

18th Weekly Crisis-era Message to Contractors from: Dr Tom Schleifer
Embracing and Implementing “Flexible Overhead”

The successful contractor of the future will modify their business model to manage overhead costs in order to profit during the inevitable market downturns like we are experiencing now. As backlog falls off and aggressive competition for the lesser amount of work drives profits down, many firms will experience a reduction in volume and profit. Despite resistance many will eventually be forced to reduce overhead personnel.

The motivation to cover this subject now is that it takes some time to understand and to decide to alter the way you manage overhead, and to be prepared to introduce it. Overhead is neither bad nor good. It is neutral, a necessary cost of doing business and should be as aggressively managed as production costs. However, in the construction industry overhead costs vary dramatically from one company to another to the extent that there is no accepted standard. In some cases, it is a loosely structured expense. Overhead is a control function but in some companies, it has expanded to comfort where, for example, standard office facilities and company cars can get the job done but luxury offices and cars can get it done in greater comfort. I am not assessing, just illustrating. Overhead should be scrupulously managed, re-evaluated annually, and the determinant should be necessary versus unnecessary.

When the declining market eventually recovers, and it will as they always have, overhead will have to be put back in place to deal with increasing sales. That may be some time yet but between now and then is the time to learn about, evaluate and implement the *flexible overhead* concept. Many firms will have laid off people, but to be sure the best of the best employees will still be there. Most say, “*all my people are great or I wouldn't have them*”, but the reality is that organizations mirror the population. Some managers perform well, some very well and some great. No one lays off their best performers so the least of the well will be gone and the others will be doing fine, but as more work comes in they will need help. Your choice is to put the same positions back in place or to maintain your existing core high-performance team and supplement them using flexible overhead principles. The added overhead will require no long-term commitment and you can reduce it within a week. Every time your work falls off, short-term or long, you will be glad you did. Coming out of a downturn is the easiest time to initiate *flexible overhead* because it requires no displacement of core personnel. Just the addition of non-permanent employees and resources.

As an example, let's look at one department of a self-performing general contractor doing \$40 million a year. (The principles are the same for a firms doing less than \$5 million or more than \$100 million.) In the accounting department the CFO had four assistants with separate responsibilities i.e., accounts payable, accounts receivable, payroll, general ledger, etc. Work slowed to the point that one had to be laid off. With minimal cross training the remaining three took over. In the subsequent recovery with more work coming in the three needed help. The choice was to reemploy the same person or skill set or to reconsider the entire accounting department process. All skilled employees spend some of their time doing nonskilled work such as copying, filing, running errands, etc. Instead of re-dividing the skilled activities to four people a part time clerk was hired (or you can use a temp agency) to assist the three with the nonskilled portions of their work which expands their time for the skilled activities. This new position was engaged with a written understanding that it was temporary as-needed employment and that hours worked may be reduced or increased or the position terminated with one (or more) days' notice. I can hear the objections already and my response is: this is being done all over the country and it works. Just try it. They didn't need a skilled bookkeeper to make copies or run errands. If growth eventually requires this position to become full time, it may be appropriate to make it a permanent

position and use part time temporary help to continue the process. Operational planning should concentrate on needs and positions not employees.

Using the same guidelines, you can re-engineer the workflow of every department: marketing, administration, the shop, the yard, etc., and most controversial of all, estimating. Everyone draws the line at estimating protesting, *“it is far too complex, the lifeblood of the company, an extremely skilled position”*, etc. However, estimators spend hours a week making copies, filing, looking up products, sending out drawings and specifications, chasing down vendors and subcontractors and the list goes on. Ask any estimator if they could use a gofer, a messenger, or a runner to lessen their workload, increase their output and improve their productivity--all of which tends to enhance their accuracy. The overall company-wide business objective should be to maintain and support the highly skilled core people in good markets and bad.

The same process is use on the production side of the business. There are as many ways to organize and manage field operations as there are companies so no single example is illustrative. Once flexible overhead guiding principles are applied in one area of an organization managers come to understand how it works and begin to apply it in other areas in unique ways that best suit their organization. Flexible overhead is a state of mind as much as it is a process. Managers begin to analyze workflows identifying the skilled activities required to accomplish the throughput and the unskilled activities necessary to assist, support, and facilitate the skilled core team. Almost every position in a construction organization can be augmented by having less-skilled people supporting the skilled core employees. It is economical and, once you learn how to use it, more efficient. Of greater importance it is temporary, able to be shed in less than a week, and the employment of your core team is secure. (And they know it.)

Another huge benefit of embracing flexible overhead is that it enables you to profit from unexpected growth opportunities because the skill set used to reduce overhead quickly also shows you how to engage temporary resources on short notice. If the right project comes along when you are already busy, you will have the skill set and experience to temporarily expand the capacity of your core group with additional temporary support that can be disbanded when no longer needed. Next week we will cover implementing flexible overhead in the shop, yard, and field.

Next week: Implementing Flexible Overhead continued.

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Note: Information on overhead management can be found on letstalkbusiness.net click on “Manual” and go to Managing Overhead in the table of contents.