

The following construction contract tips and information are to be used as a basic guide only. Always consult with a lawyer before signing any contract or adding any of the following language.

- **Recommended Contract: AIA A101**

The AIA A101 agreement is a standardized contract that is used by owners and contractors. It is fair and balanced. Any changes that are made are noted or stricken so all parties can see the modifications. Using this agreement will lessen the need for an attorney review or limit the attorney review time. Most general contractors should be very familiar with this contract, and they should have no problem using it. This will allow the owner to be in control of the contract versus the general contractor supplying it. This is not to say the owner cannot use the general contractor's contract. Just remember that the contractor wrote it.

- **Contract Basics**

Everything that is in the plans needs to be included. Make sure the general contractor covers the entire plan for the home, then clearly lists the exclusions and the allowances. There should be nothing left up in the air. Here is an example.

This contract covers all pages of plans for \_\_\_\_\_ Owner  
\_\_\_\_\_ address \_\_\_\_\_ generated by  
\_\_\_\_\_ Architecture Firm, dated \_\_\_\_\_. These plans are final  
and approved by the City of Santa Rosa. There are no further revisions.

The exclusions to the construction drawings are:

(listed in detail)

The allowances/Owner options in the contract are:

(listed in detail)

**Note:** Carefully verify what is being excluded to make sure there are no gaps in what the general contractor is covering. There could be additional items that would need to be budgeted for. Also if getting multiple bids, verify that the exclusions match for all general contractors. The difference in exclusions could account for why one general contractor's bid is lower than another.

**Note:** Allowances or Owner options are variable costs that can add up. Pricing should be largely defined in the bid and contract. It is fine to have a couple of small allowances that make sense. Too many allowances are red flags and could allow a contractor the ability to increase the contract amount well over the base contract. If there are Owner upgrades that were not identified at the time of Contract signing, but options the Owner elected to add to the contract work, a separate Change Order should be prepared outlining the additional work, and the document should be signed by both the Owner and the Builder.

- **Architect Responsibility**

The architect should put all of the specifications for the home on the plans. This includes cabinet quality and style, countertop type, appliance brands/type, lighting and plumbing fixture specifications, flooring type/selections, etc. Specifications will allow contractors to bid it apples to apples for accurate pricing and to make sure that the homeowner is covered so that change orders do not occur because of missing information. Change orders can be a costly addition to a project especially when a contractor comes in with a low bid.

- **Change Orders**

Change orders are an area where contractors can make up a lot of ground on a low bid. It will be tough not to have an occasional change order, but the key is to limit the exposure and put the contractor on notice that change orders will be scrutinized.

Example: “All change orders must be agreed to and signed by both parties before starting work. Any unsigned change order could result in the contractor not getting paid for the work or the work not being performed. The owner reserves the right to get additional bids for change orders and or a third-party review of the cost and scope of that work.”

- **Insurance**

The general contractor and all subcontractors need **to name the homeowner as an additional insured**, and it should be spelled out in the agreement.

**Liability insurance:** Minimum One Million Dollars (single claim), with Two Million Dollars aggregate limits. Be sure to verify if this is a per location limit or total for the entirety of the project. Builders can group individual home rebuilds together as a single “project.” If there IS NOT a per location limit, then losses at other addresses can diminish the limits of coverage and impact you in the case of a claim.

**Workers compensation:** One Million Dollars

**Employee automobile coverage:** One Million Dollars

**Additional insurance:** Builders Risk (this can be provided by the owner or the contractor). Builders risk covers all property during the rebuild. This includes raw materials like stacked dry wall but also the house during construction as it isn't a completed building. Some homeowner's insurance companies will cover the builders risk exposure during the rebuild. Verify who will be providing this insurance with your builder and insurance company.

**Professional Liability:** Verify that all architects and engineers have professional liability or “errors & omissions” insurance. Most general liability policies do not cover professional services.

- **Construction Schedule**

There needs to be a defined construction schedule in the agreement. The homeowner should be able to track where the home will be by certain dates and when they can expect completion. A construction schedule cannot be prepared until building plans have been approved but the City, so make sure you clarify with the Builder when you should expect a construction schedule following Plan approval.

