

## *Construction Management vs. General Contractor Method of Contracting*

### **POINTS OF VALUE OF THE CONSTRUCTION MANAGEMENT METHOD**

In an effort to take advantage of our opportunity to discuss with the Owner the merits of negotiating Construction Management services for your facility needs, I would like to highlight for you a few of the many advantages of the Construction Management Method.

#### *Benefit Number 1: Construction Management Contracts Better Serve to Align the Contractor's Objectives with Those of the Owner*

The primary difference between negotiated and hard bid contracts has to do with the incentives for performance. A General Contractor, "lump sum" contract uses 100% completed drawings to establish a set price for the construction of a project and the General Contractor is rewarded to the extent that the project costs are less than the bid price. This is the case because the difference between the project costs and the bid amount is Fee for the General Contractor (GC). As a result, it becomes the objective of the GC to construct the Owner's facility at the least cost possible. The problem is, as the GC determines ways in which to reduce cost, the Owner receives no added benefit. The objectives of the Owner and the General Contractor are at odds from the beginning.

In a Construction Management (CM) contract on the other hand, the Fee is established as a fixed amount. Beyond the fee, everything else is a "cost of the work" providing no other opportunities to the Construction Manager for additional fee. As a result, the Construction Manager and the Owner share a common objective to get the best price, from the right contractor or supplier, for the cost of the work. In this fashion, the Owner, Architect, and the Construction Manager work together to ensure the project's success. The animosity inherent in the GC approach is avoided under the CM approach. It becomes the duty of the Construction Manager to protect the Owner's interests with subcontractors and suppliers throughout the construction process.

#### *Benefit Number 2: Negotiated Contracts Allow a Construction Manager to be "On-Board" Early and Participate in the Preconstruction Process*

There have been many studies done about the design process throughout the years, and they all continue to arrive at a similar conclusion. That conclusion is that the decisions made at the early stages of the design process have the most impact on the success of the project. This is true not only with respect to satisfying the program needs, but also in terms of establishing a project's budget and schedule as well. Given this understanding, the role of the Construction Manager as a part of the pre-construction phase/design phase cannot be over-emphasized.

During the Pre-construction Phase, an Owner can expect their Construction Manager to provide information, both data and recommendations that will enable the Owner to make the best design decisions possible. In this role, the Owner can rely on the Construction Manager to provide input about the project with respect to:

- ✓ Estimates of the cost of construction
- ✓ Estimates of comparative costs for different systems (i.e. structural frame, HVAC, exterior skin, roofing, etc.)
- ✓ Alternatives to materials, systems and design approach
- ✓ Schedules for design and construction
- ✓ Develop value engineering alternatives to design
- ✓ Estimates of permitting times and requirements
- ✓ Recommendations for material and equipment selections
- ✓ Price checks on the design as it progresses to ensure it stays within the budget
- ✓ Recommendations for subcontractors and the bidding process

There are, of course, a variety of other issues which the Construction Manager will focus on during the preconstruction phase as well, but those listed are necessary to the Owner's and Architect's decision making process. With both accurate and timely input from the Construction Manager, the Owner is best positioned to make good decisions and therefore is able to maximize the use of his construction dollar.

Another important role throughout the design phase for the Construction Manager is the role of design reviewer. As such, the Construction Manager troubleshoots the design to prevent change orders and redesign. By reviewing the design, the Construction Manager can also advise on subtle changes that drastically affect the ability of the project to be constructed.

### *Benefit Number 3: Construction Management Contracts Allow for Flexibility in Defining and Changing the Project Scope*

Construction Management contracts, unlike any other type of delivery method, are exceptionally good at providing a means to allow flexibility for an Owner during the development of a facility. Because CM contracts align the objectives of the Construction Manager with those of the Owner, they in fact create the resources necessary to respond to an Owner's needs throughout the process. The collateral costs and challenges faced with Owner directed changes during both the design and construction process can be met with contract defined processes to manage the changes. Because changes do not provide a means for the Construction Manager to enhance his fee, they can be dealt with in an open book fashion jointly with the Owner and Construction Manager.

