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CONSENSUSDOCS 290 GUIDELINES FOR OBTAINING OWNER FINANCIAL INFORMATION

(with Owner Financial Questionnaire, ConsensusDOCS 290.1)

This document was developed through a collaborative effort of entities representing a wide cross-section of the construction industry. The organizations endorsing this document believe it represents a fair and reasonable consensus among the collaborating parties of allocation of risk and responsibilities in an effort to appropriately balance the critical interests and concerns of all project participants.

These endorsing organizations recognize and understand that users of this document must review and adapt this document to meet their particular needs, the specific requirements of the project, and applicable laws. Users are encouraged to consult legal, insurance and surety advisors before modifying or completing this document. Further information on this document and the perspectives of endorsing organizations is available in the ConsensusDOCS Guidebook.

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A. INTRODUCTION

In any contractual venture, each Party has a legitimate interest and responsibility in ascertaining whether the other Party is fully capable of performing all of its contractual obligations. In an owner/contractor relationship, before entering into a contract with a contractor, an owner often requires financial statements and bank references from the contractor, and may require a surety bond which guarantees both project performance and payment obligations.

The proven ability to pay is just as important as the proven ability to perform. A contractor, therefore, has an equally valid interest in receiving assurances that a project owner has sufficient funds available to make payments in accordance with the terms of the construction contract. Too often the contractor does not have this information—either because the contractor fails to ask for it, is reluctant to ask, or the owner refuses to provide the information. Because of a desire to "get the job" and then to avoid confrontation at the outset of a project, some contractors do not pursue this issue and proceed on "blind faith" or with simple assurances that sufficient funds are or will be available.

It is important that both Parties to a construction contract have satisfactory information about the other's financial capability. In ConsensusDOCS 200, Standard Form of Agreement and General Conditions Between Owner and Contractor (Where the Contract Price is a Lump Sum), Paragraph 4.2 relates the owner's responsibility to provide the contractor with financial information. Obtaining the owner's financial information is a condition precedent to the contractor's commencing or continuing work. The owner also has the affirmative duty of notifying the contractor of any material change in the owner's project financing.

AIA Document A201-2007, General Conditions of the Contract for Construction, contains a similar provision. Subparagraph 2.2.1 of A201 provides that a contractor has the right, both prior to commencement of the work and at any time thereafter, to require the owner to furnish "reasonable evidence that financial arrangements have been made to fulfill the Owner's obligations under the contract." Unless the information is provided on request, the contractor has the right to refuse to commence or continue work or to terminate the contract (A201, Clause 14.1.1.4).

Regardless of the contract documents being used, the contractor should require the same financial information from the owner as the contractor would expect to receive if either ConsensusDOCS 200 or A201 was being used.

The purpose of these Guidelines is to identify for the contractor the type of information that should be requested and the reasons why particular information is important. Where either ConsensusDOCS 200 or A201 is being used, the contractor has an absolute right to receive "evidence" of financial capability. Although "evidence" is not defined in ConsensusDOCS 200 or in A201, these Guidelines and the accompanying Owner Financial Questionnaire are designed to identify what "evidence" would encompass. Where either ConsensusDOCS 200 or A201 is not being used, these Guidelines and the Questionnaire will assist the contractor in justifying a request for financial information from the owner.

The Guidelines and the Questionnaire are not all encompassing. Individual project conditions or contractual arrangements may create unique circumstances that require different or additional information. In certain cases, depending on the owner or on the contractor's relationship with the owner, the contractor may not wish to ask for all of the information specified on the Questionnaire. These Guidelines, as their name suggests, are just guidelines, and the Questionnaire is simply a standard form for obtaining information, which, in most cases, should be sufficient for permitting the contractor to ascertain an owner's financial capabilities. However, in all cases, a contractor is encouraged to evaluate whether additional information is required by the conditions of the project or the contractual relationship with the owner.

