مدیریت کسب‌وکار در صنعت ساخت
(Construction Business Management)

ماژول ۳: ارزیابی کسب‌وکار

بخش دوم: اجزای موفقیت و شکست سازمان

ارائه دهنده:

سید محمدرضا علوی‌پور

(PhD, PMP, CMIT)

CMAA Authorized Trainer

دانشگاه Illinois Tech آمریکا

What we will learn?

- Primary Causes of Business Failure
- Leadership Challenges
- Ethics
- Capitalizing on Experience
- Increase in Project Size
- Unfamiliarity with New Geographic Areas
- Moving Into New Types of Construction
- Changes in Key Personnel
- Lack of Managerial Maturity in Expanding Organizations
- Exercises

Primary Causes of Business Failure

Primary causes of business failure

- Few construction firms fail from a single cause or from a sudden, catastrophic event.
- **One** cause may **predominate**,

  but inadequate response to several interrelated factors is the typical cause of business failure.
- The primary causes of failure can be grouped into **two categories**:

  external influences and internal problems.

External influences

- The **major external influences** on business failure are
  1. Prolonged economic recession,
  2. Loss of a major customer,
  3. New competition, and
  4. Shortage of skilled labor.

External influences

- Recessions result in **reduced construction activity**, which drives **more construction companies to compete** for that work which is available.
  - An **oversupply of contractors** pursuing limited work often leads to
    1. Reduced profit margins,
    2. Jeopardizing the economic viability of winning construction firms.
- A construction firm's **major customer may significantly reduce** its construction activity or even may **go out of business**.

External influences

- **If** the construction company does **not have other customers**,

  the **loss of a major customer** may cause **severe financial strain** on the company.

  - **New competition** also presents **threats** to the construction firm, particularly if the **size of the market** is not increasing.

- **Without an adequate** supply of skilled craftsmen,

  a construction firm may be **unable to produce quality work** desired by its customers, resulting in the **loss of reputation and business**.

Internal problems

- **Despite the external threats** discussed above, the **primary causes** of construction firm failure are the result of **one or more internal problems**.

These are discussed below.

Internal problems – Strategic planning issues

- **Pursuit of volume**
  - To many people in the construction industry, **business volume** is a measure of **success**.
    - ✓ While it may indicate the significance of a firm in its relevant market, **profitability is a more important** measure of success.

Internal problems – Strategic planning issues

- **Lack of comprehensive business plan**
  - Construction companies **often do not have business plans** that guide their business decisions.
    - ✓ They may **simply react** to the market.

Internal problems – Strategic planning issues

- **Lack of comprehensive business plan**
  - Business planning requires an understanding of the market, of
    1. **How** construction **procurement decisions** are made, and
    2. **Competitive advantages** of the firm.
    - This **knowledge** is essential in
      1. the selection of services to be offered,
      2. the selection of market area and focus, and
      3. the selection of people and equipment required.
  - In addition to understanding the market, construction company **leaders** must
    1. **Understand** their firms' financial condition and
    2. Devise **strategies** for financial success.

Internal problems – Strategic planning issues

Diversifying into unfamiliar types of projects

- There is **high risk** in diversifying into **unfamiliar types** of projects, because
  1. **Appropriate suppliers** and **subcontractors** may not be known, and
  2. The **technical requirements** may exceed the expertise of the company's project management staff.
  - ✓ **Costs** may be **underestimated**, resulting in **unprofitable projects**.
- Similarly, pursuing projects using **unfamiliar contracting approaches**, such as design-build,

  often results in **significant financial risk** to the construction company.

Internal problems – Strategic planning issues

- **Diversifying into unfamiliar geographic areas**
  - Entering an **unfamiliar construction market** poses great risk to a construction firm.
    - ✓ **Potential** customers, suppliers, and subcontractors are **unknown**.
    - ✓ If the **location** of the new market is a **significant distance** from the company's **normal area** of operation,
      - there will be **little ability** to augment project management staff with other company resources;
        - placing **greater stress** on the project management team.

Internal problems – Strategic planning issues

Lack of managerial maturity

- Construction firms often are **founded** by one or two people.
- As a firm grows, its **management system** must mature to accommodate **increased scope of work**.
- **Additional managers** are needed, and the founders must de**legate some authority** for making business decisions to others.
  - ✓ **Continuing to centralize** all decision making in one or two people does not provide the responsiveness needed to react to **changing business conditions**.

