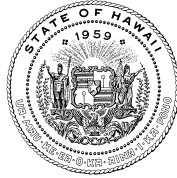


JOSH GREEN, M.D.
GOVERNOR
KE KIA'ĀINA



KEITH A. REGAN
COMPTROLLER
KA LUNA HO'OMALU HANA LAULĀ

MEOH-LENG SILLIMAN
DEPUTY COMPTROLLER
KA HOPE LUNA HO'OMALU HANA LAULĀ

STATE OF HAWAII | KA MOKU'ĀINA O HAWAII
DEPARTMENT OF ACCOUNTING AND GENERAL SERVICES | KA 'OIHANA LOIHELU A LAWELAWÉ LAULĀ
P.O. BOX 119, HONOLULU, HAWAII 96810-0119

WRITTEN TESTIMONY
OF
KEITH A. REGAN, COMPTROLLER
DEPARTMENT OF ACCOUNTING AND GENERAL SERVICES
TO THE

COMMITTEE ON GOVERNMENT OPERATIONS

FEBRUARY 4, 2025, 3:05 P.M.
CONFERENCE ROOM 225 AND VIA VIDEOCONFERENCE, STATE CAPITOL

S.B. 1587

RELATING TO RETAINAGE

Chair McKelvey, Vice Chair Gabbard, and Members of the Committee, thank you for the opportunity to submit testimony on S.B. 1587.

The Department of Accounting and General Services (DAGS) offers **comments** on this bill which proposes to amend HRS 103-32.1 to change the amount and way retainage is withheld from contractors.

The measure introduces the term “total project budget” (page 1, line 4) but does not define that term or provide guidance as to how the term may be interpreted; e.g., as the budget for the subject contract (such as the construction budget), or as the budget for all goods and services associated with the project (which may include budgets for planning, land acquisition, design, construction, equipment, furnishings, and other project costs), or a range of other potential interpretations. The measure should provide

such guidance. We would humbly recommend the committee consider the definition for the term “total project budget” be specified as the contract amount which may be increased or decreased through contract amendments and supplementary contracts.

The proposed amendment will change the amount of retainage from “five per cent of the total amount due to the contractor” to “one percent of the total project budget” (page 1, lines 8-9). We caution that this significant reduction in retainage will likely result in a lessening of the state’s ability to encourage satisfactory contractor performance.

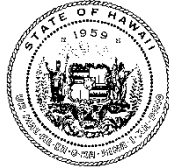
Although currently found in the existing statute (HRS 103-32.1 (c) (1)), we would like to share our recommendation regarding the language on page 1, lines 10-12 provides that assessment of retainage shall be ceased “after fifty of percent of the contract is completed and progress is satisfactory”. While that language is useful regarding the current provision for retainage calculated on the amounts owed to the contractor, it may be confusing or counter-productive for the proposed regime, given that the one percent retainage on the total project budget would most effectively be levied at the commencement of the contract (and at the commencement of any subsequent contract amendment or supplementary contract) and should not be reduced through the life of the contract except if the contract amount is reduced. The department suggests that the language from the comma on line 10 through the comma on line 13 be deleted; and further that the phrase “sums not exceeding” on lines 14-15 also be deleted.

With respect to the proposed language for new subsection (c) the department suggests that:

- The number of days be set at 120 calendar days;
- The language at page 2, line 7 be amended to read: "... contract (including any contract amendment and/or supplementary contract) is completed and satisfactory; provided that ..."; and
- Completion of contractor warranties should be considered integral to the satisfactory completion of the contract. Therefore, to clarify that intent, the language at page 2, line 10 should be amended to read: "... satisfactory and all contractor warranty periods have been completed."

The department also suggests that the measure be amended to clarify that the new statutory provisions are intended to apply only to contracts executed after January 1, 2026. This clarification is necessary to permit agencies to continue to withhold retainage at the existing rates for contracts in progress and provide agencies sufficient time to revise procedures, specifications, and contract provisions prior to actual implementation of the measure's provisions. This will also allow prospective contractors to consider the costs and other effects of the revised retainage provisions.

Thank you for the opportunity to provide testimony on this measure.



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**TESTIMONY
OF
BONNIE KAHAKUI, ADMINISTRATOR
STATE PROCUREMENT OFFICE**

**TO THE SENATE COMMITTEE
ON
GOVERNMENT OPERATIONS
February 4, 2025; 3:05 PM**

**SENATE BILL 1587
RELATING TO RETAINAGE**

Chair McKelvey, Vice Chair Gabbard, and members of the committee, thank you for the opportunity to submit testimony on Senate Bill 1587, which allows procurement officers to withhold a retainage fee of one per cent of the total budget from contractors to ensure satisfactory project completion and requires the retainage fee to be paid to contractors within a certain number of days of project completion.

The State Procurement Office (SPO) provides comments and recommendations.

The purpose of Section 103-32.1 Contract provision for retainage; subcontractors, Hawaii Revised Statutes, is to provide assurance that contractors will perform properly.

The SPO respectfully recommends that the term "total project budget" in 103-32.1(c) of the bill be replaced by **"total contract amount,"** as the contract amount which may be increased or decreased through contract amendments and supplementary contracts. The total project may likely also encompass multiple "smaller" contracts.

