

**PROCUREMENT POLICY BOARD (PPB)**  
1151 Punchbowl Street, Conference Room 410  
Honolulu, Hawaii 96813

Regular Meeting  
June 18, 2009  
1:00 pm

AGENDA

- I. Call to Order.
- II. Approval of Minutes – Meeting of May 21, 2009.
- III. Board’s request to discuss the process on how items are to be included on the agenda.
- IV. Request by Lance Inouye, General Contractors Association, regarding proposed change to HAR Section 3-125-13 (Addition to the Price Adjustment Clause in Construction Contracts).
- V. Executive Session to discuss personnel matters in the recruitment for Administrator, State Procurement Office.
- VI. Announcements.
- VII. Adjournment.

Agenda and available agenda items may be viewed at <http://hawaii.gov/spo/procurement-policy-board-minutes-of-meeting>. Individuals may present testimony on matters on the Procurement Policy Board’s agenda when the agenda item is being discussed by the Board. Individuals intending to testify should contact the State Procurement Office at (808) 587-4700 at least 48 hours before the scheduled meeting. Written testimonies will be accepted through e-mail at [procurement.policy.board@hawaii.gov](mailto:procurement.policy.board@hawaii.gov) or faxed to (808) 587-4703 until 1:00 pm, June 16, 2009. Testimonies received after the June 16, 2009 deadline will be forwarded to the board as time permits. Individuals submitting written testimony at the meeting and would like the written testimony distributed to the board at this meeting, are requested to provide 12 copies.

Individuals requiring special assistance or services may call (808) 587-4700 by 1:00 p.m., June 15, 2009 to discuss accommodation arrangements.

# Agenda Item IV



"Lance Inouye"  
<lance@rsinouye.com>  
05/12/2009 08:45 AM

To <aaron.fujioka@hawaii.gov>  
cc  
bcc  
Subject Proposed Change to HAR Sec 3-125-13

History: This message has been forwarded.

Hi Aaron,

Thanks for the call last evening reminding us of the need to submit our proposed rule changes for consideration by the PPB next week. Attached is another draft that I tried to whip up as fast as I could (*needless to say, I didn't get it done by last night as I hoped due to prior personal commitments*). I am off to a set of meetings but will have my cell phone on (Cell: ). Please feel free to call me on my cell with any questions whatsoever...as always, your suggestions/comments on the draft are certainly welcome. If I don't answer my cell because I am in a meeting, please leave a message and I will return your call at the next break.

Again, thanks a lot for your continued assistance in the process.

Lance Inouye



090512.Proposed Act 291 Addition to Price Adj Clause-PPB w-just.doc

(Previously Agenda Item VI on the 5-21-09 Agenda)

**Proposed Act 291 Addition to the Price Adjustment Clause in Construction Contracts, HAR §3-125-13  
05-12-2009**

**Proposed Change:** Add the following within the "Price Adjustment Clause" of HAR §3-125-13:

*"(3) Determining the cost or credit. In determining the cost or credit to the State resulting from a change, it will not be considered unreasonable to apply the following allowances for all overhead, including extended overhead resulting from adjustments to contract time (including home office and branch office overhead) and profit combined:*

- (A) For the contractor, for any work performed by its own labor forces, twenty percent (20%) of the direct cost;*
- (B) For each subcontractor involved, for any work performed by its own forces, twenty percent (20%) of the direct cost;*
- (C) For the contractor or any subcontractor, for work performed by their subcontractors, ten percent (10%) of the amount due the performing subcontractor.*

*Not more than three markup allowance line item additions including the percentages shown above will be allowed for profit and overhead, regardless of the number of tier subcontractors.*

*This section shall not be construed to impair the right of a contractor and government agency from mutually agreeing to a price adjustment as specified in section (1)."*

**Justification:** A few State agencies are **requiring** Contractors to submit change order proposals for **negotiating** a fixed price using the pre-Act 291 15% markup for self-perform work, and 7% on top of subcontractor change proposals (hereinafter referred to as the 15%/7% markups). The GCA and BIA respectfully feel that this is contrary to the spirit and intent of Act 291, Section 4 (effective July 1, 2007) and will have a detrimental effect on the orderly delivery of construction services in the State. The proposed change would permit State agencies and Contractors the latitude to negotiate a fixed price change order in good faith without dictating a format ahead of time.

**Discussion:** Prior to Act 291, both the Hawaii Administrative Rules (HAR §3-125-13) and the DAGS Interim General Conditions of Contract 1999 (IGC) dictated the 15%/7% markups. During legislative deliberations of Act 291, construction industry groups noted that the 15%/7% markups were, in many cases, insufficient to compensate them for change orders requested by the State. In fact, many years ago before those markups were specified in the HAR and IGC, corresponding markups of 20%/10% were permitted and considered the norm. We (GCA/BIA) respectfully maintain that the intent of Act 291 was to restore the 20%/10% markups that more fairly compensate Contractors and Subcontractors for change order work. Accordingly, Act 291 increased change order markups to 20%/10% respectively, but only when no fixed price agreement can be reached and the default force account (for values not exceeding \$50K) or unilateral change order (for values exceeding \$50K) method is implemented

Although, technically, Act 291 does not **require** use of the 20%/10% markups when **negotiating** a fixed price change order, it also does not **require** use of a lesser set of 15%/7% markups nor does it require use of a greater set, such as 25%/12% markups. Because the applicable amended section of Act

291 provides great latitude in coming to a fixed price agreement on the price of change orders<sup>1</sup>, we feel it is against the spirit and intent of the new law for State agencies to *dictate* the markup percentages for negotiating a fixed price agreement.

Moreover, those agencies insisting on having Contractors negotiate using the outdated 15%/7% markups are creating logjams for the orderly progress of construction projects. This is because the Contractor's primary recourse is to disagree and apply the force account/unilateral change order provisions of Act 291 which require using the 20%/10% markups. Defaulting to the force account method of proceeding could be both inefficient and costly for both parties and detrimental to the overall success of the project. For the State, it would require costly close monitoring of the activities associated with the change to ensure the charges are appropriate as well as potential claims of extended overhead due to long negotiations to settle the change. For the Contractor, it would require more paperwork to keep track of the time and materials associated with the change. (Some say certain Contractors prefer the force account method as an opportunity to assign the least efficient workers on the force account work.) Those additional costs incurred and time spent by both sides to monitor and track force accounts are of no real benefit or value to the project's overall success.

The proposed addition to the "Price Adjustment Clause" would give all applicable agencies the comfort level that negotiating change order proposals using the 20%/10% markups would not be unreasonable and many change orders could be amicably negotiated to a fixed price amount. It would still permit both parties to negotiate amicably to a fixed price by lower or higher percentages depending on the circumstances. For example, some have negotiated using reduced percentages due to a tight budget amount or an amount remaining in the project.

It is hoped that the proposed addition would streamline the delivery of a construction project to the benefit of both the State and the Contractors.

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<sup>1</sup> HRS §103D-501(b) provides four methods of negotiating a fixed price change order, the last of which reads: "(4) In any other manner as the contracting parties may mutually agree upon before commencement of the pertinent performance..."