BCPM0052 – Week 3 topics for discussion.

1. One of the hardest items to value in the construction contractor's statement of financial position (balance sheet) is the work-in-progress consisting of unfinished contracts. This is often a substantial item. An accountant's rule-of-thumb is that only two thirds of the profit earned to date on unfinished contracts should be taken into the current financial year and the rest deferred against future possible claims by the client or defects or other losses. On the other hand accountants insist that the full amount of any known contract losses should be taken into the current year's Statement of Comprehensive Income (Profit and Loss Account). Is this fair? Accountants are taught to be cautious, conservative and prudent in their accounting whereas Quantity Surveyors (from whom the contract information comes) are taught to claim the maximum they can from clients. Is there a culture clash which makes it difficult to get a true and fair view of a contractor's financial performance?

2. When a main contractor such as Carillion becomes insolvent it is usually holding a large amount of money owed to sub-contractors for work they have already performed and materials delivered to site. However in the queue for the payout from an insolvent contractor, trade creditors (which are mostly sub-contractors and suppliers) come very low down the list. Essentially main contractors are in one sense merely the vehicle through which money passes from the client to pay for what is mostly sub-contractor's work. As a result the insolvency of a major contractor can cause a number of sub-contractors to follow them into insolvency. Can you think of some fairer methods or systems for safeguarding sub-contractor's or supplier's debts when a contractor becomes insolvent?

3. Economists took a long time after Adam Smith to get to grips with the theory of the firm. Two problems in particular were evident. Firstly why do we need firms at all? Why does the market for goods and services take care of all necessary transactions? This was the key question asked by Ronald Coase in 1937. Secondly, how can we be sure that the management of a company is running the company for the best interests of its shareholders and not their own individual interests? This was the question asked by Berle and Means in 1932.

4. Think of all the ways in which construction markets depart from the requirements for perfect competition. Since a contractor does not know their required output in any given time period – are the concepts of marginal cost and marginal revenue actually useful? If we can regard contractors instead as buyers and sellers of risk (like insurance companies) does that provide a better model to think about the way contractors behave in the marketplace?

5. If we accept the model that contractors (and sub-contractors) are effectively in a flexible (flex-price) market when selling their services and a fixed (fix-price) market for procuring inputs, to what extent does this

explain the sort of behavior for which builders are notorious – making additional claims, taking on too much work, finishing work very late, poor quality, failing to rectify defects, collusion in bidding and other faults?