

The Developer's Dream

Fielding the Dream Team



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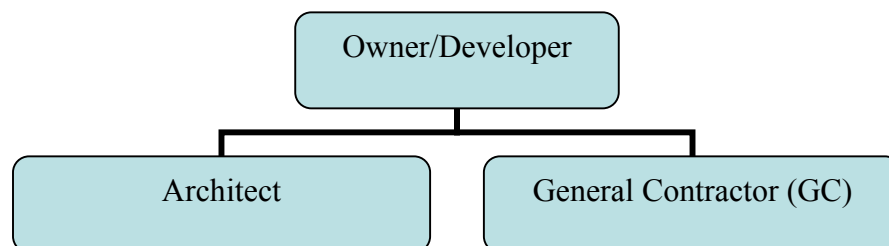
This paper examines the considerations that arise in pursuing the developer’s dream, from the viewpoint of assembling the dream team. The criteria for selecting the proper team players will be the development experience, construction expertise, and goals of the developer. The section dealing with large developers examines multiple contractors and construction management. Design/build contracts, and their pros and cons, are addressed in the small developer section. Fast track projects, and another perspective on design/build, are discussed in connection with non-developers, e.g., a doctor building an office for her practice and the neighbor building an extension or doing a renovation. The considerations are the same whether the developer is large or small, or whether the owner is not a developer at all.

Different Clients, Different Perspectives, Different Answers

Development clients who have a track record of successful projects, in-house engineering and architectural expertise, budgeting experience, inspection capabilities, and general knowledge about building, need different advice than a medical professional who is building a new office. The difference is not in *how much* advice each needs, but in *what kind*. The sophisticated developer wants to do more complicated things, or the same things in new ways, in order to save money; your advice helps to channel that desire. The unsophisticated developer hears about how she may save money by *not* using a tried and true technique; in that case your advice has to explore whether the specified technique REALLY works. In other words, the question remains the same, but the answers change depending on the client.

The Traditional Model

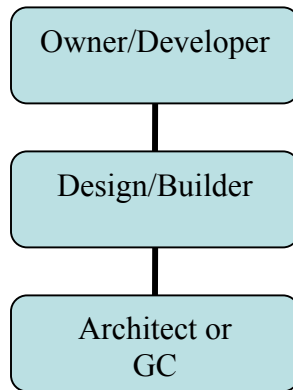
The short description of this program refers to the “required” design professional and a contractor. However, the dream may be achieved without the developer hiring a design professional, or may involve more than one contractor. Often a discussion of the engagement of construction team members, and their relationship to one another, is accompanied by diagrams. The traditional or typical model is as follows:



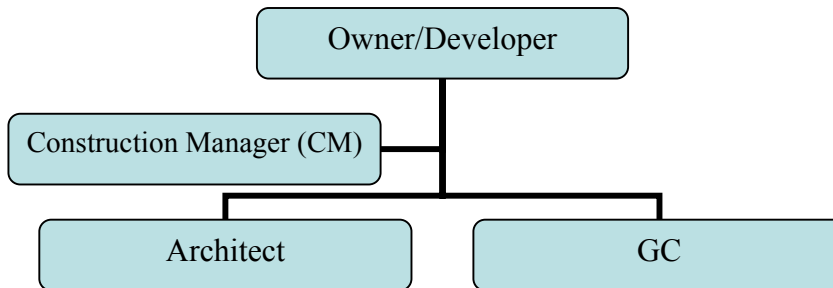
Some Alternate Models

The dream team members can be arranged other than as shown in the traditional model. Common variants include design/build and construction management, which can be visualized as follows:

