

**Are you about to remodel or build a home?
Ten things every homeowner should do when hiring a contractor.**

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Having a construction project at your home can be a trying experience, even without major problems. But when disputes arise it can be an absolute nightmare. Fortunately, many of the common issues faced during construction projects can be mitigated by adhering to the best-practices and contracts terms discussed below.

- 1) **License and insurance** – *Homeowners should always confirm their contractor is licensed, bonded, and insured.*

These three items provide a baseline level of protection to your project. Construction licenses are issued by the California Contractors' State License Board ("CSLB"). A contractor's license provides a vital level of assurance that your contractor is experienced in construction and knowledgeable of construction codes and principles. It also insures he will be accountable, as he will be under jurisdiction of the CSLB disciplinary powers. You can check a contractor's license status at the CSLB website.

All licensed contractors are required to maintain a bond in favor of project owners, in the sum of \$12,500. The bond status and surety name can also be reviewed at the CSLB website. The \$12,500 can be sought in the event your contractor abandons the project, performs defect work, etc.

Finally, insurance is also a key protective element to any project. Your contractor should have both worker's compensation insurance and general liability insurance. The former is required by the CSLB for all contractors who use employees. To confirm policies are in place, you can request that your contractor provide you certificates of insurance relative to their policies.

- 2) **Written contract** – *Homeowners should always enter into a written contract with their contractor.*

It is always a good idea to have a written contract with your contractor. A written contract provides an opportunity for homeowners to state clearly what they are agreeing to and what they expect from their contractor. A written contract is much easier than an oral agreement to enforce in litigation. At a minimum, the contract should state the scope of the work to be performed and the agreed price. But, a good construction contract will address all of the issues pointed out in this article (and others), and incorporate other documents pertinent to the project such as construction plans and the contractor's proposal for the work.

3) **Lien releases** – *Homeowners should always get mechanic’s lien releases from their contractor, his subcontractors, and their suppliers.*

California law provides that unpaid contractors are entitled to record a mechanic’s lien against the property where they have performed work. This includes general contractors, and their subcontractors, and material suppliers. A mechanic’s lien can be foreclosed in court, resulting in the sale of the property to satisfy the debt. They are a very unwelcome prospect to homeowners.

To protect yourself from a mechanic’s lien, condition payment to your contractor on receiving mechanic’s lien releases from him, his subcontractors, and their suppliers. The release acknowledges payment and waives a lien claim for the amount paid.

To be enforceable, lien releases must be in the form prescribed in California Civil Code §3262. That section provides lien releases for both progress payments and the final payment made to your contractor. The conditional releases should be secured prior to payment, and the unconditional releases following payment. These releases will insure you do not face a mechanic’s lien after you have in-fact paid your contractor, particularly from his subcontractors and suppliers.

4) **Written change orders** – *Homeowners should demand their contractors provide them written change proposals, with a price, prior to performing any extra work.*

A change order is an agreement between the homeowner and contractor to modify the scope of work, with a corresponding change in the contract price. Change orders typically occur when it is discovered during the project that additional work needs to be performed, either because the building authority directives or site conditions necessitate it, or the homeowner makes a decision to modify the project.

Disputes concerning change orders often arise because the contractor did not secure an explicit agreement from the homeowner authorizing the additional work, and/or failed to make clear what additional amount would be billed as compensation for the additional work. Often times what the contractor asserts is “additional work” the homeowner believes was part of the original contract scope of work.

The likelihood of these types of disputes can be greatly reduced by requiring your contractor to provide written change orders prior to commencing any additional work. The parties should further agree that to be effective the change order must be signed by both parties.

- 5) **Progress payments** – *Homeowners should always pay contractors in periodic installments in a proportional amount equal to the completion of work.*

The most effective point of leverage a homeowner has to ensure a project is completed and performed as expected, is control of the purse strings. To maintain this leverage, a contractor should never be paid for any portion of work before he has performed the said work. Typically, contractors are paid via “progress payments”, i.e. periodic installments in a proportional amount equal to the completion of work. For example, if a contractor has performed 15% of the project during the last month, he should be paid 15% of the contract price, and no more. This creates a *quid pro quo* exchange in performance, and ensures the contractor keeps the project moving forward toward completion. It is prudent to agree on progress payment schedule at the outset, and insert it into the contract.

