

COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 1273-03
Bill No.: HB 641
Subject: Contracts and Contractors; Bonds - General Obligation and Revenue
Type: Original
Date: February 25, 2013

Bill Summary: This proposal specifies that no public owner, contractor, or subcontractor shall withhold retainage on public works projects if the public owner has obtained a bond.

FISCAL SUMMARY

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND			
FUND AFFECTED	FY 2014	FY 2015	FY 2016
Total Estimated Net Effect on General Revenue Fund	\$0	\$0	\$0

ESTIMATED NET EFFECT ON OTHER STATE FUNDS			
FUND AFFECTED	FY 2014	FY 2015	FY 2016
Total Estimated Net Effect on <u>Other</u> State Funds	\$0	\$0	\$0

Numbers within parentheses: () indicate costs or losses.
This fiscal note contains 7 pages.

ESTIMATED NET EFFECT ON FEDERAL FUNDS			
FUND AFFECTED	FY 2014	FY 2015	FY 2016
Total Estimated Net Effect on <u>All</u> Federal Funds	\$0	\$0	\$0

ESTIMATED NET EFFECT ON FULL TIME EQUIVALENT (FTE)			
FUND AFFECTED	FY 2014	FY 2015	FY 2016
Total Estimated Net Effect on FTE	0	0	0

- Estimated Total Net Effect on All funds expected to exceed \$100,000 savings or (cost).
- Estimated Net Effect on General Revenue Fund expected to exceed \$100,000 (cost).

ESTIMATED NET EFFECT ON LOCAL FUNDS			
FUND AFFECTED	FY 2014	FY 2015	FY 2016
Local Government	(Unknown over \$100,000)	(Unknown over \$100,000)	(Unknown over \$100,000)

FISCAL ANALYSIS

ASSUMPTION

Officials at the **Office of Administration - Division of Facilities Management, Design and Construction** assume this proposal would have no fiscal impact on the Division. However, due to the many unknown variables of the elimination of contract retainage; the provisions of this proposal could affect our ability to assure that contracts satisfy their obligations to complete a construction project.

Officials at the **Department of Conservation, Department of Economic Development, Department of Labor and Industrial Relations, Missouri Department of Transportation, Metropolitan Community College** each assume there is no fiscal impact to their organization from this proposal.

Officials at the **University of Missouri** assume this proposal would eliminate retainage from University construction contracts. The elimination of retainage from construction contracts will have a negative effect on the University's ability to enforce completion and manage claims. The cost of this change is difficult to estimate but given the volume of construction the University performs could easily cost more than \$100,000 per year in delay costs and settlement of closeout claims.

Our experience is that sureties may provide payment and performance bonds, however in practice they are in the business of protecting their own interests, not the interests of the owner or University. The university has an exemplary record of prompt payment of its contractors and intervening on behalf of workers and subcontractors who have not been paid promptly. Without retainage we will no longer be able to do this.

Officials at the **Missouri State University** assume this could have significant costs. Bonding companies do not adequately provide the coverage or leverage an owner needs to have projects completed in a timely fashion. The bonding companies primary concern is no loss of money. Finishing a project is secondary. When an owner needs to get a project completed through the bonding company, the owner loses all control over when a project would be finished.

Officials at the **City of Kansas City** assume potential increased project costs because the City may be forced to appropriate additional funds to complete a particular project if a contractor fails to complete a project for any reason. If there are no retainage amounts available on a project the only recourse a City may have is to declare default and rely on a surety to complete the project. This can be a costly and cumbersome process with no guarantee that the surety will live up to its

ASSUMPTION (continued)

obligations. Furthermore, some projects cannot wait to be completed until the surety resolution process runs its course. Consequently the City will be forced to appropriate additional funds to complete a project; essentially paying twice for the same work.

There are also costs associated with the surety resolution process. Additional internal staff time has to be devoted to the resolution process, thus driving up administrative costs for each project. In some cases, where complex issues are involved, the City may look to outside legal counsel to assist in the resolution process. Again driving up the administrative costs of the construction process.

Officials at the **University of Central Missouri** estimate a potential substantial fiscal impact for the following reasons:

1. Acting as the Owner in the contractual relationships we rely heavily on withheld retainage as leverage to cause Contractor's to complete the final punch list, Owner Training, Equipment Start-Up and Final As-Built Drawing turnover requirements.
2. The term 'substantial completion' used to mean 'the Owner has beneficial use of the building or space'. In my opinion, Contractor's will push for 'substantial completion' when significant amounts of completion items, equipment start-up, commissioning, air and hydronic testing, adjusting and balancing, punch list remain to be completed. Without the leverage of withheld payment in the form of retainage, it would be even more difficult to keep Contractor's engaged to complete these important items. If the Owner had beneficial use of the space as defined above, the issues I have identified to justify withholding retainage would not exist.
3. We understand that the intent of the proposal is to reduce the amount of time it takes for release of final payments to contractors; however, we would be more in favor of the proposal if retainage and final payment release for these projects included more language defining substantial completion as identified above so the lost leverage of no longer withholding final payment is no longer a factor.
4. Cost impacts could be significant on a per project basis. If the Owner becomes required to make final payments before all final work is complete, the Owner could incur the costs associated with finishing the incomplete items if the lost leverage of no longer motivates the contractor to return to the job to finish. The dollar amounts on a per project basis could be substantial but would typically be less than what we would consider taking legal action for or going after a performance and payment bond.

