

Understanding the Contract

INFORMATION SHEET



So, you have your design, you've found your builder, Council have given you the permits... you're almost ready to go but not quite. The final step is the signing of the contract.

Now, first of all, we are not lawyers so please do not treat this information sheet as specific advice. It is general information which we hope will make you understand the contract a little better. If in doubt, please speak to a lawyer.

Most builders are members of either the Housing Industry Association or Master Builders Association. Both organisations have various proforma, plain English contracts for different types of projects. The Royal Australian Institute of Architects also has its own set of contracts. Please speak to your architect about those contracts. Generally, the builder will decide on the contract to be used. However, on occasion the architect may request a certain type of contract – particularly if they will be acting as supervising architects.

As we are members of the HIA, we will concentrate on the contract generally used when HIA members build a house or extension – HIA's Plain Language Domestic Building Contract.

Read Everything Beforehand

The first thing we suggest is that you ask your builder for a copy of the contract and all other documents which form part of the contract (such as the Council approved plans and specs, soil test, schedules for provisional and prime cost sums, special condition schedules and so on) before meeting to sign. Take the time to read these in detail. Keep a note of any questions you may have for your builder or lawyer.

Signing

All parties will need to sign, and be witnessed signing, copies of the contracts and addendums. You will need to initial all changes.

Time for Completion

The contract will detail the number of working days the builder has to complete the works after commencement. You need to agree with the builder how long is reasonable. There are damages if the builder fails to complete on time, or if the client creates a delay. These are negotiable. Delays caused by variations, bad weather, late approvals and various other causes can be claimed back by the builder.

Source of Funds

You will be required to show proof of where the funds will be sourced from – either recent bank statements or a letter from your mortgagor.

Responsibility for Approvals and Permits

You will need to state whom is responsible for procuring these. Generally, it is the client. You will also have to detail when these will be obtained. If that point passes, then either party can terminate the contract.

Mediator

In the event of a dispute both parties can agree to mediation. The default mediator for the HIA contract is the Institute of Arbitrators and Mediators.

The Builder's Margin

This is the amount a builder is entitled to charge on top of the cost of materials and labour supplied. As builders tend not to draw a regular wage, this is how they make their living. The default amount is 20% but, again, it is negotiable. For example, you ask the builder to supply and fit a mirror not detailed in the contract. The cost to the builder is \$100. The agreed margin is 20%. He will charge you \$120 plus GST.

Progress Payments

Progress payments are generally made at the following stages and, although negotiable, the standard percentages are: Deposit (3% if contract value is over \$20k), base (15%), frame (15%), lock up (35%), fixing or fit out (25%) and practical completion (remainder). Please be aware that some builders will try and front load these payments. Mortgagors tend to view this unfavourably and will only make payments based on the value of work done.

Prime Cost (PC) Items

PC's are fittings, fixtures and materials that have either not been selected or for which the price is unknown. Common examples are tap ware, tiles and light fittings. To avoid surprises, it is very important that you are happy with the sums detailed for PC's. The PC sum should include the cost of the item and GST. It does not include the cost of delivery and builder's margin. You should also make sure the list is complete and covers all PC items.

Make sure the allowances are sufficient and be aware that you will have to make up any shortfall between the amount detailed in the contract and the actual amount. Vice versa, if the PC item is actually less you will be due a refund. You are entitled to see any relevant invoices and a detailed breakdown of how any difference is calculated.

Be aware that unprincipled builders will either omit items completely or deflate the amount allowed. This is done to make the contract price look artificially low. The client will be faced later on by "extras" bills.

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Provisional Sum (PS) Items

PS's are used when the builder cannot give a definitive price for certain works. Common examples are excavation costs and concrete costs. The builder will make an informed estimate as to the likely cost plus GST. If the actual cost is less, then the owner is given a credit. If it is more, then the client has to pay the difference plus the builder's margin.

An example of a PS adjustment would be were the builder has allowed \$15k for excavations. Unfortunately, he hits rock and incurs \$20k of costs. The builder can then claim the extra \$5k plus his margin.

Again be aware that the unscrupulous builder will under provide for provisional sums. This makes his overall contract price look low. The reality is that his price will be the same as the builder who provides appropriately.

Our advice with both PC and PS items is to ensure that all quoting builders are providing for the same items and amounts. Detailed plans and specifications are essential. It is also possible to tell the builder what work/items to provide for. For example, it is easy to determine how much concrete will be required for the slab if no problems are encountered. Let's say it is \$20k. Tell all your builders that this is what you want their PS to be. That way all the quotes will be comparable. Please call us if you would like help with this.

Another option, if you feel ill-equipped to detail the sums, is to make a schedule of every builder's PC and PS items from their quotes. Then make sure they have all covered the same PS and PC items. Deduct those PS and PC sums from each builder's total build price, and add back an overall average figure from all quotes for the PC's and PS's. This will give you a more easily comparable total cost. Please feel free to ask us how to do this correctly.

Variations

A variation occurs when there is a change to the building work agreed in the contract. Either the builder or the owner can instigate a variation. For example, it was agreed to provide aluminium windows. The client then decides to upgrade to uPVC windows. The builder is entitled to charge the extra cost plus margin and applicable GST.

Good builders dislike variations. They are a source of disagreement. Sometimes they are unavoidable but generally they are changes that should have been "designed" out beforehand. If a variation is requested, a good builder will detail the work and extra cost or saving in writing within five days.

Bad builders love them. For example, the client decides to change the flooring from laminate to solid timber. The unprincipled builder, who knows the client cannot go to anyone else for a second quote, will charge excessively. To avoid this situation, make your decisions as to finishes as early as possible. Be detailed. Get it in writing. Query the cost.

The Start and Finish

At Blue Gum, to avoid any confusion, we will give you written confirmation that building work has commenced. You will be notified when each stage payment becomes due. We also issue a letter of practical completion at the end.

Water, Power and Access

The owner must ensure that there is power, water and access to the site. This may require a temporary utilities hook up or the laying of a rough driveway. Discuss these issues with your builder.

Insurance

The builder must carry insurance against liability for (a) the physical loss, destruction or damage to the building works and any materials on site and (b) personal injury, death, property loss or damage arising out of the works for an amount of at least \$5,000,000. You, or your lender, should ask to see a copy of the builder's "Contract Works Insurance".

Final Inspections

The builder must give the client five working days' notice of when "practical completion" will be reached. Practical completion is defined as "when building works are complete except for minor defects or omissions which do not prevent the building from being reasonably used for their usual purpose". A final inspection then takes place, and if the client agrees that the work is completed, final payment becomes due. If the client feels that certain work is unfinished they must provide the builder with a defects list. The builder then has five working days to address those defects. The defects will only be allowed to delay payment if they are not minor – they have to be sufficiently serious to prevent the building from being used for its normal purpose.

Defects Liability Period

Within three months after the date of practical completion, the client must give the builder a list of any defects. The builder then has 20 working days to make good those defects. At Blue Gum, we write to our clients at this point to ensure there are no outstanding issues.