

# Building Contract in Germany

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## Legal points, approval and warranties

### Introduction

The German word for contract is “Vertrag” and it is parent with the verb “vertragen” means to tolerate each other.

To construct a building, parties can also enter into a contract verbally, but it is good advice to introduce a written contract. It is much easier to tolerate each other if both parties remember the initial agreement. The most important thing is to describe the work and the aims clearly and carefully detailed, then there is a good chance of not finding each other sitting in court.

In this case, we take a look at:

- Legal points
- Different building contracts and examples
- New methods for building contracts

### Legal points

#### **Contract to produce work – “Werkvertrag”(BGB 631 ff)**

If you are ill and you go to a doctor, than you will pay for the treatment and not for the result (*service contract*)

If you want to build a house, it is the exact opposite: You pay the craftsman for the finished work and not for his effort to finish the work.

The *contract to produce the work* means that the contractor is obliged to deliver the promised work, and the employer to pay the agreed remuneration.

And, this is an important item, the contractor is obliged to finish his work, prior to the contract being agreed as fulfilled. The promised work has to be free of material or legal defects and remuneration has to be paid after acceptance of the work. After approval, the risk allocation changes from the contractor to the employer.

## **German Construction Contract Procedures (“VOB”)**

Like everything in Germany, all aspects of tendering, the execution of construction work, the perimeter and standards and the settlement of building projects are regulated by a degree. In this case it is regulated by the *German Construction Contract Procedures* or *Construction Tendering and Contract Regulations*; in Germany called “Verdingungsordnung für Bauleistungen (VOB).

The contracting parties of a building contract can agree on applying to the VOB to receive uniform basic rules. The VOB consist of 3 parts:

- VOB/A: Regulates all parts of the submission or tender.
- VOB/B: Regulates all aspects concerning the period of construction: Delays, interruptions, changes in construction, elimination of defects, warranties, payments and acceptance.
- VOB/C: Generally accepted rules of technology (DIN)

## **Different building contracts**

We take a look at the different kind of building contracts. The general items of all contracts are:

*Define promised work:* To define as clear as possible, take the establishing tender, plans etc. in the enclosure. The work has to conform with building codes and generally accepted rules of technology (DIN). Agreement of applying to the VOB or the German federal law (“BGB”)

*Period of construction:* Commencement of work and completion date. Delays and interruptions are regulated in the VOB.

*Remuneration:* Different kinds of payments like *Price per unit, Lump-sum, Hourly-Rate*. Regulation of part payments.

*Contractual penalties:* If work is delayed due to reasons for which the contractor is liable.

*Guarantees:* The warranty period is five years according to BGB, four years according to VOB, and two years for other work. There are different warranties such as *performance bond* or *warranty bonds*.

*Approval/Acceptance:* Regulation of the requirements of acceptance. After acceptance, remuneration becomes due and the risk changes from the contractor to the employer. Acceptance is the start of the warranty period.

### **The Unit Price Contract**

*Remuneration:* Deduction takes place at the agreed unit prices. The remuneration in the contract is preliminary, the invoicing will be finalized after taking the measurements on site.

*Pro and cons:* Cost accounting on the basis of actuals. A risk of decreasing construction costs if the establishing submission is not as exact as it should be. In this case, the preferred contract of the craftsman.

*Recommend usage:* Predictable building constructions with clear determined masses and qualities.

*Example Akelius:* Karoiviertel/Hamburg – Facade insulation  
Vereinstr.40/Hamburg – Change Windows,  
balconies, attic extension.

### **Lump-Sum Contract / Lump-Sum Turnkey Contract**

*Remuneration:* Consolidation into a lump sum based on the unit prices of the submission. Progress payments according to the building progress.

*Pros and cons:* Less risk of increasing construction costs due to increasing masses, but the risk of overpayment due to declining masses. Less effort due to the accounting control. Turnkey: One contractor across the gaps who is responsible for the whole construction and the coordination of the different technical crews. Disadvantage: GU-premium at the remuneration.

*Recommend usage:* Unpredictable and risky measures (for the employer). Recurring and even measures.

*Example Akelius:* Beckstr. 8-21/Hamburg – Renovation of 14 staircases.  
Hamburg – 20% of the flat refurbishments

## **Global Lump-Sum Turnkey Contract**

*Remuneration:* Consolidation into a lump sum based on a functional tendering. Progress payments according to the building progress.

*Pros and cons:* Risk reduction by risk transmission. The GU is responsible for determining the perimeter of construction. Disadvantage: “Risk-addition” and GU-premium leads to paying exorbitant prices the more complex the measures are.

*Recommend usage:* Unpredictable and risky measures (for the employer).

*Example Akelius:* Lindenstr.13/Hamburg – Loft apartment house  
Ahrensburger Str.61/Hamburg – new attic storey  
Hamburg – Flat refurbishments

## **Hourly Rate / Costs Plus Contract**

*Remuneration:* Cost accounting on basis of actuals (Time and material).

*Pro and cons:* Time is a factor, which is difficult to control. The risk is transferred to the employer.

*Recommend usage:* Advisable only for minor measures.

*Example Akelius:* Small refurbishments or reparations.

Of course, there is a disagreement concerning risk reflection between the employer and the contractor. The pros and cons are from the point of view of the employer. Due to risky and unpredictable building constructions, it is good advice for the employer to go for a lump sum contract while every craftsman tries to set a unit price contract.

Regardless of the chosen contract, the VOB regulates the execution of construction work.

## **New methods for building contracts – Pre Fair**

Due to huge and complex building constructions, there is a new procedure developed from the industry and the big General Contractors called *Pre Fair*.

The establishing idea is to replace the price competition with a competence competition in two steps:

Step 1: Already in the planning phase, the contractor and the employer are working closely together and create the tender process together. The advantage is the in-depth input of expertise and knowledge concerning cost reduction from the pre-fair contractor. In fact, 90% of construction costs are affected in the planning phase and only 10% in the building phase.

Step 2: The pre-fair partner and other GU's submit their tenders. Of course, the advantage of getting the contract is on side of the pre-fair partner. In the building phase there is almost no risk of

increasing costs due to supplements if the Pre Fair-partner becomes the order.

## Summary

Building contracts in Germany are so called *Contracts to produce work* ("Werkvertrag"). The contractor is obliged to deliver the *promised work* and the employer to pay the *agreed remuneration*.

The *German Contract Procedures* ("VOB") is a well balanced measurement which regulates all aspects of building constructions, beginning with the tendering procedure and finalizing with the setting of standards and perimeter of the building construction.

Generally, most of the German building contracts are based on the "VOB" to get a uniform basic measure.

There is a difference between the building contracts concerning the payments: *Unit Price Contract*, *Lump Sum Contract* and *Hourly-Rate Contract*.

The new *Pre Fair* procedure is a good way of getting the highest planning and cost security. But be aware, *Pre Fair* is developed from the big General Contractors to minimize their losses (due to functional tendering) and to reduce the competition with other GU's.