*Benefit Number 4: Construction Management Contracts Provide an Owner Access to All of the Project Costs*

One of the primary by-products of a CM contract is the Owner's access to actual costs. With a hard bid project, the General Contractor bills for an estimated percentage of completion for scheduled values of work. Therefore, the Owner is left to judge whether the scheduled value of work as well as the estimated percentage of completion is accurate. As a result, the Owner pays for work that may or may not be completed at that time. With a CM contract, an Owner only pays for costs that are actually incurred, much like you do in your own business. The burden is on the Construction Manager to provide the backup to substantiate costs and to the extent that backup cannot be provided; the Owner is not required to pay.

*Benefit Number 5: Construction Management Contracts Allow for Flexibility in the Bidding Process*

The CM delivery method allows an Owner and Construction Manager to design a bidding process specific to the needs of the project. For example, if a project has short construction duration, but the construction schedule is constrained by the sitework, the Construction Manager can design an early bid package to competitively bid just the sitework, while the rest of the design is being completed.

Another tangible benefit to the Construction Manager's involvement in the bidding process is the ability to pre-qualify a select list of subcontractors and suppliers. In doing so, the Owner can be assured that each bidder will have the capacity and resources necessary to complete the work to the satisfaction of both the Construction Manager and the Owner.

*Benefit Number 6: The Selection of a Construction Manager Focuses on Qualifications*

An Owner not only wants the lowest cost facility, but an assurance that they will receive the best quality for the money and a timely delivery. The General Contractor approach really only considers lowest cost when selecting a Subcontractor. The other, more qualitative variables tend to be overshadowed as though they are equivalent for each candidate.

The CM process on the other hand, recognizes that 90% of the job costs will be competitively bid among contractors and suppliers, and given that assurance, the important criteria to be evaluated when selecting a Construction Manager are mostly qualitative.

Therefore, the Construction Management approach focuses on characteristics such as:

- ✓ Company experience
- ✓ Company resources
- ✓ Preconstruction performance
- ✓ Approach to Owners and Architects
- ✓ Experience of project team
- ✓ Track record for delivering similar projects

Obviously, this list is abbreviated, but the point is that the CM contract seeks to develop a "team" of professionals skilled in developing your project and as such, recognizes the importance of qualifications in ensuring success.

*Benefit Number 7: Construction Management Contracts Result in Fewer Change Orders to the Contract*

Recognizing that the Construction Manager has participated throughout the design phases of the pre-construction process, it is reasonable to assume that the Construction Manager should have a broader perspective of the potential issues that may arise during construction and which may ultimately requires changes to the work. As a result, for example the Construction Manager will be better prepared to address modifications to related to unknown conditions or the clients/architects request to make changes to the scope of the project.

Minimal changes are directly related to the ability to establish a budget on a CM project and manage the changes that invariably occur on every construction job. Although often unwanted, it is prudent for an Owner to recognize that many of these changes are inevitable and result from factors outside of the architect's practice. The design and construction of a facility is not a static process with predictable and controllable variables, although that is what a bid method assumes. The design process instead, is an evolution of requirements, methods, and materials changing from design through construction and ultimately into the Owner's move-in period. With the General Contracting approach, the flexibility to respond and manage these changes is limited; and typically, the result is an increased project cost, since many of the changes are unavoidable. The Construction Management approach, however, enables an evaluation of the changes, consideration of alternatives and options, and a balancing of the budget to maintain the anticipated cost.

### *Benefit Number 8: Real Savings for Tax-Exempt Organizations*

One of the significant advantages of Construction Management is the ability to save on sales taxes on tax-exempt organizations. Although these entities are tax exempt, some cannot pass on their tax exempt status to a third party. They must actually write the checks for materials. These are significant dollars.

