



## **FIVE WAYS OWNERS CAN CONTROL CONSTRUCTION COST OVERRUNS**

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### **The Cost Overrun Problem**

Every project owner wants a successful construction project – one that finishes on time, on budget, without defects in design or construction and with minimum conflict among the project parties. Construction cost overruns can convert a potentially successful project into an unprofitable boondoggle. Controlling cost overruns is key to achieving a successful project.

Cost overruns on construction projects seem to be the rule, not the exception. Research by Dodge Data & Analytics shows that projects frequently are delivered over budget and late. According to a McKinsey & Co. survey, large projects across asset classes typically take 20% longer to finish than scheduled and are up to 80% over budget.

Overruns often occur even before construction commences. Typically, the owner engages the design team, establishes project parameters, sets a budget and receives a set of plans. Commonly also, the owner thereafter receives construction bids which significantly exceed the project budget, with the result that the project has incurred overruns even before the construction work has begun.

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Construction overruns also frequently occur after construction begins. Construction projects are famous for generating multitudes of change orders while the construction is ongoing, with resulting cost overruns.

### **What Causes Cost Overruns?**

Overruns commonly occur where initial cost estimates are inaccurate. Many owners rely heavily upon project designers (architects and engineers) for initial cost estimates. However, designers who may be highly qualified in technical architectural or engineering areas may not be equally skilled in cost estimating, which is an expertise unto itself.

Also, designers generally will not guarantee the accuracy of their cost estimates. Under the standard form of architect's contract published by the American Institute of Architects, the architect disclaims any guarantee that actual construction costs will meet the owner's budget or the designer's cost estimates. Most standardized agreements between owners and designers contain a similar provision.

Overruns also occur where design or construction errors are discovered in the field, requiring redesign, repair and/or replacement of installed work, and by excessive changes made by the owner after construction has begun.

### **Five Ways Owners Can Minimize Cost Overruns**

Project owner can minimize cost overruns in a variety of ways.

*Establish a Firm Budget.* While every project has a budget, some budgets are firmer than others. To reduce the risk of overruns, the owner should establish a firm budget and direct the architect and engineers to design to that budget. Also, the contracts with the designers could require them to revise the plans at no or limited cost if the bids exceed the budget by a stated percentage, although such a provision is difficult to obtain.

*Obtain Independent Cost Estimates.* Another way to limit overruns is to obtain independent cost estimates as the design progresses. Although this service involves an extra expense, the expense is modest and well worth the cost.

*Use “Add and Delete” Alternatives.* Under this approach, the design team preplans certain components of the work which the owner may delete if the bids come in too high and add if the bids are lower than expected. Preplanned “add and delete” alternatives protect the owner from the delays, disruption and extra expense that inevitably result from redesigning the project to cut costs after high bids are received.

*Peer Review the Design.* One of the best ways to control cost overruns is to have the best, cleanest, most error-free and easiest to execute set of plans possible. Peer review involves an independent architect or engineer reviewing the plans in an effort to uncover errors, omissions and inconsistencies. The modest cost is justified by avoiding the delays, disruptions and extra costs which usually are involved when design errors are discovered in the field after construction is underway.

*Review the Plans for Constructability.* “Constructability” describes the ease and efficiency with which structures can be built. The constructability of a building depends largely on the quality of the designs—if the design documents contain errors or are difficult to interpret, the project will be more difficult to build. Having a qualified contractor evaluate the plans for constructability before construction begins helps assure that the plans can be efficiently implemented in the field so that change orders are minimized. Again, although this service involves an extra expense, it is a modest expense which is well worth the cost.

Construction projects are renowned for debilitating cost overruns. Controlling cost overruns is critical to achieving a successful construction project.

Greenberg Traurig, LLP Shareholder Robert C. Epstein represents clients in the area of construction law, contracting and litigation.