



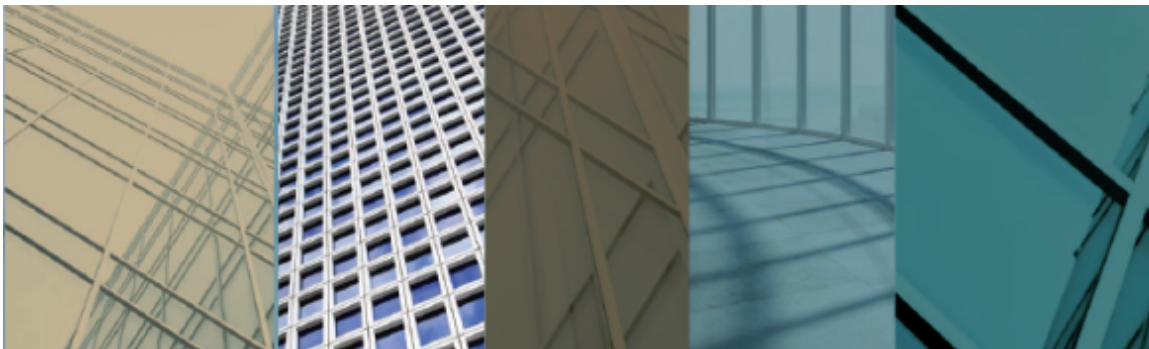
For General Information Only
Owners of Single Family Residences
California Only

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CONSTRUCTION CICERONE

Construction Contract Issues for Owners of Residences

Repair and or Renovation General Considerations



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What “legal world” do board members live with?

Why should an owner consider hiring an attorney for a proposed construction contract?



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Should an Attorney assist review a construction contract?

Typically, before a general contractor starts “ on the road” to completion of a major reconstruction project based on design documents an architect has prepared, several contracts that should lay out the “rules of the road” to project success have already been signed. A number of events that usually arise during a repair process can have significant impact on an owner can occur without an agreement prepared by counsel(see road map slides (end of presentation below)



Renovation Repair Contracts Overview

What is a Contract?

- The function of any contract is to record the terms of the agreement between the parties. A renovation/repair contract should define the scope and price of the product and services to be provided and, among other things, allocate the risk inherent in the construction industry between the owner and the contractor and architect.
- An important function of a written contract is to give a level of predictability to the parties when certain events arise. Written contracts help the parties predict what consequences will flow from particular events. Stated another way, from a drafting perspective, the parties need to ask themselves “what if” a particular event occurs.



Renovation Repair Contracts Overview

What is a Contract?

- Examples of “events” the Owner should consider to be covered in the agreement between owner and contractor?
 - Contractor’s crew member performing elevated deck work or roof replacement work is injured while performing their work, or causes damage to adjoining areas not a part of contractor’s work;
 - Contractor runs into unknown conditions after the repair work starts and then contractor requests a change order;
 - Design or scope has problems the contractor points out to owner;
 - How does owner and or architect respond to these issues?
 - A contract can allocate the risks and/or respective responsibilities between each other when these events occur.

Note this list is not exhaustive, but rather, an illustration of events that can occur.



CLASSIFICATION OF CONTRACTS

Repair/Renovation contracts can be classified according to the method of pricing the work.

General approaches include:

- Lump sum contracts:
- Cost-plus contracts (or costs plus a fee);
- Cost-plus a guaranteed maximum.



CLASSIFICATION OF CONTRACTS

Lump Sum Contracts (Less price risk to Owner)

- In a lump sum or fixed price contract, the contractor agrees to complete the contract as described in the contract documents for a fixed price;
- A fixed price contract may also have a fixed price per unit for each of several items of work that must be done (e.g., for each cubic yard for fill);
 - Although the price per unit (or yard) is fixed, the total cost of the job will depend on the amount of work (or yards-units that must be done);
 - The units can be spelled out in a document attached to the contract or the bid customarily called a “schedule of values” or a “schedule of unit costs.”



CLASSIFICATION OF CONTRACTS

Cost Plus Contract (More price risk to Owner)

- A cost plus contract provides that the contractor is reimbursed (usually on a monthly basis) by the owner for all cost of construction, plus an amount to compensate the contractor for its overhead and another amount to constitute its fee or profit. The fee may be a percentage of the contract price or a fixed amount paid in monthly increments. The advantage of a cost plus contract to the owner is that the owner pays only costs actually incurred in the prosecution of the work. One disadvantage to the owner is that neither the contractor nor subcontractors have a strong motive to economize.