Internal problems – Strategic implementation/control issues

- **Increase in project size**
  - **Unrealistic increase** in project size may lead to **financial difficulties**.
  - **One large unprofitable project** will have a greater adverse impact than will a **small** unprofitable project.
  - Large projects may **stress managerial expertise**, subject the firm to greater risk, and **require more capital** to finance cash flow requirements.

Internal problems – Strategic implementation/control issues

- **Unplanned loss of key personnel**
  - **Unplanned loss** of key personnel can **severely stress** construction firms, particularly **small ones**.
    - ✓ The loss can be due to death, to illness, or to resignation.
  - **Unplanned loss** of management or technical expertise may take **considerable time** to overcome and **places small** firms at great risk.

Internal problems – Strategic implementation/control issues

- **Poor cost-estimating skills**
  - To **ensure** that a company remains a **profitable** business enterprise, construction firm managers must understand the **anticipated** costs and risks of each project and price the **work at a level** to cover all costs and provide a profit.
    - ✓ Because of some adverse condition, the project **may not** provide the **anticipated profit**,

      but construction company **managers** should not pursue volume at the expense of profitability.
      - This means that **bids** and **cost proposals** should not be reduced just to increase the company workload,

        because **with greater work volume** the company incurs **more risk.**

Internal problems – Strategic implementation/control issues

- **Lack of equipment control**
  - The **cost** of **owning** and **operating** equipment is a significant part of the construction business.
  - **Controlling** equipment costs is controlling the amount of equipment owned, leased, or rented.
  - **Investing** too much of a company's financial resources in **equipment** may degrade the firm's ability to **finance** its cash flow requirements.
  - Idle equipment represents an **overhead cost** that should be avoided.

Internal problems – Strategic implementation/control issues

- **Poor internal communications**
  - **Poor internal communications** between project sites and the home office plague many construction companies.
    - ✓ Consequently, there may be **little warning** of project execution problems or financial difficulties.
    - ✓ In most instances, it **only takes one** or **two disastrous** projects to bring down a company.
      - o **Early warning** is essential if corrective action is to be taken on time.

Internal problems – Financial management issues

- **Poor use of accounting systems**
  - A **number of contractor failures** are caused by poor accounting practices or by a failure to review accounting records to determine the financial status of projects.
  - A **delayed customer payment** often results in inadequate cash flow.
  - By **not using** the current balance sheet, income statement, and job cost reports, **managers may be unable** to identify financial difficulties until it is too late to take corrective action.

Internal problems – Financial management issues

- **Excessive debt**
  - **Cash flow requirements** must be met either from internal resources or from debt.
  - Some contractors **rely on debt** to compensate for the lack of business capitalization or equity.
  - **Excessive debt** may cause such a drain on income that the **capital resources** of the firm do not grow or may even decline.
    - ✓ The **cost of borrowing** should be included in company overhead margins.
      - o **Too high margins** may make the construction company noncompetitive in tight markets.

Leadership Challenges

Leadership challenges

- Construction company leaders should also be **good managers**.
- The **basic management functions** that they perform are
  1. Planning,
  2. Organizing,
  3. Staffing,
  4. Leading, and
  5. Controlling.

Leadership challenges

- The basic roles of a company leader have been described as the following:
  1. **Interpersonal role** based on the formal authority defined by the company organization chart.
  2. **Informational role** as a recipient and transmitter of information.
  3. **Decisional role as** a decision maker.

Leadership challenges

- Company leaders need to understand these **roles** and **how their actions influence** the attitudes, values, and performances of others within their companies.
- Leadership is the **process** of **creating** a **vision** of what the organization is to become and **having the ability** to translate that vision into reality and sustain it.
- A **good leader needs** the following:
  1. Ability to create a vision and pull people forward toward its accomplishment.
  2. Ability to communicate effectively.
  3. Ability to empower subordinates by sharing power with them.
  4. Ability to recognize their own strengths and weaknesses.

Leadership challenges

- The **vision**
  1. Guides the decisions of company leaders and
  2. Aligns the work of employees

     so that they work together in the pursuit of common goals.

Leadership challenges

- Many successful construction company senior executives devote their efforts to
  1. strategic planning,
  2. employee selection and development, and
  3. customer interaction.
  - They **leave** the **day-to-day management decisions** to mid-level leaders.

