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# **Streamlining Government Change Order Processes – Can It Be Done?<sup>1</sup>**

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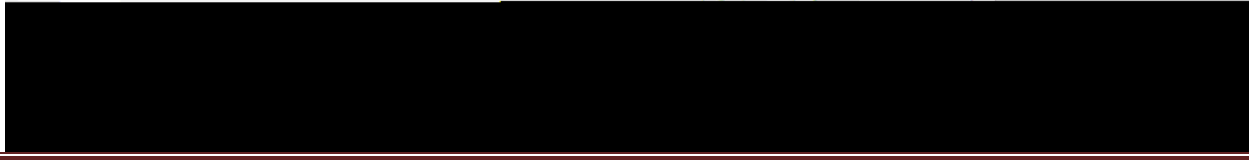
## **Introduction**

Change is the norm on construction projects. Change is, at times, beneficial for both owners and contractors. Owners can modify the project after contract award, if needed, while contractors can increase their scope of work and project profitability without needing to compete for additional work. At the same time, change, can be and often is, detrimental to both owners and contractors. Change often causes projects to complete later than planned by owners and over their planned budget. And, owner change order processes are often lengthy and cumbersome, detrimentally impacting contractor cash flows. As a result --

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<sup>2</sup> The Navigant Construction Forum™ is "The industry's resource for thought leadership and best practices on avoidance and resolution of project disputes globally", located in Boulder, CO.



“Contractors universally agree that slow processing of change order requests by public project owners coupled with slow payment for extra and changed work are major problems threatening project success and contractor viability.”<sup>3</sup>

As a result of this belief, efforts have been initiated by legislatures and various governmental entities across the nation to “streamline” or speed up change order processes. There is little doubt that typical governmental change order processes should be streamlined. The impact of lengthy and convoluted change management processes drive up project costs, strain contractors’ cash flow, and jeopardize contractors’ financial situations. As one article noted:

“The Los Angeles Metropolitan Transit Authority reported in 2013 that ‘...risks associated with change order resolution and related delays in payment have a significant impact on construction costs on Metro projects. These risks fall disproportionately on small and disadvantaged businesses that rely on uninterrupted cash flows to meet payrolls and sustain their businesses.’”<sup>4</sup>

The purpose of this paper is to explore current efforts to streamline change order processes. The paper also discusses the difficulties in speeding up such processes and why, in the opinion of the author, such efforts are quite often doomed to fail – due mainly to a disagreement over when does a change actually start and when does the change order process commence?

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<sup>3</sup> Daniel F. McLennon, *California Needs Legislation Requiring Timely Processing of Change Orders on Public Construction Projects*, Engineering News-Record Law Today, May 30 - June 6, 2016.

<sup>4</sup> Los Angeles County Metropolitan Transportation Authority Revised Memorandum re: Construction Change Order Initiative. November 6, 2014. Cited in Daniel F. McLennon’s article cited above.



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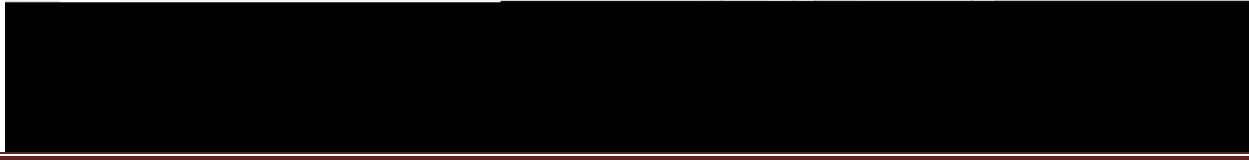
## What is a Change Order?

The term “change order” is a generic term. For the purposes of this paper the change order nomenclature includes claim settlements (on the project), contract amendments, contract modifications, requests for equitable adjustment, work change directives, and variations. One general definition of a change order is set forth below.

“Direction by the Employer or authorized representative directing the Contractor to construct some portion of project in manner different from that described in plans & specifications for which the Contractor or Employer may be entitled to an adjustment in contract price and/or time.”<sup>5</sup>

A more robust definition of change order is found in the U.S. Postal Service’s Contract Administration Manual and is set forth below.

*“Change Order.* A written order, signed by the contracting officer, directing the contractor to make a change that the Changes clause permits the contracting officer to order without the contractor’s consent. Change orders are another type of unilateral modification. They can be issued for several reasons, including a change in the needs of the requesting office, defects or ambiguities in the specifications, and factors (such as weather



*Contract Modification.* Any written alteration in the specification, delivery point, rate of delivery, contract period, price, quantity, or other contract provision of an existing contract.”<sup>6</sup>

Different contract documents, of course, have somewhat different definitions. Notwithstanding these different definitions, the term change order is an owner directive to perform some work differently or perform different work than the original contract called for and provides for an equitable adjustment for either the owner or the contractor as a result of the change.