CLASSIFICATION OF CONTRACTS

Cost plus a guaranteed maximum price (Price risk compromise between Owner and Contractor):

- Comment: a contractor may be motivated to economize by a guaranteed maximum contract price so that the owner reimburses the contractor for costs, overhead and fees as in a cost plus contract, but stops paying when the guaranteed maximum contract price is reached.



Significant Contract Issues

Parties

- Make sure you have the correct party you are contracting with who is also the party who is licensed. This is an Owner due diligence issue;
- An unlicensed contractor who performs work on the project may under certain circumstances, be considered an “employee” of the owner, with significant legal consequences.



Significant Contract Issues

Description of the work

- Important to list this in a detailed fashion. Consider a performance criteria if applicable;
- Consider meeting the contractor at the site to discuss the scope of work before entering into the agreement, and to ensure the contractor and owner understand the scope.

Contractors pre-job investigation

- Get the contractor to visit the site to become familiar with conditions that should be included in the bid.



Significant Contract Issues

Time for start and completion

- Identify when the contractor will commence and complete its work; and on site work requirements, such as hours of operation, clean-up, and associated owner issues;
- Who is going to regularly check the contractor's work to insure completion? The contract can spell out a procedure the owner wants included ensuring contractor performance on a monthly basis before payment is required.



Significant Contract Issues

Delay

- Owner will attempt to limit delays for such items as weather and or material problems outside of the control of the contractor and contractor will want extensions of contract time to account for these issues. Point is; contract clause should cover this issue.

Permits

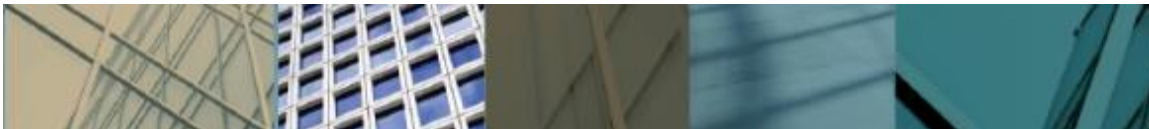
- Contract should identify who pays for and who is required to “pull them” or obtain permits; as well as who “calls” for permit related “building department” inspections.



Significant Contract Issues

Requirements for payment of labor and material

- Must be specially negotiated to correspond with owner schedule;
- Consider use of joint checks to protect owner in case the general contractor the owner hired with does not pay its subcontractors;
- Who is going to check that work is done before an agreement for payment is made? A contract condition could be added here to protect owner
 - Owner or construction manager?



Significant Contract Issues

Contract requirements for payment of labor and material

- Include written provisions that at the time each application for payment is made during the progress of the job, mechanic's lien releases are provided on statutory form for that portion of the work associated with each payment application.
- Someone representing the Owner (i.e., Construction Manager and/or attorney) should be advised to track lien releases from those sub-contractors and suppliers who had provided the required 20-day preliminary notice. This is the only way the owner can make sure at the end of the job that all required lien releases from sub-contractors and material suppliers are provided.



Significant Contract Issues

Extra Work/Changes and Deletions

- Contract clause should not allow contractor to perform extra work without owner's written authorization in advance;
- Allowances—Note: contractors use “allowances” to charge the owner for something the contractor is not willing to offer a fixed price on. Owners should carefully consider these before an agreement to same. On some projects allowances cannot be avoided;
- Deletions/Modifications-should not be agreed upon unless in writing. If attorney is hired, attorney should review.



Significant Contract Issues

Insurance requirements

- Contract clause – requirement in the contract to provide notification to the owner when contractor's insurance lapses or license status changes;
- Owner should consider having its insurance broker review all insurance provisions;
- Find out what type of insurance the contractor is offering- All risk insurance versus specific perils versus claims made.



Significant Contract Issues

Insurance requirements

- Who pays for deductibles?
- Certificate of insurance provided to owner appears now to be a standard provision;
- Owner should be made additional insured on contractor policy – and on subcontractor’s policy-it appears in today’s marketplace that all these are standard requirements;
- Insurance amount;
 - Issue to consider: should it cover potential risks, or just the contract price?