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B. STEPS TO ENSURE A FINANCIALLY TROUBLE FREE JOB

1. Have a signed contract before commencing work. This is simple and sound advice that is nevertheless often overlooked.
2. Require that the contract provide for the owner's compliance with a request for financial information (particularly important if ConsensusDOCS 200 or A201 is not being used).
3. Identify the owner of the property on which the project is being constructed, as well as the contracting Party. Is the construction financing secured by the land?
4. If using the owner's contract form, get a legal review of the document. This review is essential to ensure proper risk allocation and can prove cost effective in the long run.
5. Even if an ConsensusDOCS or AIA contract form is being used, review carefully to be sure applicable standard provisions have not been modified or deleted.
6. Insist on contractual provisions that you feel are fair and essential. Do not be afraid to suggest an alternate contract form. Both ConsensusDOCS and AIA publish contract documents that enjoy industry-wide acceptance.
7. Obtain a copy of the owner's financial statement -- preferably certified by a Certified Public Accountant (CPA). If available, obtain a report from Dunn & Bradstreet. This can provide substantial financial data and other information about the owner.
8. Obtain a credit report on the owner -- your bank can assist in this effort. Also, if the owner is a publicly held company, obtain and review its annual report.
9. Obtain a copy of the owner's construction loan agreements for construction and permanent financing. A copy of the loan documents is preferable over a simple commitment letter, because the loan documents will include all of the lender conditions and requirements. Of significance are the requirements for notification to the lender, whether the lender must approve changes, and assignment of the contract to the lender.
10. Beware of a loan commitment that covers items other than construction.
11. Request a lender's "set-aside" letter that acknowledges the portion of construction loan proceeds available exclusively for payment of construction draws.
12. Identify whether the available funds are sufficient not only for the original contract amount but also for contingencies, such as changes and extras. If money is not set aside at the outset for contingencies, as changes or extras arise, the contract must make a separate request for financial information pertaining to the change. A procedure should have been established for notifying the lender of changes.
13. Determine the sources of funds, the method and time of disbursement and the persons through whom the funds must pass before reaching the contractor.
14. Investigate the stability of the lender. (Periodic meetings with the lender during construction to review project status are also valuable.)
15. Determine the legal structure of the owner. If a corporation, determine who is authorized to sign on behalf of the corporation by requiring a corporate resolution. If a partnership, determine who are the general partners and which partners can legally bind the partnership.
16. Request a list of the owner's prior projects. Investigate the owner's payment performance on previous projects.

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17. Do not ignore the project architect. What roles does the architect play in the payment process? Investigate the architect's reputation relative to expeditious contract administration, particularly regarding processing payment requests.
18. Ask for a copy of the owner's agreement with the architect. This will assist in assessing whether sufficient funds are available to cover the owner's financial obligations, particularly if loan proceeds can be used to pay design costs. It will also identify the architect's contract administration responsibilities and whether the architect's responsibilities are consistent with the provisions of the general conditions (ConsensusDOCS 200 or A201) for the project. In addition, the owner/architect agreement will help determine whether the architect has professional liability insurance. The latter point is important because it could materially affect the owner's financial capabilities if claims are ever filed because of design errors and the architect is uninsured.
19. Check the applicable lien statutes relative to the contractor's rights and those of subcontractors and suppliers and the procedures to enforce those rights. Do this at the outset of the project. Pay particular attention to the contractor's standing relative to the construction lender. If ConsensusDOCS 200 is being used, Paragraph 4.5 provides the right to such information. If A201 is being used, Subparagraph 2.1.2 gives the contractor the specific right to this information.
20. Obtain information regarding the owner's property insurance coverage. Be aware of the policy provisions regarding deductibles and contract clauses requiring waivers of subrogation.
21. If some portion of the project funds is being provided by a governmental entity, determine the nature of the funding programs; whether the portion is a loan, a grant, or a bond issue; the name of the grantee if a grant, or the bond trustee if a bond issue; the name and address of the agency contact person; and the expiration date of the grant, if applicable.

C. SOURCES OF INFORMATION

1. Owner Financial Questionnaire attached to these Guidelines.
2. Contractor's Bank -- Bankers have access to information that individuals can not easily obtain themselves—credit reports, for example. A contractor's banker has an interest in the contractor being paid; otherwise, the contractor could be forced to use its own resources, such as lines of credit, to meet its obligations. The contractor's bank should be cooperative in assisting the contractor in learning as much about the owner's financial capability as possible.
3. Contractor's Bonding Company -- The surety has a vested interest in a contractor's performance and in the contractor's ability to obtain timely payment. Payment by the owner is generally a condition precedent to the bonding company's surety obligation. The bonding company's obligations could be extinguished by an owner's failure to make payment. However, contractor nonpayment not only will adversely affect the contractor's financial condition but could increase the bonding company's risk relative to other projects of the contractor bonded by the surety. The nonpayment would decrease the contractor's working capital and also reduce net assets available to indemnify the bonding company if claims are made against a bond. Therefore, the surety should be interested and cooperative in assisting the contractor in obtaining financial information about the owner.
4. Contractor's Attorney -- The contractor's attorney can be helpful in obtaining land title information, such as legal ownership, amount of security interests on the property, liens, and whether there are restrictive covenants, or other property use restrictions which the proposed construction would violate. Sometimes use restrictions can be overlooked in the permit process. When discovered, they could stop construction or the owner's use of the property, which in turn may stop the flow of funds and thus payment to the contractor. The attorney also can be helpful in researching court records to see if the owner is involved in any litigation on previous projects. An attorney with a construction law practice can be a valuable source

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of information regarding the owner's reputation in the industry.

5. Other contractors, subcontractors and suppliers with whom the owner has done business.

D. OWNER FINANCIAL QUESTIONNAIRE

The following are comments regarding specific items on the Owner Financial Questionnaire.