## **Why Do We Need a Changes Clause?**

One of the premier texts concerning change orders, *Government Contract Changes*<sup>7</sup>, summarizes the four principle purposes of a Changes clause in a construction contract in the following manner.

1. To assure that project owners have “...a wide degree of flexibility...” during the performance of the project work to make changes;
2. To facilitate suggested changes to the work of the contract by the contractor;
3. To providelex 6)xr3.6 (h6 6) lexul6 (TJlst3 ty5 12 fo 3 . c o n o



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## Different Types of Changes

In the most general terms, there are three types of changes – **Directed changes**, **Constructive changes** and **Bilateral changes** (also known as **Agreed changes**).

- **Directed changes** – Directed changes are those change orders issued by the owner that the contractor is obligated to perform.<sup>8</sup> Under the heading of a directed change are two types.
  - **Bilateral changes** – A bilateral change order is one where there is total agreement between the owner and the contractor as to the scope, time and cost of the change and is executed by both parties. Typically bilateral changes are executed on a lump sum basis.
  - **Unilateral changes** – A unilateral change order is one which is executed by the owner that contains a scope of work but there is no agreement on the time and cost of the work to be performed. The contractor is obligated to follow such a change directive and typically performs such work on a time and material, force account or cost reimbursable basis.
- **Constructive changes** – “A constructive change order has been defined as an oral or written act or omission by the Contracting Officer or other authorized



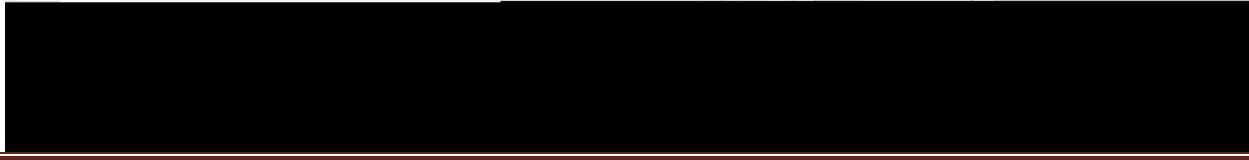


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## Elements of a Typical Change Order

What is included in a typical change order? There are three elements in most change orders as follows.

- – This is, generally, a narrative description of the work the owner wants changed, modified, added or deleted from the current scope of work. It may be accompanied by sketches, drawings or other visual depictions of the changed work and may also be accompanied by technical specifications.
- – This is, on prospectively priced changes, the agreed upon price for the changed work including direct, indirect, delay and impact costs plus overhead, profit and bond costs. On unilateral changes, which are retrospectively priced, this may represent the owner's estimate of the changed work; may be a "not to exceed" cost<sup>11</sup>; or may be filled in with the words "To Be Determined" or "TBD" which will be ultimately based on actual costs of the changed work tracked on a



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calendar or working days (depending upon how the Time of Performance clause in the contract is stated). In the event the owner issues a unilateral change order, this portion of the change order will likely have TBD.

- – Yes. It is uncommon for a change order to have either a disclaimer clause or reservation of rights language.
  - – Many prospectively priced change orders will contain some form of disclaimer clause indicating that the terms and conditions of the change order constitute “full and final settlement” of all time and all costs of the change order.
  - – In the alternative, if the owner and contractor cannot come to terms on the time and cost of the changed work, it is at all uncommon for contractor to include a “reservation of rights” clause either on the face of the change order or by attaching a letter to the proposed change order reserving their rights to some or all aspects of the change – typically the cost, the time, and the impact of the change on unchanged work.

## **What Causes Delay in the Change Order Process?**

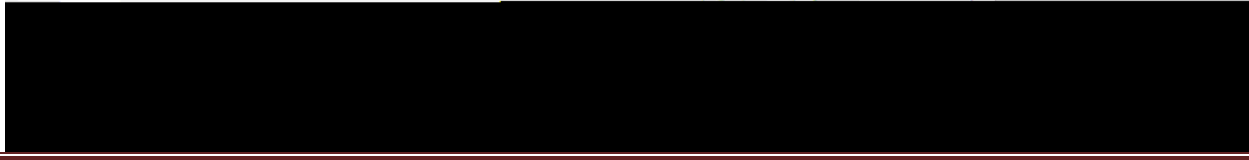
As noted earlier there are many complaints concerning lengthy change order processes which substantially impact the finances of contractors. One recent article has this to say concerning such lengthy processes.

“Contractors are required by contract to perform extra work and maintain the project’s schedule before the owner entity processes a change order

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<http://www.mpug.com/articles/time-impact-analysis-extra-work-effect-finish-date>. The definition of a time impact evaluation is the same but with a different name.