Significant Contract Issues

Contract clauses dealing with correcting defective work

- Provisions should not only provide that the contractor warrants his work, but spells out what steps the contractor will take to deal with problems in his work as they arise.
- Industry “form” contract language does not go far enough on this issue



Significant Contract Issues

Indemnity (Owner risk shifting provisions)

Given typical owner budget limitations, owner should obtain contract requirement that shifts responsibility for claims made arising from the contractors work to the contractor when the claim is submitted to the owner

Arbitration

- Pros and cons of arbitration versus litigation/attorney should explain/contract clause identifies owner choice



Significant Contract Issues

Attorney's fees should be included in every contract.

Lien Issues that should be spelled out in the contract

- Require the contractor to use “best efforts” to prevent “others” from filing of any liens;
- Contract provision allowing Owner to withhold payment in the amount of liens actually recorded;
- Contract provision allowing use of two-party checks when lien issues arise;
- Contract provision requiring lien releases at progress and final payment points before owner's payment obligations arise.



Significant Contract Issues

Termination

- Terminate for convenience
 - Meaning: no reason needed;
 - How is contractor compensation measured – owner should tie this down;
- Terminate for default
 - Reasons: Non-performance – Bankruptcy – Notice
 - owner's rights
 - Related issues: liquidated damages – cost to cure.



Significant Contract Issues

Termination

- The owner should ask its attorney to negotiate with the contractor provisions which would allow the owner to terminate the contract without cause. Many owners would like to have flexibility in being able to “get out of” the contract for whatever reason.



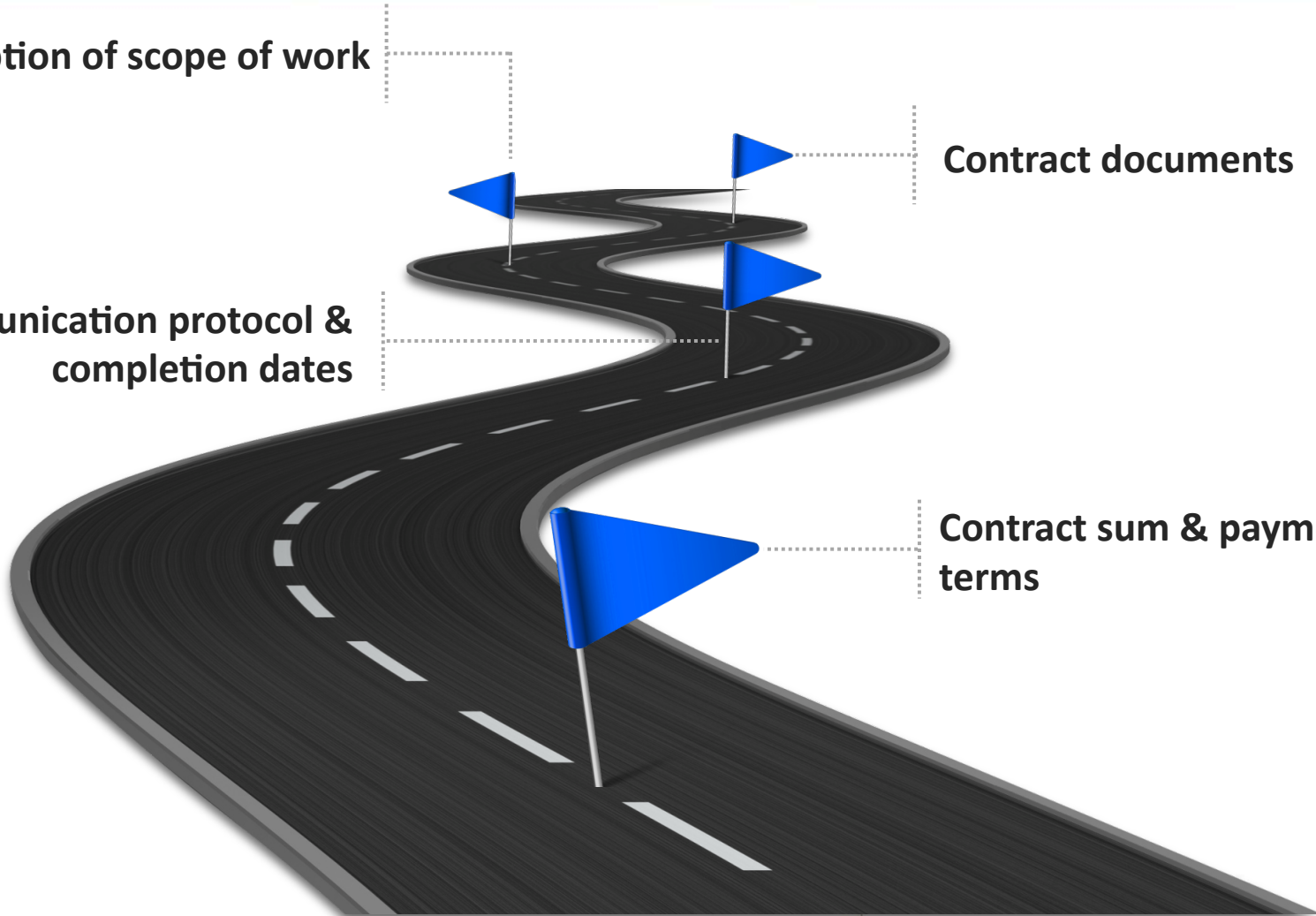
Twists and turns on “road” to renovation repair “success”