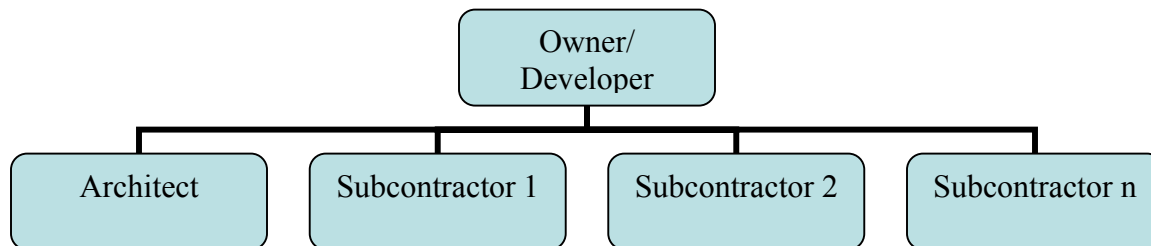
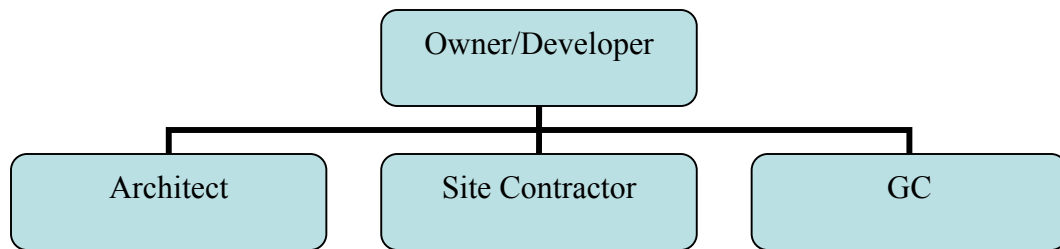
Design/build:



Construction management:



We will contrast the traditional model with those common variants, and with fast track projects (which can take the form of any of the models) and the following additional models reflecting direct engagement of subcontractors:



Analyzing the Models

The team members selected by the developer should reflect the needs, actual or perceived, that the developer anticipates requiring during the project. Those needs vary by the sophistication of the developer and the project, as well as the constant goal of saving money.

I. The Big Time Developer:

The sophisticated and large developer wants to save money. Sometimes this is phrased as “saving time.” Time usually translates into money. Time also implies “fast track” construction. Fast track construction will be discussed in connection with the non-developer, i.e., an owner not in the development business, building for its own use. Typically, larger developers engage design consultants and contractors, and consider it a cost of doing business. They hire these parties using their own developed-over-time documents or commercially available form documents with changes they have worked out over many transactions. Large developers tend to use team members repetitively, with structures or relationships between team members falling into patterns established by that developer. These clients come to you with inquiries about ways to save money or time by doing “something different.”

A. Saving Money with Additional Contractors. For example, why pay the general contractor to do everything if you can do some of the work “yourself.” We all know that the general contractor marks up the costs of the separate subcontractors. Can’t the developer hire

the subs directly, and save the middleman's profit? This answer is certainly yes, but at what risk?

Hiring all the subcontractors directly is an extreme position, and not one that sophisticated developers usually employ.¹ Their business is development, and they are familiar with development risks. There are different risks in pursuing the construction itself. One of these risks, and a major one, is that of coordination. If the developer is responsible for line item 1 or line item 17, the timing and quality of that work has ramifications that impact all subsequent steps. If the subcontractor has dropped the ball on step 1 or step 17, the developer not only has no recourse for that mistake, except against the subcontractor responsible for that piece of the work, but the developer may be liable for the added costs and delays of all the contractors and subcontractors doing the later steps of the entire project. It is the rare subcontractor performing line item 1 or 17 who will agree expressly to be liable for the additional costs of all the other contractors and subcontractors of the entire rest of the project. Even if a subcontractor were to undertake this risk, most are not strong enough to be able to live up to such a liability.²

B. Saving Money with One Additional Contractor. Developers in the single family housing field often engage the site work contractor directly. Many such developers do their own construction, but do not have the expertise to do site work, and have not invested in the equipment with which to do it. Once the site work is complete, the land value is significantly increased, and the single family home developer can sell off portions at a profit and keep the rest to build out itself. For such developers, site work can be viewed as a separate construction project, especially when the schedule for all of the rest of the houses does not follow immediately on completion of the site work. The developer can reasonably conclude that it does not pay to hire a general contractor to accomplish the site work because all that would do is add the mark up of the GC to the cost of the job.