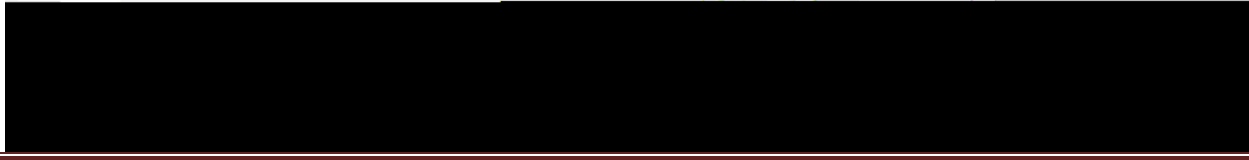




request for that work. Until the change order is processed, there is no contract amount for the contractor to bill against. Thus, trade contractors end up financing often significant parts of the public entity's construction project for extended periods of time.

For example, average change order processing in New York City in 2008 took more than 300 days. A local law firm reported an estimated \$600 to \$800 million in unprocessed change orders in 2008 for the New York City Public School Authority alone. The carrying cost to trade contractors for such amounts is enormous. Of course, this problem is not restricted to New York and is reported across the country.

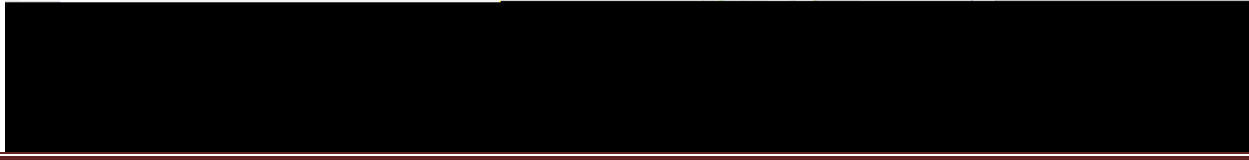
Furthermore, stories abound in the construction industry about multi-year projects where processing of change order requests has been put off until project completion. By that time, contractors desperate for payment may fall prey to predatory owner practices of overstated back charges and liquidated damages.



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concerning the need for streamlining government change order process but are commonly known on project sites globally.

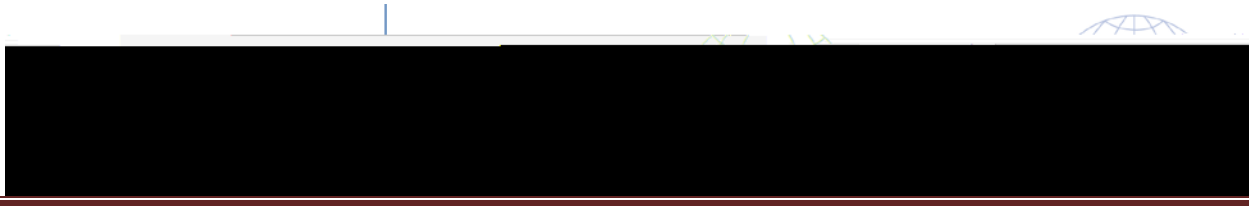
- - It is not uncommon for owners to request time and cost proposals on changed work they have reached a final decision on the full scope of work. All too often, the initial change order proposal requests received from the owner lack the detail necessary to properly plan and price a change order. When contractors receive such requests and start asking questions to help them understand exactly what the owner wants changed and how, owners frequently take their time reaching their conclusions and responding to the contractor. Such lack of detail and lack of prompt decision making causes delay to the finalization of a change order.
  
- - All too many contracts specify that contractors submit change order cost quotations within a very short timeframe – 14 to 30 days. This is, in many cases, insufficient time to prepare a detailed cost and time estimate for proposed changes. As a result, contractors prepare order of magnitude estimates and reserve their rights to impact costs and time. Owners and contractors, in situations such as this, often find they cannot negotiate and prospectively settle the change order. This type of situation frequently results in time and material change orders, further delaying the final resolution of the change.
  
- - As so much work on projects today is subcontracted,



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suppliers will raise questions to the general contractor, who must pass them to the owner and await the owner's response.

- - In addition to preparing a cost estimate, most contract documents demand preparation and submittal of an estimate of potential delay likely to result from the changed work. This time estimate typically requires preparation of a TIA or TIE. What many owners fail to realize is that a TIA or TIE requires a detailed plan for the performance of the changed work, which in turn requires that a detailed scope of work has been agreed to between the owner and the contractor. The failure to reach agreement on a detailed work scope prevents or, at least, slows down preparation of a TIA or TIE.
- - If the owner is hoping to execute a prospectively priced, firm fixed price change order (one that includes full agreement on scope, time and cost) then the contractor must also estimate the potential impact costs of the changed work. This includes, but may not be limited to, delay costs, impacts on unchanged work, lost productivity, potential idle equipment costs, etc. As these costs are somewhat speculative. It is often difficult for owners to negotiate settlement of such costs since they are based on assumption and "soft costs".
- - Given all of the above, it is difficult for owners and contractors to reach a quick resolution of all change order impacts. This difficulty results in multiple negotiation sessions,



change. That is,



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## When Does a “Change” Start & When Does the “Change Order Process” Start?

