RISK ALLOCATION DURING THE BIDDING AND CONSTRUCTION PROCESSES FOR MUNICIPALITIES AND MUNICIPAL AUTHORITIES

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I. Introduction

a. Objectives in planning projects

i. cost efficiency and avoidance of waste

ii. quality and programmatic content

iii. timeliness of completion

b. Dealing with claims – active role for counsel

i. marshaling the facts

ii. securing expert analysis

iii. managing the municipal response

2. Preconstruction

a. Best time to reduce construction-phase risk

1. construction contract risk

b. Fallacy of the budget

3. Terminology

a. **Definitions – a problem in the construction world**

   i. **Program – content, quality, and functionality of the project**

   ii. **Design Review – an independent undertaking performed by third-party design professionals**

   iii. **Construction Manager – either at risk CM (i.e. holding contracts) or "agency" CM (i.e. serving only as an advisor or consultant)**

iv. **Bidding or Strict Bidding – pricing by qualified contractors on the basis of a fixed design and delivery date and award to the lowest bidder**

v. **Negotiating – discussion of and changes to the work and its cost prior to award**

vi. **Risk management – the adoption of strategies for construction contract risk reduction**

vii. **Risk allocation – the explicit assumption of an unavoidable construction contract risk by a participant in the project**

viii. **Scope – the general description of a project**

4. **Risk allocation and risk reduction - making explicit what is often unarticulated by the parties**
    a. Missed opportunities to make the construction process more efficient and cost effective
5. **Public contract formation requires a comprehensive and tailored set of contract documents**
    a. Discussions should address risk allocation and risk reduction
    b. Draft to minimize and allocate risk

c. Avoid drafting unreasonable and potentially unenforceable clauses

d. Describe the relationship between and among project participants

e. Effective clauses track how the parties actually perform

6. Start with form agreements

a. Several national organizations

b. Get licenses

c. Forms are a starting point

d. Use of forms gives participants a familiar structure

   i. Comparisons allow for focus on the changes

7. Revise and supplement

a. Revise in accordance with risk reduction/allocation strategy

b. Don't overreach

   i. Overreaching creates bid contingencies, disputes, delays, and litigation

c. Workshops to discuss risk

i. Admittedly without direct contractor participation

ii. Informal "workshops" with design professionals and project managers, and attorneys, present and actively engaged

iii. Advisory committees for larger construction programs

iv. Discussions can occur outside of a specific bid on a project

- d. Core topics
  - i. Management of the processes
  - ii. Risk reduction and allocation

8. Risk analysis
   - a. Who does this now?
     - i. Architects and engineers?
     - ii. Facility managers?
     - iii. Construction managers?

b. Our analysis in the late 1980s and early 1990s

c. Focus on project-specific risks

i. Questions?

ii. Answers!

1. We have yet to encounter a risk that cannot be reduced if not eliminated

2. Remaining risk is "baked in" to the project

3. Addressing every conceivable risk would be wasteful
4. Best return results from identification of risks more likely to arise
5. Do this as early as possible

9. How to start

a. Reported cases

i. Each decision represents a failure to allocate risk clearly

b. Your own program and other construction in your state or region
    i. Don't fight the last war
c. Risk that cannot be eliminated must be allocated clearly and explicitly
    i. Particular role does not automatically determine allocation
    ii. Allocate remaining risk to the participant best able to manage that risk
        1. Subsurface and undisclosed site conditions
        2. Coordination of trade contractors

10. Known Risks: A Checklist of Recognized and Unnecessary Costs, Change-Orders, and Claims

a. Categories:

1. Undisclosed geotechnical site conditions.
2. Unexpected presence of environmental hazards and conditions.

3. Bidder inspection failing to disclose site condition.
4. Failure of owner to disclose information within its control.
5. Estimated or anticipated quantities exceeded or not met.
6. Drawings and specifications with inaccuracies, inadequate detail, inadequately coordinated.
7. Phasing or sequencing misrepresented or not fully described.

8. Drawings and specifications impossible to perform.
9. Denial of site access, lack of permits, and unavailable right of way.
10. Changes in owner's requirements.
11. Delay in award of contract or delayed authorization to proceed.
12. Failure to coordinate multiple-prime contractors either through a lead contractor or project manager.

13. Failure to review and approve shop drawings, to respond to requests for information, or to perform testing promptly.
14. Owner's direction of means, methods, durations, and sequences in a detailed construction schedule.
15. Inadequate scheduling.
16. Inadequate documentation during project.
17. Delays, inefficiencies, and impacts caused by other contractors.
18. Failure to assign and delegate decision-making responsibilities.