Description of scope of work

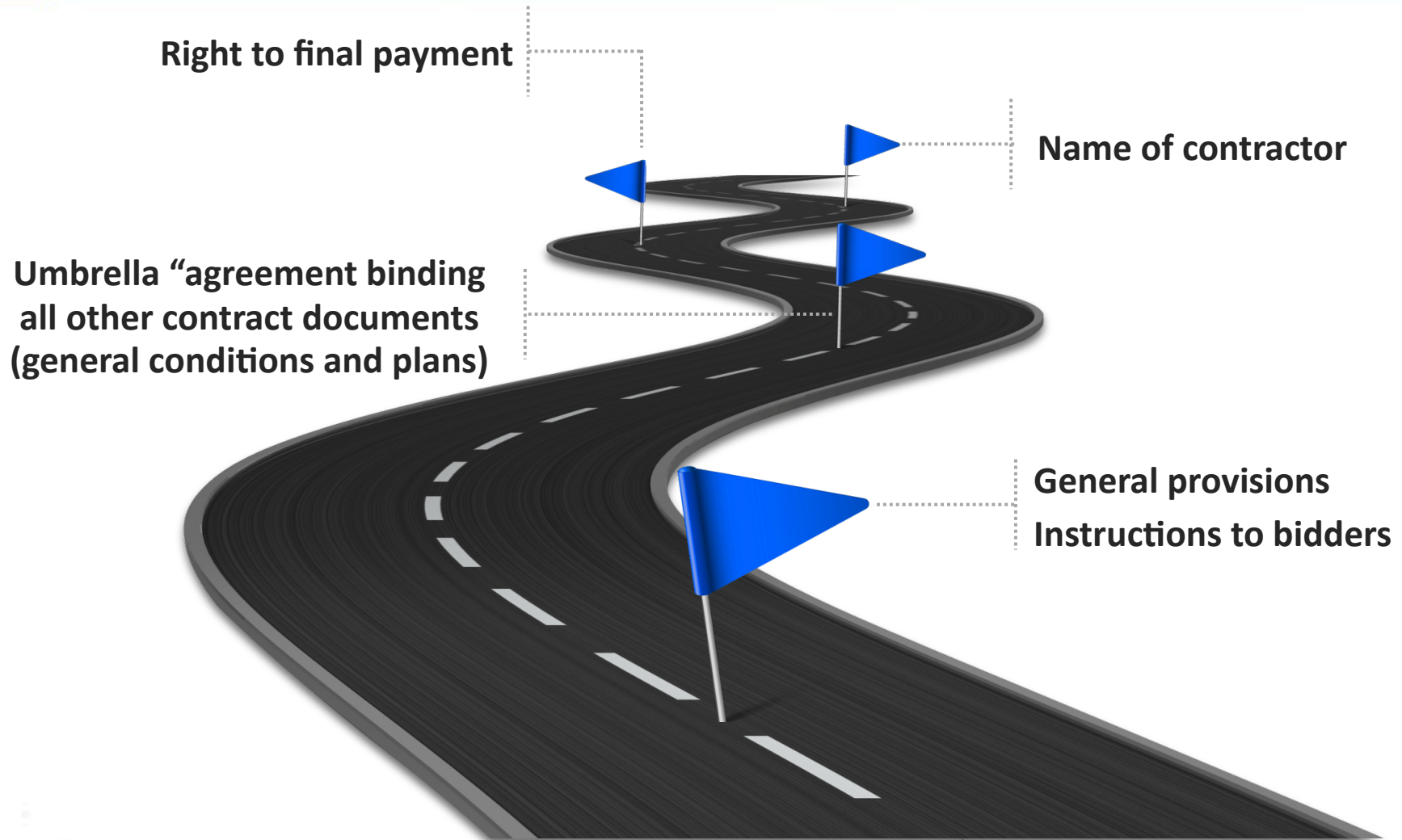
Contract documents

Communication protocol & completion dates

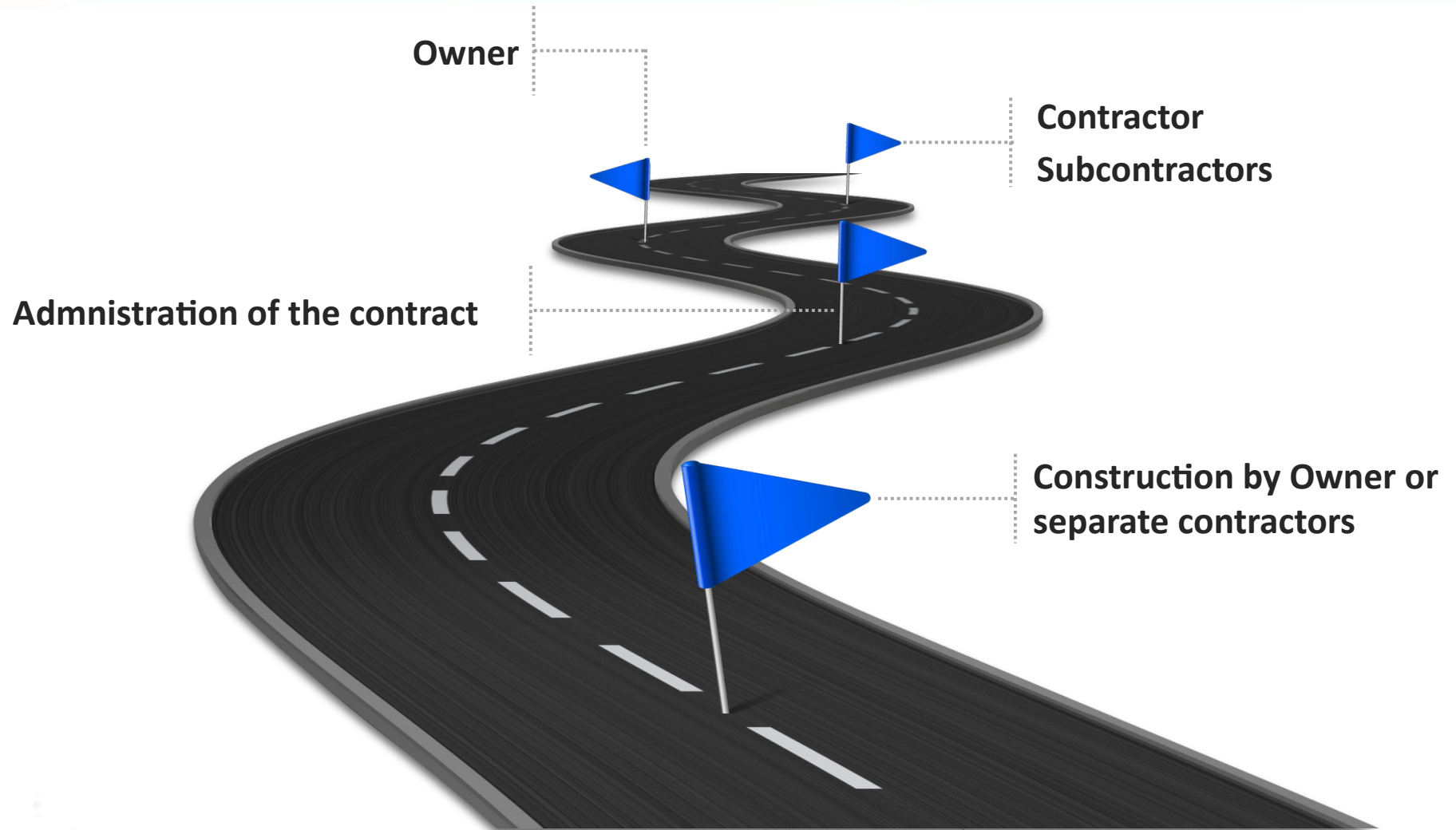
