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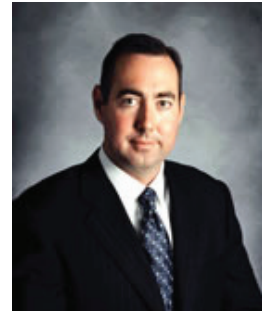
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## BUILDING A NEW HOME?

By: David A. Holmes  
August 2007



Building a new home can be the most complicated and expensive transaction of an individual's life – one that is often entered into with little preparation or experience. Here are a number of considerations to keep in mind.

Plans and Specifications. A successful project starts with a good set of plans and specifications. These are the instructions the builder will follow in constructing the home. A comprehensive and thorough set of plans and specifications leaves guesswork out of the equation and minimizes the possibility of misunderstandings about the scope of the project. Also, the plans are used to price the project. It is therefore critical to make sure that every feature and component expected in construction is set forth in these documents. You should assume that anything not included will not be provided and will cost extra if requested later.

The Contract. The construction contract sets forth the rights and responsibilities of the owner and the builder and should always be reviewed by an attorney before signing. When properly drafted, the contract must cover a number of critical elements. A few are discussed below.

Price. The most basic element of the contract is the price term which is typically addressed in one of two ways. Each approach carries its own advantages and disadvantages.

Fixed Price. Most residential contracts are for a set price that includes the builder's cost of construction plus an undisclosed margin for overhead and profit. Under a fixed price contract the risk of inflation is borne by the builder. Thus, the margin the builder includes in the fixed price typically includes an allowance for unexpected increases in the cost of labor or materials and for unforeseen contingencies. If neither occurs, the builder realizes additional profit. If such conditions do arise, the owner is protected from incurring additional cost.

Cost Plus. Under this arrangement, the owner agrees to pay the actual cost of construction plus a set fee which can either be a fixed amount or a percentage of the cost of construction. An owner can usually negotiate a fee that is significantly lower than the builder's margin under a fixed price contract where the builder bears the risk of inflation. This advantage comes at the price of the owner bearing the risk of inflation. It also removes the builder's incentive to negotiate the best possible prices with subcontractors and material suppliers. The key to success in a cost plus project is to have a well-defined scope of work backed by comprehensive plans and specifications and a budget where the costs of the major divisions of construction are known going in. When these critical elements are missing, costs can quickly exceed what was expected.

Price Increase Provisions. The construction industry in Florida experienced tremendous inflation in the wake of the hurricanes of 2004. Many builders working under fixed price contracts sought to protect themselves by developing contract provisions that allow the builder to pass on significant price increases to the owner. Many owners, believing they were working under a fixed price contract, were surprised when they received bills for price increase items. Obviously, an unexpected price increase can drastically affect the budget of a construction project. Make certain you know whether your contract includes provisions and how they can impact you.



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Warranty. Every construction contract should include a warranty with respect to materials and workmanship. Many builders attempt to impose a time limitation on warranty claims. There are a number of technical issues regarding how such limitations work. Nevertheless, make sure you understand any time limitations in the contract warranty, and make certain you notify the builder of known warranty issues within that time. If a dispute arises, be sure to consult with an attorney.

Time for Completion. To an owner, delay can be one of the most frustrating parts of the construction process. The form contract used by most residential builders will have no guarantee of completion within a stated time. In the absence of such a provision, remedies for delay can be difficult. Consider negotiating a guaranteed completion date with an agreed amount to be deducted from the contract price for each day of delay thereafter.

Progress Payments and Liens. Florida law imposes a number of significant responsibilities on owners to see that payments to the builder, subcontractor, and suppliers are properly administered during the construction process. Such matters are beyond the scope of this article. See Farr Newsletter: "The ABC's of Florida's Construction Lien Law" by Will W. Sunter, August 2006.

Changes in the Work. Inevitably, as construction progresses, there will be items that the owner wants to add to or delete from the project. Most contracts simply state the change in the contract price (increase or decrease) must be agreed to at the time the change is requested. Negotiating the price of a major change in mid-construction can be difficult. For this reason, even in a fixed price contract, consider adding a provision stating that all changes in the work will be priced on a cost plus basis.

Communication is Key. By necessity, building a house creates a long term relationship between the owner and contractor. As in any relationship, good communication is essential. Too often frustration leads to animosity and a breakdown in communication which inevitably results in major problems between owner and builder. Choose a builder you can get along with. Even when difficult problems arise, do your best to maintain good lines of communication. Following this and the other suggestions herein, can contribute to a successful project.

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