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Manipulating Bid Packages

As most of you are aware, Construction Managers and General Contractors, often see self performed work as an opportunity to make additional fee. In this area, we have seen CM's and GC's, in different parts of the country, employ similar strategies in manipulation of bid packages. This bid package manipulation allows the CM to perform the bid package work as if they were a subcontractor, for a fixed price. The basic scheme is fairly easy to understand and surprisingly easy to pull off, apparently. If you are the CM, the scheme is as follows: 1 - Develop one or more bid packages where the scope is so general in nature that there is no subcontractor willing to bid on that package. 2 - Turn in a lump sum price to the Owner or yourself, for that Work. 3- Ask the Owner to authorize you to do the Work. 4- Bill the Work on a lump sum basis.

As absurd as it may seem, we have seen bid packages, within the last year, where buying coffee for the GC's personnel, among other items, was included as a part of the bid package for General Trades work. In fact, General trades work (many of us still call this General Conditions) is the most common "package" that a CM tries to bid out if they are trying to manipulate the sub bid process. Since this General trades work can include: misc. blocking, clean up as needed, dewatering as needed, safety protection, coordination of LEED dumpsters, and punch list coordination, you can see why no real subcontractor would bid such

work. They would have to have a crew, including a superintendent, on the job, full time, from beginning to end, just in case they were needed on a given day. Of course the whole scheme does work better, for the CM, if they can actually get at least one bid from a real subcontractor, and it does not hurt if that bid is ridiculously high. In fact, this last year we have seen one GC create fake sub bids for bid package work, when an adequate amount of real bids were not available, just to make the CM's own self performed bid look better and more legitimate to the Owner. We have also seen cases, on two separate projects, where the CM was a JV and one of the joint venture members took turns in "bidding" on these manipulated bid packages, just to make sure both companies got their share of the additional profit. Also this JV arrangement had the added benefit of contractually allowing the JV/CM entity to say that they did not do any self performed work.

Another manipulation of bid packages that we saw this year was a CM attempting to bid out a "hoisting package" which included cranes, man hoists, and forklifts. No subcontractor or single rental company would be willing to bid on this scope, yet that is exactly the scope that was presented to the Owner as a bid package that the CM wanted to "also" bid on as self performed. In this case, the Owner with our assistance rejected that package and instructed the CM to perform the necessary tasks as Cost of Work, without additional self performed fee.

Our advice is to review all bid packages carefully, don't allow any self performed work to

be performed on a lump sum basis unless there are extraordinary circumstances, and be especially wary if a bid package has one or less bidders.

When Self Performed Work isn't Self Performed

Dovetailing with the previous subject is the situation that presented itself many times this last year; A CM is allowed to self perform some scope of work, only to discover during the audit, that the actual Work was performed by subcontractors, whose cost was also in the Cost of Work. General cleanup is one such item, where the CM required the subs to participate in a composite cleanup crew to clean all unidentifiable debris. The CM, in this case, actually incurred no cost for cleanup, even though \$50,000 was billed to the Owner. Another case involved a CM who billed an Owner for installing doors, frames, hardware, and also misc. blocking, when in fact the drywall sub performed the blocking, and a misc. specialty sub did the doors and hardware installation.

A takeoff on the same theme is the case where the CM tells the Owner that they were going to self perform drywall and actually subbed all of the work to a real sub. On a Hospital project the CM told the Owner that they were going to self perform the purchase and installation of the mechanical equipment screens for a price of \$40,000 and actually subcontracted the work to the Mechanical sub. Both the actual cost and the \$40,000 were billed to the Owner.

The largest additional self performed fee money maker for CM's is the Concrete package. Here the CM includes all concrete related work in one package and asks the Owner to allow them to bid on this work as well. The concrete package would include, concrete materials, concrete pumping, horizontal place and finish, vertical place and finish, forming, rebar materials, rebar installation, reinforcing steel and installation, placing of embeds, and perimeter protection. In the list here, often only vertical place and finish and placing of embeds is actually performed by the CM's employees. As much as 85% of the

Cost of the Work is either subbed to other companies or simply purchase orders for materials. Because so much of the work is not actually self performed, you can guess that few subcontractors are in the business of bidding on all of that work. Even if a sub was willing to bid the work, most would also be aware that the CM would have the upper hand in negotiating with the Owner for this work, so there may be very little chance of getting legitimate bids anyway. Requiring the CM to break up these concrete packages into smaller chunks and getting real bids from subs that are really going to do the work, is the only way to keep from paying an extra fee for nothing.