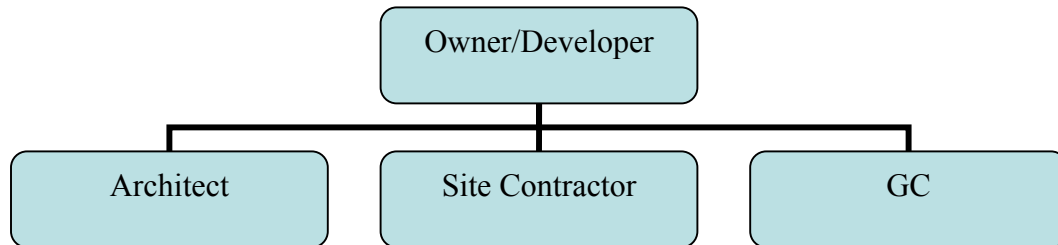
The developer of an office park, mixed use residential and retail project, or shopping center may come to the same conclusion, but with a bit more risk. Since site work is a substantial cost, the potential gain is the sizeable GC mark up on the site work contract. The down side is that in these examples of construction, the rest of the project is usually scheduled immediately upon completion of site work, and often starts on one portion of the site even before the site work is completed on the remainder.

Since the site work contractor is the first contractor on the site, half of the timing risk (someone else delaying this contractor's start) is removed. The other half of the risk is that if the site work is not completed on time, the GC doing the buildings will not be able to start on time. Site work contractors cannot avoid the risk of weather delays. On the other hand, site work contractors can often direct more manpower and equipment to a job, without causing obstacles to other trades, in order to meet a deadline. Site work contractors are often substantial

¹ Construction by State governmental units is often required to be in "multiple prime" format, i.e., separate, direct contracts with the major trades.

² Experience with multiple prime construction has led to various efforts, even by State related entities, to AVOID this requirement whenever possible precisely because of the coordination effort and risk that would fall to the State if it does not have a general contractor to manage the job.

enough to be able to shoulder the cost of a delay and related damages they may cause to the entire job (or substantial liquidated damages). A diagram of this team would be as follows:



If the developer wants to pursue this dollar saving approach, someone must be substituted for the GC’s oversight function and responsibility. If the developer has that expertise in-house, then carving out this subcontract from the larger general contract can make sense. Similarly, if the developer can purchase this expertise through the architect or a construction manager, for less than the GC’s mark up, the same result can apply. Even with this in-house or purchased expertise, the developer needs an appropriate level of confidence in the site work contractor.

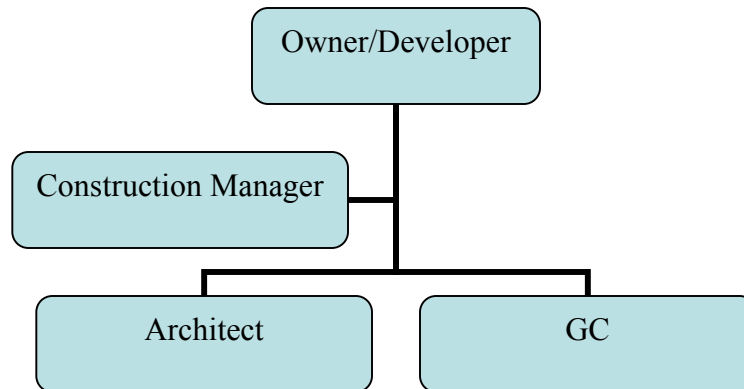
C. Saving Money with Construction Management. Not long ago, construction management was the hot, new, sure-fire way to bring in projects on time and under budget. It added value engineering, better management, and no additional employee overhead to the developer. According to the CM’s, this technique *saves* money, but at the very least it *does not add* to the cost of the project.

It is instructive to recognize that architects and contractors scrambled to call themselves construction managers, and packaged the value of all the other things they could do for a project (after “beating up” the project architect and GC to keep costs down) under the rubric of construction management. For example, the AIA form architect agreements have lists of additional or extra services, for extra payment. Some services are preceded by the phrase “If requested by the Owner”³ or contemplate later changes to the contract.⁴ CM’s offer to provide the very services already available in the agreement with the architect.

The picture for the construction management model of services is below:

3 See Section 2.5.5 of the current form AIA Document B141 - 1997 Part 2, Standard Form of Architect’s Services: Design and Contract Administration. The AIA Document B151 - 1997 Abbreviated Standard Form of Agreement between Owner and Architect provides for services beyond basic services, contingent additional services, and optional additional services in Section 3. These are “only ... provided if authorized or confirmed in writing by the Owner” (Section 3.1.1)

4 See Section 2.8 of the AIA Document B141 - 1997 Part 2, Standard Form of Architect’s Services: Design and Contract Administration.



