

CONTRACTING FOR AGRICULTURAL CONSTRUCTION

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INTRODUCTION

In the past, many farm contracts were sealed with a handshake and nothing more. The farmer's and the contractor's words were their bond, with both sides believing that necessary details could be worked out at the project site during construction, without the need for a written contract. In many cases, written contracts were viewed as unnecessary, too technical, and a waste of time.

In today's farm economy, however, the farmer who continues to contract for services based upon a handshake is taking a great risk. Faulty construction can threaten the farmer's economic well-being, and subject both parties to lawsuits for personal injury, environmental damage or economic loss. A written contract for construction services should be a standard operating procedure for every farm.

Purchasing a new building is a major capital expense. The whole process of getting bids, signing a contract, and con-

struction can be quite intimidating because it is not a common procedure for most people. The important decisions you must make may be unfamiliar, and the information you need at each step is not always easy to get. A contract is a way to assure that all the parties understand what is required of them, and a way of determining beforehand what to do if a problem develops.

This bulletin provides basic background information on the contracting and construction of agricultural projects. It will help you understand the basic approach to planning a project, bid preparation, drafting and executing a contract, and the construction of the project.

Arranging financing, listing specifications, and soliciting and evaluating bids will be described; the basics of a legal contract will be discussed; and some elements usually contained in construction contracts will be explained.

Figure 1 shows a schematic of the steps followed in the contracting process.

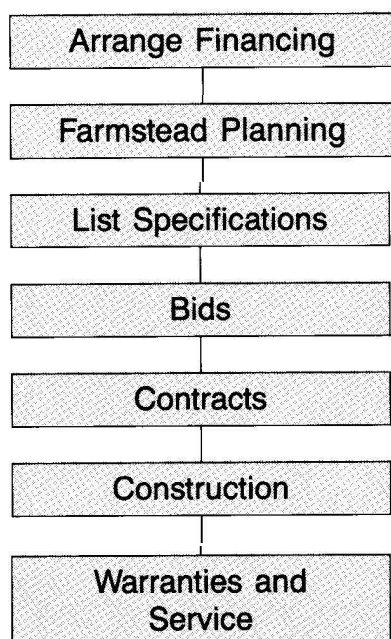


Figure 1. Simplified schematic of Contracting Process

ARRANGING FINANCING

Your decision to build should have a sound business basis. Will this structure improve your farm enterprise or just be another expense? Develop a budget before you talk to a builder, so you'll have some guidelines on affordable alternatives.

Work with your lender and your county Extension agent to develop a realistic budget. Determine the source of financing and interest rates, and obtain approved financing. Your county agent can help you analyze your farm enterprise and make an economic decision that includes tax implications and cash-flow analysis for the project.

In some cases you may contact builders to determine approximate costs of buildings to help you and your lender set a realistic budget. Remodeling existing facilities may cost less, but may not serve your needs. A builder can decide if a project is feasible based on the budget you supply. You may have to build the project in phases in order to stay within your budget.

FARMSTEAD PLANNING

Develop a farmstead plan by sketching building sizes and locations, utilities, topography, and other pertinent details. Consider your short- and long-term goals for the farm at this stage. Look at a 5-, 10- and 20-year horizon for your farmstead. A farmstead plan will help you sort out goals

for the project and identify the limitations you must deal with. Site the new building on the farmstead plan and determine how it will fit into the overall operation. Plan for future expansion when siting a new building, and remember that you may also want to expand nearby buildings.

LIST SPECIFICATIONS

You'll need to develop a set of specifications before you get bids from builders. The specifications are just a list of things you require in the project. Allow some leeway in your specifications so that builders can use their standard dimensions of construction.

Specifications for a building include size, types of equipment, snow and wind loads, color, concrete quality, and other items that describe how the building should be built. This list becomes part of the contract as listed on the building plans or as a separate document. You can use the specifications list to help resolve any dispute that develops during construction.

