



## Newsletter

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Contact us Toll-Free: 1-866-474-5529 ext. 251  
(info@lhrlaw.net)

10 Key Points to a Construction Contract:  
Don't Be Caught Without Your Essential Contractor Provisions  
By David A. Loewenthal, Esq. – [daloewenthal@lhrlaw.net](mailto:daloewenthal@lhrlaw.net)

This article will outline those elements, terms and provisions that a Homeowners Association should include in any contract with a general contractor and/or a subcontractor. By the time, an association is ready to execute a written contract, you should already have taken the necessary steps to ensure that your contractor is licensed, bonded, competent to perform the work in which you are engaging him and reasonably priced. Once the pre-contract background checks have been completed; it is imperative that the contract contain certain critical terms and conditions so that all parties understand their rights, duties and obligations pursuant to the contract.

Always remember that if you fail to specifically set forth a term in your contract and a dispute arises in the future; such ambiguity could favor the contractor. Any and all agreements or understandings reached between the Homeowners Associations/Owner and the contractor should be placed in writing. Memories have a tendency to fade and be blurred over time; therefore, never rely upon oral promises by the contractor to perform certain work that is not specifically written into the contract.

Often, parties will use forms from the American Institute of Architects (AIA). These are well established forms which have various options depending on the type, scope, etc. of the job. Generally you need the form agreement, a general conditions package plus some modifications to make it applicable to your Association.

The following terms, conditions and provisions generally should be included within the contract:

#### 1. Type of Contract:

There are several types of contracts and depending on what you choose will affect risks and costs. A "Fixed Cost Contract", is where all work is to be performed for a specified amount of money. A "Time and Material" contract is one where the contractor charges a certain rate for all labor, time, material and surcharges. Between these two - a fixed cost contract may be more beneficial to an owner due to the fact that the contract amount is specifically known as opposed to a time

and material contract being based upon the speed and efficiency of the contractor. Other types of contracts include "Cost Plus", i.e., the actual cost of work plus a fixed percentage. A "Guaranteed Maximum" contract sets a ceiling for the cost of the work with provisions for the contractor to obtain competitive bidding for subcontractors. This may also include a cost savings provision.

#### 2. Scope of Work/Contractor Compliance with Building Standards:

The contract should specifically set forth the job description of what the contractor has agreed to perform. In addition, the contract should identify the specific materials or named brands of materials to be used if applicable. As an example, a contract with a plumber should include the location (e.g. bathroom) that is to be plumbed, as well as specific brand identification for fixtures. Further, the contract should specifically state those items that are **not** included within the contract.

For example: a concrete contractor who has not contracted to place a waterproofing membrane between a topping slab and a structural slab should specifically state that the contract excludes a waterproofing membrane. Also, contracts should state that the contractor will comply with all plans, specifications and building codes, as well as obtain all necessary permits. By specifically setting forth within the contract the scope of contractor work **and** exclusions; discrepancies in the future as to the duties and obligations of the contractor should be greatly minimized.

#### 3. Time is of the Essence:

Generally, Homeowners Associations/Owners have a specific time frame during which they expect the work to be commenced and completed. This is especially true when the work that is to be performed is structural in nature, as opposed to merely cosmetic.

For example: a contract to have a new roof installed on a building will generally require completion prior to the commencement of the rainy season. Thus, a specific completion date is necessary. Also, by including a "time is of the essence" clause, the contractor is advised at the outset of the contract that he will be obligated to provide an ample crew to perform work on time.

#### 4. Liquidated Damages:

The purpose of a liquidated damages clause is to place a penalty upon the contractor for failure to complete his work on time. This provision ties directly into the time is of the essence

clause and basically states that if the work of the contractor is not completed by a specified date or within a certain number of days from the date of commencement the contractor will be either obligated to repay monies to the Owner or forfeit a certain amount of money for each day beyond the original completion date of the contract. Often a contractor will agree to liquidated damage provisions if the owner agrees to an incentive provision for early completion.

