

# THE RISK ILLUMINATOR

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## Change Order vs. Construction Change Directive.

Change Orders...Construction Change Directives. Each may seem to describe the same change - but there are important differences between the two. Differences that all parties need to understand, so as to minimize confusion, delays - and potential liability.

First, there is the need to identify whether the change is a major change, or a minor one. If the change is minor, the Architect generally has the authority to order minor changes in the work via a Construction Change Directive, as long as it does not involve adjustments in the contract sum, the contract completion time, or the collateral performance. But, if the change does involve adjustments to time, money, or both - *these requests for adjustment result in the contractor generating a **Change Order Request (COR)*** . **The result of these requests become either a Change Order (CO), or a Construction Change Directive (CCD).**

**Change Order** - is a written order completed by the Architect, and signed by both the Owner, and the Contractor. This form describes the date, the change (sometime by reference to other forms such as construction bulletins or requests for information), the amounts involved, the time increase or decrease, and a recap of the status of the original contract as affected by cost or time - and *requires agreement among the Owner, Architect and Contractor*. **Each change order is a contract that requires the same legal consideration as any contract.**

**Construction Change Directive** - is a written order prepared by the Architect - and signed by only the Owner and Architect, directing a change in the work, as well as a proposed basis for adjustment in Time, Cost - or both. **The Construction Change Directive is used in the absence of total agreement on the terms of a Change Order.** The Contractor executes the CCD, although they may not agree with the terms of the directive. Disagreement may be centered around Time, Cost, or both - but the agreement is to complete the work based on the terms of the Directive - and work out the final terms of the adjustment after the work has been completed.

### How does this affect the Lender?

As a Lender, you need to keep in mind the following:

**1. You need to stay on top of all construction Change Order Requests.**

Realize that these requests may turn into Construction Change Directives, that may impact the filing of liens against the property if agreements cannot be made by the end of the project. This is no place for micromanagement - but, you need to determine where funds will come from to rectify disagreements.

Funds generally come from 4 sources:

- Other Line Item Savings (no net change in contract amount)
- Equity (i.e. Borrowers pockets)
- Contingency Funds
- Loan Increase



## Topics In This Issue

Change Order vs. Construction Change Directive

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Hard-Hat University - Pop Quiz #

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### **Lender's Quality Assurance**

1553 W. Todd Drive, Suite 207  
Tempe, AZ 85283

ph: 480 897 3999  
fx: 480 897 3444

email: [lqa@earthlink.net](mailto:lqa@earthlink.net)  
Web: [www.inspectnet.net](http://www.inspectnet.net)

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## Lender's Quality Assurance

1553W . Todd Drive, Suite 207  
Tempe, AZ 85283

# Label

ph : 480 897 3999  
fx : 480 897 3444

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### Change Orders vs. Construction Change Directives - continued:

**2. Does the change materially affect my collateral / appraisal value?** Size of adjustment is irrelevant - you need to determine if the change will have an impact on overall value of the project. **Example #1-** A cheaper entry lock on hotel room doors may result in hotel guests feeling less secure, making it harder to sell hotel rooms, decreasing the income and subsequently lowering the value of the property.

**Example #2-** Reducing paving thickness on a parking lot might decrease the useful life of the parking lot, increasing annual operating expenses, and decreasing the value of the property.

Although a lender should not engage in micro-management of the lender's borrower's business, it is very important to understand how construction changes can effect its collateral position.

Notice our new newsletter format? We've updated the look - and, moving forward, we will be making our newsletter available electronically!

Want to receive future issues in your email? Send us a request to join our email list by dropping us an email at:

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## Lender's Quality Assurance



1. Kaolin
2. Kerf
3. Knurl
4. Laitance
5. Lagging
6. Loggia
7. Lumen

### Hard Hat University

#### Definitions - Construction Terms

- A. Thermal piping insulation used to minimize heat loss through the pipe wall.
- B. A fine, white clay used to make porcelain.
- C. A roofed room, arcade, gallery, or other enclosed area, open on one side, usually to the outdoors.
- D. The cut or groove made by a saw blade; the width of any cut.
- E. To make straight line or diagonal cross-hatch depressions in a metal surface to roughen it.
- F. A measure of efficiency of a lamp.
- G. A white, dusty film on the surface of cured concrete - occurs when there is too much water in the mix.

Answers: 1 - B, 2 - D, 3 - E, 4 - G, 5 - A, 6 - C, 7 - F