One issue that common to efforts to streamline change order processes is the total failure to when the change order process actually starts? Some examples follow.

“The new Metro policy and adopted procedures sets a goal of 60 days for the timely processing of all construction change orders to minimize costs and risks to contractors and subcontractors.”<sup>14</sup>

“The bill would require a public entity ... upon receipt of a claim sent by registered or certified mail, to review it and, within 45 days, provide a written statement identifying the disputed and undisputed portions of the claim ... The bill would require any payment due on an undisputed portion of the claim to be processed within 60 days ... The bill would provide that unpaid claim amounts accrue interest at 7% per annum.”<sup>15</sup>

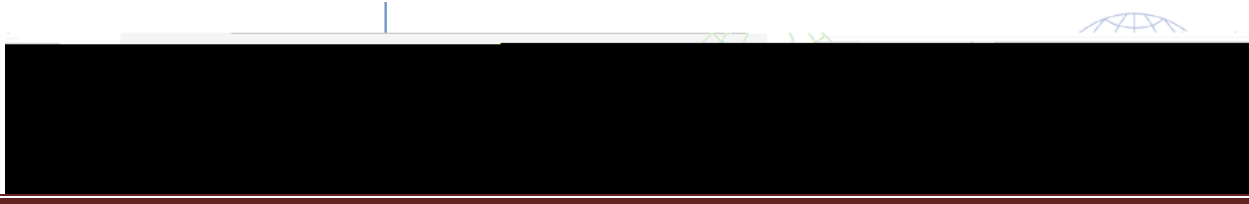
“The City is streamlining its procedures to reduce change order processing time by 50 percent – to 150 days or less – for changes caused by unforeseen field conditions, and will institute measures to hold agencies accountable for failing to meet this target.”<sup>16</sup>

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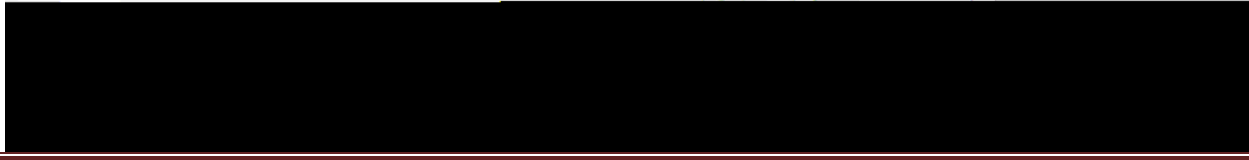
<sup>14</sup> [Vendor/Contract Management Insider](http://media.metro.net/eblast/enewsletter_vendorinsider.htm), Los Angeles County Metropolitan Transportation Authority, January/February 2015. [http://media.metro.net/eblast/enewsletter\\_vendorinsider.htm](http://media.metro.net/eblast/enewsletter_vendorinsider.htm).

<sup>15</sup> California Legislative Counsel’s Digest, Assembly Bill (“AB”) 1347, *An act to add and repeal Section 9204 of the Public Contract Code*, February 27, 2015. The California Legislature passed AB 1347 to promote change order reform in 2015 but the act was vetoed by the Governor.

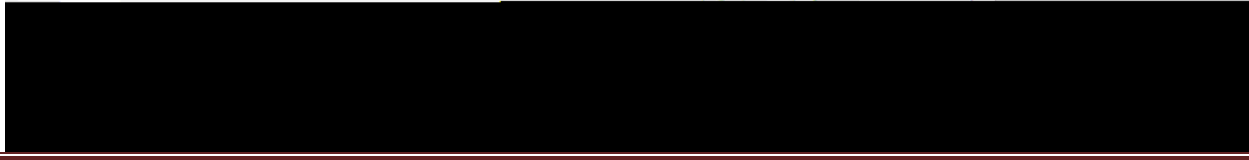
<sup>16</sup> Office of the Mayor Press Release, PR-291-08, July 28, 2008, *Mayor Bloomberg Announces Reforms to Make City Capital Construction Projects More Affordable and Efficient – Strategic Plan 30.08.3 Co)3 (E)2 (i)2.2 (i)6 (i)3 (i)4.3 (a)3 g3*



“(h)(1) With respect to a proposed change to a contract entered into by a non-Department Federal entity with which the Secretary has entered into



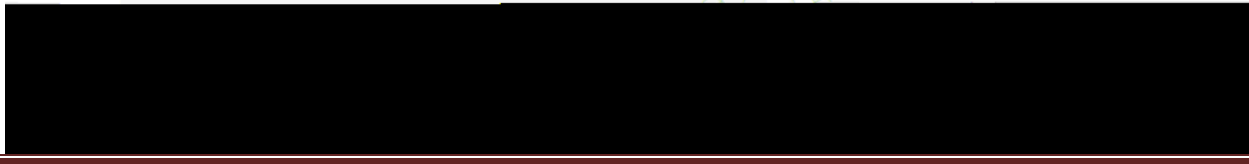
While the starting date of a change order in this situation is well defined and documented, half or less of the change order disputes the author has been involved in have started with the issuance



