Mitigating Risk: Managing the Construction Claims Process

Presenter: Timothy G. Wentz, PE, HBDP | Fellow/Presidential Member ASHRAE

Kansas City Chapter
January 7, 2019
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- Collect at the end of the meeting
- Compile the attendee rating on the Event Summary Critique
- Send the completed Event Summary Critique to your CTTC RVC and ASHRAE Headquarters

Forms are available at: www.ashrae.org/distinguishedlecturers
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ASHRAE Members who are active at their chapter and society become leaders and bring information and technology back to their job.

YOU ARE NEEDED FOR:
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- Society Standard Committees
- Chapter Membership Promotion
- Chapter Research Promotion
- Chapter Student Activities
- Chapter Technology Transfer

Find your place in ASHRAE and volunteer!
Goals

• Identify claim conditions and how they evolve
• Eliminate the adversarial environment that creates claims
• Strengthen project management strategies to anticipate and avoid claims
Our Industry

- Our industry is a people-based business
Our Industry

- J. P. Kotter & J. L. Heskett, ‘Corporate Culture and Performance’, research sponsored by Harvard Business School

Businesses that focus obsessively on meeting the needs of clients:

- Revenues increase 4 times faster
- Job creation is 7 times faster
- Owner equity grows 12 times faster
- Profit performance is 750 percent higher
Construction Claims

• Why is the topic so important?
  • Destroys relationships
  • Can have huge financial impact
    • Legal cost
    • Settlement
    • Your time
    • Company lack of focus
  • Risk can be disproportionate to Reward
Risk is Disproportionate to Reward

• Often, contractors/engineers/architects face an inordinate amount of risk for a small reward
Risk is Disproportionate to Reward
Construction Claims

• Legal approach to construction claims in the United States
Claims as an Ethical Issue

• Rank the five most critical issues you face in your work

   5. Bid shopping
   4. Change order games
   3. Payment games
   2. Unreliable contractors
   1. Claim games

What is a Claim?
“15.1.1 A claim is a demand or assertion by one of the parties seeking, as a matter of right, payment of money, a change in the Contract Time, or other relief with respect to the terms of the Contract. The term “Claim” also includes other disputes and matters in question between the Owner and Contractor arising out of or relating to the Contract.”
Claim Components

• Entitlement
• Damages
• Relief
I. Entitlement

A. Why are you entitled to receive a change in cost, time, both, or “other relief”.

B. This is what I spend a lot of my time doing as an expert witness. This is an expense that could easily be avoided.

   1. A change occurred

   2. The change was unexpected

   3. The risk for the change is borne elsewhere
Strategies to Avoid Claims

• Create a non-adversarial environment
  • Avoid Owners that are a living, walking claim
  • Understand the scope of work
  • Clear assessment of risk
• Strong mitigation strategies
Creating a Non-adversarial Environment

• Risk Management
  • Identify the risk
  • Measure the risk
  • Account for the risk
Creating a Non-adversarial Environment
Creating a Non-adversarial Environment

- Integrated design team
  - Engineers
  - Architects
  - Contractors
  - Manufacturers
  - Owners
  - Service contractors
  - Facility managers
  - Commissioning agents
  - Others
Creating a Non-adversarial Environment

• What is a contract?
  • Determines the relationship
  • Defines scope
  • Assigns risk
    • What changed?
  • Sets realistic expectations

I. Identify and Avoid Claims Before you Sign a Contract

A. Determines the relationship between the parties

B. Reassigns the risk among the parties

C. What are some of these risks?

  1. Entitlement
     a. What are changes?

     b. What is your duty (job) as a PM?
How Can a Contract Generate a Claim?

- Creates an atypical relationship
- Offloads risk to another party
- Lack of mutual understanding of scope
• Reading the Fine Print

A. A recent study indicated that 49% of all contractors read the contract alone. Moreover, most believe that the comprehend their contracts.
Creating a Non-adversarial Environment

- Read the contract
- Read the contract
- Read the contract
Creating a Non-adversarial Environment

• Do simple things well
• Be a partner in the process of perfecting the scope of work

Managing Client Expectations

A. Walt Disney was once asked, “Where did the magic of Disneyland come from?” He replied, “There is no magic, only good management of details.”

B. Concentrate then on:

1. Show up to meetings early
2. Return phone calls promptly
3. RFI’s are timely
4. Be prepared for meetings
5. Be honest

C. Be a partner in the process of perfecting the scope of work
   1. Develop a problem solving process
   2. Make sure it is measurable!
Creating a Non-adversarial Relationship

- Well defined roles
- Eliminate the source of claims
- Clear and equitable change provisions throughout
- Enforceable prompt payment clauses

Prof. Wentz’s top contract clauses to avoid an adversarial relationship
Creating a Non-adversarial Environment

“*The Contractor and the Owner waive Claims against each other for consequential damages arising out of or relating to this Contract.*”

*AIA-201, 2017 Edition, Article 15.1.7*

I. Waiver of Consequential and/or Incidental Damages (This is a two-way street)
   A. Consequential damages include:

   1. Damages incurred by the Owner for rental expenses, for losses of use, income, profit, financing, business and reputation, and for loss of management or employee productivity or of the services of such persons.