You Just Think the GC Bought SubGuard

We have been warning you of the various tricks a CM may try when using SubGuard. We have recently heard from industry sources that some of you are resisting using SubGuard altogether. On larger projects, where the average bond cost is less, this may be a very prudent decision. On smaller projects we have encountered a situation recently that we had not seen previously. The CM told the Owner that they were purchasing SubGuard or something very similar that they called SDI (subcontractor default insurance). However, when we went to audit the actual cost of such insurance and to verify that the insurance existed, we were told that there was no policy at all. The CM had self insured all of the risk, rather than having a large deductible as in SubGuard. While the Owner has the protection of the GMP in these cases (meaning even if there is a sub default the maximum amount the Owner can pay is the GMP), we wonder how many CM's are doing the same thing and pocketing about 1.2% of the subcontract values from unsuspecting Owners.

Our advice is to require the CM to prove that the subs and PO's that they are billing you SubGuard (or SDI) for are actually enrolled in the SubGuard program. The same thing can go for sub bonds. Before you pay for a sub bond, get the CM to show you the bond itself.

Should all Insurance Deductibles be included in Fee?

The true value of an insurance deductible can be extremely difficult to determine. Actuarial assumptions or recommendations from insurance companies and agents can be manipulated. In most situations these deductibles are related to GL insurance, but W/C insurance can also have large deductibles also. In fact, it is common that a CM will attribute over half of their GL cost to the value of the deductible. Since we regularly see CM asking for 1.2% to 1% for GL, you can see that up to .5% of the total contract amount is subject to value that is somewhat arbitrary and certainly biased.

One of our clients has sought to take this impreciseness out of the negotiations by stating in their contract that all insurance deductibles are not reimbursable. A CM with a large GL deductible may, therefore, end up having a higher fee but a correspondingly lower Cost of Work. Some CM's may elect to buy down the deductible for a given project. Buying down the deductible requires that the CM purchase additional insurance. This insurance premium is reimbursable. On one project this year for this Owner, the CM had originally asked for .4% to cover their GL deductible risk. The GL actual deductible buy down policy cost only .1%. Therefore, the Owner saved .3%, or \$210,000, on a \$70 mil. project.

What is needed to arrive at a GMP?

On two different projects this year we ran into a CM who had intended to establish an initial GMP with the electrical and mechanical subcontractors and then ultimately convert these GMP's to a lump sum after all of the design documents were fully completed. The reason for entering into a subcontract before the documents were complete was that the CM wanted to get the subs input on design issue and some work needed to start prior to drawing completion.

This scenario probably does not seem unusual to most of you, and while this is somewhat common, we would be concerned that the

conversion of the GMP to lump sum would be accomplished only if the Owners' interests were best served by this conversion. After all, if we have a GMP, why would we convert to a lump sum for the same price? But on these two separate projects with different CM's, we had other problems, one of the CM's never asked for the subcontractor's fee, just their GMP. On the other project, the CM asked for a fee % but never defined what the Cost of Work was or wasn't.

Many Owners want to let the CM control the process as much as possible and they do not want to be too meddlesome, but asking a few questions of your CM might be good, because as you can imagine, it is hard to have a GMP without the fee or Cost of Work defined.

Retirement of a CCM Original

One of our original members, David Butler, retired in September of 2011. Dave worked with some of us at Trammell Crow and then came over in 1992 when CCM was formed. Most of our clients have had Dave on audit assignments, but because some of us took the more vocal roles, few knew how integral and important Dave's role was on each project. Imagine a person in your organization that can do everything and in most cases better and faster than you could even fathom it could be done. That was Dave to CCM. Since we first met Dave in 1988, we have been constantly asking for another Butler, someone who could do what Dave did. Unfortunately, 24 years later, we are still searching for another one.

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