Contract sum & payment terms



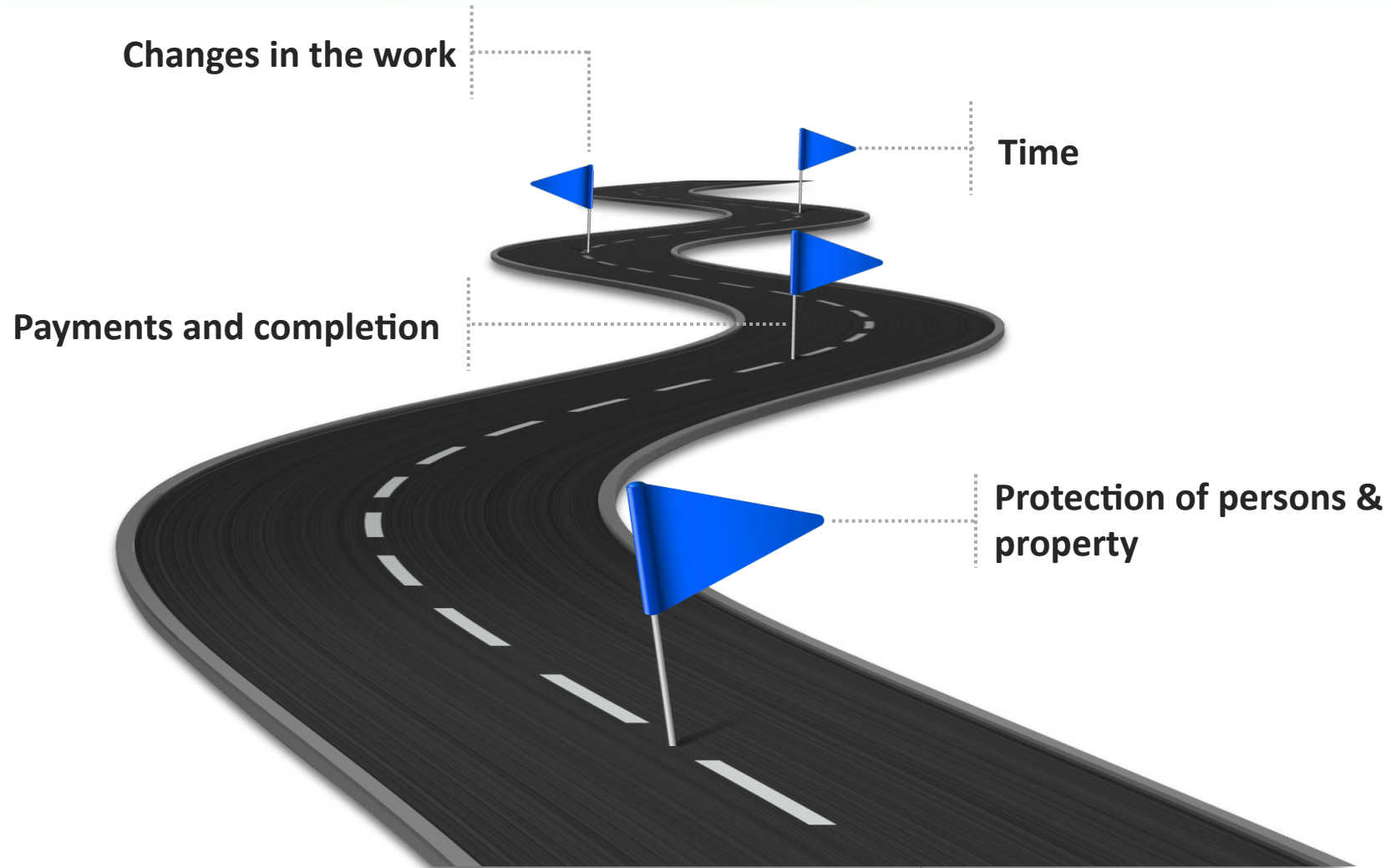
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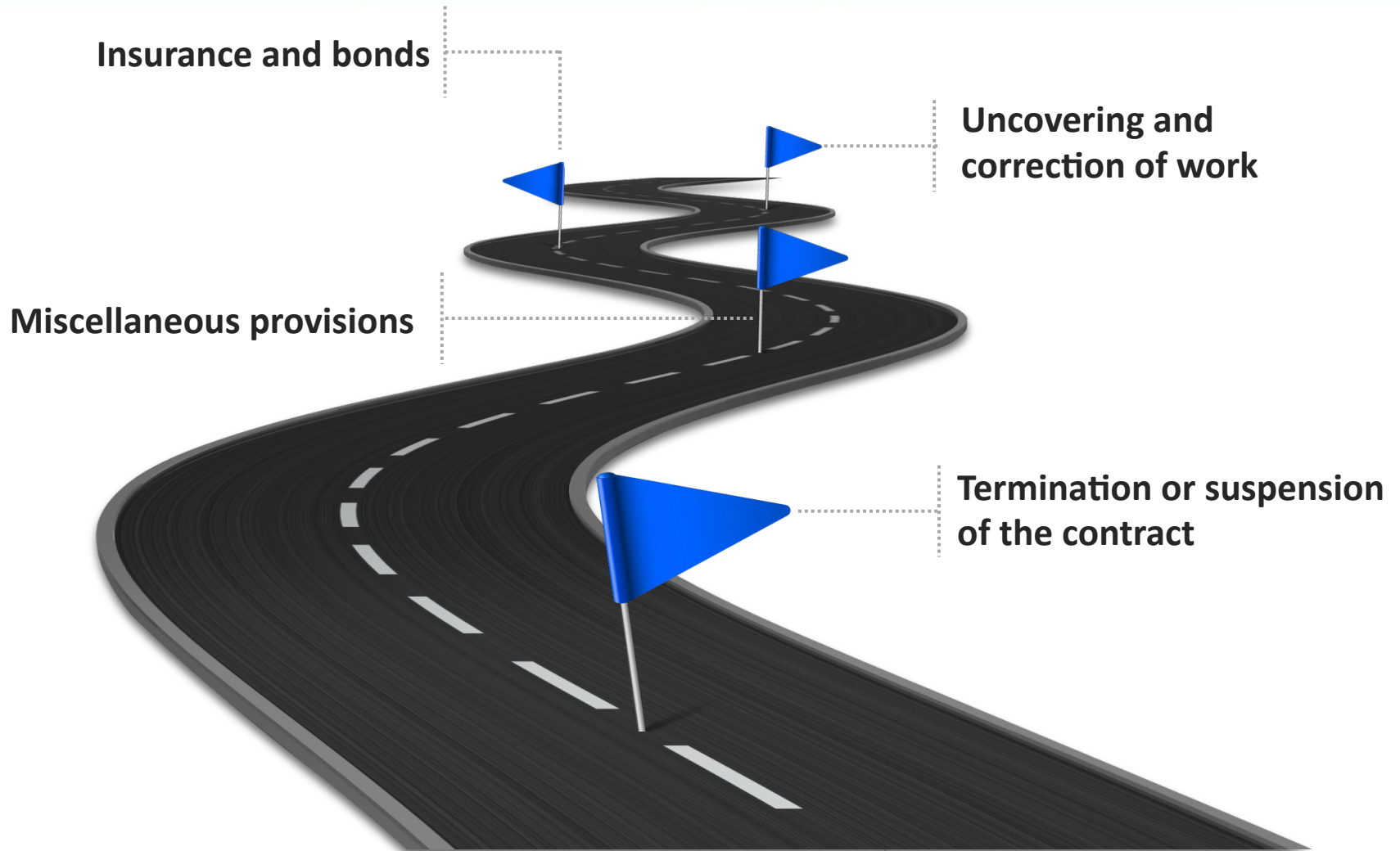
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Twists and turns on “road” to renovation repair “success”



Twists and turns on “road” to renovation repair “success”





For General Reference Only Board Members Common Interest Developments

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