In this diagram, picture the CM whispering into the developer’s ear. If the large developer has the in-house expertise, that person (or group) can do exactly the same thing as a CM. Recognize, however, that in such large organizations, the people who have this expertise are frequently pulled in many directions, and management can direct attention away from any particular project at the critical moment that project requires all the attention a CM would have paid had he/she/it been hired. Another way to look at the CM relationship is the fact that an outside architect holding out its CM services implies that the project architect could do the same thing. The same thought process applies for the outside GC who is a possible CM.

The developer must decide if it is willing to bring another team member on board for the sole purpose of having a different perspective. On complex projects, the in-house people cannot be assured that they will have the time to study or comment on, or to garner the political support within the organization to question, the design and construction means and methods of the paid, outside team members. In those circumstances, a separate CM can make sense by providing another pair of eyes, without vested interests in what is on paper already.

There is no question that a second pair of eyes is beneficial. A knowledgeable attorney reviewing a document that has been created from scratch will usually give insightful, substantive, beneficial suggestions. So, too, can a design professional or experienced builder make a contribution to a construction project. From construction management agreements, as well as a Construction Management Association of America trade association support this aspect of the industry. But, while the cost of the CM service may be quantifiable going forward, the benefit is not. On larger projects, the design enhancements (not necessarily “look” or artistic aspects) and value engineering from a fresh perspective may outweigh the cost for a construction manager’s rates; that is the quintessential business decision. On smaller and less complex projects, the likelihood of such benefits decreases.

Whatever the size of the project, the CM is not usually hired full time to guide the developer in all aspects of the project. Therefore, the CM will propose a limited menu of services. After the sales pitch, the need for each aspect of such specific assistance needs to be reviewed.

Construction management is no longer the unequivocal way to proceed. Despite the theoretical benefits of the second pair of eyes, after the architect and contractor have been selected, the developer or owner does not usually want to contract with someone else, thus complicating the arrangement with the architect and GC. If the developer needs extra services, sometimes the architect or contractor simply does it as part of the job. Sometimes they charge for it. Sometimes the requests for the added work are documented. And, sometimes there are disputes.

The allure of the extra care that the CM could bring to the table even resulted in a joint AIA/AGC hybrid document. The “A121 CMc 2003 and AGC Document 565 Owner - Construction Manager Agreement” reflects the added care and value that construction management contemplates, without the fourth party added to the team. This form contemplates a construction manager who is a GC being engaged for the planning phase, to work with the architect. After the planning phase there is an opportunity for the resulting plans to be bid on and performed by someone other than the CM/GC involved in the planning. The opportunity for someone else to be the successful bidder is not the expectation. Other bidders have such a significant disadvantage in their knowledge of the project, compared with the GC who is involved in the plans, that the process is rarely taken to the point of even seeking other bids to do the work.

D. Clerk of the Works/Project Representative. Before construction management was formalized, developers often engaged someone to be their eyes and ears on a job site. Even if the architect had been engaged to monitor construction, the architect would not be at the site all the time or even every day. An experienced construction person, often a retired builder or contractor, could be paid to be at the job site more frequently, and to funnel information to the developer or architect. These proto-CM’s are called “owner’s representatives” or “clerks of the work.” While these arrangements do not have the cachet that is attached to CM contracts, in practical ways these team members supplement the developer’s in-house expertise with a continuous presence, at a price that entices even small scale developers.

This clerk of the work practice is still alive, but it often calls itself construction management. It can be invaluable, no matter what it is called.

II. **The Smaller Developer: Opportunistic/Entrepreneurial**

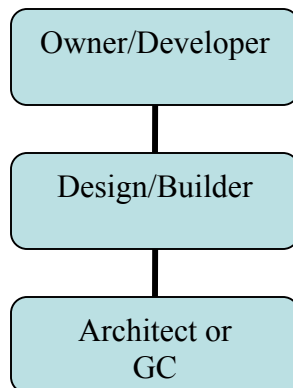
Other than by the dollar size of projects, it is hard to define the smaller developers. They may be doing 10,000 to 20,000 square foot office buildings, strip shopping centers, or smaller residential on top of commercial developments. They may do some of each. They may do a couple of projects in a year, in lieu of one big job every few of years. They may be developers only, or general contractors who turn to development. The role of counsel varies greatly. These developers have one major similarity with large project developers; they want to save money, perhaps even more than the large developers.