- **Construction Delays**

There needs to be some language that protects the homeowner in the event there is a delay that is inside of the contractor's control where they can terminate the agreement, especially with the projected labor shortages and other factors. An example could be if the project sits for 30 days with no progress or if the job is more than 60 to 90 days behind schedule, the owner has the right to cancel the agreement.

- **Draw Schedule**

There needs to be a clear understanding in the agreement of the how and when the contractors will get paid. If there is a mortgage company holding the insurance funds, there is a timeline that needs to be understood so that the contractor's payment draw schedule can be reconciled with release of insurance proceeds. The last thing anyone wants is a misunderstanding of funding. The contractor and subcontractors could pull off the job if they do not get progress payments in a timely manner.

- **Funding**

Unlike a new construction loan, where the funding is dictated by a construction draw schedule provided by the Contractor, in a fire-rebuild, the money to pay the Contractor comes from the Mortgage company. Customarily, the Mortgage company will issue the insurance proceeds in thirds. The initial one-third of the insurance proceeds is released upon receipt of the above-listed documents and the payment check(s). It is not uncommon to have to wait 3-4 weeks for that first payment to arrive. The second installment payment from the Mortgage company is issued at 50% completion of the construction, and the final one-third draw is issued at substantial completion (95% or better) of the project. The Mortgage company will need to be notified by the Owner as the 50%, and substantial completion phases approach since they will send inspectors to verify the construction progress before they will issue payments. Some mortgage companies may be willing to issue draws in different increments, but that is something to address once you know what your Contractor's requirements are for their payment draws. At any rate, the communication between you and your Contractors is pivotal and it will help the entire process along, and keep cash flowing for the contractors.

### Insurance Deprecation Hold-back

The insurance company is likely to hold back 20-25% of the initial payout. Once the project is completed they will release the depreciated funds that are held back. Check

with your Adjuster to see if they can promptly release those funds and how many days/weeks until they expect you to receive supplemental payments. If there is a mortgage company, the insurance supplemental check(s) will be made out to the homeowner and the mortgage company. This customarily adds 3-4 weeks from the time of your receipt of the insurance payments to the time those funds are processed and issued by the Mortgage companies. Make sure to request overnight delivery of all payments from the Mortgage Company, and that all of the check(s) that you send to them are overnighted as well. This could save weeks between deliveries.

### Documents Needed for Draw Release

The contractor must submit the following for progress payments. These documents are for Mortgage Company disbursements and protection of the homeowner. The Mortgage Company may require less documentation, but the homeowner must get the following to protect themselves:

- \* An invoice for the percentage of work completed in accordance with draw schedule outlined in the contract.
- \* Before paying a conditional lien release on progress payment from their company and all subcontractors and material suppliers.
- \* Proof that the general contractor has verified that the subcontractors have paid their employees in accordance with the new state law that went into effect January 1, 2018.

Once paid, the contractor, subcontractors, and material suppliers must provide an unconditional lien release on progress payment. Future draws will not be issued until all unconditional lien releases for prior payments are given to the owner.

### Final payment:

- \* An invoice for final payment in accordance with the draw schedule outlined in the contract.
- \* The contractor must have all City sign-offs for the owner to occupy the home.
- \* Before paying a conditional lien release on final payment from their company and all subcontractors and material suppliers.
- \* Proof that the general contractor has verified that the subcontractors have paid their employees in accordance with the new state law that went into effect January 1, 2018.
- \* Notice of competition must be filed within 10 days of final payment.

Once paid by the owner the contractor, subcontractors and material suppliers must provide an unconditional lien release on final payment.

- **Dispute resolution**

In the event, there is a dispute between the owner and the contractor it is best to have language that spells out dispute resolution. Always consult with a lawyer for the best language and advise. The example below allows for steps that will not end up in a court but will be decided by binding arbitration which is much quicker and less expensive.

Sample Language: “The parties will attempt to resolve any dispute arising out of or relating to this Contract through friendly negotiations amongst the parties. If negotiation does not resolve the matter, the parties will resolve the dispute using the below Alternative Dispute Resolution (ADR) procedure.”

Any controversies or disputes arising out of or relating to this Contract will be submitted to mediation in accordance with any statutory rules of mediation. If mediation is not successful in resolving the entire dispute or is unavailable, any outstanding issues will be submitted to final and binding arbitration under the rules of the American Arbitration Association. The arbitrator's award will be final, and judgment may be entered upon it by any court having proper jurisdiction.