

Approved: 3/1/10  
Date

MINUTES OF THE HOUSE COMMERCE AND LABOR COMMITTEE

The meeting was called to order by Chairman Steve Brunk at 9:02 a.m. on February 1, 2010, in Room 784 of the Docking State Office Building.

All members were present except:

Representative Broderick Henderson- excused

Committee staff present:

Art Griggs, Office of the Revisor of Statutes  
Renaë Jefferies, Office of the Revisor of Statutes  
Jerry Donaldson, Kansas Legislative Research Department  
Dennis Hodgins, Kansas Legislative Research Department  
Stephen Bainum, Committee Assistant

Conferees appearing before the Committee:

Larry R Baer, League of Kansas Municipalities  
Erik Sartorius, City of Overland Park  
Derreld Ellis, Westar Energy

Others attending:

See attached list.

**HB 2238:** **Amending the fairness in private construction contract act and the fairness in public construction contract act regarding retainage.**

The Chairman thanked everyone for coming back on Monday and reopened the hearing on **HB 2238**. Trudy had nothing further to add to her testimony. There were no question for her from the committee.

Melissa Wangemann, Kansas Association of Counties, provided written only testimony on **HB 2238** (Attachment 1). They are opposed to the bill because it would impede the counties' ability to contract the best deal possible for public construction.

Dale Goter, City of Wichita, presented written only testimony in opposition to **HB 2238** (Attachment 2). The city currently retains 10 % of earned contract fees to ensure satisfactory completion of construction projects. The percentage has proven to be a sufficient incentive to ensure compliance.

Larry R Baer, League of Kansas Municipalities, gave testimony in opposition to **HB 2238** (Attachment 3). The most significant changes would be allowing the contractor or subcontractor to use alternative security. Each of these forms of alternate security have inherent issues. Although the Grange Amendment makes some improvements, it still allows the use of alternate forms of security. Therefore the League continues to oppose this bill.

Representative Suellentrop asked if we were not incurring cost increases now because some of the early completion contractors have to allow for a delay in receiving their payment. Larry said that was plausible.

Representative Brunk asked if he was aware of a pattern of significant problems with subcontractors not receiving their retainage. Larry said that it was not an issue that had been brought to their attention on a regular basis.

Erik Sartorius, City of Overland Park, testified in opposition to **HB 2238** (Attachment 4). The City supports the current statutory framework for paying contractors. Their position is that 10% is the proper amount of retainage. Owners should not be mandated to accept "Alternate security" as a substitute for retainage.

Representative Tietze asked if they had to accept the lowest bidder. Erik said there was flexibility in some instances but in other cases they had to take the low bidder.

Representative Grange said that we may be receiving bids from all over the country because there is no work in their part of the country. The problem with using them is that problems show up later and you can't get

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CONTINUATION SHEET

Minutes of the House Commerce and Labor Committee at 9:02 a.m. on February 1, 2010, in Room 784 of the Docking State Office Building.

them back to fix them.

Representative Suellentrop asked if architects have the same retainage in their contracts? Erik passed that question to Trudy Aaron who said that they retain 20% for the end of construction and then 2 ½ % is retained until the "as built" are delivered to the state.

Representative Brunk asked if Erik or Trudy was aware of a problem across the state of owners not paying the retainage within the prompt pay time. Trudy answered absolutely not since the prompt pay bills were passed.

Representative Grange asked if on a cost plus job there would be no retainage. They were not sure of the answer on that and said that they would check into it.

Darrelld Ellis, Westar Energy, testified in opposition to **HB 2238 (Attachment 5)**. Westar's primary objection is that it would limit their ability to manage contractors on major construction projects. Retention is used to incent a contractor to complete the details of the work.

Representative Worley asked that if 25 to 30 states have changed their laws to 5% retainage, what is your organization hearing from them. Are they experiencing more difficulties since changing to 5%? Darrelld said that he did not have the answer to that.

Representative Brunk asked the proponents if there was a rampant problem with paying retainage or if it was isolated and more random. Bill Miller, American Sub-Contractors Association replied that the pattern was not random, it was happening throughout the state. The problem is the extended period of time that it takes to actually get the retention.

Representative Jack asked Eric Stafford, Associated General Contractors of Kansas if reputation can be a stick to get the job done. Eric replied that everyone wanted to have a good reputation and that one bad job would not prevent you from getting work. However if you had a series of bad jobs word would get around and cause a lack of work.

