

Real Estate Strategies

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Soaring Construction Costs Demand Smarter Project Management

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HERE'S THE SITUATION: YOU ARE A COMMERCIAL USER OF OFFICE SPACE, EITHER A TENANT OR BUYER, AND YOU ARE NEGOTIATING A NEW LEASE, OR RENEWING YOUR LEASE, OR PURCHASING A BUILDING FROM A LANDLORD.

With construction material prices rising on average 25% - 30% during the past year in North America, construction budgets are tight and estimates have to be right. Many landlords have responded to these higher costs by reducing what they give for tenant improvement allowances and build outs for tenants and buyers. In short, the landlords have changed the rules, and you better protect yourself by doing your homework.

Tenants and buyers typically overlook key components of construction pricing comparison in reviewing their options for a lease or property ownership. While it's important to compare construction bids on an apples-to-apples basis, some apples are indeed quite different. In other words, do not look at the bid price alone, look at what's included.

Here are some tips to save time, money and aggravation:

- If you are required to use the landlord's contractor, request that the contractor receive bids from three (3) subcontractors.



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- When hiring a general contractor yourself, consider making the general contractor your partner on the project and bid out the work to three subs.

- Know what the definition of “Base Building” really is in your lease or contract, and what is being provided at the landlord’s expenses. In buying a property, be aware that some landlords are broadening their definition of a base building, in order to scale back their costs. For example, where the landlord once provided parabolic lighting stacked on the floor, the lights are now priced into the user’s build-out budget.

- Test fits should be carefully scrutinized. If the landlord’s architect creates an 8x11 area replica, make sure to determine the real costs of per square foot build out costs. Be sure that all contractor estimates are based on actual per square foot costs that are based on the building’s standards, or upgrades if required by tenant. Anything less will lead to big cost overruns.

- To make the comparison of the preliminary bids easier, have all the contractors use the same specific

form to establish 16-line item breakdown.

- If you don't have prior knowledge of the construction companies doing your work, make sure they are bonded to handle the project and check their prior experience. Make sure the landlord will approve these companies to work in the building. Many times, this indicates whether the construction firm is credible.

If using preliminary plans for pricing, the price will only be as good as the details provided to the construction company. If the plans are short on details you or your architect should do a systematic review of the plans and identify budgets to be used for carpet, vinyl, wood. Do the plans call for painting or wall covering?

After receiving the bids, remember that the cheaper price is not always the best price. Do a detailed review of the bids. This may uncover missing items or a better pricing alternative than the original plan.

If there's a significant pricing difference in a bid category, that's a red flag. For example, if one contractor prices electrical at \$50,000 and another bids \$30,000 there are probably big differences in how each interpreted the plans. By going through each line item bid with the contractors, you can often create cost savings.

In many instances, having the preliminary pricing budgeted can also provide a checklist when final pricing is completed. If nothing was changed on the plans, there should be very little or no change on the final pricing. However, contractors provide pricing on

multiple projects and can get different prices from their subcontractors due to many reasons. By developing preliminary pricing documents, you not only qualify the best contractor, but you also confirm that the final construction bid is within budget, and you avoid huge surprises at the end of the construction project.

By managing the process closely, you will create cost savings and value by avoiding cost overruns and construction problems.

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