Assess your management style to see how it fits with the features of the building you're planning. Use as many sources as you can find to help make your list of specifications. Use Midwest Plan Service Handbooks and other materials to develop a rough plan for the building. Talk to neighbors, Extension agents, lenders, and builders, and take building tours to gather ideas.

You may want or need to consult government agencies when you develop your specifications. Cost-sharing from the Agricultural Stabilization and Conservation Service; Department of Natural Resources (DNR); and Department of Agriculture, Trade and Consumer Protection (DATCP) for manure storage and barnyard runoff control may offset some of your construction costs, but you'll have to satisfy Soil Conservation Service specifications. DNR has priority watersheds that also may have cost-sharing for certain projects that protect groundwater and surface water. DNR also has waste-handling regulations, depending on the size of the operation. DATCP has regulations for grade A milk standards and milk-production facilities.

Several state codes affect agricultural construction. The electrical code covers electrical requirements. The well code covers well construction and location. The state building code exempts buildings used exclusively for farming from building-code requirements. However, local codes may have more stringent requirements. Setbacks, property lines, zoning ordinances, and waste-handling regulations all need to be considered in the building project.

Risk Allocation

Every contract should consider the risks associated with the project and who should bear the risks.

For projects involving an architect or other designer, a construction contractor, and subcontractors, you must ensure that each of the parties understands which risks they will bear and which risks other parties will bear. As a rule, the more risk that the designer or contractor accepts, the more the project will cost you. On the other hand, it may be better to pay a little more to ensure that the designer or contractor bears the burden of doing a good job.

Time Limits and Delays

Every contract should clearly state when the project should be completed. Without time limits, the contractor may perform the contract on a piecemeal basis, leaving you open to economic problems or liability from state agencies.

Other types of delays that can be anticipated should be stated, and responsibilities for the delays should be allocated. For example, if labor problems arise, the contractor would normally take responsibility. If a tornado occurs, the contractor may be exempt, since a tornado is considered an act of God. State time limits carefully and clearly, and hold the contractor to meeting them.

Special Clauses

Each contract contains special clauses that attempt to anticipate problems at the construction site. Standard contracts contain a series of sections regarding these problems. Your situation may require a different approach. Read standard contracts very carefully to ensure that any special problems that could occur in a project are anticipated and properly handled.

Some commonly used special clauses, and the reasons for them, follow.

1. *Disputes*—A difference of opinion can arise even with a carefully worded contract. After signing a contract, nobody wants to go to court to try to work out a dispute. Therefore, most contracts contain dispute-resolution sections in which the parties agree to mediate or arbitrate major problems. Dispute sections allow quick and reasonable resolution of disputes, so as not to endanger the ongoing project.

2. *Differing Site Conditions*—Sometimes a project is bid on the basis of poor or incomplete information concerning the construction site. A site that is much different geologically than anticipated can cost the contractor a good deal of

money. Most contracts allow a change in the contract due to differing site conditions.

3. *Changes*—As your project is built, you may decide that some small changes would make the project more functional. For example, your contract may require a certain window placement, but during construction, you and your contractor agree that a different type of placement would be better. Most contracts have "change order" provisions that allow you to quickly make these sorts of changes without having to renegotiate the contract. Be sure to keep written records of all change orders.

4. *Insurance*—The contractor must have the resources available to protect you, the purchaser of services, from lawsuits or other problems if the contractor is unable complete the project. Most contracts require the contractor to have insurance that protects you. Some contracts may require you to provide insurance coverage for construction-site related problems such as fire, wind damage or vandalism.

5. *Construction Liens*—By state law, anyone who does construction work or provides materials on a project has a lien against the property for payment for services. Liens are generally used by subcontractors but can also be used by the general contractor.

You should receive a notice of lien rights as part of the written contract. (Where there is no written contract, a notice of lien rights should be prepared separately and given to the owner.) Give copies of the lien notice to your lender.

