

# Real Estate / Construction

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## Contractor Failure Is Easy, Too

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While it may be easy to get into the construction business, it's also easy to fail, since contractors face one of the highest business-mortality rates, says a local surety bonding agent.

"In many trades, you can just put tools on and say, 'Hey, I'm a contractor,'" said bonding agent John Maloney of **Maloney and Associates**. "But while some may be great at building things, they may not have the business skills that they need to survive."

Maloney lists several danger signals contractors should be wary of to keep their businesses on-course:

### •Poor risk analysis

"Contractors must be aware of onerous owners, onerous contract documents, onerous job site conditions, insufficient completion time frames, poor designs, excessive liquidated damages, as well as the specific complexities of the job itself," Maloney said.

"The first thing you have to verify is that the money is there to pay you. Also, different public entities can be more difficult to work with than others, such as not approving change orders quick enough, or being too quick to assess liquidated damages if the project has slowed down somewhat.

"There's always a gray area and contractors should choose owners who have the willingness to fairly negotiate the gray areas."

Maloney added that poor risk analysis is a major factor in inadequate pricing, which could lead to cash flows drying up — a leading cause of contractor downfall.

### •Poor financial management

"Cash flow is critical," Maloney said. "If owners don't pay on time, contractors must still pay their laborers and suppliers, so they use their bank line of credit. But if their credit is maxed out, it ceases to be a safety net.

"Bottom line: you have to be aggressive in collecting your accounts receivables."

Maloney said that contractors also need to be aware of any and all unapproved change orders, "underbillings," and "overbillings" on each job as well as the specific reasons for each situation.

"A contractor must constantly — and that means on a daily basis — be aware of schedules, budgets, costs, and the status of each job's profitability."

Being on top of the job in the field means good communication between the office and the field superintendents.

### •Poor project management

"Some superintendents may have come from a labor field background, so while they know how to build, but they may not have the business and accounting perspectives."

Field superintendents should be well aware of schedules, budgets, and job costs on a daily basis — and be able to communicate that information to the office also on a daily basis.

"They have a lot of plates spinning on sticks and it takes a really qualified and strong person to make sure the job gets done with no mistakes and that the office constantly stays informed.

"On the positive side, I've seen superintendents use digital cameras daily," Maloney said. "They can take a picture on the jobsite and then use their computer laptops to e-mail the pictures to the office or to their bank or surety agent to show what they've been doing. They even e-mail photos to the architect or the owner for change order requests, along with all of their projected costs."

### •Jobs too geographically dispersed

"If you have jobs all over the place, it's hard to control them," Maloney said. "If there's a problem, you react slower and the problem gets magnified."

Contractors who have successfully expanded their territories have thoroughly done their homework and may have also opened satellite offices.

"It takes a lot more planing to go away from home — different soil condition, different labor conditions," he said. "The contractor needs to assess how he will minimize each potential risk.

"Also, maybe the owner and subs in a different area won't like them for coming there and will do something to adversely affect them. That happened to one of my clients in Hawaii — they didn't like California contractors coming there.

"If you're going to grow outside your area, don't go straight to San Francisco or Seattle — go to Riverside first."

### •Growing too fast

"Growing fast is not dangerous. Growing fast without planning and realizing what is happening while the growth is occurring is what breaks contractors," Maloney said. "A contractor needs to develop his system and overall organization at the same pace as his job growth."

"That doesn't mean just more of the same, though. Their level of sophistication has to increase as well."

Maloney added that a good professional support team, including

accountants, bankers, bonding agents and, if needed, attorneys and claims consultants, can help contractors transition well into bigger companies.

### •Loss of focus by the owner

"I've seen contractors who have been extremely hard-working, and when they have reached a certain level of success, they say, 'Okay, I'm going to go skiing a lot more.'

"That's okay, if they put in a good management structure where they delegate their responsibilities."

Letting go of the control of the business can be the most difficult task for an owner, especially during a business's succession. Maloney said many contractors have a tough time actually thinking about the company's life without them at the helm.

### •Poor business succession

"People don't want to address their own demise," Maloney said. "Other times, contractors are too busy building things to think about what would happen if they were not around.

"You don't have to be old, though, you can also get hit by a truck."

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