Small developers feel that they can build everything. They feel they can develop anything. Even if they are not design professionals, they can design warehouses, offices, stores and homes, and then get the drawings reviewed and sealed. Counsel's input into the method of providing construction services is often limited to having an opportunity to express a concern as to why something that has always been done will not work in this instance, or why the new method the developer has insisted on for this project is the wrong method at the wrong time. For example, counsel may be able to raise worrisome issues such as the complications caused when the new project is not completely on spec and there are tenants waiting to get in, and there is no schedule, or completion date specificity in the general contract. These issues may not worry the developer who has worked with this contractor and the same subcontractors before. Counsel can point out that the existence of specific end users requires a different way of proceeding.

A. The Design/Build Solution. If the developer decides that this is the project in which it wants to try out a design/build model, it is imperative to find out whether the developer has the people on staff who can develop performance specifications that provide the guidance a design/build contract contemplates. The theory behind design/build is that the developer determines the functional requirements. In this regard, the non-developer may have more expertise than the large or small developer. The developer specifies these requirements to the design/builder, and the design/builder figures out the best way to achieve them. The level of plans need not reach that contemplated by the term "construction drawings" in other owner/contractor forms. All that is needed here are drawings sufficient for issuance of permits. Thus, if the developer wants 5 bays of a certain size, 14' ceilings, and 10% office space in each bay, when the finished offices have exposed conduit and decorative duct work up to the roof (like that found in trendy restaurants) it may be too late to retrofit a different ceiling without significantly increasing the overall cost.

Similarly, if this is the developer's first office project, it needs to know whether there is anyone in the organization who can specify the lighting at desk height, or the security/access/record keeping system for the building. If not, the developer allows the design/builder carte blanche to supply a design, and the developer needs to find out if the design/builder has sufficient expertise to provide a workable design.

Another frequently mentioned benefit of design/build is a single point of responsibility. In a design/build arrangement, neither the designer nor the builder's finger pointing matters to the developer. If there is something wrong, responsibility for both design and construction lies with the same person. That is best shown in the following picture of the design/build relationship:



No finger pointing is allowed because the developer only has a relationship with one party.

If, after the design is complete, the developer *does* find aspects of the design/builder's plans that do not suffice, either the design/builder will get its nose out of joint for the extra design costs or it will pass the costs on to the developer. Without a tactful way of altering the design/builder's design, the developer belatedly reviewing the plans, or without the expertise to review plans, risks fraying the relationship with the design/builder or resigning itself to a less than completely satisfactory design. That dissatisfaction can occur also if the building is truly one of a kind, if the user or tenant will give a strong need for its own imprint, or if it is a leased facility where the tenant will have detailed tenant specifications. Any one of these facts may mitigate against design/build, because all of these factors imply that some design criteria do matter strongly to someone. Too many of these criteria means that some will collide with others, and if these overlaps are not noted early, in a formal planning process, the end result may be jerry rigged (and unsatisfactory) or, worse yet, impossible. When "impossibilities" are found late in construction, costs, and even tenancies, may be at risk.

This is not intended to suggest that design build is not a preferred method, in appropriate cases. Where the construction is not complicated, such as in a warehouse, this method may be ideal. Even in a more complicated project, if the design/build team has worked on similar projects for this developer in the past, the "next" building might reasonably be done on a design/build basis. If the developer has planning expertise in-house, to direct the design/builder with sufficient detail about the functionality needs of the purchaser or tenants, design/build is ideal. This is especially the case if someone in the developer's organization can comprehend whether the design achieves the desired functionality. With these conditions satisfied, design/build can achieve the cost savings and eliminate the delays possible where two organizations, the builder and designer, are each protecting themselves from the other.

B. The Common Solution. The foregoing discussion is not intended to imply that the only model for small developers is design/build. Where the developer is not its own design/builder, it may engage architects and GC's as needed with the same considerations as large developers. "As needed," however, is more frequently preceded by "can I do this myself, and save the money."