Most projects are about one half material and one half labor. For instance, a million dollar project would include about one half million dollars of materials. Nine percent of \$500,000.00 is \$45,000.

We have developed a system that allows the materials to be purchased directly, thus saving the sales tax and at the same time hold the contractor responsible for materials, quantities and cost increases.

### *Benefit Number 9: Construction Management projects allow for the Owner to evaluate the risk and necessities of bonds.*

Most General Contractor projects are bonded. The GC provides the bond for his work and the work of his subcontractors. These costs are included in the bid and can range from 1 to 4% depending on the financial strength of the GC. With a GC project, bonding provides financial assurance to the client for GC and his subcontractors. The GC's bond covers a subcontractor, even with horrible financial problems. Should the subcontractor "go broke", the GC must complete the work.

With Construction Management projects the Owner, with the assistance of the CM can evaluate the risk and the cost of the bond for each contractor. Depending on the financial strength and longevity of the contractors, the Owner may opt to not require a bond on a case by case basis, thus saving the dollars he feels are at almost no risk.

With tax-exempt organizations, where the materials are purchased direct, the material bills are paid and lien releases are secured. Should a contractor fail to make a payroll, he is usually out of business. As the material bills are paid, the financial exposure is only one pay period, thus eliminating the necessity of bonding. Generally there is about a 1% savings in the overall project costs due to lesser financial exposure and bonding requirements.

Even for tax-exempt organizations, there are a few cases where a bond is prudent. For example, a church may opt to require a bond on a concrete contractor due to the disproportionate cost to remove and replace unacceptable work.

## *Summary of Advantages of Construction Management Contracts*

As a recap, and in no particular order, I have tried to itemize the advantages to the Owner of the Construction Management approach discussed herein:

1. The CM can orchestrate the bidding of individual bid packages to enable a fast-track approach to construction.
2. The earliest possible starting and completion dates are obtainable due to phased construction.
3. The objectives of the Owner and Construction Manager are aligned. The Owner, Architect and CM work together towards the project's success. The animosity attributed to other contract formats is avoided under the CM methodology.
4. The CM acts to protect the Owner's interests with subcontractors throughout the Construction phase.
5. The Owner is able to maximize the use of his construction dollar due to the cost input during the design phase.
6. Pre-purchasing of long lead items is available in order to prevent delays in the construction phase.
7. The CM troubleshoots the design to prevent change orders and redesign. The CM also checks constructability and construction methodologies.
8. It is possible to redesign certain portions of the project without affecting the schedule during construction.
9. Price checks by the CM throughout the design phase keep the project in budget and on schedule by preventing redesign.
10. The CM schedules and administrates the bid process.
11. The CM works on a fixed fee or percentage fee basis with all of the construction savings being returned to the Owner.
12. There is input on costs, materials, and scheduling throughout the design phase. The Owner is best positioned to make good design decisions when armed with accurate and timely information through the preconstruction involvement of the Construction Manager.
13. The Owner is afforded an open-book to job costs and is billed actual costs rather than an estimate of costs.
14. There are typically fewer change orders on CM projects than there are on bid jobs.
15. The selection process for Construction Manager focuses on qualifications rather than price.
16. Bids are received from a select list of prequalified subcontractors, thus giving the Owner the benefit of a bid project.
17. Costs are paid for after they are incurred. The Owner is not expected to cash flow expenses.
18. There are real savings for most tax-exempt organizations.
19. The need for bonding can be evaluated on a case-by-case basis.

Obviously, it is our opinion that the CM methodology offers the Owner the greatest benefit in terms of construction value for the dollar. This methodology also allows the Owner the greatest degree of flexibility in determining the specifics of his design. The Construction Management contract format has become increasingly popular as it offers the Owner the preconstruction expertise of an entity that is actually involved in the construction of the project. We have used this contract format with a number of different clients throughout the Tulsa metro area and are confident that this is the appropriate approach for the Owner as they embark on their new project.



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