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## What Do We Audit in a GMP Contract?

The simple answer is that we review both the calculations that have led up to the final contract value and the reimbursable cost and fee calculations that must be compared to the final contract value to determine the ultimate lower cost to the Owner.

Sometimes, as we describe the various audit exceptions, it can be confusing whether an exception is ultimately affecting the calculation of the contract value or the reimbursable cost and fee. We have also, over the years, had Owners question the relevance of a contract value exception when it appears as if the contractors cost plus fee would be higher than the contract GMP. One of the reasons that many Owners become confused as to how to interpret the audit exceptions is that many Owners, as the project progresses, pay interim pay applications, at least in part, from a schedule of values presented by the GC. In that situation it appears as if credit adjustments to the contract value and credit adjustments to billable costs have the same effect, lowering the interim billings. However, at the end of the GMP project, the Owner is typically going to pay to the contractor the lower of the adjusted GMP or the cost plus the fee. So, when the project has ended, the audited final GMP and the audited final cost and fee must be determined to see which is less. Hopefully, in an attempt to clear up the possible confusion and to give examples of what typical audit exceptions are, we offer the following discussion:

### **Auditing the GMP and Types of Audit Exceptions**

– We refer to the audit of the calculations that make up the final GMP contract value as Auditing the GMP. When auditing the ultimate contract value there are many items to review. The most common areas are making sure that the change orders have been processed and calculated per the terms of the

contract and that allowances have all been reconciled properly. When reviewing the change orders we want to make sure that markup's and fees for both subcontractors and the GC have been calculated per the contract and that all scope deletions have a corresponding Owner deductive change order. An example of some typical markup audit exceptions would be; 1 - where the GC did not net additive and deductive change orders when adding fee if the contract requires them to do so; 2 - where an allowance was not reconciled and that the actual cost to the GC was less than the allowance amount, or; 3 - where the GC took a credit from a sub for a scope deletion but that same deletion was not processed to the Owner. All of these types of exceptions would serve to reduce the final GMP amount while not necessarily affecting the contractors actual reimbursable cost.

Because of the nature of GMP contracts, these previous audit exceptions would be identical if there was a GMP contract or a Lump Sum contract. Sometimes, if the GC has reported that their cost plus the fee is significantly in excess of the contract value, and once we have verified that that situation does indeed exist, we will focus totally on the audit of the GMP and not spend any time further on the reimbursable cost. We have seen situations where the GC knew early in the project that the actual cost would exceed its estimated cost. This situation could cause the GC to look for ways to increase the contract value more than allowed, or not decrease the contract value as much as required. We often have substantial GMP audit exceptions in these instances partially due to this predictable GC behavior.

**Auditing the Reimbursable Cost and Final Fee Calculation** - Auditing the reimbursable cost is what most Owners think of when an audit is performed. Approximately 70% of the contracts we audit have

some type of contract savings, meaning that the reimbursable cost and fee is ultimately less than the adjusted GMP contract amount after change orders. In these circumstances any cost that the GC has included in the Cost of the Work, that is found to be not reimbursable, will lower the ultimate final cost that the Owner owes to the GC. Examples of typical cost or fee calculation exceptions would be: 1- Home office employees charged to the Cost of the Work, 2- Labor burden payroll taxes in excess of actual payments for same, 3- Cost charged for GC owned equipment in excess of fair market value, 4- Subguard cost charged on estimated subcontract amounts rather than on actual final subcontract amounts, and 5- Fee only added to additive change orders and not credited on deductive change orders.

Because of the nature of GMP contracts, the above reimbursable cost exceptions would be identical on a Cost plus a Fee contract with no GMP. In a situation where the GC is in a significant contract savings and there is no savings bonus given to the GC, we will often focus almost solely on the examination of the reimbursable cost. In situations where the GC knows that the estimated cost is significantly greater than actual cost and has been allowed to bill off a schedule of values or has not been providing full actual cost backup in the billings, we have seen variations between cost billed and actual cost greater than \$1,000,000.

**Final Audit Reconciliation** – At the conclusion of the audit, a final contract reconciliation is needed to determine if the final audited contract GMP is less than the audited reimbursable cost plus fee or visa versa. Typically an audit report will contain both types of exceptions, audit adjustments to the contract GMP and audit exceptions to the reimbursable cost and fee. As you can see from the discussion above, one type of exception is not the same as another. This is why we separate the two types of exceptions in our audit reports so they will not be confused with each other. We hope this discussion makes the process a little more clear and helps you interpret our audit reports, short of asking us, of course.

### **Some New CCIP Overcharges**

CCIP, or Contractor Controlled Insurance Programs which typically include GL, Excess Liability and Workers Comp. insurance, have become almost as widespread as Subguard. Why you ask? There is money in it, for a start, and if you are involved in a residential project some types of insurance may not be readily available to many subs, causing a Owner to have to either consider a CCIP or a OCIP. We would

like to deviate from the question of whether CCIP's are a good idea on your non residential project (often they are not a bargain at the price you are asked to pay) and discuss some other creative ways a GC can increase cost to the Owner in CCIP's.

One creative overcharge involves the GC including the agreed to CCIP cost in subcontract values and also including it as a line item in the schedule of values. The GC adds a percentage to the low bid sub's price for the CCIP insurance that is actually being purchased by the GC. The GC has no intention of paying this amount to the subs, it is just less obvious to anyone that may look at the billings. The Owner is then asked to pay the GC upfront most, or all, of the CCIP amount. The Owner is not aware that the GC has included a similar amount in the subcontracts as well. The GC then requires the subs to bill all of this extra insurance in their first pay application. The GC collects this insurance amount from the Owner in addition to the CCIP amount disclosed in the pay application, pays the sub only the subs actual cost, not the CCIP amount that the sub was asked to bill, and therefore collects twice, or close to twice, the CCIP estimated amount from the Owner very early in the project. If the Owner catches on at the end of the project then the total CCIP cost is reconciled, but of course the GC has had the Owners money for a year or more. If the Owner does not catch on and there is no audit performed then.... well you get the idea.

A second issue is requiring the subs to provide proof of additional insurance. The main point here is why the Owner agreed to CCIP in the first place. Many of you have heard the GC spiel of why CCIP's are a good thing for the Owner. A single source of insurance for all claims, less cost, and finally, better coverage than many subcontractors can afford, thereby allowing smaller, and possibly disadvantaged, subcontractors a more realistic opportunity to bid on work. On this last point we have seen recently where smaller subs who did not meet the GL requirements of a certain GC were required to buy insurance at higher limits. This additional insurance was then added to the subs bid, thereby increasing the bid and increasing the cost to the Owner. Now, tell me again why we are letting a GC charge us for CCIP's?