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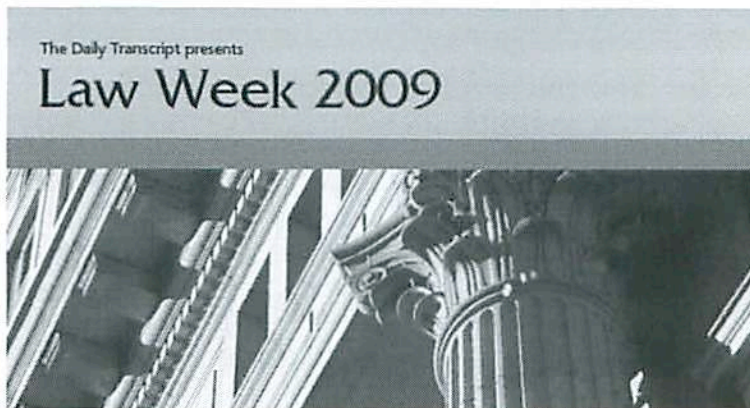
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Friday, May 1, 2009



Construction project risks increase in a difficult economy

By JOHN VAN BLERCK, JVB Construction Management Inc.

Friday, May 1, 2009

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As the construction industry continues to operate in one of the most difficult markets in many decades, the risk of projects failing from a quality, time and cost perspective have increased significantly.

Specific concerns and items to be aware of in embarking on a construction or renovation project include the following:

Project costs

Many projects now being bid by public agencies and others are bidding well below (25 percent to 35 percent) the engineer's or owner's cost estimate. The reasons for the decline in bid amounts are partially due to markets being flooded by contractors seeking new work and ready to reduce profit and overhead margins to get the work. The risk for a project owner is that claims for extras are far more likely, as contractors have simply not bid enough to complete the project with the required labor, materials and overhead required.

Another cost-related problem is contractor lack of cash flow. Contractors being unable to fund current cash flow requirements can result in numerous problems, including unpaid workers, unpaid subcontractors and suppliers, and the withdrawal of subcontractors and suppliers from projects, causing delays in construction. Another cause of contractor cash flow problems stems from suppliers no longer extending generous credit terms to contractors, and requiring either cash on delivery or more aggressive account terms.

Performance

In some sectors such as residential, where work has all but dried up, many contractors are retooling and switching to other sectors of the market they have not previously worked in, such as schools, defense or military. These sectors are very different from the residential market in that they have different performance requirements, along with intense and detailed paperwork and logistical requirements, which are typically not required in the residential, private market.

Problems arising from these differences include contractors being unable to properly furnish required paperwork in a timely manner, and conflicts due to heightened inspection/logistical requirements.

Project controls

It is now more important than ever that traditional control documents be properly used and diligently pursued through completion. These include i) standard pay request forms such as the AIA G702 Form, which provides a template for inclusion in the contract, and for periodic pay requests with a detailed breakdown of construction

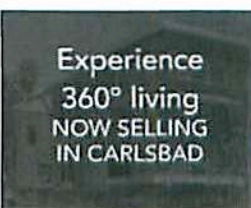


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contract costs and services for payments due based on work completed; and ii) obtaining lien releases from suppliers and contractors as work proceeds (both conditional and unconditional).

Other controls that may be considered include fund controls, in which an owner has construction payments administered through a third party fund controller, which will bring some level of protection to the owner, in that the fund control typically request lien releases prior to recommending requests for payment.

Insurance certificates

Check insurances to ensure contractors have all the required levels of insurance for workers' compensation, general liability and automobile, and errors and omissions (if applicable).

In addition, where possible, contractors should name owners as additional insured on insurance policies to provide an added level of protection to owners in the event of a claim or accident.

Form of contract

Contracts should be clearly worded, with a well-written scope, and provide the owner with adequate cancellation clauses should the need arise. Contracts should clearly spell out dispute resolution procedures and remedies. Payment terms should be clearly stipulated on the contract, and should allow for retentions to be withheld from progress payments until all work has been approved by the owner and/or the construction manager.

Van Blerck is owner and principal of JVB Construction Management Inc., a Poway-based construction management firm.

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