- This approach serves **two very important functions** for a construction firm.

Leadership challenges

- This approach serves **two very important functions** for a construction firm.
    1. First, it **frees** the **senior executives** to focus on long-range planning issues.
    2. Second, it provides **professional development opportunities** for the mid-level leaders and demonstrates the trust placed in them.

Leadership challenges

- To be **able** to **delegate** day-to-day decision making,

  the **company leaders need** to **ensure** that the organizational structure of the company **supports decentralized** decision making and that appropriate management processes have been implemented.

  - While **decision-making authority** can be delegated,

    the **ultimate responsibility** for the **well-being** of the **firm** still rests with the senior leaders.

Leadership challenges

- Construction company leaders need to understand that their companies have two sets of customers, internal and external.
- Good leaders
  1. have a sincere and **obvious caring** for their subordinates and
  2. are willing to invest in employee **training** and **development**.
- These leaders **align their talent development** strategies with the strategic plans of their companies.

Leadership challenges

- Company leaders get things **accomplished** through the members of **their company teams.**
- These leaders make decisions, allocate resources, and motivate others to accomplish company goals.

Leadership challenges

- They should possess **four types** of skills to be successful.
  1. They must have the **technical skills** to understand the technical aspects of the construction business.
  2. They must **possess** the **people skills needed** to work with, **understand**, and **motivate people**, both individually and in groups.
  3. They must have the **communicative skills** to be able to communicate effectively with employees, customers, and the media.
  4. Lastly, they should have the **conceptual skills** needed to be able to analyze complex situations and identify alternative solutions.

Ethics

Ethics

- A company is judged by the **integrity** that it demonstrates in conducting its business and how it treats its employees.
- A key component of a company's **reputation is the ethics** of the company leaders and the company's employees.
- Ethics are the **moral standards** used by people in making personal and business decisions.
- The set of **moral standards** that we use to guide our decision making are our ethics, which help us to decide **"what is right and what is wrong."**
- An example of an ethics guide is the **so-called Golden Rule**, which is, to treat others as we would **wish to be treated**.

Ethics

- Many professional organizations have developed **codes of ethical behavior**, such as the one shown in **Figure 1.2** developed by the <u>Associated General Contractors of Washington.</u>

FIGURE 1.2 Sample Code of Ethical Behavior

Associated General Contractors of Washington

CODE OF ETHICAL CONDUCT

I believe that each of us, as individuals and organizations, owe our community, colleagues, customers, and each other a duty and responsibility to conduct ourselves in an honest and ethical manner.

To further express my commitment to the principles of skill, responsibility, integrity, and community, I pledge to conduct myself according to the following standards:

My word is my bond and is stronger than a written contract.
I will treat others as I desire and expect to be treated by them.
I will put safety and compliance with codes, laws, and regulations above profit.
I will respect and protect the environment.
I will do my best to produce quality projects on time, at good value.
I will assume responsibility for my actions.
I will strive to reach accord through personal negotiations and do my best to resolve disputes quickly, with integrity, and without personal attack or rancor.
I will endeavor to persuade others within my organization and all for whom I am responsible to embrace these standards.

Ethics

- Ethics involve
  1. Determining **what is right** in a given situation, and then
  2. Having the **courage to do** what is right.
- Generally there are considered **three primary ethical directives**:
  1. Loyalty,
  2. Honesty, and
  3. Responsibility.

Ethics

- Loyalty may be requested from many groups and institutions:
  1. Friends,
  2. Family,
  3. Employer,
  4. Profession, and
  5. Society.
- Honesty is **more** than **truth telling**.
  - It involves **not lying**, but, more importantly, involves the **correct representation** of ourselves, our actions, and our views.
- Responsibility means
  1. **Anticipating** the **potential consequences** of our actions and
  2. **Taking** responsible measures to **prevent harmful** occurrences.

Ethics

- A construction firm's **ability** to acquire and maintain customers will be greatly influenced by the **potential customers' perception** of the ethics of the construction company and its employees.
- **Company leaders** establish the **corporate culture** regarding ethical behavior and establish the **standards** for their employees by their own personal actions.
- Subcontractors, material suppliers, and project owners may choose **not to do business** with general contractors who have a reputation for **unethical behavior**.

