

# How to Avoid a Disaster When Hiring a Builder



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This document contains a brief description of some key components that are important when selecting and hiring a home builder. The topics discussed are complex and variable and this paper is not intended to be a comprehensive guide to construction contracting. Entire books could be devoted to some of these topics alone. This overview is intended to assist those considering building a new home examine some of these key principles. Building a new home is a big complicated job so do your research before you begin.

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## 1. Look at Examples of the Builders Work

A builder's finished product tells a lot about the quality of work produced. The completed project will indicate the level of fit and finish one can expect. Make a point of walking through one or more homes completed by the builder.

While the specifications for your project may be different from the sample you are comparing you should be able to obtain a feel for the level of quality and care put into the work.

If you have a chance to visit a project in progress, do so as this too will help you evaluate the builders work style.



## 2. Check References

The two best groups to speak with about a potential builder are past customers and subcontractors. These two sources will offer a distinctly different perspective that is extremely valuable in measuring if the builder is right for you and your project.

Some questions to ask the customers are:

- How was the builder's communication?
- Were the contract documents clear?
- Was he/she prompt in communicating?
- How were discrepancies dealt with?
- Would you rehire this builder for another project?

Questions for the subcontractor would include:

- Is the builder organized and does he provide you timely clear communication?
- Is the builder reliable when it is time to pay for work?
- Does the builder provide qualified skilled supervision?

Do not be alarmed if you hear some negative comments from the customers or subcontractors. Construction projects provide lots of opportunities for mix-ups. Try and get a sense of how quickly and effectively the builder dealt with problems. This will provide valuable insight about your future dealings with the builder.

### 3. Contract Documents

Make sure the specifications and schedules are clear and very specific regarding what products will be incorporated into the project. The variance between the low end and high end of the spectrum for building materials, especially finishes, is enormous. A builder working on a fixed price contract without a specified selection may not choose materials that you expect.

While most of the finish schedule should be worked out prior to the start of the project there are times when this is not possible or desirable. In those cases often a dollar allowance is inserted into the contract for the yet specified items. The allowance should be as specific as possible identifying the amount and unit price for materials in the allowance. It should also be clear as to what will occur in the event there is a deviation from the allowance.

It is best to define up front how selections that exceed the allowance are treated. In addition, if there are savings from the allowance; who earns these savings? The discussion with your builder will provide important information about the builder's practices and help you determine your desire to work with this builder.



## 4. Change Order Policy & Procedures

It is common for changes to occur during the course of a construction project. The changes develop from a variety of sources including architectural plan conflicts, backordered or discontinued materials, concealed conditions or the customer shifting selections. While you may not be able to anticipate what changes may arise a clear procedure for how to deal with the change orders is imperative to avoid delays and disputes. The building contract needs to outline the policy to handle the change orders. There should be a clear description of how the change will be paid, administrative costs, impact on the schedule among others. However, try to work out and choose as much of the selections as possible before the work begins. A good builder with knowledge of the finishes will be better able to plan the construction to accommodate the finished product.



## 5. Project Schedule

After the plans, specifications and budget is established the builder can create a production timeline. A construction schedule needs to be flexible to account for a myriad of delays and obstacles that can occur while building. Therefore the builder should not be expected to provide the client a detailed production schedule. The builder can provide a production flow with milestones and a date range for completion of the project.



## 6. Construction Contract & Warranty

Most of the topics addressed in this paper should be addressed in the builder's contract. While it may be helpful to have an attorney review the contract it should be clear and understandable without a legal interpreter. Ask the builder to review the contract with you and make sure you are comfortable with the terms and conditions. Good contracts are useful tools that spell out the roles, responsibilities and procedures of the project. A lot of attorneys and banks are familiar with the construction documents published by the American Institute of Architects (AIA). These are well recognized and respected forms that also contain a procedure for payment requisitions. However, the AIA documents are rather lengthy and comprehensive in order to make them applicable to large scale complicated construction projects so some consider them too cumbersome for a single custom home.

Among the items covered in the contract should be the builder's warranty. The contract should spell out what is covered and for what period of time. It is also useful to know the builders procedure for making a warranty claim.

Some builders participate in warranty program insured by a third party. These warranty policies are very helpful as they provide performance guidelines, dispute resolution services and an insurance company to back up the property in the case of the builders' inability to cover a warranty defect. Certain states require this sort of coverage so it is worth asking your builder.

