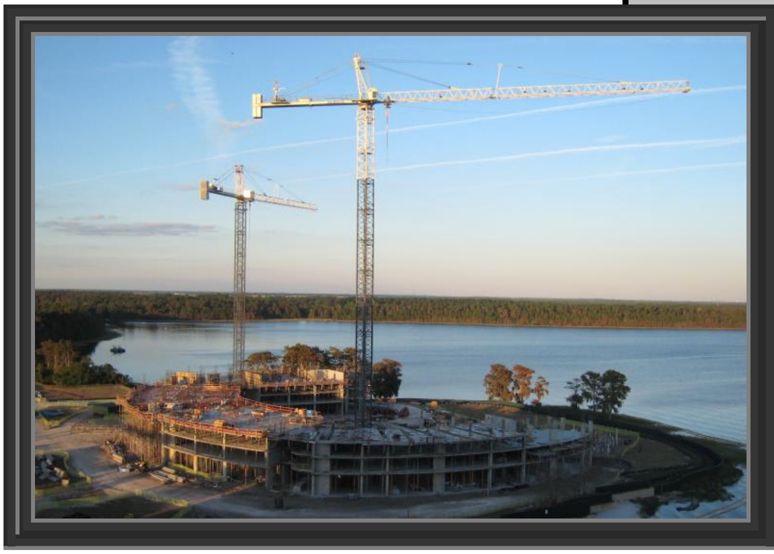
Ten Things to Consider When Contracting With MEP’s on a GMP Basis

Using a lump sum contract is a typical approach to contracting with mechanical, electrical or plumbing (MEP) subcontractors. But it may not always be the best way.

Using a GMP contract for your MEP subcontractors offers a lot of the same benefits that are gained by using a GMP contract for the prime contractor.

Potential savings is one of the main advantages. However, these potential savings can disappear quickly depending on the contractual deal that is made with the MEP subcontractor. If your contract is not specific, you may end up paying much more to the GMP subcontractor than their true costs plus the agreed upon FEE.



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Owners and their Construction Managers should consider the following ten point list of potential "hidden profit" problem areas before agreeing to the billable "costs" proposed by any GMP subcontractor:

1. Proposed FEE percentages for overhead and profit may exceed competitive FEE ranges for similar size jobs with similar commercial risks. For example, a proposed FEE of 21% would be considered excessive if the normal competitive FEE range for similar GMP MEP contracts would be 10% or less.

2. Proposed "Fixed Labor Rates" may be higher than actual wages plus actual labor burden by 10% to 50%.

3. Proposed "Fixed Labor Burden Cost Factors" may be higher than actual labor burden costs by 10% to 100%.

4. Proposed standard "discounted book" prices for commodity materials such as pipe, conduit, fittings, etc. may be 200% to 300% of actual commodity material costs.

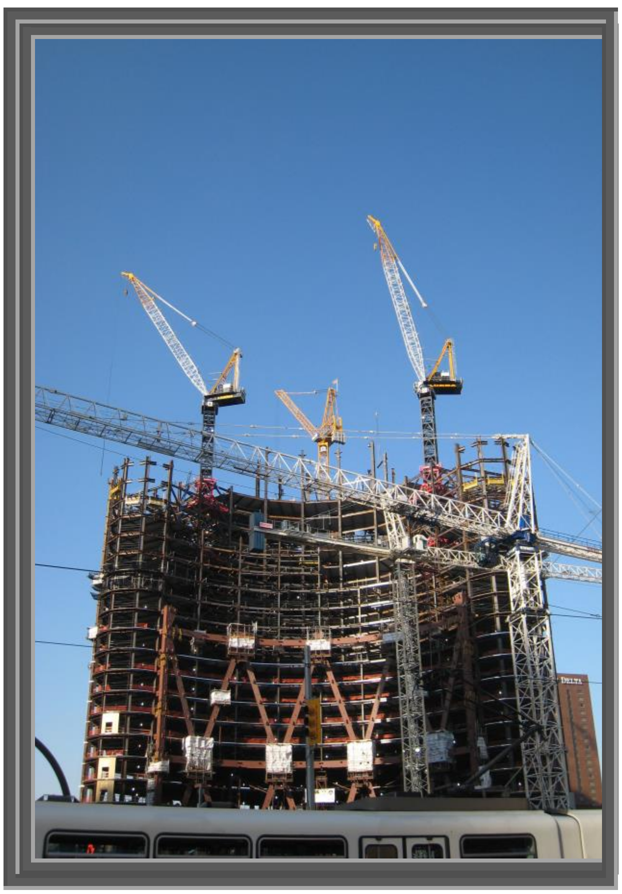
5. Proposed "Equipment Rental Rates" on equipment owned by the Subcontractor may be 20% to 50% more than actual competitive third -party equipment rental rates for comparable equipment.

6. The GMP subcontractor may end up charging 2 or 3 times the fair market value (FMV) of a piece of subcontractor owned rental equipment unless the contract establishes a limit on "aggregate" bare rental charges. Note: If you plan to let the subcontractor keep the equipment after the job is over, consider establishing a cap on aggregate rental charges as a percentage of the FMV of the piece of equipment at the time it was brought to the job.

7. Proposed "shop burden markups" on shop-fabricated material or assemblies to be delivered to the job for installation may be higher than actual allowable and allocable overhead savings gained costs. Hidden profit in these markups may significantly offset the actual labor by not assembling work in the field.

8. Proposed charges for subcontractor "post-contract warranty" costs" may range from .5% to 1% of the GMP.

Note: Many owner's draft contracts that state "warranty costs" are considered covered by the MEP subcontractor's FEE rather than being allowed as a direct reimbursable "Cost of Work".



9. Avoid the use of proposed lump sums for miscellaneous portions of scope of work to be performed by the GMP subcontractor. For example, avoid the use of paying proposed lump sum amounts for scope of work such design assist services and/or general conditions. By comingling lump sum and GMP work, the owner is taking a risk that costs attributable to the lump sum can be shifted to the Cost of Work billings effective charging twice for the same costs.

10. Proposed use of related party sub-subcontractors using lump sum subcontracts arrangements rather than GMP sub-subcontract arrangements can result in hidden excessive profits by 10% to 50% due to a possible lack of meaningful competitive bidding. Note: Related party sub-subcontracts should be GMP contract arrangements with agreed upon limits on FEE payable to the related party sub-subcontractor.

Unless properly addressed, the impact of these potential "hidden profit" cost factors on a $50 Million cost plus fee GMP subcontract could improperly add $5 million to the amount paid to the GMP subcontractor.