Ethics

- Construction **company employees** will face many ethical dilemmas in contract procurement, cost estimating, project management, accounting/financial management, customer relations, subcontractor relations, and vendor relations.
- **Ethical behavior** is a difficult area because it involves **more than simply** complying with legal requirements.
- It involves treating everyone in a responsible and fair manner.
- A company's **reputation** for ethical behavior may also affect its ability to attract needed talent.
- Ethical issues are very important, because they have the **power to damage** the image of the company and **destroy the morale** of its employees.

Ethics

- To create an ethical framework for a company, **company leaders** should create a **company statement of values** that will provide **moral guidelines** for company employees.
- A company statement of values should contain **five to ten value statements** that define the **essential characteristics** of appropriate employee behavior.
- An example statement of values is shown in **Figure 1.3.**

Ethics

FIGURE 1.3 Statement of Values for Western Construction*

We, the employees of Western Construction, are guided by the following values. They describe who we are and guide our decisions.

- *We take responsibility for the quality of our work.* We ensure that all of our work conforms to contract requirements.
- *We take responsibility for ensuring the safety of our work sites.* Our goal is no accidents on any of our work sites. We are committed to providing a safe working environment.
- *We take responsibility for providing customer satisfaction on all projects.* Our projects are completed on time and within budget and meet customer expectations.
- *We act with integrity in all that we do.* We are personally accountable for all that we do, and we act with honesty and fairness.
- *We regard suppliers as essential team members.* We owe our suppliers the same respect that we show to our customers. We treat them fairly and equitably in all business transactions.
- *We regard subcontractors as essential team members.* We owe our subcontractors the same respect that we show to our customers. They are essential team members in the delivery of quality projects. We treat them fairly and equitably.

Ethics

- Not only must the values be clear, but they must be **reinforced by the daily activities** of company leaders.
- **Another tool** for encouraging ethical behavior in company employees is a **statement of business conduct**, such as the one illustrated in **Figure 1.4.**
- This statement provides guidance to employees in **making their daily business decisions.**

Ethics

Our mission is to construct high-quality, management-intensive construction projects in the Western States and provide professional, client-oriented services. It is impossible to accomplish this mission without a commitment to the highest standards of ethics and integrity. Our standards of business conduct guide us in making decisions every day. These standards are

- *Relationships*
  - *With Customers*—We expect our customers to select us because of the quality, the service, and the cost of our services. Our projects are completed to each customer's satisfaction within a mutually agreeable time frame.
  - *With Suppliers*—We expect our suppliers to provide quality materials within a mutually agreeable time frame. In return, we provide timely payment for all materials received.
  - *With Subcontractors*—We expect our subcontractors to complete their scopes of work within mutually agreeable time frames. We do not share subcontractor proposals with others but select subcontractors based on the quality of work that they provide. We provide timely payment to all subcontractors, upon receipt of invoices from them.
- *Conflict of Interest*—We do not engage in any activity that may erode public trust in our company or provide a perception of unfairness in our relationships with others.
- *Company Resources*
  - *Time*—Time records are prepared accurately and personal business is not conducted during business hours.
  - *Resources*—Company resources are not used for personal activities and are safeguarded at all times.
  - *Information*—Company business practices are not shared outside the company unless required by law. Intellectual property is safeguarded as an essential company resource.

FIGURE 1.4 Statement of Business Conduct for Western Construction

Capitalizing on Experience

Capitalizing on experience

- Understanding the reasons **why construction businesses** lose money is the best way to prevent **unnecessary loss.**
- The investigation and resolution of **hundreds of construction company failures** have generated a significant **bank of knowledge** on the subject.
- The events and decisions that precede the failure of a construction business can be categorized and quantified in order to define the **most common causes** of these failures.

Capitalizing on experience

- One of the most interesting phenomena revealed by this study is the fact that the **events** and **decisions** that cause or contribute to a construction **business failure** take place during the **company's profitable years**.
- To look for the causes within the **difficult years** when a company is losing money or breaking even is to study the result and **not the causes**.
- It is easy to be misled in a study of bad years because **losing operations** can generate **unusual events and decisions** even if the contractor is unaware of impending loss.

. . . the events and decisions that cause . . . business failure take place during . . . profitable years.