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However, in the author's experience, owners do issue unilateral changes right off the bat. It is more likely that the owner requests and receives a time and cost proposal from the contractor. Subsequently, the owner participates in unsuccessful time and cost negotiations with the contractor. The owner then decides to proceed with the change and directs the contractor to proceed with the scope of work on a time and material basis. In the alternative, the owner and the contractor may have reached agreement on the hard dollar costs, but the time and the impact costs; or may have reached agreement on all time and costs but the contractor refuses

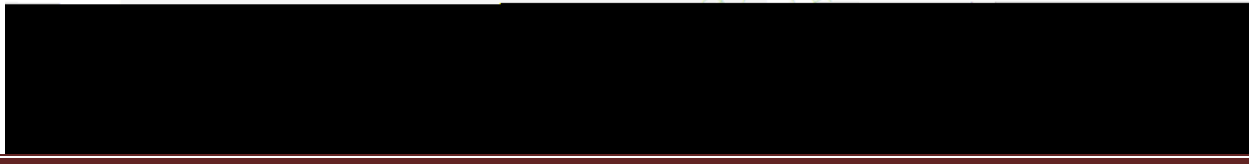




typically required to provide a notice of change. If the owner insists on their interpretation of the contract requirements and directs the contractor to proceed in accordance with their response, despite the contractor's objection, this is the starting point of a constructive change claim and its impact. Later the owner will likely take the position that the impact of the directive started when they directed the contractor to proceed while the contractor is most likely to assert that the impact began when the RFI was submitted. But the change order process actually does not start until the time and cost proposal is submitted after the disputed work was completed. Many owners, on the other hand, take the position that the change order process actually did not start until they acknowledge that their directive was actually a change to the scope of work.

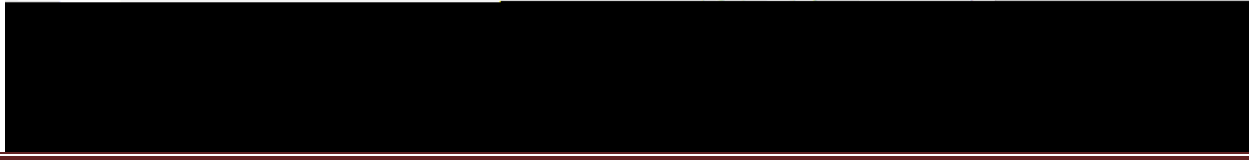
In the alternative some time may be expended arguing over the requirements of the contract. If the owner concludes that their response actually was a change to the scope of work they will advise the contractor that a change order will be issued. Most contractors will likely take the position that the change order process started when the RFI was submitted. The author agrees that while the impact of the change started when the RFI was submitted the change order process did not start until the proposed change is submitted to the contractor.

- - The scenario is nearly identical to the one above except that argument over when the change order impact began when the



- - Virtually all contracts require that contractors file notice of potential delay within a specified number of days after "... the contractor knew or should have known ..." of the delay.<sup>19</sup> So the question arises, when does the change impact start and when does the change order process start? The delay impact can be established through the contractor's forensic schedule analysis. Schedule delay analysis will demonstrate that a project delay has or will occur and that the owner, or someone for whom they are responsible, is the proximate cause of the delay. Contractors are likely to contend that that the change order process started when they submitted all of the above information and requested either an excusable or a compensable time extension. Again, owners typically assert the change order process did start until they agree that the delay was owner caused.

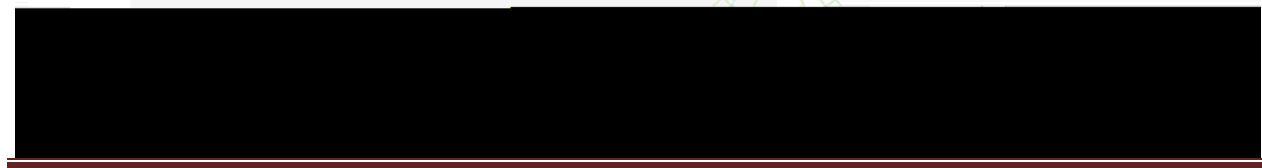
- - Directed suspensions of work ("SOW") or Stop Work Orders are fairly straight forward. Almost all contracts require that owners issue such directives in writing. The author's WJ10.0246 Td(A)nc3(n)-4



A constructive suspension of work is generally thought of as an act or omission of one party on a construction project which has the effect of unreasonably delaying the contractor's work. Examples include the owner's failure to respond to submittals or RFIs in a timely manner or late release of change orders. While the impact of such an event starts much earlier the change order process does not start until the constructive suspension is completed and the contractor complies and submits their time and cost request. Owners, of course, believe the change order process did not start until they acknowledge the delay.

