

## Contract Risk Allocation Working Group

### Recommended Practice for Managing Risks in Contracts Involving OWNER-FURNISHED PROPERTY

#### INTRODUCTION

*This document is a guideline for managing risks in contracts that involve Owner-furnished property. This document is one part of the Contract Risk Allocation Working Group's charge to address the identification, mitigation, and allocation of contract risks. Actual contract clauses should reflect the circumstances of the specific procurement.*

*This recommended practice represents a consensus opinion of a working group including attorney firms, transit systems, manufacturers, consultants, engineers and general interest groups. The application of any recommended practice, practices or guidelines contained herein is voluntary. In many cases, federal, state or other jurisdictions may require specific language that conflict or amend these recommended provisions.*

#### OVERVIEW OF THE RISKS INHERENT IN CONTRACTS INVOLVING OWNER-FURNISHED PROPERTY

"Owner-furnished property" is property in the possession of, or directly acquired by, the Owner and subsequently furnished to the vendor for performance of the contract (excluding property to be demolished or removed as the primary objective of the contract). In this context, "Owner-furnished property" shall include physical property (not intellectual property) including, but not limited to: buildings, grounds, equipment, materials and vehicles.

#### **Examples of this type of scenario may be:**

- A private vendor taking over a Paratransit bus operation in which the Owner provides the vendor with the vehicles and operating facility along with associated specialty tooling.
- The Owner provides a vehicle manufacturer (vendor) with a 2-way radio system and/or farebox for installation into a new vehicle.
- The Owner contracts for the construction of new infrastructure and requires the Vendor to utilize components provided by the Owner.

The management of risk allocation as it relates to Owner-furnished property can be segmented into the three distinct phases of a project:

- Pre-Award Risk
- Performance Oriented Risk
- Contract Close-Out Risk

These three phases are interdependent upon each other and the associated risk allocation language should be utilized as such.

#### **PRE-AWARD RISK**

The management of risk begins prior to issuance of a solicitation (IFB, RFP). It is incumbent upon the Owner to initiate the risk allocation process during the assembly of the solicitation document. Specifically, the Owner should fully describe all property to be provided. These descriptions should include, but not be limited to the condition, location, dimensions, age, projected remaining life and any unique features, requirements or hazards of the property. One may wish to consider including representative photographs, plats, drawings and similar types of descriptive material in the solicitation package. The solicitation document should also address the disposition of the property at the end of the project, whether it will be returned to the Owner (and in what condition), kept by the Vendor, or sold (and who is entitled to the proceeds).

Once the solicitation has been issued, it is in the best interests of the Owner to provide -- to the extent practicable -- the opportunity for potential bidders to fully inspect the Owner-furnished property. This pre-bid inspection affords potential bidders the opportunity to review the condition and attributes of the property and make their own risk management assessments. The intent is that the more informed the bidders are, the greater the potential that the proposals submitted will be responsive and responsible and the pricing will accurately reflect the true cost to satisfactorily fulfill the project requirements.

Insurance and indemnification requirements relating to owner-furnished property should be thoroughly evaluated and addressed and issued by the Owner as part of the solicitation documents. Administration of warranty obligations on owner-furnished property should be addressed in the solicitation documents as well.

### **PERFORMANCE-ORIENTED RISK**

Once a contract has been awarded the risk allocation process enters the next phase. The example contract terms outlined below (Items 1 through 9) provide suggested guidance for each of these steps. However, one must still consider and manage project specific risks. Examples of these may be:

- Vendor's unfamiliarity with the property
- Assumptions that had to be made about the property during bidding
- Changes in the condition of the property which may have occurred between the time of the original solicitation and the actual start-up of the project.
- Timely availability of property, particularly when it is to be provided by a third party
- Loss/damage of the property itself; Injury/Loss/damage to vendor personnel or third parties due to use of the property
- Property that does not perform as required and or does not complement/work with other project required materials

### **CONTRACT CLOSE-OUT RISK**

The final phase of the contract is the Close-out. At the completion of the contract, the return, transfer or disposition of all remaining Owner-furnished property must occur. Items 10 and 11 outlined below provide a suggested framework for those phases of the contract close-out. In addition to the transfer of the owner-furnished property, the parties must ensure that they have properly discharged any current, pending or potential liabilities associated with the utilization of the property during the term of the contract. The contract document must also allow for transfer of assets in case of early contract termination.