#### 5. Insurance and Performance Bond:

The contract should include provisions for both insurance and a performance bond. The contractor should be properly insured, including Workers Compensation Insurance and General Liability Insurance. It is essential that the contractor's insurance specifically insures the contractor to work on multi-family dwellings/common interest developments. It is generally advisable to have the contractor have the Homeowners Association/Owner named as an additional insured. By being named as an additional insured, the Homeowners Association/Owner would have direct contractual rights with respect to the insurance policy in case of damage or injury. In addition, for approximately two (2%) percent of the contract price, the contractor can also obtain a performance bond which will cover the Homeowners Association/Owner if the contractor does not perform his work completely. Thus, the performance bond is in essence an insurance policy that allows an owner to have the work completed by another contractor if the original contractor fails to perform.

#### 6. Indemnity:

Due to the litigious nature of the society in which we live, it is important to have an indemnity provision within the contract. An indemnity provision generally states that the contractor will hold the Homeowner Association/Owner harmless and agree to defend and indemnify the Association/Owner as a result of any acts and/or omissions on the part of the contractor that give rise to damage or injury to the project or individuals. This provision is extremely important in when a Board of Directors retains a general contractor to perform significant renovation to a project which has the potential to damage individual units that could lead individual homeowners to sue the board or the Homeowners Association for related damage. By having a properly drafted indemnity provision, the Board of Directors could then tender their defense to the general contractor, obligating him/her to defend and indemnify the Board against the claim.

#### 7. Payment Schedule:

The contract should set forth when payments are to be made. A contractor cannot require more than ten (10%) percent of the contract amount up front or one thousand (\$1000.00) dollars whichever is less. In addition, the payment schedule should be phased in and should never be ahead of the actual work performed. Don't pay for work that has not yet been performed. Further, the Homeowner Association should always attempt to retain a minimum ten (10%) percent

retention until the job is totally completed and accepted by the Association/Owner. To the extent that the Association/Owner can increase the retention it should. The greater the amount of the retention, the better the leverage to have the work performed properly. Always obtain lien releases, both partial and final, as payments are made.

#### 8. Warranties and Statute of Limitations:

Any warranty provided by the contractor should be specifically set forth and identified. You should also determine whether or not the statute of limitations as to a claim based upon breach of warranty is being limited by the contractual terms to less than three (3) years.

#### 9. Termination Clause:

Construction contracts will often include a termination provision. This should be viewed in several parts: (1) who is the terminating party (owner or contractor) and (2) is it for cause or without cause. Generally an association/owner should attempt to limit any termination fees to simply the value of the work performed at the date of termination. Again, the methodology of termination and the fees are negotiable.

#### 10. Attorney's Fees/Alternative Dispute Resolution:

Often, parties to a contract will wish to have a provision stating that disputes or claims arising from the contract or the work will be submitted to Alternative Dispute Resolution (A.D.R.) or Arbitration. A.D.R. can include, but it is certainly not limited to the American Arbitration Association (AAA) Judicial Arbitration and Mediation Services (JAMS), etc. Generally, the inclusion of an A.D.R. provision will be premised upon the fact that both parties have agreed to waive their rights to the filing of a judicial lawsuit. Binding arbitration is not appealable, except for very limited reasons. Also, the arbitrators have wide latitude in making their decisions. Further, arbitrators charge for their services.

The contract should also contain an attorney's fees provision which states that if a dispute arises as a result of the work that is to be performed under this contract, that the prevailing party in any such dispute is entitled to the recovery of reasonable attorney's fees. This provision provides a heavy hammer that can be used to try to force the non-complying party, whether it be the contractor or the owner, to comply with the contract.

Based on these general guidelines, conditions and provisions, a contract will be clearer and more comprehensive with all parties understanding their rights, duties and obligations.

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