



Audit Update Pitfalls of Lump Sum Self-Performed Work

SELF-PERFORMED WORK (SPW)

Many Construction Manager (CM) firms who work for Owners on a Cost Plus Fee with a Guaranteed Maximum Price (GMP) (CM-at-Risk) basis are capable of self-performing scopes of work such as concrete, carpentry, masonry and what is often called General Trades.

There are pros and cons to letting CM's bid on self-performed work.

One of the pros is that the project may be able to be completed more efficiently when the CM performs certain scopes of work.

One of the cons is that the amount paid to the CM for self-performed work may be more than the fair market value of the work performed.

This update is to highlight the risks of potentially paying too much for Self-performed Work (SPW) when you compensate the CM on a lump sum basis.

Is 100% Fee on SPW Reasonable?

On one recent CM project, the agreed upon lump sum amount for SPW was approximately \$1 million. According to the Construction Manager's cost accounting records the actual cost to perform the work only amounted to approximately \$500,000. The \$500,000 balance of the lump sum amount was the effective Fee earned by the CM on this SPW scope of work.

Advantages of "Open Book" SPW

On a recent \$100 million CM-at-Risk project, the CM submitted a \$4 million lump sum bid to self-perform a combination of general trades bid packages.

The Owner's contract stated no self-performed work could be performed on a lump sum basis. The contract went on to say if the CM's competitive bid was considered the best value, the CM would be compensated on the basis of the contractually defined Cost of Work ("open book") plus a SPW fee of 7.5% with a Guaranteed Maximum Price (GMP) equal to the amount of their "best value competitive bid".

The Owner insisted that the SPW be performed on the actual costs ("open book") plus fee with a GMP basis versus on a lump sum basis. The end result was that the actual audited SPW costs plus fee totaled only \$3 million and the Owner saved \$1 million.

Potential Pitfalls of Lump Sum SPW

- The typical bid packages for trade contractors cover scopes of work such as a concrete, masonry, drywall, painting, roofing, mechanical, electric, plumbing, etc.
- The trade contractors end up bidding against their peers and the trade contractor determined to submit the "best value" bid is usually awarded the work. This typically works well when there is normal competitive bidding by a sufficient number of trade contractors.
- When the CM is submitting their competitive bid against trade contractors for scopes of work like concrete, carpentry, masonry, etc., the dynamics of healthy competitive bidding may change. Some trade contractors may hesitate to seriously compete for the work because they do not want to harm their relationship with the CM. They may elect not to bid or they may submit what is called a "complimentary bid" which is usually higher than a normal trade contractor competitive bid. It is even more difficult to obtain meaningful competitive bids when a CM puts together a bid package for "General Trades".
- Typical "General Trades" bid packages often cover scopes of work that the CM would typically perform on a cost reimbursable basis with no additional fee.
- Some CMs create "General Trades" bid packages for miscellaneous scopes of work such as layout, cleanup, dumpsters, temporary protection, crane operator, hoist operator, miscellaneous equipment rental, and scope gaps such as roof/wall blocking, irrigation sleeves, installation of metal frames, etc.
- These miscellaneous "General Trades" scopes are not standard bid packages that are typically bid by typical trade contractors or even by other general contractors. As a result, the scopes of work are typically too random to effectively obtain competitive bids.

Other Pitfalls of Lump Sum Self-Performed Work

One organization was billed double for the cost of the self-performed work.

One organization was billed and paid for self-performed work not complete.

One organization was billed for SPW scopes that were duplicated in subcontractors' scopes of work performed by the subcontractors.



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WHAT TO DO?

- Require the CM to perform all self-performed work on a cost-plus basis "(open book") with a maximum.
- Avoid paying an extra fee to the CM on scopes of work described as General Trades. Instead establish negotiated Not-To-Exceed amounts for agreed upon reimbursable costs of General Conditions, General Requirements, and miscellaneous scopes of work that will be performed by the CM.

If you cannot resist the "simplicity" of lump sum SPW contracts for General Trades or other SPW scopes of work such as concrete or carpentry, etc., this is what we suggest:

- Require the CM to provide very detailed quantity based estimates of the labor, hours, labor rates, material quantities, equipment hours, etc. that is covered by their proposed lump sum SPW bid package so you know exactly what you are paying for.
- Include specific rights to audit the CM's cost accounting and other records related to their SPW.
- Audit the scope of work covered by other trade contractors to verify that portions of the SPW scope of work not actually awarded to a trade contractor without a corresponding credit to the SPW contract value.
- Audit the costs charged to reimbursable general conditions and/or general requirements costs to make sure they are not charging supervision, labor, material or equipment to those direct reimbursable cost accounts when they should be charged to the SPW contract.
- Periodically inspect the job to see what work is actually being self-performed by the CM.

Dumpsters that are usually reimbursed as general conditions or general requirements should not be included in Lump Sum General Trades Self-Performed Work bid packages. The actual cost of dumpsters should be handled on a cost reimbursable basis with dumpster rental and pull charges. If more than one dumpster service provider is available, comparable competitive rates should be obtained and reviewed for best value. Require the CM to bid out any third party work such as dumpsters. There is NO reason for dumpsters to be wrapped into a lump sum package.

In conclusion, there appears to be more pitfalls to allowing the CM to perform SPW on a lump sum contract basis versus on a cost reimbursable ("open book") basis.



TRAINING

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QUESTIONS?

If you just have questions about how to contract for and or monitor the costs of self-performed work, please do not hesitate to contact us for a free consultation.

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