Lien rights can be waived by the contractor or subcontractor at any time during the project, even before it starts, by signing a lien waiver. To avoid problems, do not make the final payment to the prime contractor until all subcontractors have signed lien waivers.

Express Warranties and Damages

In addition to specifications, a contract may contain a warranty stating the purpose of the project. If a dispute arises, the court will look to see if a warranty is expressly stated in the contract. The wording of this expressed warranty is very important should a problem develop.

The court may also determine whether a project is fit for its intended purpose, and could imply a warranty into the contract even though none is expressly stated. Courts do not lightly imply warranties into contracts, so state desired results in the contract whenever possible. For example, if your project must meet state law, then compliance with state law should be an express warranty in the contract.

the builder absorbs the cost of mistakes, and the project cost to you will not change.

Owner Hires a New Consultant

You can hire a consultant to provide you with professional expertise in designing your facilities. The consultant will draw a set of plans and specifications for you. You can use them to solicit bids to build exactly what the plans indicate. The consultant may also oversee construction to make sure plans and specifications are followed correctly, thus freeing you from having to oversee the project. The consultant receives a fee for his/her services, and accepts responsibility for project completion.

Evaluate and Accept a Bid

Evaluating and accepting a bid proposal can be complex. You must develop a set of criteria by which to compare bids. These criteria include builder's reputation, size of the project, quality of the bid proposal, and your list of specifications. Doing the groundwork—listing specifications and plans for the project, will simplify the process of comparing bids.

Determine the builder's experience. Look at the size of the company, the number of years in service, and any experience in your type of project. Look for qualities indicating the builder's expertise, professionalism, and knowledge of agriculture. Is the builder capable of handling the project? Will you feel comfortable working with the builder and is there mutual trust between you? Determine the builder's credentials and financial status. Carefully check builders with short track records in your area. Have they just come into the area to grab a few quick sales and then leave, or are they moving into new territory from other established areas? Remember that the builders will have to be around for 10 to 30 years if you hope to get any service out of them.

Compare and evaluate proposals based on your specifications. Using your list, go through each bid. Are the proposals complete, including all you asked for in your specifications? Note any differences on each bid for future reference. This way you can compare bids on an equal basis. You may want to question the builders if their bids differ from your specifications, and allow them to correct their bids if you are interested in having them do the work. Make sure the completion date is realistic, and get a guaranteed price for the project.

Beware of a bid that is much lower than the others. Builders can make mistakes as they prepare bids, but you can have them corrected before you make a final decision.

Some builders may make a very low bid, then come back after you've accepted to ask for more money to build the building you really wanted in the first place. Your list of specifications will keep this from happening. Do not base your decision on just one factor (in particular, price).

GENERAL CONSIDERATIONS

Following a few basic rules will help to ensure the best results on any construction project—large or small.

1. *Be As Specific As Possible.* While you don't need to know every last detail of your project, you must have a firm idea of what you want to achieve. The more specific the direction you can give contractors, the easier time you will have comparing bids. If your project must comply with a state law, for example, all bidders should know they must meet the state's regulations.

2. *Get Everything In Writing.* Never enter into an oral contract for construction work. The quality of work delivered may not be up to what you expect, but without a written contract, it is your word against the contractors. Even with a signed contract, get in writing all agreed-upon changes during construction. This is the best way to protect yourself should something go wrong.

3. *Keep Complete Records.* Keep records of all transactions leading up to the contract, the contract itself, during construction, and after-construction maintenance. Complete records will help you to reconstruct the facts in your favor should a problem occur. For example, keeping photos of the work done during construction will show how carefully the contractor performed the job. Photos are especially useful if work will be covered by a wall or floor, where poor construction will not be seen. Also, the contractor might be more careful if he/she knows that you're taking photos.