Neal Angrisano, Johnson County Government, said that retainage is the only tool we have when the one out of ten or one out of twenty fail to get the job done.

The Chairman closed the hearing on **HB 2238**.

The next meeting is scheduled for February 2, 2010.

The meeting was adjourned at 9:58 a.m.

COMMERCE & LABOR COMMITTEE

DATE: 2-1-10

NAME	REPRESENTING
BILL MATHAM	ASA
Ken Keller	ASA - Western Extralite Co
Tom Burgess	ASA -
Phyllis fast	st. of KS. - DEM
Eric Staffal	AGC of KS
COREY PETERSON	AGC of KS
Judy Gron	Am Inst of Architects
Stuart Little	Johnson County Govt.
Mark Schweber	Westar
DARRELD ELLIS	WESTAR
Berend Koops	Hein Law Firm / ABC
Kendra Hanson	Hein Law Firm
Ron Seiber	KLFA
Dale Gofar	City of Wichita
Bob Johnson	Federico Consulting
LARRY R BARR	LKM
DAN MORGAN	Buildings Assn. & KC Chaptr, AGC
Darci Meese	Water One.
Tom Kuhn	JRASB
Dan Carroll	Dept. of Admin.
Larry Oppitz	JFA
Travis Lowe	Little Govt Relations
TED HENRICH	CAPITOL STRATEGIES.
ERIK SARTORIUS	City of Overland Park



TESTIMONY OF THE KANSAS ASSOCIATION OF COUNTIES  
TO THE HOUSE COMMERCE COMMITTEE  
JANUARY 28, 2010

Chairman Brunk and Members of the Committee:

The Kansas Association of Counties opposes HB 2238. We are concerned that the provisions offered in the bill and the balloon amendment will impede counties' ability to contract the best deal possible for public construction.

Retainage is an important component in forcing a contractor or subcontractor to complete its work in an accurate and timely manner. Because taxpayers are ultimately footing the bill for construction of any county building, it is imperative that counties be able to negotiate and enforce construction contracts in a manner that ensures we pay only for projects completed correctly and on time.

Most notably HB 2238 adds a new requirement that counties accept an "alternate security" which can be a bond, letter of credit, certificate of deposit, bond, or other type of asset or security. We are concerned that enforcing payment on these items will be a prolonged process: Will the bank uphold the letter of credit? Must we wait for the CD to mature? How many conversations must we have with the surety before it pays out on the bond? The best motivator for a contractor to complete its work is cold, hard cash. Thus, we believe retainage is the best method for ensuring that construction of county buildings is delivered on time, in a high standard, as appropriate for tax payer money.

I appreciate the opportunity to submit testimony today and apologize that I cannot appear in person.

Respectfully Submitted,

Melissa A. Wangemann

General Counsel and Director of Legislative Services

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House Commerce & Labor  
Date: 2-1-10  
Attachment # 1



Dale Goter  
Government Relations Manager

# TESTIMONY

City of Wichita  
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## House Commerce and Labor

### Hearing on HB2238

**Thursday, 1/28/2010, 9:00 AM, Rm 784 DSOB**

Chairman Brunk and members of the House Commerce and Labor Committee:

The City of Wichita stands in opposition to HB2238. This proposed legislation would deal a substantial blow to the efficiency of the city's current construction contract process, and is potentially quite costly to local taxpayers.

Under current practice, the city retains 10 percent of earned contract fees to ensure satisfactory completion of construction projects. This percentage has proven to be a sufficient incentive to ensure compliance, while not working any significant hardship on the contractors involved. By retaining city funds as security, there is no collection risk, effort or expense to the city. This bill would change this entire approach, substantially to the benefit of contractors.

The bill would limit retainage to a maximum of 5 percent on a contract, and would further eliminate the ability to withhold any retainage at all if a performance bond or "alternate security" or provided by the contractor. Currently, performance bonds are required for construction contracts, in addition to the retainage process.

This bond serves as a means to ensure that subcontractors are paid in a timely fashion, so that general contractors do not attempt to shift the effect of poor business decisions onto the subcontractors they engage. The city's experience with collecting on performance bonds has been spotty. Bonding companies have been known to aggressively defend against the obligation of payment. This leaves the subcontractors unpaid, the project incomplete, or both.

Substantial time, persuasive effort, and occasionally litigation, are required to enforce performance bonds. This problem could be even worse if alternative forms of security were allowed. This could lead to disputes or improper practices in valuing alternative security. It is easy to imagine the City stuck with an unsalable property with a clouded title as valueless security if ever pressed to recover.

