

Are Your Contracts Bulletproof?

by Gary Moselle

Effective July 1, 2009, the state of Pennsylvania will require a written contract for nearly every construction task in or around a residence — even minor repair work like repainting or reroofing. If the value of work exceeds \$500 and the contractor expects to get paid, he or she will need a written contract.

Under Pennsylvania's Home Improvement Consumer Protection Act (HICPA), the written agreement has to include all the usual facts, plus a few you might not expect to see in a small job contract: the attorney general's phone number, the contractor's street address (a P.O. box won't do), specific start and completion dates, a description of the materials to be used and a set of specifications, the contractor's property damage and liability insurance limits (\$50,000 minimum), and a list of all subcontractors, including phone number and street address.

Under HICPA, if disputes are to be settled by arbitration, the arbitration clause has to be in 12-point bold caps and must specify whether documents will be confidential and whether the arbitrator's decision is final. If the contract price exceeds \$1,000, the down payment can't exceed a third of the total price plus the cost of any special order materials — which have to be listed in the contract. Time-and-material contracts (cost-plus agreements) are unlawful under HICPA because the contract has to show a contract price, not an hourly rate.

HICPA also makes the entire contract unenforceable by the contractor if any of 10 formerly common clauses appear in the document. The poisonous 10 include hold-harmless clauses and any terms that would award attorney fees to the contractor.

A National Trend

If you live elsewhere and think that what's happening in Pennsylvania doesn't affect you, consider that several states, including New Jersey, New York, Florida, and Texas, now give the homeowner the right to sue for triple damages plus attorney fees — and even expose the remodeler to criminal penalty — if the contractor omits

certain state-mandated disclosures. That's heavy stuff for a simple clerical error, but it's the law. It also means that a contractor using an obsolete form can't collect under the agreement and may have no lien rights.

It's part of a recent trend in which state legislators, trying to protect homeowners from unscrupulous contractors and dissatisfied with the courts' interpretation of the federal Consumer Protection Act in construction cases, have begun to pass laws that micro-manage home-improvement contracts. The good news is that there are loopholes in these laws — ways to turn the bias back in your favor and limit your risk.

For starters, understand that HICPA and other state laws give you a leg up in the negotiating process: If your client suggests using an AIA form or some other boilerplate contract, explain that the document offered is unlawful and that using an unlawful contract would be considered an unfair or deceptive practice. Instead, offer your own contract; this will allow you to take control of the job at the outset.

Even under HICPA — one of the more severe state laws — it's easy to write agreements that protect your interests. The following suggestions comply with Pennsylvania law and the law in most of the other 49 states. (For a summary of what your state prohibits and requires in construction contracts, go to construction-contract.net.)

Let Your Estimate Define the Scope of Work

When you bid the plans and specs, you're agreeing to complete work as defined in those plans and specs — even if your estimate omits something that turns out to be essential to the job.

Here's a safer protocol: The contract price should cover only what's in your estimate. Anything omitted from your estimate isn't part of the job. For example, don't agree to install "a new shingle roof and replace deteriorated flashing" simply because the plans you're bidding say so. That turns your contracting business into an insurance company, and you'll end up paying for

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surprises. Instead, let your estimate show “2,000 SF of shingles and 100 LF of flashing.” If more material is needed, indicate that there will be an extra charge. That’s completely fair and perfectly legal under HICPA and other state laws.

How can you make sure the estimate defines the work? Easy — simply identify the estimate as part of the contract and add a few words: “The estimate defines the work required, no matter what appears in the plans and specs.”

Write a New Contract for All Changes

Changes are inevitable in construction. Most boilerplate construction contracts require that changes be done on a time-and-material basis, usually with little or no markup. That won’t work if a state law like HICPA makes cost-plus home-improvement contracts an unfair or deceptive act or practice. Instead, changes require mutual agreement and a signed change order.

Your contract should spell out that, if necessary, contract negotiation starts again any time an owner or the inspector wants a change in the scope of work, and that both required and discretionary changes will be done on your schedule and at your price.

It’s actually a “prohibited act” under HICPA to agree to any material change without a written contract modification. So when you get a request for changes, fire up your contract-writing software and create a new contract covering just the change the owner wants — at the price you need to charge.

Control the Payment Schedule

Although HICPA limits the down payment to a third of the contract price on

jobs of \$1,000 or more, it says nothing about progress payments. You’re free to draw up a front-loaded progress-payment schedule that keeps receipts well ahead of expenses.

Allow for Attorney Fees To Be Collected

HICPA makes any contract totally unenforceable against the owner if “the contractor shall be awarded attorney fees and costs.” Yet the law doesn’t void a contract clause that awards attorney fees to “the prevailing party.” That seems to be okay under HICPA, even if the contractor is the prevailing party. This is an important distinction.

The possibility of an award of attorney fees is a heavy incentive to settle most disputes. With no risk of being charged attorney fees, and with a chance of collecting attorney fees under the Unfair Trade Practice Act, a devious owner could threaten to litigate even the smallest issues. I believe that eventually Pennsylvania courts will come down on the side of contractors, for a very practical reason: Courts are too congested already. The threat of an award of attorney fees keeps most disputes out of court.

Make the Owner Liable for Unknown Conditions

Until you open up a wall, there’s no way to be sure what’s in the cavity. And as you know, nearly all surprises on a remodel increase costs. So it’s prudent to include a “differing site conditions” clause in every contract. Nothing in HICPA requires that contractors absorb the loss when something doesn’t go as planned.

Nearly all contracts for large construction projects include a differing site conditions clause. The U.S. version is Federal Acquisition Regulation Section 52.236-2.

If it turns out that something isn’t what the owner represented or what the contractor could reasonably expect, a differing site conditions clause provides extra pay for extra work. Both the owner and contractor benefit: The owner gets a bid based on what can be reasonably expected, not the worst case; and the contractor is protected if costs escalate due to surprises.

Make the Owner Share Liability for Delay

HICPA classifies failure to complete work on time as “home improvement fraud” if the contractor doesn’t comply with a demand for a refund. On contracts for \$2,000 or less, failure to complete work on time is a first-degree misdemeanor (five years in jail). Contracts over \$2,000 earn a third-degree felony charge (seven years).

I don’t believe the legislature’s plan is to populate Rockview State Prison with tardy home-improvement contractors, but regardless, it’s easy to avoid these penalties. HICPA doesn’t define excusable delay, so simply define the term very broadly. Then incorporate a “worst case” construction schedule in your contract. That takes the pressure off.

Be aware that there’s a bigger issue lurking here. HICPA comes down hard on contractors who have trouble staying on schedule. That’s fine. But what about homeowners who delay the job or who don’t make payments on time? Turnabout is fair play, in my opinion. Nothing in HICPA restricts charging the owner for delay. Pennsylvania courts routinely enforce contract clauses that make the owner liable for delay of the work. Your contracts should support delay claims.

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