4. *Read Contracts Carefully.* Many contractors today use standard contract forms. These forms can be useful, since they cover many of the most important issues. However, these forms often place the risks on the purchaser of the service, rather than on the contractor. To ensure that you don't accept a risk that you don't want, read each contract very carefully, and discuss the language with the contractor. Don't be afraid to demand a change in preprinted language on a contract. For complex contracts or large projects, you may want to have your attorney review the contract to ensure that you understand it fully.

Never sign a contract without first reading it. Contractors may pressure you to do so, but taking the time to fully understand each paragraph in a contract is the only way to protect yourself.



CONTRACTS

Keep contract documents in a safe place for future reference. The documents should include:

- Contract
- List of Specifications
- Plans
- Building Permits
- Lien Waivers
- Warranties
- Insurance
- Change Orders

BASIC ELEMENTS OF A CONSTRUCTION CONTRACT

A contract performs four basic tasks.

1. It should state exactly what you want the contractor to do.
2. It should state what you will pay the contractor for the service.
3. It should attempt to state the risks associated with the project.
4. It should state what will happen if a problem keeps the contractor from meeting the agreed-upon completion dates.

Each of these tasks should be carefully thought through, so that the contract wording is clear to both parties. Some basic elements in a normal construction contract follow.

Specifications

The specifications section in a contract should clearly state what services the contractor is to perform.

Some contracts may be very general and state only that the contractor shall perform a certain task, such as constructing a barn. These general contracts can be risky.

Other contracts will be very specific, stating the exact types of material and the performance standard to be achieved—such as what type of nail or screw should be used in a given part of the project. The more specific you can be, the less room you allow for the contractor to use substandard materials or claim that substandard performance meets the contract requirements.

If the project must meet a state or local requirement, such as an administrative code regulation, the contract should state that the project will meet all relevant state codes. If the government orders you to make changes, you want to ensure that the contractor pays for those changes.



Midwest Plan Service and the Northeast Regional Agricultural Engineering Service have handbooks on agricultural construction. The American Society of Agricultural Engineers has standards for snow- and wind-load design for agricultural buildings. Contact your county Extension office or an agricultural engineer for these materials.

BIDS

Potential Bidders

Locating bidders may be as simple as looking at magazine and newspaper advertisements, or choosing a builder who did previous work for you. Look for new construction in the area and ask neighbors and lenders for recommendations. Go to farm shows and talk with builders. Look for a builder who will not only sell a building but also provide professional expertise and service with the bid price. Select and accept proposals from builders with proven track records.

On a new project, get written bids based on your specifications from two, or at most three builders. Don't swamp yourself with too many bids—you'll get confused and find yourself using price as the bottom line, which you may regret later. Get general information from each company. Allow each builder time to prepare a written bid. Several

weeks is enough. Don't let a builder pressure you with a "special offer" tied to a deadline. This is usually a tactic to get you to sign up today without looking at the competition. Ask for customer references, and go see the plant where the building is constructed. Tour buildings that have been built by the builders you are considering.

On subsequent projects, get a bid from your previous builder if he/she did well, but also get an additional bid from someone else to check prices.

Obtaining Bids

Each builder may build a slightly different building and offer slightly different services. Some builders may offer a "turnkey" building, putting all the construction and equipment into one package. Other builders may only construct the shell of the building; you'll have to hire concrete work and order equipment. Make sure you understand what each builder can do for you and the risks involved in these different contracting relationships.

Owner Acts as a General Contractor

When you act as a general contractor, you hire and coordinate the entire project construction. This may include hiring several subcontractors to do various jobs. Each subcontractor will have a contract with you to perform some task—perhaps site work, building shell, concrete work, plumbing, electrical, or equipment installation. You will also need to coordinate the construction of the project with all the subcontractors.

If you act as a general contractor, you may spend less money, but you are taking more risk and should understand the construction process thoroughly. Mistakes and unforeseen conditions in construction often occur. If the contract doesn't cover them, you may pay the cost. This can raise the cost of your project considerably.

