent of an employer, who fails to file any wage report or contribution return by the last day of the month following the close of each calendar quarter to which they are related shall pay a penalty as provided by this subsection (a) for each month or fraction of a month until the report or return is received by the secretary of labor. The penalty for each month or fraction of a month shall be an amount equal to .05% of the total wages paid by the employer during the quarter, except that no penalty shall be less than \$25 nor more than \$200 for each such report or return not timely filed. Contributions and benefit cost payments unpaid by the last day of the month following the last calendar quarter to which they are related and payments in lieu of contributions unpaid 30 days after the mailing of the statement of benefit charges, shall bear interest at the rate of 1% per month or fraction of a month until payment is received by the secretary of labor except that an employing unit, which is not theretofore subject to this law and which becomes an employer and does not refuse to make the reports, returns and contributions, payments in lieu of contributions and benefit cost payments required under this law, shall not be liable for such penalty or interest if the wage reports and contribution returns required are filed and the contributions, payments in lieu of contributions or benefit cost payments required are paid within 10 days following notification by the secretary of labor that a determination has been made fixing its status as an employer subject to this law. Upon written request and good cause shown, the secretary of labor may abate any penalty or interest or portion thereof provided for by this subsection (a). Interest amounting to less than \$1 shall be waived by the secretary of labor and shall not be collected. Penalties and interest collected pursuant to this subsection shall be paid into the special employment security fund. For all purposes under this section, amounts assessed as surcharges under subsection (j) or under K.S.A. 44-710a, and amendments thereto, shall be considered to be contributions and shall be subject to penalties and interest imposed under this section and to collection in the manner provided by this section. For purposes of this subsection, a wage report, a contribution return, a contribution, a payment in lieu of contribution or a benefit cost payment is deemed to be filed or paid as of the date it is placed in the United States mail.

(2) Notices of payment and reporting delinquency to Indian tribes or their tribal units shall include information that failure to make full payment within the prescribed time frame:

- (i) will cause the Indian tribe to be liable for taxes under FUTA;
- (ii) will cause the Indian tribe to lose the option to make payments in lieu of contributions;
- (iii) could cause the Indian tribe to be excepted from the definition of “employer,” as provided in paragraph (h)(3) of K.S.A. 44-703, and amendments thereto, and services in the employ of the Indian tribe, as provided in paragraph (i)(3)(E) of K.S.A. 44-703, and amendments thereto, to be excepted from “employment.”

(b) *Collection.* (1) If, after due notice, any employer defaults in payment of any penalty, contributions, payments in lieu of contributions, benefit cost payments, or interest thereon the amount due may be collected by civil action in the name of the secretary of labor and the em-