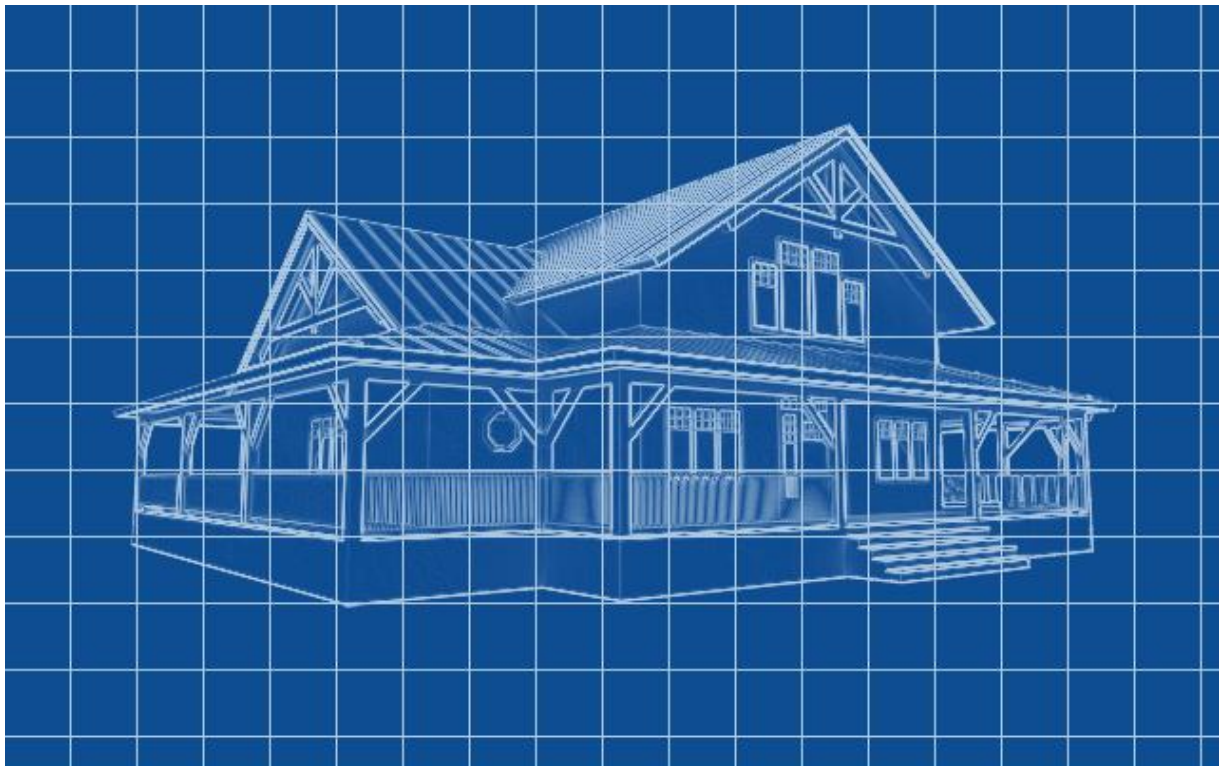


A BLUEPRINT FOR A REMODELING HORROR STORY AND

10 LESSONS TO HELP YOU AVOID ONE ON YOUR REMODELING PROJECT



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A BLUEPRINT FOR A REMODELING HORROR STORY

By Lynn Hammerschmidt

The fodder of cocktail party conversations, everyone has had, or knows someone who has had, a horrible experience with a contractor and is happy to share it. What homeowners often don't realize is that the traditional *Design – Bid – Build* process is inherently dysfunctional and that they may have inadvertently contributed to creating their own horror story. This article provides information on how we identified what was wrong with the process and also how we re-invented our own business model and stopped participating in the cycle. Most importantly, it will give you the information you need to avoid a horror story on your own remodeling project.

Coming from the corporate world 15 years ago, I joined my husband in his booming remodeling company with the idea that I would manage the “Business of the Business” and dig him out from under a mountain of paperwork. I set out to learn more about construction and before the end of my first week it became clear that something was terribly wrong. I was shocked at how poorly we were treated. Customers and potential customers assumed that they were smarter than we were and gave no value to our experience in remodeling. They assumed we were trying to rip them off and that they could decide, even after we had agreed on a price, that they did not have to pay the amount to which they agreed, and that we did not have to make a profit to stay in business.

While most of our relationships with customers were not stressful, there were enough to warrant a review of why these came to be and in so doing it became clear that the whole process of remodeling was broken. We were continually presented with beautifully-drawn sets of plans and asked to estimate them. We spent countless (unpaid) hours creating accurate estimates only to see the look of shock on the homeowners' faces as we presented the estimate. They told us that they discussed their budget with the design or architecture firm who drew the plans. They asked why we were “so expensive.” When we explained that our estimate was a reflection of the cost of constructing the plans as drawn and it was not what they wanted to hear, one of three things happened: 1) the customer tried to find a contractor to do the work within their budget 2) the plans were redrawn (with a smaller scope) at additional cost and rebid or 3) the project was abandoned.