The bill would also impose a maximum retainage amount of 150% of the value of work left undone. This represents incomplete security for the city or other owner. The retained amount may not be sufficient incentive for the contractor to complete the contracted work. However, due to mobilization and demobilization costs necessary to obtain an alternative contractor or lack of interest by the

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Attachment # 2

construction community in completing the project remainder, the cost of completion could greatly exceed the 150% retention amount.

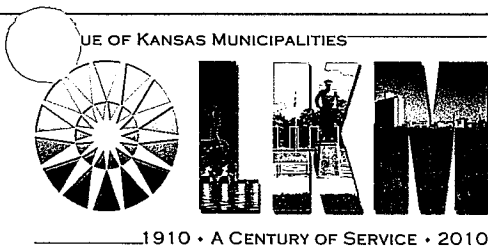
Additionally, the bill would beg for disputes between contractor and owner on what constitutes substantial completion and appropriate retention. It would impose an 18% per annum interest on the disputed amounts.

One further glaring deficiency is that the statute would provide for all contractors, irrespective of past performance or established relationships, benefits that can be earned or even negotiated under the current law.

Scaled reductions in retention amounts are a commonly considered option when contracting with contractors of established reputation and proven performance. This bill would withhold from cities and all other owners the security they need in exactly the occasions when they need it most.

For these reasons, the City of Wichita urges the committee to reject HB2238.

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Date: January 28, 2010  
To: House Committee on Commerce and Labor  
From: Larry R. Baer  
Assistant General Counsel  
Re: HB 2238  
Testimony in Opposition

Thank you for allowing me to appear before you today and present testimony in opposition of HB 2238 on behalf of the League of Kansas Municipalities and its member cities. HB 2238 proposes to amend both the Private and Public Construction Acts. The provisions applying to the Public Construction Act are found in sections 3 and 4. This testimony relates only to the Kansas Fairness in Public Construction Contract Act.

HB 2238, as currently written, includes a number of changes to current law. The most significant of these are the provisions allowing the contractor or subcontractor to use alternative security, the limitations placed upon the amounts retained from each payment and the total amount of retainage that may be held.

#### **Alternative Security**

HB 2238 would allow a contractor or subcontractor to unilaterally request and use a retainage bond, bank letter of credit, certificate of deposit or cash bond in lieu of having retainage withheld by the owner. The owner has no input and must accept the decision made by the contractor or subcontractor. This is contrary to good business policy and negotiated contract terms. Also, each of these forms of security have some inherent issues. Letters of credit are subject to expiration and withdrawal or termination by the issuer. Bonds require premiums to be paid which could increase the cost of a project if the contractor adds the cost of the bond back into project costs. With both letters of credit and bonds the owner is dealing with a third party when it comes time to collect or get performance. This potentially adds time and expense in reaching resolution. Also, there is an increased potential for the need for litigation when dealing with both issuers of letters of credit and bonding companies. This adds potential cost and delay to the project completion. Finally there is no mechanism regarding how a certificate of deposit would be handled as security or the method of collection.

#### **Limitations on Retainage Amounts**

HB 2238 would reduce the allowed retainage from 10% to 5% (Sec. 4(a)). This does appear to be in conflict with Sec. 4(f) (former Sec. a). The total amount of retainage would be restricted to 150% of the value of the incomplete work. Again, these statutory limitations infringe upon the parties' right to contract.

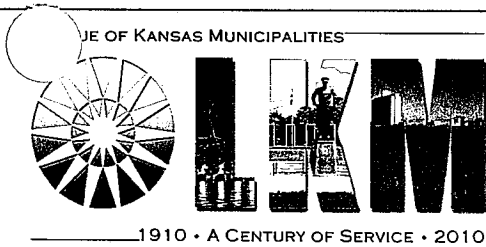
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The parties to a contract should be able to negotiate the terms of the contract. The form of retainage acceptable to the parties, the amounts to be retained and the retention time, and the method of payment of the retained amounts are all simply terms of the contract to be negotiated and contained in the project contract. Contracts should not contain unilateral terms. The inclusion of provisions which do not allow owners input on the form of security in lieu of retainage is not a sound business practice and is poor public policy.

The League's opposition is primarily based upon the public policy of allowing municipalities the flexibility to contract for public improvement projects to the benefit of the public and to negotiate such terms and conditions as are in the best interest of the public. Municipalities should not have their hands tied in negotiating for public construction projects.