I. Project Owner -- These questions are designed to identify the owner and its legal structure and, therefore, identify the ultimate responsibility for payment. Legal structure is particularly important. If the ownership entity is a corporation, particularly a small, closely held corporation, the contractor may want to consider obtaining a personal guarantee from the principal stockholder(s). Pay particular attention to subsidiaries of even well-known corporations, which may have no assets of their own. A corporate resolution would also be appropriate to identify the authorized officers who can sign on behalf of the corporation.

II. Project Information -- It is essential for the contractor to understand the basic parameters of the owner's project. As a result, these questions will identify important project information, such as the project name and location, the name of the project owner's authorized representative, the method of construction contemplated, the name of the architect/engineer, and bond requirements, if any. The questions also address liquidated damages and payment and retainage information.

III. Land Information -- These questions will identify whether the person or entity named as the "owner" in the agreement holds the legal title to the project property. It is essential that the contractor have the correct name of the property owner and the legal description of the property if a lien has to be filed. Forwarding this information to the contractor is a requirement under Paragraph 4.3 of ConsensusDOCS 200 and under Subparagraph 2.1.2 of A201. The contractor also must know what encumbrances are recorded against the property and which have priority over a contractor lien claim. The most recent title binder or abstract would show this information. This will help the contractor assess whether the land offers any security if an owner defaults on payment. Where the land has little security value to the contractor, the contractor may want to pursue other forms of security, such as a personal guarantee. This information is requested primarily because of its relationship to an owner's financial capabilities.

IV. Financing Information -- Sources of Project Financing -- These are the most critical questions because they relate to the actual intended source of funds. Beware of commitment letters that are general in nature and do little more than identify the amount of the loan. The actual loan document, often called a Construction Loan Agreement, is far more important because it sets forth all of the conditions and requirements of the loan, including what the loan proceeds can be used for and what rights the lender may reserve to use the loan proceeds for, such things as "prepaid" interest, which can reduce the actual amount of funds available for construction draws. The loan agreement may list continuing obligations of the owner, which if not satisfied, could be grounds for the lender to stop funding the project while in progress. A lender's "set-aside" letter, as requested in Item V of the Questionnaire, is an important document, because it represents an acknowledgement by the lender as to the amount available for construction draws and the lender's agreement that such funds will be applied only to construction costs. However, be aware of any qualifications in such a "set-aside" letter that could limit the lender's obligations. If government funding, either by loan, grant or bond issue, is being used for the construction, the information listed on the form is needed and must be evaluated by the contractor as to its sufficiency to the same extent as a traditional construction loan.

V. Copies of Relevant Documents -- This section identifies six items that are useful to the contractor in assessing the owner's financial capability. The owner's responses to other portions of the Questionnaire may dictate that other documents are also required. This list is a general guideline of documents that should be requested in most cases.

a) Owner's Certified Financial Statement -- Make every attempt to get a financial statement certified

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by a CPA.

b) Construction Loan Agreement -- This has been explained above.

c) Lender's "Set-Aside" Letter -- Explained above.

d) Owner/Architect Agreement -- This is important in order to identify the amount of the architect's fee which, if payable out of the construction loan proceeds, will affect the amount of funds available to pay the contractor. It will also identify the architect's project administration responsibilities and its insurance obligations.

e) Owner's Property Insurance and/or Builder's Risk Policy -- If the owner does not have adequate insurance, the funds available for construction could be adversely affected should losses occur during construction.

f) Architect's Professional Liability Policy -- In addition to verifying that the architect has professional liability coverage, the policy will identify the nature and extent of such coverage and the degree of potential exposure the owner may have to claims relating to design errors.

E. SUMMARY

The three essential elements of any contract are an offer, acceptance, and consideration. In a construction contract, consideration on the part of the contractor is the construction; on the part of the owner it is payment. An owner, in an effort to obtain assurances that the contractor can fulfill its obligations, will often require financial and performance information from the contractor and possibly a surety bond before awarding the contract. Contractors have similar interests and also a right to obtain information sufficient to assess an owner's ability to meet its payment obligations. These Guidelines and the accompanying Questionnaire will assist the contractor in identifying the types of information needed from the owner to make this assessment. The information requested by the Questionnaire is reasonable information that is consistent with the requirements of ConsensusDOCS 200 and the 2007 Edition of AIA Document A201. Likewise, the financial information requested can be fully justified as accepted industry practice in a situation where either ConsensusDOCS 200 or A201 is not being used. The Guidelines will assist the contractor in justifying its request. The Questionnaire, as a standard form, will make it easier to obtain the requested information. When this information is evaluated, contractors will be better able to assess the owner's ability to pay and to make more informed decisions when considering entering into construction contracts. Contractors should insist that notification be given by the owner of any changes or modifications to the financial arrangements which occur at anytime during construction of the project. In addition, contractors should not be reluctant to exercise their right to make periodic requests during construction. Experience shows that owners respect such a conservative approach by their contractors as a demonstration of financial acumen and sound business judgment -- thus beginning the relationship on a positive note.