HOW TO GET QUALITY COMPLETION ON TIME?
By: Bill Preston

In Western Canada's construction demand market (owners want more done faster than contractors can supply), this has certainly become a dominant challenge. In Alberta and Saskatchewan, as measured by dollar value, the industry is expected to annually fast track nearly twice the value of projects with ten percent fewer experienced site supt's and foremen than was the case ten years ago! What incentives can/should an owner choose to be sure that their project is not dragged out beyond the expected/required completion date? Traditionally, owners have relied upon contractual penalty clauses. Indeed, the City of Saskatoon incorporated the below penalty clause together with a performance holdback clause into its design-build contract for the Saskatoon South Bridge project, which is now forecasted to be ten months delayed, namely:

> "If the Contractor fails to achieve Traffic Availability on or before the … Target Date, then … the City shall have the right to set-off … amounts owing to the Contractor … of ($10,000.00) per day as liquidated damages for late Traffic Availability for each calendar day between April 1st and October 31st inclusive annually or part thereof between the Traffic Availability Target Date and Traffic Availability."
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> "If … the Contractor has not achieved Construction Completion … the City may hold back an amount equal to two (2) times the cost, estimated by the City acting reasonably, of achieving Construction Completion."

As the Lac La Ronge Indian Band harshly learned and as Saskatoon's Mayor now appears to recognize by his public statements, "We'll negotiate," penalty clauses supported by a performance holdback clause are no longer a perfect incentive in our construction industry. In the Lac La Ronge v. Dallas Contracting Ltd. Case, the Band announced that it critically required completion of a new sewage lagoon before winter conditions and thus, it included in its Bid Documents a penalty clause to motivate Dallas' completion by November the 12th, 1996, but by November 12th, Dallas was nowhere near completion and its Work which had been performed have serious defects! What was the Board to do given the unpaid balance of Dallas' Contract Price was at least $250,000.00 short of the Band's anticipated costs to terminate Dallas and hire a substitute to finish the project next spring? The Band chose to terminate Dallas and look to Dallas' performance surety to pay both its delay costs as well as the replacement contractor's completion costs. What the Band actually experienced was:

- For eight years, it had to finance all of the resultant costs while the case made its way through the Saskatchewan court system;
- In Court, Dallas defended by arguing that the Band's consultant had caused the delay, not Dallas; and
- In Court, the surety argued both that Dallas was wrongfully terminated and, in any event, the performance bond excluded responsible for the Band's delay costs.

Also, the Band experienced that, during the eight-year court process journey, Dallas had become insolvent with insufficient assets to cover any of its responsibilities to either the Band or to the surety. At the end of this legal journey, the Band found:

.1 Penalty clauses are not a perfect incentive for timely completion;

.2 The law gives contractors many arguments (e.g.: not my fault; owner failed requisite notices; daily penalty amount is unreasonable) to weasel around penalty clauses; and

.3 The Dispute Resolution Clauses (in this case, the court system) gives the contractor lots of opportunity to become judgment proof while most performance bonds are written so that the owner's delay claim is inferior to the surety's claim against the owner for all of the unpaid contract price performed by the defaulting contractor.

What else has been tried to assure that the contractor timely completes your project, and what has been my experience with these alternatives?

1. A SITE LEASE/LICENSE FEE

For an earlier project, the City of Saskatoon included a contractual clause which required that the contractor pay a daily site rental for access to the construction site to perform work after the completion date, and the contract also linked this provision to a clause permitting the City to set off these rentals against the unpaid Contract Price. Did this incentive work? No. Again, this was a civil works project where the schedule was actually 150% of the initial project completion forecast. Now, the City of Saskatoon did not go to Court; rather, it negotiated. Thus, I was not able to find any court decisions which decided whether this form of a penalty clause would checkmate a contractor's complaint that the City had caused the delay and thus, the rental was not payable. My research is that at the bottom line, I doubt that this attempt by the City of Saskatoon would have checkmated all of the difficulties which the Lac La Ronge Band had experienced.