Owner Hires Turnkey Project

When you hire a builder to do a turnkey project, the builder assumes the responsibilities and risks of the general contractor. This is often called a design-build contract. You work with the builder to design the building; the builder then constructs the project.

You pay the builder to select subcontractors, coordinate the construction, and accept responsibility for project completion. The builder may do much of the work himself and hire subcontractors to perform other tasks. Trying to coordinate several subcontractors on even a small project can be complex, and mistakes may occur. In a turnkey project,

You may lose money if a contractor doesn't finish on time. In order to keep a contractor on schedule and avoid a court fight if the schedule is not kept, many construction contracts require the contractor to pay liquidated damages for contract default.

The liquidated damages could reflect incidental damages, such as your increased operation and administrative costs; and also could reflect consequential damages, such as lost profits. If a court reviews a liquidated-damages clause, it will attempt to determine whether the clause is reasonable and whether the damages agreed to are foreseeable. The court will not enforce liquidated-damages clauses that it considers punitive. Penalties are seen as against public policy.

CONSTRUCTION

You may need to have certain things ready before the builder will begin construction. This depends on what is covered in the contract.

For example, the site may have to be ready for the builder, or the builder may prepare the site. Water or electricity may be required at the site before work can proceed. Make sure that the contract clearly states what is expected of you before the construction starts.

Routinely inspect the work during construction. Ask questions and check materials or special items that are covered in the contract and specifications. Check concrete reinforcement before the concrete is poured to ensure that the proper materials are used. Take pictures during construction and keep them with the contract for future reference. If changes are required during construction use a written change order to supplement the contract so that there is no question later that you asked for the work. If you think workers are doing something wrong, stop the work and talk to the builder. When a misunderstanding occurs, it's easier to stop construction and correct it than to come back later and tear it out.

The contractor will receive a final payment after the project is finished. This final payment protects you from getting an incomplete or unsatisfactory building. You don't have to pay the final installment until you're certain that the contract is fulfilled. Tour the finished building with the builder. Note any problems, such as unfinished work. Make the builder perform these changes before final payment. Builders are more likely to make the changes right away if they are waiting for payment.

WARRANTIES AND SERVICE

There are some specific warranties on materials in new buildings, such as steel, treated wood, and equipment. The duration varies, depending on each material's warranty.

Steel manufacturers may not warrant steel in animal housing if the steel does not have a protective covering, such as insulation, vapor barriers, or plywood liners, on the interior of the building.

Treated wood has a warranty against rot, but it only covers material cost, not the cost of removing and replacing the wood. The builder may or may not cover those additional costs. The equipment installed in a building may also have warranties for service.

If you have a problem with a building, notify the builder in writing and ask him to correct it. Try to work out the problem with the builder and give him an opportunity to correct the situation. Keep records of your requests. You may need them in the future if litigation is required to settle the dispute.

SUMMARY

With farm costs rising and environmental and other liabilities increasing, written contracts for farm construction are more important than ever.

If you're thinking about building, negotiate a contract and be sure that the contract accurately states what you expect from the contractor. Even after you've negotiated a good contract, you'll need to keep good records of the construction, as well as maintenance and inspection records. This is the best way to ensure that you get your money's worth and protect your interests in your farm property.

WEX University of Wisconsin-Extension, Cooperative Extension, in cooperation with the U.S. Department of Agriculture and Wisconsin counties, publishes this information to further the purpose of the May 8 and June 30, 1914 Acts of Congress; and provides equal opportunities in employment and programming including Title IX requirements.

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Produced by the Department of Agricultural Journalism, University of Wisconsin-Madison.

This publication is available from your Wisconsin county Extension office or from:

Agricultural Bulletin, Rm. 245

30 N. Murray St.

Madison, Wisconsin 53715

Phone 608-262-3346



Editors, before publicizing, contact Agricultural Bulletin to determine availability.

I-03-90-2M-70-S

A3490 CONTRACTING FOR AGRICULTURAL CONSTRUCTION 1990