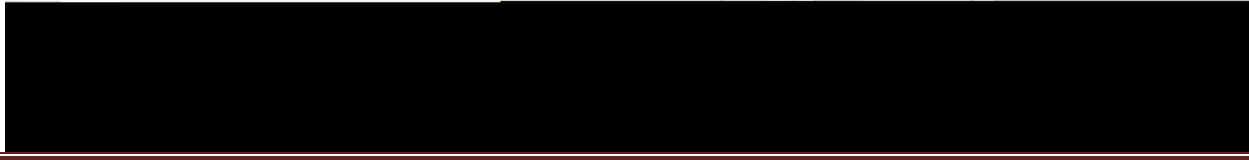
- – “Constructive acceleration occurs in the absence of an owner directed acceleration, such as where the owner has refused a valid request for time extensions or threatened other action which requires the contractor to accelerate its work to avoid liquidated damages or other loss or risk of loss. The classic case is when a request for a time extension for excusable delay is denied and the contract provides liquidated damages for late completion. The law construes this as an order by the owner to complete performance within the originally specified completion date, a shorter period at higher cost than provided for in the contract. The constructive acceleration doctrine allows recovery for the additional expenses the contractor can establish.”<sup>21</sup> The impact of constructive acceleration starts when the contractor files the notice of constructive acceleration and the owner ignores the notice. Contractors generally believe that the change order process starts when the contractor's acceleration efforts are completed and the cost and time impacts are submitted to the owner in the form of a request for equitable adjustment. Again though, owners feel the change orders





## **Legislative Efforts to Streamline Change Order Processes**

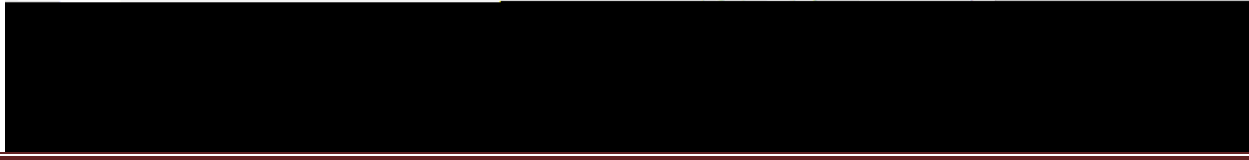
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good. However, this is a statutory requirement in Washington so this Construction Bulletin is more of a reminder to the WSDOT staff.

The Office of the Independent Budget Analyst produced a report in 2012 recommending approval of a proposal to change the authority for City agencies and department to approve change orders from \$200,000 to \$500,000.

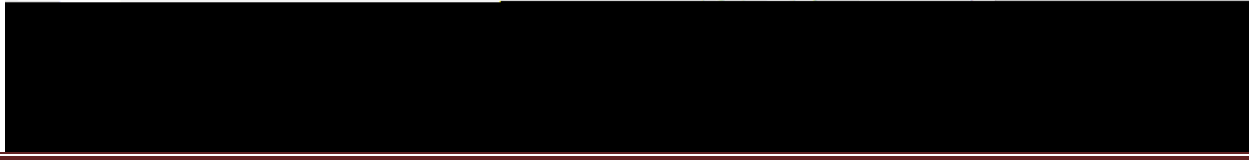


and material costs for each task required for the change order as included in the bid documents at the time of bid;

- (ii) A force account;
- (iii) A construction change directive; or
- (iv) A time and materials basis.

(2) If a procurement officer and a prime contractor do not agree that work is included within the original scope and terms of a contract, nothing in this section:

- (i) Prohibits a procurement officer from issuing an order to a prime contractor to perform work or to furnish labor or materials determined (a) - 9 (i) 12 (n) 3.1 (ed) (a) - 9 (i) 12 (n) 3.y ( a) - al

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1. Determine the actual quantity used to complete the contract; and
  2. If necessary, issue a final adjustment change order to the contractor.

(c) If the amount to be paid under an approved change order does not exceed \$50,000, a unit shall pay an invoice for work performed and accepted under the change order as provided for in the contract within 30 days after the unit receives the invoice and in accordance with § 15-103 of this subtitle.

(d) Within 5 days after receipt of a written change order, a prime contractor shall provide a subcontractor with a copy of the approved change order and the amount to be paid to the subcontractor based on the portion of the change order work to be completed by the subcontractor.

(e) Before January 1, 2017, the Board shall propose regulations that provide for an expedited change order process for change orders valued at more than \$50,000.

(f) (1) On or before December 31, 2016, each unit shall issue guidelines for the unit's change order process.

