

Practice Update

New 5% Retention Cap for California Private Projects: Key Impacts for Contracting Parties

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Effective January 1, 2026, California will implement significant changes to private construction payment practices. Joining nine other states, Senate Bill 61, signed by Governor Gavin Newsom on July 14, 2025, amends California's Prompt Payment Statute to establish a mandatory 5% cap on retention for private construction contracts. Until now, California law set no statutory cap on private project retention — though parties have typically withheld 10%. The new rule aligns private projects with the 5% retention limit long applied to public works.

Under the amended statute (*Civil Code* § 8811), owners, direct contractors, and subcontractors may not withhold more than 5% of any progress payments as retention. Additionally, the total retention withheld over the life of the contract cannot exceed 5% of the contract price. The 5% cap flows down the payment chain. Moreover, in contracts between a direct contractor and a subcontractor (and further down the chain), the retention percentage cannot exceed the percentage specified in the owner-direct contractor agreement. The 5% cap is non-negotiable — any contract provision providing for higher retention will be unenforceable.

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The statute also includes a mandatory attorneys' fees provision for prevailing parties who successfully enforce compliance, heightening the potential legal and financial risks associated with nonconforming contract terms. (*Civil Code* § 8811(c)).

There are two exceptions to the 5% cap:

1. The cap does not apply if, before or at the time of bidding, a direct contractor or subcontractor notifies a subcontractor that a performance and payment bond is required, and the subcontractor fails to provide such a bond (*Civil Code* § 8811(b)(2)). Note, this exception is not written to apply between the owner and direct contractor.
2. The cap does not apply to residential projects that are not mixed-use and do not exceed four stories (*Civil Code* § 8811(b)(3)). Note, neither "residential" nor "mixed-use" are defined by the statute.

This statutory change will affect how payment security and project risk are managed throughout the construction chain. With less retention available, owners and developers may look to adjust project controls through enhanced performance monitoring, tightened milestone-based payment schedules, and a reassessment of prequalification and bonding requirements.

The key takeaway is that this new law does not eliminate financial risk — it redistributes it. With the new year approaching, owners, developers, and all parties subcontracting work should review their contract templates, master agreements, and project administration procedures to ensure compliance before the January 2026 effective date. Akerman's construction team is available to help you navigate this transition by evaluating your current practices and updating contract language to align with the amended Prompt Payment Statute.

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