ASSUMPTION (continued)

Officials at the **Northwest Missouri State University** assume there would be minor savings on projects between \$25,000 - \$50,000. Without a future project list they are unable to determine an exact impact.

Officials at the following cities: Ashland, Belton, Bernie, Bonne Terre, Boonville, California, Cape Girardeau, Clayton, Columbia, Dardenne Prairie, Excelsior Springs, Florissant, Frontenac, Fulton, Gladstone, Grandview, Harrisonville, Independence, Jefferson City, Joplin, Kearney, Knob Noster, Ladue, Lake Ozark, Lebanon, Lee Summit, Liberty, Louisiana, Maryland Heights, Maryville, Mexico, Neosho, O'Fallon, Pacific, Peculiar, Popular Bluff, Raytown, Republic, Richmond, Rolla, Sedalia, Springfield, St. Charles, St. Joseph, St. Louis, St. Robert, Sugar Creek, Sullivan, Warrensburg, Warrenton, Webb City, Weldon Spring and West Plains did not respond to **Oversight's** request for fiscal impact.

Officials at the following schools: Blue Springs Public Schools, Branson Public Schools, Columbia Public Schools, Fair Grove Schools, Francis Howell Public Schools, Independence Public Schools, Jefferson City Public Schools, Kirksville Public Schools, Lee Summit Public Schools, Mexico Public Schools, Nixa Public Schools, Parkway Public Schools, Raytown School District, Sedalia School District, Sikeston Public Schools, Silex Public Schools, Special School District of St. Louis County, Spickard School District, St Joseph School District, St Louis Public Schools, St. Charles Public Schools, and Sullivan Public Schools did not respond to **Oversight's** request for fiscal impact.

Officials at the following counties: Andrew, Audrain, Barry, Bates, Boone, Buchanan, Callaway, Camden, Cape Girardeau, Carroll, Cass, Clay, Cole, Cooper, DeKalb, Franklin, Greene, Holt, Jackson, Jefferson, Johnson, Knox, Laclede, Lawrence, Lincoln, Marion, Miller, Moniteau, Monroe, Montgomery, New Madrid, Nodaway, Ozark, Perry, Pettis, Phelps, Platte, Pulaski, Scott, St. Charles, St. Louis, St. Francois, Taney, Warren, Wayne and Worth did not respond to **Oversight's** request for fiscal impact.

Officials at the following colleges: Crowder, Harris-Stowe, Jefferson College, Southeast Missouri State University, State Fair Community College, St. Charles Community College, Three Rivers Community College and Truman State University did not respond to **Oversight's** request for fiscal impact.

Oversight will reflect in the fiscal note, costs of Unknown over \$100,000 for all political subdivisions including colleges and universities.

<u>FISCAL IMPACT - State Government</u>	FY 2014 (10 Mo.)	FY 2015	FY 2016
	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>

<u>FISCAL IMPACT - Local Government</u>	FY 2014 (10 Mo.)	FY 2015	FY 2016
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LOCAL POLITICAL SUBDIVISIONS

<u>Cost - Local Political Subdivisions until to withhold retainage</u>	(Unknown over <u>\$100,000</u>)	(Unknown over <u>\$100,000</u>)	(Unknown over <u>\$100,000</u>)
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ESTIMATED NET EFFECT ON LOCAL POLITICAL SUBDIVISIONS	(Unknown over <u>\$100,000</u>)	(Unknown over <u>\$100,000</u>)	(Unknown over <u>\$100,000</u>)
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FISCAL IMPACT - Small Business

No direct fiscal impact to small businesses would be expected as a result of this proposal.

FISCAL DESCRIPTION

This proposal increases from \$25,000 to \$50,000 the threshold dollar amount of a public works project that requires a contractor to purchase a security bond. Public owners, contractors, and subcontractors are prohibited from withholding retainage on public works projects if the public owner has obtained the security bond. If the public owner is not required to obtain a bond because the cost of the project is not estimated to exceed \$50,000, the public owner may withhold retainage on the project in an amount not to exceed 5% of the value of the contract or subcontract.

This legislation is not federally mandated, would not duplicate any other program and would not require additional capital improvements or rental space.

SOURCES OF INFORMATION

City of Kansas City
Department of Conservation
Department of Economic Development
Department of Labor and Industrial Relations
Missouri Department of Transportation
Metropolitan Community College
Missouri State University
Northwest Missouri State University
Office of Administration
Division of Facilities Management, Design and Construction
University of Central Missouri
University of Missouri



Ross Strope
Acting Director
February 25, 2013