2. BID DOCUMENTS WHICH ACCOMMODATE SPEC'ING CONTRACTORS' PROJECT LEADERSHIP

This alternative is based on the wisdom that if the project is being performed by a contractor, project manager, and site superintendent/foreman with a reputation for timely performance of quality, experience persuades that this is the owner's best chance of getting what it requires. To use this alternative, what owners have done is they have modified their procurement documents so that:

- If the Project is a Design-Bid-Build, the owner's privilege clause permits it to ignore the lowest bid and award to the bidder whose reputation and named project manager and site supt in the supplements of the bid have the most satisfactory history; and

- The Construction Contract also requires that these names proffered by the bidder in its bid form supplements must exclusively work on the Owner's project and they can only be changed by a written change order signed by the owner, thus giving the Owner a timely opportunity to assess and negotiate the scope, price, and completion time.

Yes, the standard of "exclusive commitment" certainly can invite disputes, but most construction contract language requires that these disputes be, in the first instance, resolved by the owner's consultant. So while my experience has been limited, these contractual provisions give the opportunity to, as early as possible, assess and negotiate. On the other hand, of course, if the owner must select the lowest compliant bidder (I'm thinking of Governments), this alternative isn't available.

3. BONUS CLAUSE

I've seen a number of bonus clauses (CCDC has a standard option for bonuses), but the alternative which I recently witnessed is found in an Integrated Project Delivery Agreement. The Agreement which I witnessed was incorporated into the Contract language for a new hospital construction project in Saskatchewan with a 20-month construction schedule. I'm still watching to see whether it works. The scheme of this contract is persuaded by the wisdom that too much productivity is lost and thus, construction schedule is wasted, when all of the participants on a project minimize communication, see their role at the project as a silo and bring with them the attitude of: To hell with what happens to the others. Basically, the contract tries to checkmate this silo mentality with the following:

- The owner only pays for completed milestones;
- The value of each milestone does not encourage front-end loading of the project's budge price;
- These milestone payments cover only the verifiable direct costs of the designer, general contractor, and major trades;
- For owner changes in work, the price adjustments will include ripple effect impact costs to the productivity of the designer, contractor, and major trades;
- A 15% bonus/profit fund is payable only upon completion, and the owner has a first claim to deduct all of its budgeted overrun costs and its delay costs;
- And, only then, is the balance of the 15% bonus/profit fund divisible among the designer, general contractor, and major trades according to their originally agreed shares adjusted by the degree to which they're responsible for delays or overrun costs suffered by the owner or others in the pool.

What I noticed is that if the owner's overrun costs and delay costs exhaust the 15% bonus fund, then the designer, general contractor, and major trades make no profit! Also, if there's not enough money in the 15% profit/bonus fund to cover all of the owner's overruns and delay costs, then the owner eats the excess. It's a glorified holdback scheme; but, while it's not been legally dealt with by the courts, my initial opinion is that the owner's claim for overrun costs and delay costs will likely trump the unpaid lien claimants' entitlement to any more than 10% of the direct costs. Also, these clauses seem to be a good incentive for everyone to optimize everyone's productivity and communicate early. The short-coming with this alternative is that the direct investment in preconstruction negotiations and monitoring/negotiating throughout the

performance of the project means that the direct costs must be more than $45 million. It doesn't work for small projects.

4. PERFORMANCE HOLDBACK

Where the project budget is less than $45 million or where the owner must select the lowest bidder regardless of its reputation for quality on time, I've recommended the below supplementary general condition as a performance holdback term which is intended to assure that all of the participants on the project have substantial skin in the game until completion, and my experience has been that this term does not seem to attract higher pricing, namely:

> No statutory holdback will be paid until the contractor is substantially performed; while, until the *Work* is 95% performed, the amount claimed shall be for the value of the *Contract Price,* proportionate to the percentage of *Work* performed and *Products* delivered to the *Place of the Work* at that date. Thereafter the amount claimed and certified shall be for the amount of the *Contract Price* less the reasonable costs for a qualified and alternate contractor to complete all the deficient *Work* and *Products* not delivered to the *Place of the Work* at that date.

5. CONCLUSION

1. I'm not a fan of penalty clauses because it's well-known in the construction industry that the contractors can weasel around them.

2. I like the bid documents alternative, particularly where it gives the owner an opportunity to assess the reputation and resources (does the contractor validly use a CPM schedule) for timely completion, but some owners don't have the requisite bid evaluation discretion to use this alternative.

3. I expect that for project budgets greater than $45 million, the Integrated Project Delivery Agreement will have all the right bells and whistles, but I'm still in the wait-and-see phase.

4. Otherwise, all that's left is a performance holdback term supported by a payment certifier who does not buy in to the wisdom that they can buy harmony on the construction project by certifying the contractor's front-end loaded payment applications.