   And

   2. Damages incurred by the Contractor for principle office expenses including the compensation of personnel stationed there, for losses of financing, business and reputation, and for loss of profit except for anticipated profit directly arising from the work.
Creating a Non-adversarial Environment

"Prior to commencement of the Work and upon written request by the Contractor, the Owner shall furnish to the Contractor reasonable evidence that the Owner has made financial arrangements to fulfill the Owner’s obligations under the Contract. The Contractor shall have no obligation to commence the Work until the Owner provides such evidence."

AIA-201A, 2.2.1, 2017 Edition

- AIA-201A, Paragraph 2.2.1, 1997 Edition
  A. Highlights the difference between Plan & Spec and Design/Build or Service.
Creating a Non-adversarial Environment

“The Owner’s and the Architect’s interpretation shall govern the scope and performance of the Work and no allowances shall be made in behalf of this subcontract for error or negligence on his part in this connection.”

Modified version of AIA-201A, 4.2.11, 2017 Edition
Creating a Non-adversarial Environment

“If Contractor shall desire the Work of the Subcontractor hereunder to be performed with greater speed than is herein contracted for, the Subcontractor shall, without affecting or abridging the rights of Contractor set forth in any Article hereof, upon receipt of written order from Contractor, employ overtime work as so directed. The actual cost of such overtime work as shown on time sheets checked and approved each day by Contractor shall be paid by Contractor to Subcontractor, but no overhead, supervision costs, commissions, or other costs shall be charged thereon.”
Mitigation Strategies

• Strong documentation
• Go/No Go process
• Shared scheduling, including manpower loading charts
• Resolve to employ “win/win” negotiation tactics

Prof. Wentz’s top mitigation strategies to avoid a claim
I. Documentation
   A. The lady pictured is the foreman of your jury. You must document such that she can understand the documents. (i.e., it must be simple, straightforward, & routine) (WHAT TYPE WORK FOR YOU?)
   B. Types of Documentation
      1. Contemporaneous Documents
         a. Dairies
         b. Daily reports or job log (on microcassette)
         c. Daily labor records
         d. Equipment utilization reports
         e. Accident reports
         f. Progress photographs
         g. Video
         h. Weather data
      2. Financial Documents
         j. Conversation memos
         k. Notices and correspondence
         l. Web site
Mitigation Strategies

• **Documentation as a strategy**
  • Prompt written notice (a contractual duty)
    • Gives the Owner/Contractor/Engineer/Architect as much time as possible to solve the problem
    • Creates more options
  • Improves productivity
  • Prove you mitigated the damages (a contractual duty)
    • Relationship building
Mitigation Strategies

• What is the most important piece of documentation you can generate on any project?
Mitigation Strategies

- Clear identification of risk
- Have a written process!
- Prioritize risks
  - Checklist form
    - Financial
    - Operational
    - Hazards
    - Strategic
  - Calculation form
  - Determine RLH

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<th>Average</th>
<th>Mid-Low</th>
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Total Project Risk Score: 0
Corporate RLH Value: 0
Mitigation Strategies
Mitigation Strategies
Mitigation Strategies

• You are in the 8th month of a 20 month project
## Mitigation Strategies

### Two Week Schedule

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<th>Activity</th>
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<th>LF CODE</th>
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<td><strong>Area 3</strong>:</td>
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<td><strong>Start RC</strong>:</td>
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<td><strong>Area 3 is Ready to Move to Area 1</strong>:</td>
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<td><strong>Release Restroom Banks on 4/1/07</strong>:</td>
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*Use Pallets*

*Includes Testing*

*Includes Rough-In*

*Includes Start Rough-In*

*Includes Start RC*

*Includes Start RC Activities*

*Start RC Activities*

*Start RC Activities*
Mitigation Strategies

• Creative negotiating
The Spearin Doctrine

A. The quotation is from the National Institute of Construction Law (1996)

B. This is what separates a:

1. Plan and specification contractor
2. A Design/Build Contractor
3. A Service Contractor
Creative Negotiating

- Vendor produces foam insert on HD seats
- Contractor asked to add chilled water piping to new molds to increase production
Creative Negotiating

- **Forward pricing of change orders**
  - Assessing change order costs prior to the project
  - Contractor waives their right to claim
  - Owner waives their right to Liquidated Damages/claim

Forward Pricing

A. A process of assessing change order costs prior to the project starting.

A. Forward Pricing Model I am using comes from

  W. A. Botting Company
  Seattle, Washington

They used this model successfully on the West Point/Renton Wastewater Treatment Plant. $735 million dollar project that came in on time and $16.5 million dollars under budget. The project almost immediately headed for serious claims when artifacts turned up on site. This process really saved the job.
### Forward Pricing

<table>
<thead>
<tr>
<th>FACTOR</th>
<th>Percent of Loss if Condition</th>
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<tr>
<td>1. STACKING OF TRADES: Operations take place within physically limited space with other contractors. Results in congestion of personnel, inability to locate tools conveniently, increased loss of tools, additional safety hazards and increased visitors. Optimum crew size cannot be utilized.</td>
<td>Minor</td>
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<tr>
<td></td>
<td>10%</td>
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<tr>
<td>2. MORALE AND ATTITUDE: Excessive hazard, competition for overtime, over-inspection, multiple contract changes and rework, disruption of labor rhythm and scheduling, poor site conditions, etc.</td>
<td>15%</td>
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Forward Pricing

Complexity Calculations:
Conclusion

• Select the right clients
• Make a commitment to form strong relationships
• Avoiding claims and good management practices go “hand in hand”