## 7. Fixed Fee vs. Cost Plus Contract

Most people are familiar with a fixed fee contract. The scope of work is described in the contract and the builder is paid a defined amount for performing this work. The final price exclusive of any change orders or contract addendums is referenced in the contract documents. The builder assumes the risk of price fluctuations. Because of this potential risk of cost increases a successful builder factors this contingency into the contract price. While the customer may feel secure in knowing they have a certain price, this price includes any uncertainty of the builder.

An alternative to a fixed price contract is one that is based on the actual cost of the labor and materials plus a fee for the builder. The fee can be a fixed negotiated sum or a percentage of the overall costs. While it is counterintuitive to most people, a cost plus contract is usually less expensive for the customer and not as lucrative for the builder.

The customer can still know what the job is going to cost prior to starting the project by establishing a budget as part of the contract. But any savings accrue to the customer and the builder does not need to add dollars to the contract for assuming the risk of the fixed price.

By eliminating the fixed price the custom builder does not have to include as much money in the contract to cover contingencies.

## 8. Financial Terms and Conditions

There are several different financial scenarios that can be utilized for the disbursement of funds from the client to the builder. If you are purchasing a new home or a property owned by a builder and the builder is financing the construction it is typical for the customer to provide the builder a 10 to 20% deposit with a possible progress payment and the majority of the balance due upon completion.

However in the case of a custom home built on the owners lot usually the owner through its independent financial resources or with the assistance of a construction loan pays the builder in periodic installments. The progress payments are based either on the completion of milestones, or as is becoming more prevalent a percentage of completion basis. Often a third party, such as the architect or an independent inspector verifies and approves the builders request for a progress payment. Expect to pay a portion of the contract prior to the commencement of construction as the builder will incur permit fees along with mobilization costs.

Some contracts call for the progress payments to deduct for a 10% retainage. The retainage is funded but held from payment to the builder until the completion of the entire project. The retainage is not a requirement and while intended to provide a level of protection for the customer by withholding payment until the final project is inspected and verified, it may have the unintended consequence of causing a higher cost for the customer. It is not uncommon for subcontractors to increase their bids to compensate for the delay in payments that result from retainage. Discuss and negotiate a payment plan with your builder that is clear and fair to all parties.

## 9. Florida Lien Law

It is important that you understand and abide by the Florida Lien Law.

Florida Statute number 713 is intended to provide property owners and contractors' rights and remedies regarding construction improvements to real property.

Failing to properly comply with these statutes can have unpleasant consequences to both the owner and contractor. The law is too complex to describe in this summary, but it is important to use a contractor that follows the statutes and if you have any questions about the application and effect of the law on your property, consult with a qualified attorney.



## ABOUT THE AUTHOR

Michael Stein is the founder, President and Chief Operating Officer of The Gentleman Builder, located in Bonita Springs, Florida. Michael has over twenty-seven years of experience in real estate acquisitions and development, new construction and renovation. Michael is responsible for planning and directing all aspects of the home improvement analysis, remodeling and new home construction.

Michael has the unique perspective of a construction expert who has purchased, developed, built and sold millions of dollars of real estate. As an owner building for his own account, Michael recognizes first the value of buildings as they relate to cost, location, features, and quality. With the ability to put this experience to work for you, Michael aims to provide customers with a superior analysis of their building issues.

Michael began his building career in the field as an assistant superintendent for a national homebuilder. After running a local home building company in Ambler, PA and working for Toll Brothers at their headquarters in Philadelphia, Michael served as president of a national homebuilder.

In 1999 Michael relocated with his family to Naples, Florida where he founded his own real estate development and building company. Michael's firms have received numerous local and national industry awards including the Professional Builder Magazine's Builder of the Year.



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A complicated project like building a new custom home requires a strong team. The project can be thrown off course by the inclusion of a weak link in the chain. There are many members of the team that contribute to the successful outcome. The key players are the owner, architect, interior designer, subcontractors, construction superintendent and project manager/builder. All successful teams share the benefit of skilled leadership and in most building projects the leader is the project manager/builder. The person performing this role establishes and selects the resources for the project, directs and coordinates the activity of the team. A skilled experienced builder will lead the project team to complete and deliver a home that will meet the owner's wishes for a building that will provide safety, security, comfort and enjoyment for many years.



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