

Retention funds: New obligations and offences with teeth

The new rules for retentions in construction contracts will provide better protection for contractors and subcontractors, and harsher penalties for non-compliant entities.

The reason for the new rules

It is a well-known issue that retention monies are commonly intermingled with other funds and are sometimes used as working capital. Unfortunately, this led to numerous instances where the retaining entity went under and the retentions were nowhere to be found – leaving contractors and subcontractors in the lurch.

Despite the changes in 2017 in the Construction Contracts Amendment Act 2015, there continued to be examples of contractors and subcontractors being unable to recover the retentions for their work due to the lack of effective protections and enforceability.

In response, the [Construction Contracts \(Retention Money\) Amendment Act 2023](#) was passed and has attained Royal Assent. The new rules will come into force on 5 October 2023.

These new rules are a further attempt to tighten up retention accounting practices with the goal of protecting contractors and subcontractors by introducing accountability for non-compliance.

The key changes

- Retentions must be held on trust for the relevant contractors/subcontractors as beneficiaries:
 - as soon as possible after being retained; and
 - in a separate account with a registered New Zealand bank (although certain compliant financial instruments may be used instead).

However, the retention holder can keep any interest earned on the retention funds.

- The retention holder must keep particular records of the beneficiary's funds. Those records must identify who the beneficiary is and the construction contract(s) to which the money relates. The trustee must also keep detailed records of each payment to and from the trust account.
- The trustee must report to the beneficiary the amount and location of the retained funds:
 - as soon as practicable after money is retained; and
 - at least once every three months thereafter.
- Non-compliance with the updated law is now punishable by fines:
 - companies may be fined up to \$200,000 for each offence; and
 - directors may be personally liable for fines up to \$50,000 for each offence.

Key takeaways

- To avoid significant fines and personal responsibility for directors, retention holders should:
 - ensure retentions are held in a separate and compliant bank account; and
 - have procedures to ensure correct record keeping and reporting.
- The reports to beneficiaries will need to be diligently prepared and regularly issued. It will be important to ensure that this task, which will require administrative effort, is not overlooked or forgotten.

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(Continued)

Want to know more?

If you have any questions about retention funds or other forms of performance security for projects, please contact our specialists [here](#).

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