The five primary elements of construction business failure

1 Significant increase in project size

2 Unfamiliarity with a new geographic area

3 Moving into a new type of construction

4 Changes in key personnel

5 Lack of managerial maturity

Increase in Project Size

Element #1. Significant Increase in Project Size

- The most common element among contractors who fail is a **dramatic increase** in the **size of projects undertaken**.

- The **change to larger projects** usually occurs <u>during profitable years</u>, and problems sometimes develop **even before the first large** project is **completed**.

Element #1. Significant Increase in Project Size

- When a construction enterprise is **operating at a profit**,

  doing a certain average-sized project and a certain top size,

  there is **no reason to believe** that it will profit if it takes on **dramatically larger work.**

- A construction firm **may be able to build** a project that is two or three times larger than it normally does;

  however, the **issue is whether** they can build it at a **profit**.

- *If a company can construct $1-million road projects or buildings, it may be able to construct a $2-million or a $3-million road project or building and get the job done. But the critical question is: will it make a profit? Making a profit on a job twice the size of a company's previous largest project would be unlikely.*

Element #1. Significant Increase in Project Size

- Making a **profit from a job three times greater** than the largest ever built is **almost impossible** **without** additional financing resources and a tremendous amount of careful planning, all of which is **unlikely** **without** **outside** **help**.
- Getting additional resources might be possible, but how would a contractor, **with no background on projects** of such magnitude, **determine what resources** would be needed? **Without previous experience**, how could they **carefully plan the work?**
- *Contractors who normally do top-sized jobs of $1 million, $10 million, or $100 million would be working in an altogether different environment than the one they are equipped for if they took on a $3-million, $30-million, or $300-million job.*

Element #1. Significant Increase in Project Size

- Let's consider an example from a case study.
- A contractor's previous largest project is **$1 million** and usually has **two or three additional jobs** at any given time of **$300,000 to $1 million** and a **number of smaller jobs under $300,000 each.**
- The company's **annual volume is $3 million**, and it is generating a **comfortable profit.**
- When work dried up and **backlog fell off dramatically**, they went after **larger and larger projects.**
- They **were able to capture a $3-million** project.

Let's look at the impact on their organization.

Element #1. Significant Increase in Project Size

- **Previously projects** took about a **year or less to complete**.
- On average, **one of their larger projects** started about the **time another finished** and a **third was at its midpoint**.
- Normally, on this **company's projects near-completion**, there were considerable retainage,
  - while the **ones in the middle** stages were generating large monthly payments, and
    - the ones **starting up** were producing good cash flow through front-loading.

Element #1. Significant Increase in Project Size

By handling jobs in sizes they **were accustomed to**,
which normally **were in varying stages**,
the company **not only had a reasonable cash flow**
but also **had the time** and **resources available** to look after all of its jobs and keep the **jobs profitable.**

Contrast this with the $3-million job.

Element #1. Significant Increase in Project Size

- At first, the **front-load was terrific**,

  but the **retainage mounted fast** and, within **six or eight months**, became a **higher amount than the company** had ever had on all jobs **combined**.

- By the **end of the job**, the retainage amount was **strangling the business**, and

  the **project took longer** to finalize than anything they had **ever undertaken**.

- While the **project type was similar** to the organization's previous work,

  they were **surprised at the level of inspection** and **supervision** they were subjected to by the **architects or engineers**.

Element #1. Significant Increase in Project Size

- On **larger projects**,
  municipality, state, and lender inspections
  generally have **more red tape** than smaller jobs,
  which may **be more than management is familiar** with or
  more than what **field staff can effectively handle**.
- **Work rules** are often **more comprehensive** on larger jobs, and
  security and **safety** requirements **broaden**.

Element #1. Significant Increase in Project Size

- The **larger project**,

  although similar to other jobs the organization **had performed**,

  was **not within its experience** or capability to **finance**.

- The company got the job done, but making a **profit was another story.**

- With **losses** out-of-pocket and **huge retainage** outstanding, the company could **not pay its bills** and is no longer in business.

Unfamiliarity with New Geographic Areas

Element #2. Unfamiliarity with a New Geographic Area

- A **contractor's primary area** maybe one county, half a state, five states, or a whole country.

- **Regardless of size**, the primary area is the area in which the organization
  1. Has regular operations,
  2. Has developed comfortability, and
  3. Has been profitable.

