

Bulletin

The Official Publication of the Washington Building Congress | May/June 2010

Feature Article

Project Cost Management Best Practices for Minimizing Claims, Cost Overruns and Other Project Risks

by William M. Kerns, CCIFP®



William M. Kerns, CCIFP®, is a director and expert witness with The Duggan Rhodes Group, a boutique construction consulting firm based in Pittsburgh, PA, with US and international clients. With more than 25 years in the construction industry, Kerns specializes in the calculation of delay and disruption related

damages, construction cost accounting systems consulting, financial reporting consulting on construction projects, and expert testimony.

Many construction professionals recognize that a competent project cost tracking process and system is essential to avoiding and reducing project risk. In this time of increasingly competitive bidding and razor thin profit margins, it is even more essential that your systems help in understanding how your project dollars are being spent. Moreover, it is just as important to define a process for timely recognition of cost overruns, so that recovery can be timely requested via change order or a claim if applicable. A few items for consideration when implementing a cost tracking and monitoring process follow.

1. Your Project Cost Accounting, Project Schedule and Project Records Should Tell the Same Story.

When trying to achieve maximum recovery of a change order or claim, it is essential that the costs incurred and the entitlement to recover such costs are well substantiated. This is best established by discretely demonstrating through the schedule, project documentation and project cost system how a contractor was impacted and the costs incurred as a result of the impact. This substantiation can be more readily provided when a systematic process for discretely tracking project progress and impacts is established and followed through the project documentation, the project schedule and the project cost tracking system. When such a process is established, the time and effort needed to substantiate a claim or request for equitable adjustment is significantly reduced. A way to ensure consistency between the project cost accounting system and the project schedule is to establish project cost codes consistent with the schedule's work breakdown structure (WBS). In the event of an impact to a schedule activity, the schedule may be used to demonstrate the effect of the impact relative to time. Similarly, establishing a cost code / WBS correlation may assist in demonstrating the additional costs incurred as a result of the impact to a discrete scope of work or activity within the schedule.

2. Project Costs Should Be Tracked Discretely.

As discussed in item 1, project costs associated with specific scopes of work should be tracked discretely. This process can assist with the timely identification and quantification of cost overruns or damages if a particular scope of work on a project is negatively impacted. However, project cost codes should not be so detailed as to impede accurate labor coding of activities in the field; simple, straight-forward cost coding in the field is critical to ensure accurate cost

tracking. For example, instead of separate cost codes for forming, reinforcing and pouring of concrete for a sidewalk, it may be more useful to set up one cost code to track “Sidewalk Installation” in total, as a system. If “Sidewalk Installation” is being performed in different areas or phases of a project, individual cost codes for each area or phase may be established to track the cost and quantities associated with the activity in each area separately. This type of cost tracking may prove to be beneficial if a scope of work in one area is adversely impacted but not in others. The resulting comparison of the impacted work to similar scopes of work in other areas can serve as a basis of comparison for a productivity or loss of efficiency analysis.

3. Segregate Costs for Out-of-Scope Changes.

Segregating out-of-scope changes from original contract work is just as essential as discretely tracking original contract costs. This can be accomplished by setting up a separate cost code prefix for change orders. For example, a cost code prefix outside the Construction Specification Institute’s Master Format divisions 1-49, such as 99, can be selected to track change orders, with the remaining digits tracking individual scope changes. Using this designation, costs associated with change order request 001 may be tracked to cost code 99-001. The benefits of discretely tracking change order costs include identifying actual costs of changed work and establishing the basis for substantiating the costs if requested by the owner under an audit clause, or in the event of a dispute. Segregation of costs also keeps the true cost of original scope items pristine because scope and out-of-scope costs are not co-mingled, an important concept in the event that a productivity analysis is required for an in-scope item. Furthermore, a proper change order cost monitoring process will help contractors monitor unrecovered change order costs and avoid a situation where unrecovered change orders erode cash flow on a project.

4. Track Productivity and Use It as the Basis to Project Estimated Total Cost.

By tracking and reporting installed quantities along with the related discrete project costs, contractors can readily track productivity and use it to project the estimated total cost for each labor-related cost code. The benefit is that your cost report can provide you with timely early warning of potential cost overruns, or claims, while you still have the time and budget remaining on the project to address, and hopefully deal with, the issue. Also, discretely tracking quantities and costs can provide a basis for demonstrating loss of productivity if a particular scope of work or area is impacted on the project.

5. Know and Understand the Contract Requirements for Requesting Additional Costs and Submitting Claims.

When a project cost tracking mechanism is implemented, the contract requirements for requesting additional costs associated with change orders and claims should be understood and considered. Contractors should consider reviewing the contract requirements and potentially adapting their cost management procedures to insure the most effective recovery of change order costs and claims within the context of contract requirements. Negotiating more favorable contract terms can also help better match a contractor’s cost tracking procedures to the contract requirements. Additionally, in understanding the terms of the contract, it is important to note different types of changes or claim requests (e.g., force majeure, design-related, owner-caused, etc.) may call for different requirements under the contract.