

Guaranteed Maximum Price Contracts Versus Lump Sum Contracts



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Guaranteed Maximum Price Contracts for churches are becoming more popular as a vehicle to minimize risks, avoid claims and integrate the diverse interests of a church building project. The Guaranteed Maximum Price contract is bid exactly the same as Lump Sum contracts. The contractor (or construction manager) assumes the same risk with a major difference; i.e., the contractor is willing to share with the church in any savings generated between the stipulated Guaranteed Maximum Price and the actual ending cost of construction.

How does this work? The best way to do this is to start off right by telling any contractor you will be asking to bid on your project that you will be working with a Guaranteed Maximum Price type of contract rather than a Lump Sum contract. With this type of contract the contractor will have to spell out his margins or fees and overhead costs for you right up front, as well as share the cost of the subcontractors, invoices and any other costs during the construction of the project. It is basically an “open book” accounting system.

What are some of the advantages? First of all, the atmosphere has changed from a possible adversarial one to a partnering one. With proper controls, and by working with the contractor as a team member, it is possible to obtain greater yields on the bottom line; ie, possible savings. With the Lump Sum type of contract there is no opportunity for the church to share in any savings.

Guaranteed Maximum Price contracts best achieves the church’s objective because a partnership is formed between the church and the contractor wherein the church agrees to reimburse the contractor for actual costs as they occur, not from a schedule of values. This eliminates the distrust between the church and the church’s architect and the contractor because of the contractor’s tendency to draw as much money up front as is possible. This is called “front end loading” and is a common practice in the construction industry. With proper controls, it also eliminates the contractor’s negligence to pay the suppliers and subcontractors.

Another good reason to use Guaranteed Maximum Price contracts is because it is the best vehicle for recovering costs when pricing on change orders becomes unreasonable. Under the Lump Sum contracts churches often don't have much choice but to pay what the contractor is quoting for a change order. Under the Guaranteed Maximum Price contract, once the work is complete and the true cost of a change order is known, even if the contractor quoted an unreasonable cost at the outset, the church is protected.

Though there are other good reasons a Guaranteed Maximum Price contract is best for a church, there is also a downside. These types of contracts require more work on the church's part to administer. The main thrust involves defining what is "cost" and monitoring the costs once it is defined. Properly set-up and administered, Guaranteed Maximum Price contracts are a win-win situation for the church and the contractor.