The SPO comments on the proposed amendment to change the retainage fee from five percent of the total amount due to the contractor" to "one percent of the total budget." The retainage language of one percent of the TOTAL PROJECT may be unrealistic and may not provide the purchasing agency flexibility on retainage fees and is likely to decrease the state's ability to encourage satisfactory contractor performance. The retainage language, on the TOTAL PROJECT, would hold all contractors liable for a higher amount, regardless of their contractual involvement and value. Thus, the SPO recommends keeping the maximum retainage to five per cent to give the procuring agency flexibility to be applied to the total contracted amount.

- The SPO makes the following recommendations to Section 1, page 1, lines 4-16, which should read as follows:

"(c) Any public contract may include a provision for the retainage of a portion of the total contract amount from the amount due under the contract to the contractor to ensure the proper performance of the contract; provided that:

(1) The sum withheld by the procurement officer from the contractor shall not exceed five per cent of the total contract amount and that, after fifty per cent of the contract is completed and progress is satisfactory, no additional sum shall be withheld; provided further that if progress is not satisfactory, the procurement officer may continue to withhold, as retainage, sums not exceeding five per cent of the total contract amount;

- The SPO comments on Section 1, page 2, lines 4-10, on the number of days that the retainage is paid to the contractor. The SPO notes that Section 103-10, HRS, Payment for goods and services says "(a) Any person who renders a proper statement for goods delivered or services performed, pursuant to contract, to any agency of the State or any county, shall be paid no later than **thirty calendar** days following receipt of the statement or satisfactory delivery of the goods or performance of the services.

The SPO provides background information from the National Institute for Public Procurement (NIGP), which defines and explains retainage:

What is retainage?

Retainage or retention or holdback, is a common practice in the construction industry where a portion of payment, typically 5-10%, is withheld until a predefined milestone is achieved on a building project. Retainage has a long history in the industry and can apply to both general and subcontractors.

The Purpose of Retainage

Retainage, when properly utilized, is designed to address several issues inherent to construction and other critical projects:

- **Quality assurance:** Retainage incentivizes a contractor and any applicable subcontractors to complete work to the owner's satisfaction. It also encourages contractors to meet or exceed quality and performance standards on a project.
- **Defect correction:** Retention provides the owner or general contractor financial leverage by withholding a portion of payments. This leverage ensures the contractor addresses defects, deficiencies, or incomplete work.
- **Project completion:** Retainage motivates contractors to complete their work within the agreed-upon schedule to avoid abandoning or leaving projects unfinished.
- Retainage offers several benefits for both owners and contractors.

Retainage offers several benefits for both owners and contractors.

- Risk mitigation: Retainage helps mitigate the financial risks associated with contractor and subcontractor defaults, delays, and incomplete or defective work.
- Quality control: As a practice, retainage encourages contractors to maintain a high quality of work throughout a project, as the release of the retained pay can be contingent on meeting specific project standards.
- Dispute resolution: Retainage provides a financial cushion for owners to address disputes, deficiencies, or disagreements that may arise during a project.

Thank you for the opportunity to submit testimony on this measure.

SAH - Subcontractors Association of Hawaii

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LATE

February 4, 2025

Testimony To: Senate Committee on Government Operations
Representative Angus L.K. McKelvey, Chair

Presented By: Tim Lyons, President

Subject: S.B. 1587 – RELATING TO RETAINAGE.

Chair McKelvey and Members of the Committee:

I am Tim Lyons, President of the Subcontractors Association of Hawaii and we highly endorse this bill. The SAH represents the following ten separate and distinct contracting trade organizations.

HAWAII FLOORING ASSOCIATION

ROOFING CONTRACTORS ASSOCIATION OF HAWAII

HAWAII WALL AND CEILING INDUSTRIES ASSOCIATION

ELECTRICAL CONTRACTORS ASSOCIATION OF HAWAII

TILE CONTRACTORS ASSOCIATION OF HAWAII

PLUMBING AND MECHANICAL CONTRACTORS ASSOCIATION OF HAWAII

SHEETMETAL AND AIR CONDITIONING NATIONAL CONTRACTORS ASSOCIATION OF HAWAII

PAINTING AND DECORATING CONTRACTORS ASSOCIATION

PACIFIC INSULATION CONTRACTORS ASSOCIATION

HAWAII ARCHITECTURAL GLASS AND METAL ASSOCIATION

Retainage has long been an issue for both contractors and subcontractors on State jobs. It is commonly heard of contractors not receiving their retainage amounts for as long as two (2) and three (3) years after the completion of the projects' work. This is a huge disincentive for contractors to participate in the public works arena.

We would like to point out that retainage is currently and would still be under this bill, imposed only on the first 50% of the budget, thereby resulting in one-half of one percent to be withheld and this retainage provision only applies to the prime or general contractor. Section 103-32,1(e) then allows the prime to negotiate his own retainage (subject to no more than ten percent 10% maximum) with the subcontractor. Subs have little negotiation power with the prime contractor so then ten percent (10%) is the norm.

We recommend deletion of 103-32.1 (e). We are also puzzled by the change from "the amount due" to "total project budget". What if a project is over or under budget?; retainage would still be calculated on the budget, not the cost?

Further, there are oftentimes allegations that while the State has released the retainage, the general contractor continues to hold on to the retainage for an extended period of time. Retainage by itself is not a bad concept. The problem is that it is not being administered properly. If a contractor isn't performing and there is concern about keeping certain sums of money in order to ensure completion then that is all based on job-site inspections and performance by the contractor.

Based on the above and in order to increase the subcontractor viability, we support this bill.

Thank you.