#### *Sample Provisions*

*The following are generic, sample provisions for illustrative purposes that deal with most situations involving owner-furnished property. These provisions should be adapted to the circumstances of a particular contract, project or property provided.*

#### **1. Transfer of Owner-Furnished Property**

The Owner shall deliver to the Vendor, for use in connection with and under the terms of the contract, the facilities, equipment, or other goods described in the contract together with any related data and information that the Vendor may request and is reasonably required for the intended use of the property (hereinafter referred to as " Owner-furnished property").

#### **2. Delivery**

The Vendor shall include delivery of Owner furnished property in its Critical Path Schedule (or project plan/implementation plan), outlined in the contract, which shall be approved by the Owner, if not otherwise scheduled by the terms in the contract. As

directed by the contract's provisions, the Vendor shall schedule delivery dates for the return of any Owner furnished property in the Critical Path Schedule as well.

The delivery or performance dates for this contract are based upon the expectation that Owner-furnished property will be delivered to the Vendor at the times stated in the contract to meet the contract's delivery or performance dates.

If Owner-furnished property is not delivered to the Vendor by the required time, the Owner shall, upon the Vendor's timely written request, make a determination of the delay caused by the Owner and shall make an equitable adjustment in accordance with paragraph 8, if warranted.

### **3. Condition of Furnished Property**

If Owner-furnished property is received by the Vendor in a condition not suitable for the intended use, the Vendor shall, upon receipt or subsequent service use, promptly notify the Owner, detailing the facts, and, as directed by the Owner and at the Owner 's expense, either repair, modify, return, or otherwise dispose of the property. After the Vendor completes the directed action and upon written request of the Vendor, the Owner shall make an equitable adjustment if warranted (as provided in paragraph 8 of this clause).

#### **a) Property Inspection**

i. When the Vendor receives Owner furnished property, the Vendor shall have charge and care of the property (except as provided elsewhere in the agreement), and shall bear the risk of injury, loss, or damage to any part thereof by the action of the elements or from any other cause, whether arising from the execution of the work or otherwise. (Contract clause writers should define timetables for notification appropriate to the circumstances.)

ii. Prior to a Vendor taking possession of the property, the Owner (or an independent third party inspector) and the Vendor will conduct a joint inspection of the property. When the possession is passing from an incumbent Vendor to a new Vendor, the Owner (or an independent third party inspector), the incumbent Vendor and new vendor will conduct a joint inspection of the property. Such inspection shall document the condition and operational status of all Owner-furnished property prior to Contract start if possible and in accordance with the standards provided in the agreement. Any defects to the property shall be documented in writing and photographs taken (where applicable) with copies provided to all parties. The Owner shall make all necessary repairs to correct the defects, or agree to compensate the Vendor for correcting the defects. Upon delivery of the property to the vendor, the parties will conduct a final inspection to ensure the items noted in the preliminary inspection were corrected. In the event the final inspection reveals defects as specified in this section, the Owner will have these items repaired or authorize the new vendor to repair the items at an agreed upon cost.

In the event that the Owner elects not to correct certain deficiencies, the inspection files shall be noted and the Vendor shall not be responsible for the deficient items. In the event that said deficiencies materially impact the ability of the vendor to fully perform their obligations this agreement shall be amended accordingly.

When property is returned to the Owner it shall be in a condition in accordance with the specifications in the contract, normal wear and tear excepted. A joint property inspection will occur prior to the end of the contract and the vendor shall be responsible for the cost of repair of all defects, including those that remain on the date of transfer to the Owner.

### **4. Changes in Owner-Furnished Property**

a) The Owner may, by written notice change the type or amount of Owner-furnished property provided or to be provided under the Contract or to be acquired by the Vendor for the Owner, under this contract. The Vendor shall promptly take such action as the Owner may direct regarding the property covered by such notice.

b) If such changes cause an increase or decrease in the Vendor's cost of, or time required for, performance of any services under this contract, whether or not changed by any order, an contract adjustment shall be made and the contract shall be modified in writing accordingly. Any claim of the Vendor for adjustment under this clause must be asserted in writing within 30 days from the date of receipt by the Vendor of the notification of change unless the Owner grants a further period of time before the date of final payment under the contract.