Developers who are builders minimize the documentation for the construction side of the project. Even if the small developer observes the formality of having separate entities for ownership and construction, at most there is a construction contract in the same form they have always used, and the developer would be hard pressed to tell you what is in the contract. Arrangements with architects are often informal, perhaps because of the long relationship with the architect, and may be limited to aspects of design in which the builder has less expertise. In any event, the relationship with a separate design professional is usually less likely to be a topic raised for counsel to explore or in which to give advice.

In either event, CM's are less likely to be engaged. The small developer is closer to the expense involved in such a consultant, and, rightly or wrongly, feels it can add the same value as the CM. The small developer may, indeed, be able to perform the same functions; however, by doing so it gives up the dispassionate review that the third party CM contributes. Small developers can still profit from the clerk of the works type of additional, on site, job management, especially where the architect is not engaged to perform construction supervision.

There is a new form of design/build contract, issued in December of 2004. The new A141 replaces the former two part (for design and construction, separately) A191. The new form even contemplates separate input from a consultant, presumably an architect. That consultant would develop the performance criteria or program that the design/builder must complete (as to design) and then construct. The amount of design contracted for by the developer directly is flexible, and may be fine tuned to reflect the amount of in-house expertise the developer brings to the table.

III. Non-Developer Models.

A. Your Friend the Non-Developer. Business clients who will build a new warehouse, office, or headquarters are non-developers who need the most help. Here, counsel's relationship with the developer is most important because the maximum structuring is possible and is warranted and needed. Our discussion will focus on the example of a doctor building a new office building, but the same considerations apply to all non-developers.

The doctor may know exactly where she wants a certain piece of equipment, but getting it there may be more or less easy depending on the other requirements of the space. The critical nature of the desired end result gives a higher priority to a formal planning process than does a warehouse building. The design/build cachet, which your doctor client may have absorbed from the medico-legal periodicals, is worthy of serious discussion, but design/build probably is not the right way to go for a one of a kind building, that needs to reflect the idiosyncrasies of the doctor or the group of doctors involved. These factors are usually better addressed as part of a formal planning process.

The same result could be achieved under the new design/build form documents, with significant consultant input. However, the more consultant input there is the more the team resembles the traditional model.

B. Fast Track Construction. If the typical three party developer, architect, contractor relationship is viewed in terms of time, the architect goes first and the GC second. There is no doubt that a GC's input before the plans are finalized is beneficial, but even where that happens the overall timeline is primarily architect first. Fast track keeps the same relationships, but changes the time line so the architect and GC are more nearly simultaneous.

Fast track construction is appealing because of its promise to save time. We raise this topic here because the non-developer may more easily hear the promise and not recognize the risks. The promise is that as soon as site work drawings are finished the contractor starts that work. When the basement, or steel or framing plans are done, the GC starts, or prepares to start, that phase of the work, and does not wait for the entire set of plans to be finished. This simultaneity is not established for feedback on the plans; it is structured for speed in completion of construction.

One risk is that the concept of a firm bid for the final cost of the work, before the work is undertaken, yields to an estimate. No guaranteed maximum price that is of any comfort to the developer will be given.

In addition to cost risk, there is also design risk. Here, a piece of the work, already literally in concrete, is not amenable to a change in design requirements that becomes manifest in connection with later phases of the planning. In traditional planning processes, a design idea or need may arise at the end of the design process which requires changes to the work already thought to be finished. Because the architect has committed to the cost for design, the architect absorbs the added design cost arising from the later change. That feedback from the end of the design process back to the beginning is a beneficial aspect of the planning. In a fast track project, not only may the architect charge for re-doing design work on a bid-pack that is complete, but there may be cases where the later determined change will be impossible. Completion of planning in segments, with construction proceeding on segments as each is completed, negatively affects the value of the design feedback.

Fast track has a place, but it is not with the non-developer. The small developer, who has a sense of how the end affects the beginning, has a better chance of avoiding disconnects too large to live with. The non-developer has no such frame of reference, and the large developer rarely subjects a major project to such major risks.

C. The Client's Home Expansion/New Home. The custom home project, or the addition to the existing home project, has its own rules. In either of these situations we face the issues of lack of construction and design expertise by the owner, inability or disinclination to monitor construction, specific needs or wants in the finished product, cost constraints, and, sometimes, time constraints. The new home being built by a contractor in a development of homes is not within the ambit of this discussion.