- 6) **Retention** - *Homeowners should always include in their agreement that retention shall be withheld from payments*

Another commonly used mechanism to ensure your contractor completes the project is the withholding of a *retention* amount from payments. Retention – which is typically 10 or 15% of a payment – is deducted from each payment and temporarily held by the homeowner. For example, if the contractor is otherwise owed \$15,000, and a 10% retention was in place, he would be paid only \$13,500, and the remaining \$1,500 would be held back. Accumulated retention is then released to the contractor *upon completion of the project*. The withholding of retention motivates the contractor to complete work. Also, retention funds can be utilized by the homeowner to fix and/or complete work in the event the contractor fails to perform.

- 7) **Indemnity and “additional insured” status** – *Homeowners should always get an indemnity agreement from their contractor, and become an “additional insured” on the contractor’s liability policy.*

Construction projects are dangerous, and damage to person or property are always a possibility. Homeowners should to protect themselves against liability for such damage by securing an indemnity agreement from the contractor, and become an “additional insured” on their liability insurance policy.

Indemnity is the act of making another party whole from liability which was caused by the indemnitor. A party can obligate itself in a contract to perform indemnity, and therein can define the limits and terms of indemnity. An indemnity obligation is usually coupled with an agreement to *defend* the indemnitor from claims (i.e. pay for an attorney to represent them relative to the claim).

An indemnity obligation can be further strengthened by becoming an “additional insured” on the contractor’s liability policy. Most liability policies for

construction allow the contractor to add their homeowner clients as an insured party to the policy, which affords the homeowner coverage under the policy to the same extent as it would be provided to the contractor. Typically to perfect this process the homeowner and contractor must have a *written* contract which specifically mandates that the homeowner become an additional insured, and a *certificate of insurance* should be issued identifying the homeowner as an additional insured. The homeowner should get a copy of the certificate.

8) Completion schedule – *Homeowners should always get their contractor to agree on a completion date, and – if possible – “liquidated damages” for delays.*

A construction project at your home will almost certainly be significant disruption. It will likely necessitate ceding all or a part of the property to the contractor for the duration of the work. Unfortunately, unless controls are in place projects tend to drag on longer than anticipated, causing a major headache.

To minimize this possibility get your contractor to agree on a completion date. This date should be clearly set forth in the contract. It can either be a calendar date (e.g. January 1, 2012) or a project duration (e.g. 90 days). If the duration period is the parameter used, it is also helpful to define both commencement (e.g. issuance of building permits) and completion (e.g. final inspection by the building department).

The agreed completion schedule should be accompanied by an agreement from the contractor to pay “liquidated damages” in the event the schedule is not met. Liquidated damages are a monetary penalty assessed during the duration of the project beyond the completion date. For example, the parties could agree the contractor will pay \$500 per day the project is late. This will motivate the contractor to finish work, and ensure an adequate remedy if he does not.

9) Down payments – *Homeowners should not pay a down payment more than the lesser of \$1,500.00 and 10% of the contract price.*

On home improvement projects contractors are barred from charging a down payment of more than the lesser of \$1,500 and 10% of the contract price. Although, contractors are entitled to secure up-front payment in additional amounts for necessary deposits and down payments on materials and supplies. For example, if the project will include the installation of custom cabinets, your contractor’s cabinet maker may require a deposit. Your contractor may ask for that sum in addition to the down payment. If such event, always seek written confirmation the deposit is actually placed with the supplier. Otherwise the down payment should be limited to the lesser of \$1,500 and 10% of the contract price.

10) Get copies of the subcontracts – *Homeowners should get copies of the subcontracts and purchase orders that the contractor enters into with others who will work on and supply the project.*

Particularly on larger projects, a significant portion of the money you pay your contractor will be used to pay subcontractors and suppliers, who will perform much of the work. It is prudent to know what work these parties will perform, how much your contractor has agreed to pay them, and under what terms. Therefore, homeowners should get copies of the subcontract and purchase orders that your contractor enters into with the third-parties who will work on and supply the project. Your contract should specifically obligate your contractor to provide these documents.

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