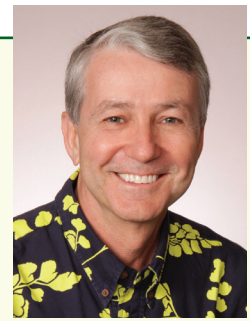


Change Orders: *Profit Centers or Profit Leaks?*



BY GARRETT SULLIVAN

Change orders can be your company's best friend or worst enemy, depending on how you manage them. That's why I recommend using a standard, rigidly enforced policy. Without one, your profit on the job will quickly evaporate. Additionally, you may have to chase down payment after the job is completed. This is the worst possible negotiating position since your extra work is already completed and the owner's budget may already be spent.

As you know, all contracts state "no extra work shall be completed unless the additional work is requested and approved in writing." The reality is that contractors and subcontractors alike often get wrapped up in completing the job and lose focus on profitability. Extra work is time consuming and costly considering the many steps involved: identifying the extra work, pricing it out, getting it approved, ordering material, completing the installation, etc. Additionally, there are hidden costs – schedule impacts, engineering time, additional non-permitted general condition costs, consumables and other factors.

Some contractors just absorb the costs, reasoning that their longtime clients do not like being "nickel and dimed." Other contractors have developed a mindset that government ordered force account (extra work known as time and material in private work) is just not worth the time to prepare all the paperwork and it's simpler to just do the extra work pro bono.

Let's take a look at the cost of

this attitude. If Kimo Construction plans a 3 percent profit (which is the national average) and there is a \$20,000 change order that includes \$1,200 profit, Kimo Construction would need to win and complete a new \$626,666 job in order to recover those costs. The cost of the extra work (\$18,800), less the profit (\$1,200), divided by 3 percent profit equals \$626,667. In today's hyper-competitive market, the prudent contractor will be certain that all extra work is documented and approved by the owner or general contractor (GC) before it is started.

Below are eight guidelines to help you get paid for extra work:

Before Work Begins

1. The most efficient way to make change orders profitable is to tie it to your employees' compensation and bonus structure. It will become an immediate priority.
2. In your pre-work briefing, ensure everyone – from the foreman level up – understands the specific scope of work your company has contracted to perform. If field personnel thoroughly understand their scope of work, they will quickly recognize what constitutes extra work.
3. Insist that no extra work may start without written authorization from a person with the authority to bind the owner or GC. At a minimum, this should be a field order.
4. Establish cost ceilings at which field personnel cannot proceed without higher approval.

Once on the Job

1. Insist that everyone use the correct forms (e.g., extra work notification, request for change order pricing, etc.). Keep change order logs and retain pictures and video in the event of a claim. Remember, without written notice for extra work (usually a very short time period), your claim for extra work may be forfeited under the contract.
2. Identify and budget the extra work as it occurs so it can be tracked for its profitability contribution to the project.
3. If you do not receive a post contract drawing, which clearly requests extra work pricing, follow a strict system of procedures to identify the extra work as it happens in real time.
4. If you are unable to stop construction due to the nature of the work, immediately provide written notice to the owner/GC, document the work with photos or video and track your costs with a signature by the owner's inspector each day. Obtain a field order from the owner/GC on the day the extra work occurred and submit pricing as soon as possible.

Remember, you, as the contractor or subcontractor, set the stage on how well you understand your scope of work. Avoid the tendency to wait until the end of a job to settle up, as you have already lost your advantage to be paid. If something is changed from the contract, it will get paid for if your team properly manages procedures for extra work. **BI**

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