Element #2. Unfamiliarity with a New Geographic Area

- While there are many **good reasons** for a company to expand into new geographic areas, such as
  1. Normal growth,
  2. Lack of work in their primary area, and
  3. Special opportunities,

  the **risks** must be recognized and planned for.

  - Again, the **question is not** whether the organization **can build** a similar product in a **different location**.

    Rather, it is whether this activity will **result in profit**.

Element #2. Unfamiliarity with a New Geographic Area

- With time, an organization becomes **accustomed** to **working** in a given area and can easily assume its **type of work** is performed the same way everywhere.

    Yet the **differences** in

    customs, methods, procedures, regulations, work rules, and labor conditions

    can be **significantly different** and **expensive** if not planned for.

Element #2. Unfamiliarity with a New Geographic Area

- Consider a **merit shop contractor** bidding outside its area **without knowing** in advance that the work would have to be performed **using union labor**.
- Or, in certain areas of the country, it is common to **install underground pipe practically underwater**

  while specifications in other areas require **complete de-watering**.
- In some states, it is almost **impossible to keep full crews** during the **first week of the deer-hunting season.**
- There are even some areas where **local suppliers** will give their **best prices** and services only to local contractors.
- Regulatory requirements and inspections may differ greatly **between a city center** and the **suburbs**, or in a **neighboring county.**

Element #2. Unfamiliarity with a New Geographic Area

- **Local help**, such as a joint-venture partner or new area-based personnel, may be needed to facilitate the project.

- **Compounding** the problem, a contractor often **takes a distant project**, much **larger than anything they have built** in the past because it **wouldn’t pay** to take projects of their **normal size so far away**, which of course **magnifies the risk**.

Moving Into New Types of Construction

Element #3. Moving into a New Type of Construction

- Contractors sometimes **change from one type** of construction to another, or **add a new type** of work to their existing specialty.
  - *Companies may change, for example, from highway work to sewage treatment plants, from heavy industrial to tunnel work, from low-rise to high-rise buildings, or from office buildings to hospitals.*
  - The **need for research** and **planning** before embarking on a new type of construction work is well **recognized by contractors**.

Element #3. Moving into a New Type of Construction

- What is often underestimated is the **entrance cost**,

  i.e. the costs **associated with the learning period** during which an organization

  adjusts to performing a new type of construction work.

- **Hiring a person** who masters the new type of work may **not be enough**.

- Companies often complete **one or more losing jobs**

  before they **can execute** a new type of construction **profitably**.

  - Unfortunately, some **companies do not survive** this period.

Element #3. Moving into a New Type of Construction

- Contractors are **more specialized** than they realize.
- Some construct **several types** of projects, for instance, but **perform and profit better** at one kind.
  - Some **may call it luck**, but it’s probably because they are **better at pricing** and **constructing** that type of work.
- **Contracting organizations** usually **start** and **remain** with types of construction in which they **have the expertise**.
- Further, they will **base growth and success** on the continued perfection of that **expertise**.

Element #3. Moving into a New Type of Construction

- **Over time** they become **better able to estimate** their kind of work and, therefore, become **more competitive** at getting it.
- They also become **better at organizing** and **putting the work in place** and become **more profitable** at doing it.
- Being able to **plan and execute** the construction of a **bridge** does not mean the same team can profitably plan and execute a **building**.

Element #3. Moving into a New Type of Construction

- A **more subtle change** in the type of work is the change from **public to private** sectors, or **vice versa.**
  - This change, **even when** the project is a **company's normal size** and in **their area**,

    has **cost numerous** firms a great deal of money.
  - Indeed, many companies do **both public and private work** and have been doing so profitably for years.

Element #3. Moving into a New Type of Construction

- There **is no suggestion here** that it shouldn't be done,

  just a report that **many contractors did not recognize the differences** in advance and proceeded to price and **produce the work for a loss**.

- There are **considerable differences** between public and private work, such as

  qualifying for bid lists, differences in criteria used for selecting the contractor, and expectations about change orders.

- The differences in **expectations** on public and private work may **not even be known by the parties**,

  possibly **resulting in disputes** that could have been avoided.

Element #3. Moving into a New Type of Construction

- While **regulations** are **changing** with the rise of **alternative project delivery** methods,

    which allow **qualifications to drive contractor selection**,

    many public organizations are **still required** by regulation to award a significant portion of the work to the **lowest bidder**.