19. Acceleration or delay of project completion at owner's direction.

20. Failure to respond to change orders, claims for damages and requests for time extensions on a timely basis.

21. Requirement that contractor perform work not specified in contract documents or work differing from that specified.

22. Requirement that contractor perform work in particular manner or method which differs from that originally anticipated through either express or implied conditions or interpretations of the specifications.

23. Owner's directive to perform work out of sequence.
24. Disruption or interruption of work or stop orders.
25. Joint occupancy during construction.
26. Additional work resulting from revised, amended, clarified or changed contract drawings or specifications.
27. Designer's improper rejection of work.

b. All types of construction

c. Not all risks are equally likely to occur

d. Each has a preventative or prophylactic measure

II. Hidden Risks: A Checklist of "Hidden" and Unnecessary Costs and Inefficiencies

a. Categories:

1. Designing up to a budget based on financial capacity rather than programmatic requirements
2. Failure to provide for independent design review
3. Failure to provide other preconstruction services, including constructability review, pre-construction scheduling, and detailed cost estimating
4. Adoption of proprietary specifications that reduce competition
5. Excessive professional fees or fees that are inadequate for the design or project management services needed

6. Reuse of design without sufficient revisions
7. Bidding documents which encourage inclusion of excessive contingency in bids and proposals (e.g., no equitable adjustment for subsurface conditions, no damages for delay, etc.
8. Contract documents which foster bid protests and litigation
9. Failure to provide adequate design, bidding and construction contingencies
10. A hidden downgrade in quality during construction

11. Billing for quantities not provided
12. Unjustified and excessive change orders
13. Construction out of compliance with specifications or requiring subsequent modification
14. A feature of the project that fails to function properly and cannot be modified
15. Accelerated progress payments to the contractor

16. Setting a construction schedule that is too compressed, too lengthy, or otherwise unrealistic
17. Contractor's failure to pay or delay in paying subcontractor or supplier
18. Contractor's work not in compliance with specifications and not monitored
19. Proceeding with high-priced change orders for finishes rather than using follow-on contractor
20. Insufficient utilization of construction change directive process
21. Inadequate disputes resolution processes

b. Again, not all risks are equally likely to occur

c. Each has a preventative or prophylactic measure

12. Use of Risk Analysis During Strict Bidding

a. Pricing on the basis of a fixed design and fixed delivery

b. Risk reduction and allocation occurs during the programmatic and design stages

c. Interaction with contractors outside a specific solicitation

d. Allocation of remaining risk must realistically reflect custom and usage is therefore reasonable and enforceable

e. Remaining risk should be allocated to the party that is in the best position to control and minimize it

f. Risks that cannot be eliminated can be assumed explicitly by the owner for the purpose of creating a uniformity among the bids and proposals

g. The owner's interests are best served by fully considering the position of the contractor
    i. Fairness translates to better pricing and fewer claims
h. Unreasonable allocations necessarily translate into contingencies in the bidding
    i. The classic example is an undisclosed site condition
    ii. Similarly, "clever" drafting of no-damages-for-delay clauses

13. Examples of Improved Outcomes

a. State building program in the mid-to-late 1980s with the annual construction expenditures approximating $150 million
   i. Responsibility for coordinating multiple-prime contractors
   ii. Critical path method (CPM) scheduling
   iii. The owner assumed responsibility for equitable adjustment for unexpected subsurface conditions

b. Local government projects with a risk reduction strategy

14. Resolving Disputes

a. Resolve disputes early

i. Tight timelines

ii. Continuing damages

iii. Require that a claim be asserted at the time of the first occurrence of damage

b. Keep the dispute process informal
c. Documentation similar to change orders
d. Initial claims management in-house
e. Use the disputes clause
f. Independent expert review of the facts
    i. Recognize the "interest" of the participants

g. Stay away from commercial arbitration

h. Review by non-neutral owner personnel and a nonbinding administrative appeal, with the right to a de novo appeal to a court

i. Be fair

15. Enforcing Risk Reduction Strategies and Risk Allocation

a. Duty of contract lawyers to monitor compliance

b. "Calling out" special provisions in the advertisement or at least in the instructions to bidders

c. Presentations at pre-bid meetings

d. Actions contrary to contract document provisions

16. Conclusion

a. Identification of risk

b. Adoption of risk reduction strategies

c. Allocation of risk that remains

d. A proactive approach to contract preparation and dispute resolution at the earliest possible time in the project

Time for Questions



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