(2) The guidelines issued under paragraph (1) of this subsection shall be updated and reissued when any




on February 10, 2016 and referred it to the Committee on Veterans' Affairs where it remains today. This proposed legislation is specifically aimed at the Department of Veterans' Affairs ("VA"). The essence of this legislative reform is set forth below.

"(h)(1) With respect to a proposed change to a contract entered into by a non-Department Federal entity with which the Secretary has entered into an agreement under subsection (e) that is estimated at a value of less than \$250,000, the non-Department Federal entity shall issue a final decision regarding such change not later than 30 days after the date on which the change is proposed.

(2) With respect to a proposed change to such contract that is estimated at a value of \$250,000 or more –

(A) The Secretary may provide to the entity the recommendations of the Secretary regarding such change;

(B) The Secretary may provide to the entity the recommendations of the Secretary regarding such change;



This proposed legislation is somewhat convoluted. While the legislation is specifically directed at the VA, it requires that the VA enter into an agreement with a "... non-Departmental Federal entity..." to oversee "... construction of medical facilities." Under this proposed reform legislation, for change orders less than \$250,000 this non-Departmental Federal entity is required to render a "final decision" within 30 days after the "change is proposed". What remains unclear under this legislation is whether the non-Departmental Federal entity has to issue this final decision on the entitlement to the claim (i.e., whether the request is a legitimate change order or not) and/or the amount of the change order, including both time and costs. For changes in excess of \$250,000 the non-Departmental Federal entity "... shall issue a final decision..." on the proposed change order. What makes this proposed legislation different from other legislative efforts to streamline the change order process is that the 30 day and the 90 day timeframes start from when the contractor provides their information on the proposed change. The author believe these timeframes are unrealistic when applied to a large or complex change order or one that involves a potential or alleged substantial delay.

The \_\_\_\_\_ determined to cut the typical change order process

"The current average time to process a change order – an agreement to alter a contract – on a City project is over 300 days. Contractors either proceed at their own risk or wait for as much as a year for approval – at a time when the cost of doing the work has increased due to construction cost escalation. This uncertainty drives up the City's costs by reducing the number of contractors willing to bid on City work. This is true even for change orders where the need for the change is straightforward, such as unforeseen field conditions like poor soil quality or where building systems to be repaired have degraded beyond expectations. The City is streamlining its procedures to reduce change order processing time by 50 percent – to 150 days or less – for changes caused by unforeseen field

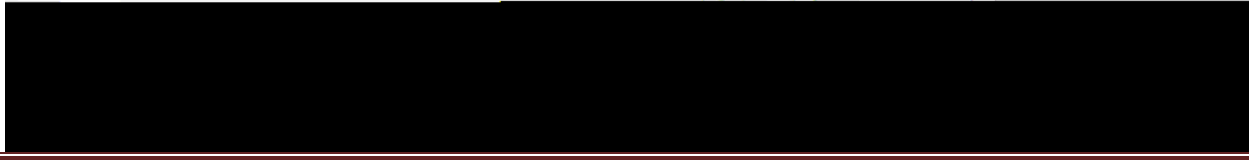


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conditions, and will institute measures to hold agencies accountable for failing to meet this target.”<sup>24</sup>

Nothing, however, in this press release provided any details on how this goal was to be accomplished. In an attempt to ascertain whether the City of New York has made progress in their effort to cut the change order processing time in half the author reached out to a senior member of a New York City department. The author was advised that there was a study conducted and this Department has been able to reduce registration beyond the Department from 120 days to 90 days. The author was also advised the report found that the largest delay in executing change orders is at the project level. Project teams are lax in “initiating” change orders; designers are slow in designing solutions; and construction manager and contractor negotiations are a long and drawn out process. At this Department most change orders are performed at risk by the contractors.

The (“Metro”) adopted a new change order policy as part of their Construction Change Order Streamlining Initiative in 2014. The memorandum recommending these change stated the following.



Another feature of the new process is that if a change order is not fully negotiated within 60 days, Metro will issue a unilateral change order, as allowed by the contract, based on Metro's ICE.<sup>25</sup> This feature has three important effects; it places a reasonable goal that is defined in procedure, it reduces the size of any dispute, and lastly it provides important cash flow to the contractor and its subcontractors, including DBEs and SBEs. This aspect of the change order process will attempt to improve the time necessary for disputes of unmerited changes to go to issues to be moving quickly to address.”<sup>26</sup>