    - This **traditional low-bid type** of contractor selection allows only **limited control** over who gets the work.

Element #3. Moving into a New Type of Construction

- A **public project** is administered "by the book," meaning the contractor intends to perform work according to the **specifications**.
    - Because future contractors are **selected based on the lowest bid** for public work,

      there are **no significant incentives** for current contractors to perform **beyond a project's set expectations**.

Element #3. Moving into a New Type of Construction

- The **opposite is true of private work** where the awarding party picks the proposers,
  - **may or may not open proposals publicly**, and
    - may often end up **working with a known or at least a pre-selected** contractor.
- The **contractor is incentivized** to perform, innovate, and deliver above and **beyond the requirements** because this can impact them being selected for future jobs.
- The same can be said in alternative delivery method projects, such as design-build (DB) and construction manager at risk (CMAR),
  - if the **selection of the contractor** relies heavily on <u>qualifications and prior experience</u> in addition to the price.
- The **incentives** change and drive **different behaviors**.

Changes in Key Personnel

Element #4. Changes in Key Personnel

- As mentioned earlier, there are **three primary functional areas** of a construction business, and each must be adequately managed and supervised in a successful contracting enterprise.
- In **every successful construction enterprise**,

  a **top-level executive** is responsible for **each of these areas**.

  - Depending on the **size of the company**,

    one person could be responsible for all of them or

    two people may share the responsibilities (e.g., one person leads operations and

    the second person leads sales and administration).

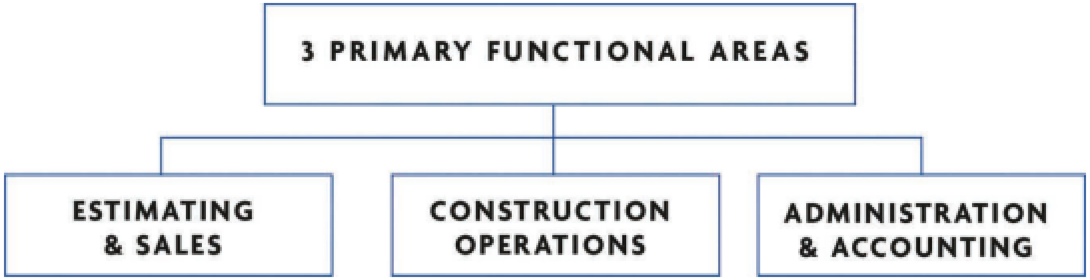
Element #4. Changes in Key Personnel

- If a company is **making a profit**,
  it is to a **large degree** because of the efforts of these **key individuals**.
  - If **one of them leaves**,
    there is by definition **no track record** of profitability for the new organization as it is reconfigured.
- This is a **simple reality in business** and even **more so in the construction business** that is so often defined by closely held **small or medium-sized companies**.

Element #4. Changes in Key Personnel

- **Some** may point to a business with **six or eight good project managers** and say, *"that's why this company makes money."*
- But **someone** may also point to the **person who is primarily responsible** for construction operations and say,

  "this company has those six or eight good project managers because of him or her."
- The **same** can be said about **two or three key estimators**, and some will say the same about the person primarily responsible for getting the work.



The three primary functional areas of a construction business.

Element #4. Changes in Key Personnel

- The **top management team** of a construction enterprise is **small** compared to other industries
  - because the **labor side of the business** is field-managed, and
    - **some contractors** even subcontract a **majority of the fieldwork**.
- The **corporate organization** is **separate** and distinct from the **field organization**.
- The **quality** of **field management** often relies primarily on the quality of the **key person or persons** responsible for **construction operations.**
- **Operations** are the core function and provide the **entire cash flow** for the company.
- **If a key person** in charge of construction **operations** **leaves** the organization,
  - the company is **permanently changed** and **at risk**
    - **until** his or her replacement **proves they can do** the work for a profit.

Element #4. Changes in Key Personnel

- On the **estimating** and **sales side** of a construction business,
  - one or more **key individuals** will be responsible for the **firm's pricing strategy.**
- This manager(s) will usually take a **firsthand part in bid preparations** and will **determine the final price**.
- The **takeoff** and **estimating staff** may be a **great asset** to the company,
  - but the **top manager(s)** put them **together** and
    - are **ultimately responsible** for the success or failure of **capturing the work.**
- If this key manager(s) **leaves the company**,
  - the organization **no longer has a proven team** that can get the work, until shown otherwise.