## **5. Title in Owner Property**

a) The Owner retains title to all Owner-furnished property until properly disposed of, as authorized by contract. Property that is leased by the Owner and subsequently furnished to the vendor for use shall be considered Owner-furnished property for purposes of this agreement.

i. Under fixed price contracts, the vendor retains title to all property acquired by the vendor for use on the contract. until turned over at the end of the contract. At which time, the Owner acquires title to property acquired or fabricated by the vendor in accordance with the financing provisions or other specific requirements for passage of title in the contract. If a deliverable item is to be retained by the vendor for use after inspection and acceptance by the Owner, it shall be made accountable to the contract through a contract modification listing the item as Owner-furnished property.

ii. Under reimbursible types of contracts, the Owner acquires title to all property for which the vendor is entitled to reimbursement, except as may be otherwise provided for in this Agreement.

iii) Special Tooling consists of equipment and manufacturing aids that are of such a specialized nature that without substantial modification or alteration their use is limited to the development or production of particular products or for performing particular services. Title to any facility, special test equipment, and special tooling acquired by the Vendor for the Owner under this contract shall transfer to the Owner when its use in performing this contract commences or when the Owner has paid for it, whichever is earlier. Special tooling does not include any item acquired by the Vendor before the effective date of a contract, or replacement of such items, whether or not altered or adapted for use in performing a contract, or items specifically excluded by the schedule of the contract.

## **6. Property Administration**

a) The Vendor shall be responsible and accountable for all property of the Owner provided to the Vendor under this contract. The Vendor shall maintain property inventory control procedures, records, and a system of identification of the property. If damage occurs to such property, the Vendor shall replace the property or make such repairs as the Owner directs. If it's limited to damage which affects the use of value of the property, Vendor is required to repair or replace, as directed by the Owner, or a contract adjustment made to the price (e.g. if a piece of equipment is "totaled" at the end of the project the Vendor could be backcharged the loss in resale value). Normal wear and tear, or inconsequential damage such as dents or scratches on a piece of construction equipment, should be excluded. However, if the Vendor cannot make such repairs within the time required, the Vendor shall dispose of the property as directed by the Owner. When property is replaced or repaired, the Owner shall make a contract adjustment in accordance with paragraph 8, if warranted.

b) The Vendor shall establish and maintain a program for the use, maintenance, repair, protection, and preservation of property of the Owner in accordance with sound industrial practice and as specified in the Contract.

c) Under those circumstances where risk has been assumed by the Owner, if damage occurs to property the Owner shall replace the items or the Vendor shall make such repairs as the Owner directs. However, if the Vendor cannot make such repairs within the time required, the Vendor shall dispose of the property as directed by the Owner. When any property for which the Owner is responsible is replaced or repaired, the Owner shall make an equitable adjustment in accordance with paragraph 8, if warranted.

d) Repair or replacement of property for which the Vendor is responsible shall be accomplished by the Vendor at its own expense. [The insurance and indemnification provisions related to owner-furnished property are set forth in the insurance and indemnification section of the contract.]

#### **7. Access**

The Owner and all its designees shall have access at all reasonable times to the property of the Owner (and/or records relating to the property) for the purpose of inspection.

#### **8. Contract Adjustment**

When this agreement specifies an equitable adjustment in time or money, it shall be made to any affected contract provision in accordance with the procedures of the Changes Clause. Although the vendor is entitled to reasonable profit on the additional work, the vendor should not be left in a better or worse profit position on the unchanged work after the change than it was before the change.

#### **9. Warranty**

Warranty administration and enforcement for owner-furnished property are the obligation of the owner unless the parties mutually agree to transfer warranty obligations to the vendor.

#### **10. Final Accounting and Disposition of Property of the Owner**

Upon completing this contract, or at such earlier dates as may be fixed by the Owner, the Vendor shall submit, in a form acceptable to the Owner, inventory schedules covering all items of property of the Owner (including any resulting scrap) not consumed in performing this contract or delivered to the Owner.

The Vendor shall prepare for shipment, delivery or disposal of the property of the Owner as may be directed by the Owner. The net proceeds of any such disposal shall be credited to the contract price or shall be paid to the Owner as the Owner directs.

#### **11. Owner Abandonment of Owner-furnished property**

Unless otherwise provided herein, by written notice the Owner may abandon any property of the Owner, at which time all obligations of the Owner regarding such abandoned property shall cease. To the extent the abandonment of the property increases or decreases the vendor's cost, the Owner shall make a contract adjustment in accordance with paragraph 8, if warranted.