For these reasons, the League of Kansas Municipalities opposes HB 2238. Thank you.





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Date: January 28, 2010  
To: House Committee on Commerce and Labor  
From: Larry R. Baer  
Assistant General Counsel  
Re: HB 2238  
Comments on Rep. Grange Balloon

Thank you for allowing me to appear before you today on behalf of the League of Kansas Municipalities and its member cities and present comments on the amendments presented by Rep. Grange. In general, the amendments posed by Rep. Grange are an improvement over the base bill.

The amendments continue to allow the use of alternative forms of security and require that the owner accept the use of alternative security. The owner does get to designate the form of alternative security to be used. This is more favorable than the term of the bill, but it does not eliminate the inherent problems noted in our testimony on HB 2238.

The apparent conflict between 5% or 10% maximum retainage has been clarified.

The retainage amount can be increased by the owner to not more than 10% under certain types of conditions. Because of the general nature of the description of these "triggers" it can be foreseen that litigation will result to resolve whether or not there has been a breach.

Even with the proposed amendments the League would continue to oppose the bill for all of the reasons stated in our testimony on HB 2238. Thank you.

# OVERLAND PARK

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Overland Park, Kansas 66212

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Testimony before the House Commerce & Labor Committee regarding House Bill 2238

Presented by Erik Sartorius

January 28, 2010

The City of Overland Park appreciates the opportunity to appear before you in opposition to House Bill 2238 and the proposed balloon amendment to the same. The City instead supports the current statutory framework for paying contractors.

The City's position is the proper amount of retainage is 10% of the value of the contract. The proposed legislation and the balloon amendment provide for withholding 5%. While the amendment does suggest that 10% could be retained, it appears to create a burden on an owner to show that the contractor is in breach of its agreement with the City before 10% can be retained. The City believes that retainage of 5% is not adequate to protect its interest.

Similarly, the City opposes limiting an owner from withholding more than 150% of the value of incomplete work as in many circumstances that amount may not be adequate to protect the City's interest.

Owners should not be mandated to accept "Alternate security" as a substitute for retainage. We know that, as a general rule, withholding a reasonable amount of the contract consideration works to ensure the project is completed. The retainage provides a readily available source of funds to cure default. The City would be opposed to being forced to utilize some other method that may not be effective and that may result in protracted litigation. For example, if the City is forced to call on a performance bond, the City is left fighting against an insurance company that will likely not want to pay out. The contractor and subcontractors are no longer interested parties with any reason to participate in the completion of the process.

It is imperative that the City have the ability to ensure that our projects are completed. The City must be able to retain the ability to incent the contractor to finish the job. At some point the above proposed changes could easily create a situation where it is more advantageous to the contractor to walk away from the project than to complete it. When the project is left unfinished, the ones who suffer are the taxpayers.

The City of Overland Park believes that adequate protections exist in current law for all parties engaged in public construction. We request that you do not recommend House Bill 2238, as drafted or with the proposed balloon amendment, favorably for passage.

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Date: 2-1-10  
Attachment # 4



**Testimony of Darreld Ellis  
Manager, Generation Contracts for Westar Energy  
Before the House Commerce and Labor Committee  
On HB 2238  
January 28, 2010**

Good morning Chairman Brunk and members of the committee. Thank you for the opportunity to provide testimony in opposition to HB 2238.

At Westar Energy, I manage the major generation construction contracts. Westar maintains good relationships with its general contractors as well as their subcontractors. Our current major projects include the installation air quality control system upgrades at the Lawrence Energy Center and the building of substations for transmission upgrades.

Although Westar has several concerns, our primary objection with HB 2238 is the provision on page 2, lines 23 – 25 and on page 4, lines 4 – 6. This provision would limit Westar's ability to manage contractors on major construction projects. We routinely require both 100% Payment & Performance (P&P) bonds, which are paid for by Westar, and 10% retention.

Retention and P&P bonds serve different purposes in the management of contractors. P&P bonds provide protection when a contractor is financially unable to perform -- i.e. a bankruptcy. Retention is used to incent a contractor to complete the details of the work.

We've learned from experience that collecting on P&P Bonds can be time-consuming, which can result in delays in completion of the project. Thus, the retention amount can be used as an incentive for the contractor to complete the work identified in the contract.

Thank you for the opportunity to testify this morning. I will stand for questions at the appropriate time.