Element #4. Changes in Key Personnel

- The areas of **administration** and **accounting** are **often overlooked** and **underrated** by contractors.
- If there are **only two top individuals** in the organization who are responsible for the **three primary functional** areas of the business,
  - **one** of them will be responsible for the administration and accounting functions.
    - Usually, these **fall to the person responsible** for getting the work because **sales and estimating** are more of an **office function** **than** construction operation.

Element #4. Changes in Key Personnel

- In **smaller organizations**, it is sometimes **difficult** to determine **who is in charge** of administration and accounting.
  - It is often relegated to **middle managers** even in medium and large-sized companies, which is **less than ideal**.
- When the business is **small**, the contractor may run the entire business, including such details as signing checks.
  - Therefore, the **contractors are close to the accounting side**, if only to pay the bills and be **informed of the bank balance**.

Element #4. Changes in Key Personnel

- If **borrowing is required**, they are the ones who explain it to the **banker**.
  - The small contractor **may or may not keep** minutes of important meetings, confirm agreements in writing, or even reply to all correspondence received.
- The small contractor is in **continuous communication** with the (relatively few) players on their work in progress, and as a result,

  the **impact** on the business of **poor paperwork and administration** is **reduced**.

As the company grows and the staff increases, administrative and accounting duties often continue to be relegated to middle managers.

Element #4. Changes in Key Personnel

If a **dedicated**, **capable manager** who takes personal responsibility for the **administrative and accounting functions** cannot be identified, the company may have a **serious problem** and is **not** organized for success.

Lack of Managerial Maturity in Expanding Organizations

Element #5. Lack of Managerial Maturity

Many entrepreneurs assume, "If I succeeded at this volume, I'll do twice or three times as well at two or three times this volume."

- At some point in the **growth of every enterprise**, however, the organization must change; it must become **more sophisticated**.

- At these junctures **more authority** must be delegated,
  more complex systems and procedures will be required, and
  more sophisticated people may be needed to handle them.

Element #5. Lack of Managerial Maturity

- **Most entrepreneurs** seem to instinctively follow a **“command and control” approach**;

  however, as an organization expands it requires **delegation and some release in control.**

  Some entrepreneurs have **great difficulty with that**.

Element #5. Lack of Managerial Maturity

- It would be easier if these changes **evolved slowly** <u>over a growth period</u> because they would be easier for the **contractor to digest**.
  - But this is **not usually** how it works because **you can’t hire half** of a person or put in **half of a new system**.
    - ✓ So, when these changes occur, they are **often significant and relatively fast**.

Element #5. Lack of Managerial Maturity

- Knowing **when and how** to make organizational **changes is an aspect of running** the business

  that tests the **true skills** of the contractor in a **growing firm.**

Element #5. Lack of Managerial Maturity

- One key to success in management is **not to eliminate all problems**,

  but to **focus on the critical problems** of the present stage of the organization's life cycle,

  so it can **grow and mature** to deal with the problems of the next stage.

Additional concerns and associated opportunities

❑The **first four** concerns are organization-related,

the **next two** are growth and market-related, and

the **last three** are people-related.

1. Business planning
2. Flexible overhead
3. Debt
4. Claims
5. Growth rate and risk
6. Market-driven, not volume-driven
7. Internal company disputes
8. Employee benefits and compensation
9. Motivation and loyalty

Exercises

Exercises

1. What are some of the issues when project size is increased?
2. How would you plan to expand into a new geographic area?
3. What are the exposures to an organization that change the type of work they normally do and how can they be overcome?
4. Why is a change in key personnel a serious issue for a small- or mid-size construction enterprise?
5. How would you go about planning for a succession in management of a construction business?

موسسه مهندسی و مدیریت ساخت علوی پور (ACEMI)

دفتر آموزش

تهران، بلوار فردوس شرق، مجتمع آبگینه، طبقه سوم اداری، واحد C42

+۹۸ ۲۱ ۴۶ ۱۰۰ ۴۵۰

+۹۸ ۲۱ ۴۶ ۱۰۰ ۴۴۵

www.dralavipour.com

info@dralavipour.com

@acemi_social

@alavipour_pm

@IRANACEMI

@alavipour_pm

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