

Getting Paid For Changes

by Gary Ransone



Recently, a builder consulted me about an owner who refused to pay overhead and profit charges on change orders and allowance work. The owner argued that the extra work was merely an "upgrade" to work that the builder already expected to do, and did not warrant payment beyond additional labor and material charges.

Is there such a thing as an upgrade that is not subject to the builder's charges for overhead and profit? The short answer is "No," but it depends on what you have agreed to in your contract. In fixed-price construction agreements, all additional work or deviations from the scope of the work should be written up as change orders and should carry overhead and profit charges.

To avoid misunderstandings about what constitutes a change order and

how changes may be billed, address the issue *before* the contract is signed and work begins. The simplest way to do this is to include appropriate language in your construction contract. If you don't, you won't have much of a case with the owner, the arbitrator, or the judge. Whoever you end up arguing with, you'll soon regret your failure to include simple contract language that deals with change orders.

Legal Road Map

Devoting a section of your construction contract to change orders creates a legal "road map" you can follow if you run into an owner who makes unreasonable demands. I include change order provisions in a section called *Changes or Deviations in the Scope of the Work* (see Figure 1).

Changes or Deviations in the Scope of the Work

A. Additional Work. During the course of the project, owner may order additional work, which will be written up as Change Orders. The net cost of these changes will be determined by the contractor, including contractor's profit and overhead at the rate of 20%.

B. Additional Work on Allowance. If the actual cost of any "allowance" work identified in the contract exceeds the allowance line item amount in the contract above, this increase in work and cost will also be subject to contractor's profit and overhead at the rate of 20%.

C. Deductive Change Orders. Contractor's profit and overhead, and any supervisory labor (as stated in this contract) will not be credited back to owner with any deductive Change Orders or with any credits related to allowance work.

D. Payment of Change Orders. Payment for each Change Order is due upon completion of change order work and submittal of invoice by contractor for this additional work.

Figure 1. These four clauses from the author's construction contract preserve the contractor's right to be paid fully for extra work, including overhead and profit. They also prevent having to refund overhead and profit charges when the original scope of work is reduced.

Each is designed to preserve my right to be paid fully for extra work, including my overhead and profit, and also to prevent my having to refund overhead and profit charges when the original scope of work is reduced.

But it's not enough simply to include the proper language in your contract — you may still have to explain the change order provisions to your client. When that happens, it helps to have a consistent line of reasoning to back you up.

Who determines cost? Some owners are uncomfortable having the contractor determine the cost of change orders. They feel they are at the contractor's mercy without any way to prevent being overcharged for the extra work they request. I insist, however, on having the last word on the cost of change orders because I am in the best position to know what the extra work will entail. If the owners think my quote is too high, I sometimes give them a breakdown of costs to show them how I arrived at the price. But if they still do not agree, I make sure my contract allows me to refuse to perform the extra work. Otherwise, I am at their mercy, without any way to prevent losing money on work that was not a part of my original contract.

Allowances. When I list allowances in a contract, the price I attach to each item includes only the cost of labor, material, and subcontractors; overhead and profit is figured into my base price. So when my clients see an allowance of \$500 for floor tile, for example, they know that it represents an installed price, and that they can spend the entire \$500 and still remain within the allowance.

When the allowance price is exceeded, however, I treat the difference between the scheduled allowance price and the actual cost of the allowance work as a change order. I am entitled to additional overhead and profit charges because I am taking responsibility for work of greater value.

Deductions. One of the most difficult concepts for owners to understand is why overhead and profit is not refunded when work is deleted from the original contract. When asked, I explain that by the time the owner deletes a particular portion of

CHANGE ORDER

ALPHA DESIGN
& CONSTRUCTION
P.O. Box 93
EAST CALAIS, VERMONT 05650
(802) 456-7429

TO: HAROLD WALSH
173 PLEASANT LANE
RICHMOND VT 05477
WALSH ADDITION
BEAR CREEK ROAD

DATE: 6-7-94
PRICE: 434.4747
NO: 00012
DATE OF ORDER: 4-21-94

1. ADD VELUX TPS-304 SKYLIGHT (W/L-FLASHING) TO M.8id. ON SOUTH ROOF PLANE. CENTER OPENING SIDE-TO-SIDE; SILL @ 40" FROM T.O.F.F.

MATERIALS \$475.00
LABOR 325.00
SUB (TAPE + PAINT) 30.00
OVERHEAD/PROFIT (20%) 66.00
TOTAL \$996.00

WE AGREE hereto to make changes as specified above, at this price \$996.00

DATE: 6-7-94
A.J. JORDO (Contractor Signature)

PREVIOUS CONTRACT AMOUNT: 147,200
REvised CONTRACT TOTAL: 148,196

ACCEPTED: The above prices and specifications of this Change Order are satisfactory and are hereby accepted. All work to be performed under same terms and conditions as specified in original contract unless otherwise stipulated.

Date: _____ Signature: _____

Figure 2. Using pre-printed change order forms is a good way to ensure you get written approval for extra work. Keep a pad of forms on site so you can take care of changes on the spot.

the work, much of my overhead is already spent on estimating costs, mobilizing equipment and labor, and coordinating subcontractors. And even though the deleted work is not performed, I still have to spend administrative time rescheduling the job to accommodate the deletion, adjusting subcontracts, and writing up the deductive change order.

Get it in writing. While it helps to have the proper language in your contract, and to review the contract with your clients, you must also follow through on the paperwork. Always put change orders in writing (even if there is no change in the contract amount) and get them signed by the owner prior to starting the change order work (Figure 2). If this is impossible, communicate by telephone with the owner, and make a written note that details the owner's authorization to perform the change order work. Then immediately provide the owner with a written change order.

Finally, be sure to consult an attorney familiar with construction law and with your business before making changes to your construction contract. ■

Gary Ransone is a working general contractor and a practicing attorney specializing in construction law. He lives in Santa Cruz, Calif.