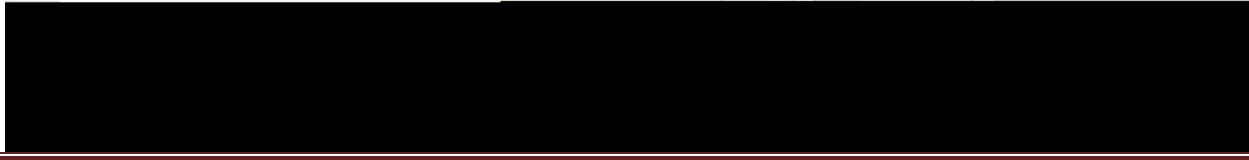
While the goal of cutting the change order process from 90+ days to 60 days is laudable, the revised policy still requires that the owner and the contractor reach an agreement on “... the full and complete definition of a scope of work ...” the change order process even starts. The 60 day timeframe is, according to Metro’s Change Control – Construction/Procurement Contracts<sup>27</sup>, does commence until there is agreement between the owner and the contractor that the request is a legitimate change and there is agreement on the proposed scope of work and/or the claim submitted is merit. The 60 day timeframe breaks down to 30 days for the contractor to submit the proposed cost and time estimate while, at the same time, the owner is preparing their independent cost and time estimate. Days 31 through 60 are committed to “Fact Finding & Negotiation”. The procedure also sets forth a dispute resolution process whose goal is to resolve all such disputes between day 61 and day 90. According to a discussion the author had recently with a member of the Metro staff indicated that some of currently active projects meeting the procedure’s timeframe but others are still running between 100 and nearly 300 days. It appears that this streamlining effort is showing some success in moving toward the established goal.

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<sup>25</sup> ICE is Metro’s Independent Cost Estimate.

<sup>26</sup> Los Angeles County Metropolitan Transportation Authority Revised Memorandum re: Construction Change Order Initiative. November 6, 2014.

<sup>27</sup> Change Control: Construction/Procurement Contracts, Procedure #CF 14, Rev. 4, dated April 7, 2015.



The (LAUSD) Office of the Inspector General – Internal Audit issued an audit report concerning the Change Order Process on March 1, 2012. This audit report noted the following.

“Although the processing time for change orders has decreased in recent years, the average processing time is still over 120 days.

The states, in part, that: “The Owner Authorized Representative (“OAR”) is responsible for complying with the following policies when administering the change order process:

Change Orders shall be processed for approval within 45 days from receipt of a valid Change Order Proposal (COP) establishing entitlement for the change and no later than 30 days after Substantial Completion.”<sup>28</sup> Recently, FSD’s Project Execution Branch developed metrics for monitoring the change order processing time from the date of the Change Order Proposal to the date of the Change Order Board Approval. The goal is 60 days.”<sup>29</sup>

This audit report also contained the process by which LAUSD intended to reach the 60 day goal for change orders. A copy of this flow chart is set forth below.

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<sup>28</sup> Los Angeles Unified School District’s Facilities Services Division, 14.17 Change Order Procedures, dated October 10, 2007 and Current Revision dated March 31, 2011.

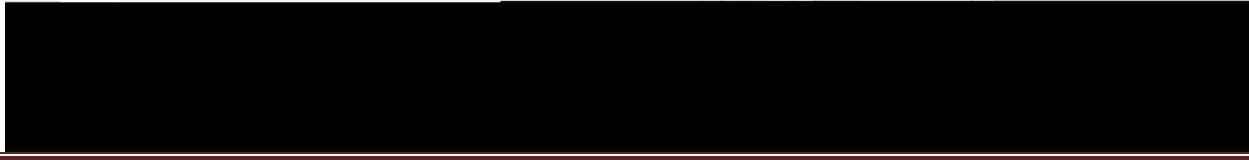
<sup>29</sup>





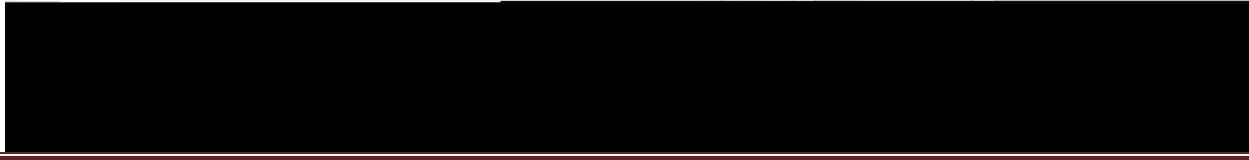






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It is the author's experience that owners and their staff are generally conservative individuals, trying to do everything right from the owner's perspective; quite often overburdened with administrative policies and procedures; and always subject to multiple layers of "oversight" by individuals or groups involved with the construction project. All too often, owner staff do not understand what contractors have to do to understand a proposed scope of work, estimate the time and cost of the change for their subcontractors and themselves, negotiate the change and perform the changed work. Generally,



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Finally, both owner and contractor staff must participate in any effort to streamline a change order process as this must be a joint effort if it is to be successful.

## **Conclusion**

There is no doubt that many change order processes need to be streamlined and sped up for the benefit of the contractor, the owner, and the project. Of this, there is little doubt in the industry. But decisions concerning how to streamline the change order process must be made by people personally experienced with the actual change order process they are trying to reform. Timeframes set in an arbitrary manner are likely to be both unrealistic and unachievable.