

BEST PRACTICE

RISK MANAGEMENT FOR OWNERS: NINE STRATEGIES FOR EXCELLENCE IN THE CURRENT CONSTRUCTION CLIMATE

BY CHAD A. WISSINGER, ESQ., BRIAN P. MALONEY, P.E., ESQ., AND JULIE A. PATER, ESQ.

Background:

Virtually every sector of Western Pennsylvania's economy is under construction. Whether it is new highways, infrastructure upgrades, office space, medical facilities, educational buildings, massive commercial/industrial plants, or housing, Pittsburgh is in the middle of a five-year trend line for total construction dollars where each successive year is the single biggest year on record. Jeff Burd noted in this magazine one year ago that virtually every union trade in Western Pennsylvania was operating at full employment, with several using travelers. Since that time, more projects have been announced than the four-plus billion dollars' worth Jeff predicted last January. Dollar Bank confirmed as much in the November/December 2018 issue of *Breaking Ground* when it concluded that Western Pennsylvania will have completed \$5 billion worth of construction projects in 2018 – a number that has never been done before.

Historically, when a building boom strikes one region, travelers fill the void. But for anyone paying attention to the national economy, the solutions this time are not so simple. Going back to their 2016 surveys, The Associated General Contractors of America (AGC) raised a host of interlocking issues that should put owners on notice. The AGC wrote that skilled craft labor shortages will continue for the foreseeable future, and are occurring in virtually every region of the country. In addition, the AGC found that knowledgeable, experienced, life-long craftspeople are retiring at paces that require massive recruiting of young employees into work that takes years to master.

The AGC summarizes nicely:

"Our study findings show that the current construction risk environment is vastly different compared to just five years ago. Owners are putting more pressure on project costs and schedules while modifying contract terms to place greater risk on all contractor levels. At the same time, contractors are winning more work and staffing projects with less skilled labor and fewer experienced field supervisors. Combined, all of these factors are adding unprecedented risk to field productivity, work quality, safety, and working capital."

In addition to labor woes, owners will receive less favorable pricing through 2019. Contractors will be more selective pursuing work, and fewer contractors will pursue any individual project. Accordingly to Archinect.com, steel tariffs will add between a 0.5 and 1.0 percent price increase to virtually any new project on structural elements alone, with short-term

supply bottlenecks leading to increasingly long lead times on already long lead time items. The tariffs on aluminum and steel will also have adverse cost impacts on everything from duct work to roof top chillers for those same projects, though the full impact is wholly unknown at this point.

So, what's an owner to do?

Spend time planning/pricing/programming:

Owners understandably are anxious to turn the first shovels of dirt on any new project. Once property and funding are secured, it seems as if demolition, site work, and foundations should immediately follow. The need for rent rolls, condominium sales, or new students drives the schedule. Unfortunately, the biggest claims we see are caused by failures in the early stages of a project, when the owner, more than any other party, is making critical decisions. Although not exhaustive, examples include the failure to adequately explore project site conditions and plan construction schedules accordingly; the failure of setting budgets too early in the design phase, and the failure to clearly, and timely, define the project's program.

Collaboration reduces risk:

Collaboration by all project stakeholders from the earliest possible stages through project completion is strongly encouraged. If the construction manager and/or general contractor can be identified during the programming phase, their input could prove valuable in terms of managing costs and avoiding mistakes. The simple act of scheduling regular meetings, and requiring key personnel to attend, can result in ongoing conflict avoidance on issues an owner might not have even considered.

Have a clear contract, but be fair, or pay:

On this point, the authors are liable to get a little pushback from owners. Conventional legal wisdom usually dictates that the party with the most influence, usually the owner holding the funds, dictates the most stringent contract possible. That goal can have adverse consequences though, particularly if the terms being demanded are "over the top." For one, many trades will build in buffers to all pricing as a defense mechanism. It might be better to incentivize key project stakeholders through sharing the leftover funds of a contingency, rather than attempting to craft an impossibly one-sided document coming out of the gate.

Excellent Scheduling with Interim Milestones:

By way of example, the standard AIA form contract between an owner and Designer provides dates only for the anticipated start and completion of construction. Much like the new college student able to put off his or her entire semester's work until two weeks before the final, using the "full credit at the end" system serves no one's best interest in construction. By including crucial milestones in the schedule, all sides are kept honest, including the owner. Moreover, these milestones should tie both to time and expenditure of funds. If coordination is key, and mandatory meetings force coordination, then working toward interim milestones further serves to focus the group toward the next most important goal. It also sets up an owner's defense against future total cost or total time styled claims, by forcing all parties to admit that milestones were met, or explain early and often exactly why any particular milestone was missed.