Custom homes, just because of the cost, usually involve a separate design professional, although in many cases where the builder controls the lot it is the builder who suggests or actually hires the architect. In the latter situation, there is a de facto design/build

relationship, although the owner may not realize it. Nevertheless, for custom homes it is clear that the idiosyncrasies are so important that the developer must have a substantial planning process with the buyer. Failure to do that will result in customer unhappiness and bad word of mouth reputation. Thus, even though it may be design/build in name, it is virtually a traditional three party arrangement.

Expansion or renovation, however, unlike the custom home situation, is most frequently controlled by the builder. The owner finds out, from friends, which contractor has done renovations with which they were pleased, and the world consists of the contractors who did those jobs. Only if the owner goes to an architect first is it common to have an architect involved directly in the project. The lawyer cannot make the technical decision as to whether the complexity of the renovation or expansion warrants a design professional's input, but it is a proper matter to raise for the client to consider. In cases where no architect is separately engaged, the skill, competence, and reputation, of the contractor will be of paramount importance.

In these situations, the one critical writing is the scope of the work, the list that sets out, in all the detail your client can muster, what is to happen in each room to be touched. Next, a schedule is crucial so the family can plan how to move their lives and their furniture so as to be able to function during construction (or whether to move in with their neighbor the lawyer). Counsel may also suggest that there are short form commercially available contracts, such as the AIA series for projects of a limited scope, that may apply to whatever the relationship is between the owner and the builder. However, these forms do not necessarily address the true relationship between the parties, and the level of administrative and oversight rigor contemplated in those forms is often not warranted by the scope of the job. Warranted or not, little or none of the oversight contemplated by form contracts is actually imposed by the owner in these circumstances.

Other Concerns Affected by Team Membership

I. The Lender:

Lenders have been known to specify, in their commitments, that developers must have a fixed price contract. That is rarely imposed, even if it is in the commitment; a cost plus contract with an acceptable guaranteed maximum price is almost always acceptable. On the other hand, lenders sometimes are not as ready to accept a design build contract when it appears for the first time at the closing table. In most cases a lender can be made to feel comfortable with design/build when it is discussed in advance on the terms raised above.

Lenders do not want to fund fast track projects as a real estate loan. If the developer has sufficient credit, lenders can fund a fast track project.

II. **Payment:**

After the team is selected, the job does not run without payment. Except in those circumstances where payments are based on milestones (usually in home renovations or expansions, or very small commercial projects), bills are based on the portion of the work completed to date. Where there is no person independent of the contractor to make that decision, a developer is at a handicap. The more construction expertise there is in-house, or available via a consultant, the less that handicap will be. A project lender may determine that the contractor is asking for too much at any particular time. A developer cannot rely on that, because the loan documents exculpate the lender if it does not raise the issue. CM's and project representatives, as well as architects, may perform this cost monitoring function if the developer does not have the expertise.

Conclusion

The team players for any project need to be assembled as carefully as the athletes on a sports team. The developer can picture itself as the general manager of the team, deciding what strengths are already in-house and what strengths are still needed in the lineup. The common denominator for the developer and the general manager of the team is cost.

Traditional developer-architect-GC construction is broadly applicable because of the flexible arrangements that can be made, primarily in the architect agreement, for the level of service needed by the developer. More design and construction expertise in-house means less needs to be purchased outside. Sufficient expertise in-house facilitates design build arrangements, and design/build's attraction is the perceived cost savings and single point of responsibility. Even without in-house expertise, additional help can be obtained, from the project architect or from a construction manager, clerk of the works, or project representative, to justify design/build.

Cost savings can be achieved by direct engagement of subcontractors. The trade off for such potential savings is the risk to the developer if the directly engaged subcontractor does not perform as expected. Cost savings, measured in time, is available by fast tracking a project. There the risk is in the fact that design that can only be one step ahead of construction; later perceived construction or design needs cannot necessarily be accommodated by the earlier construction phases.

The discussion of the various options for assembling the team has been narrowed to address large developers, small developers or non-developers. This was for convenience in the analysis; we wish to make it clear that any of the methods of assembling the team can work for any kind of developer and any project. In addition, the acquisition of expertise by means of consultants, CM's, project representatives or clerks of the work are ways to make almost any combination of team members work for any developer or project.

The lawyer's role is not to make these decisions, but to be able to bring these alternatives to the client's attention when the proper circumstances arise.