Go out of your way to insure quality supervision:

Given the labor issues discussed above, it is not enough to simply hire an experienced CM, or a well-reputed general contractor. The actual personnel those entities put on a project matters much, much more than owners frequently realize. It is of little help to an owner who goes out of his way to hire an independent scheduling firm if it turns out that the person doing 90 percent of the work has never worked on a large project before nor has any experience corralling the sometimes challenging personalities in this business. Clients will often tell you in the legal world that they hire lawyers, not law firms. Many owners fail to take the same approach when it comes to personnel on their projects.

Safety Matters:

According to the OSHA Fact Book, construction jobs account for seven percent of the U.S. economy, but 21 percent of work place fatalities. According to the National Institute of Occupational Safety and Health, "(c)onstruction workers already suffer the highest number of fatalities in any U.S. industry. But the death rate among construction workers 55 years and older was nearly 80 percent higher than that of construction workers under 35 in 2007. And like the rest of the workforce, the average age of a construction worker is rising." Not surprisingly, immediately after older construction workers, the most likely segment of people to be injured on a construction site according to the Bureau of Labor Statistics are workers with less than one year's experience. Those individuals cause 34.9 percent of serious construction industry injuries. When you put the demographics of the Western Pennsylvania construction force together, a large portion falls into the two most dangerous categories for workplace accidents, at a time when literally every member of every trade will be actively employed.

Chuck Yorio, a safety expert and Principal at EPIC Insurance, says that the more time all parties involved spend planning to avoid safety issues, the better off everyone on the project will be. Although many owners tend to think of jobsite safety as not their issue because ultimately they may not hold specific responsibility, Chuck reports that the fallout from any incident can cause significant potentially negative press, schedule delays, and significant time in litigation, just to name a few adverse consequences. As such, while it is always important to evaluate why something happened after the fact, owners would be well-served by making sure their partner contractors front load effort to ensure that all risks are minimized.

Engage in exhaustive ticking and tying:

The act of ticking and tying, or "truing up" inventory to purchase orders, for example, is accounting 101. But for owners, particularly ones without significant construction experience, ticking and tying documents may seem not worth the time. Unfortunately, after a default notice is drafted, it is too late to confirm if a subcontractor had executed its contract, provided appropriate proof of third-party insurance coverage, etc. Kurt Karstens, Chuck's colleague on the insurance side at EPIC noted that, depending on the project duration, many if not all designers, contractors, and subcontractors will go through at least one insurance renewal period during a large project. Appropriate updated information is almost never obtained at this juncture.

Comprehensive insurance program:

Every owner should engage in a thorough insurance analysis well in advance of the start of construction. Not only can such an analysis help an owner determine what levels of coverage should be requested of each player for a project, but Kurt Karstens also noted that frontloading the insurance analysis will allow owners, on larger projects, to timely consider comprehensive insurance remedies like Owner Controlled Insurance Programs (OCIP). OCIPs will protect against any potential individual insurance lapses on a project, can be very cost-effective, and permit centralized claims control, among other benefits.

Be vigilant:

As we dissect the "what went wrong" on project after project, it becomes clear in every complex series of relationships that everyone's attitude is positive at the beginning. Owners often permit this fact to lull them into a false sense of security. The reality is very different. If an owner does not actively work to maintain a team mentality, and is not in constant communication with all the key stakeholders, any number of small issues can grow large enough to derail a project. On the most contentious projects we see, rarely is there a single issue that creates

litigation, but death by a thousand cuts is the norm.

Owners should not simply entrust their designer to review and sign off on pay applications. The designer can be a key component to review, but a vigilant owner should not be afraid to make clear early on a project, by withholding some portion of a payment pending completion of a recovery schedule, for example, that scheduling milestones are to be met. It is also critical to insure that lien and claim waivers are executed monthly, and by all contractors, subcontractors, and suppliers.

Parting shot:

Western Pennsylvania has a relatively tight knit and somewhat collegial construction industry, across many trades and professions. Owners are well-served to capitalize on this in an effort to actively steer their project to final completion. The worst thing an owner can do is turn over the keys at groundbreaking, and hope for timely completion. **BG**

Chad Wissinger, Brian Maloney and Julie Pattter are attorneys with Cohen and Grigsby, P.C.