We often lost projects to companies we knew were underbidding to get the jobs – knowing they would try to make it up throughout the job, or who had bid jobs lower than we could because they did not carry appropriate liability or workers compensation insurances. As the “Bearer of Bad News” we were in a no-win situation. More than once we got a call from a homeowner, after the

fact, who said “We wish we had chosen you, you told us the truth.” While it felt good to hear that someone realized we had been straightforward with our quotation, it didn’t change the paradigm. And, it just didn’t make sense for everyone concerned. Read more to find out how contractors got such a bad name and how we “*remodeled our remodeling business*” to help you avoid a construction horror story of your own.

10 LESSONS LEARNED

The blueprint for a construction horror story offers within it the ways to avoid problems on your remodel. Here are the 10 lessons learned.

1. A craftsman decides to become a general contractor.

He’s a good craftsman and a likable guy but he has no business experience. He doesn’t understand even basic accounting principles. He doesn’t know his overhead costs and how to price jobs to cover his costs, his overhead, and produce a fair profit.

Lesson: Make sure the company you choose to remodel your home understands the business of construction as well as how to build.

2. The contractor estimates based on what he thinks the market will bear.

The estimate is generated based on what the contractor feels is competitive to get the job. It is not based on fixed price bids from suppliers and subcontractors. It may or may not have a separate line for each item, i.e. demolition, concrete, framing, electrical, plumbing, etc.

Lesson: The price for the job should be based on the actual costs to build the project

3. The contractor uses allowances not actual costs for finish materials and labor.

Allowances rather than firm costs for specific fixtures and finishes are included for items such as plumbing fixtures (sinks, faucets, toilets, bathtubs, shower valves) electrical fixtures (can lights, exterior and interior light fixtures, outlets/switches, trim) flooring (hardwood, carpet, tile) cabinetry and cabinetry hardware, tile, countertops, windows, doors and door hardware, finish trim for doors, windows, baseboard, crown molding, appliances (refrigerator, oven, cook top, vent hood, dishwasher, microwave, garbage disposal, siding or stucco, painting (brand of paint and sheen, number of colors)

Lesson: Specify the exact fixtures and finishes to be installed and have actual costs for them included in a Fixed-Price Quotation for the job.

Unless all materials and labor are fixed priced costs, you truly have an “estimate” of what the final project price will be. While all of the rough materials, labor and subcontractor costs should be fixed prices, understand that the homeowner controls up to 50% of the final price by their choice of finishes. If the contractor did not include a large enough allowance for the finishes, the homeowner will be presented with a change order for the difference in price (plus margin) for the increased cost. As construction is already underway, the homeowner has very little choice but to sign and pay for the Change Order.

4. The customer believes they are exercising *Due Diligence* by obtaining three bids.

In a Design-Bid-Build model, contractors know they are bidding against other contractors. From experience, they have found that they are rarely rewarded for telling the truth on their bids; rather they are rewarded for making their make bids look good. Some may low-ball a bid, hoping to make it up with Change Orders during the process. Or, they may exclude some things that are not obvious to a homeowner or architect to get the job. Worse yet, they may not even realize that they have bid a job under their actual costs and won't find out until they don't have enough money to pay for the labor, subcontractors and materials.

Lesson: Obtaining three bids is not due diligence – no matter what anyone tells you.

Homeowners want to think that the reason some bids are lower is that all contractors know their costs and the lower-priced bid is from a contractor who is willing to make less money, or who has some inside knowledge of getting a job done for less. The homeowner selects a bid between the highest and lowest-priced bids and thinks they are being prudent by not choosing the lowest price. Unless all of the bids are generated with the exact same assumptions, it is almost impossible to compare them apples-to-apples. Due diligence is selecting a firm that you respect who incorporates accurate construction cost information throughout the design process.

5. The contractor controls the cost of the project.

One of the ways homeowners contribute to horror stories is by being unrealistic about what the project will cost. Wishful thinking by homeowners leads them to believe what they want to hear even if it isn't logical. They believe that if they chose a contractor with a lower price they can just manage him better to get the same results as a high-priced contractor. They want to

believe that the quality of work for a low-priced contractor is the same as for the higher-priced contractor. They want to believe that some contractors have a secret way of getting the job done for less.

Lesson: Unless all materials and labor are fixed-priced costs, you have an “estimate” of what the final project price will be.

While all of the rough materials and labor costs should be fixed prices, understand that the homeowner controls up to 50% of the final price based on their choice of finishes.

6. Everyone is excited and wants to start right away.

The contractor starts the job right away because he needs the money. He either asks for a deposit to start the job (more than \$1,000 is illegal in California) because he has past due bills

Lesson: The time spent before the project begins to design to a budget and select the exact fixtures and finishes to be installed virtually eliminates change orders and schedule slippage. Any time spent before construction begins to assure the plans are complete and all materials are specified is time well-spent.

7. The contractor’s cash flow is nil and he is in arrears for materials and labor from previous jobs

The contractor did not bid jobs based on actual costs and overhead and is underwater. He is using money from the current jobs and to pay bills from past jobs. He was lucky to make payroll. He has no money left. There are still unpaid subcontractors and material suppliers from previous jobs. They are hounding him and he stops returning their calls. He has to find new subcontractors for the current job that he has not used before. And, they may or may not work for the amount he has estimated. This is a vicious time-wasting cycle.

Lesson: Assure that the contractor has the experience to run a business.

8. He asks the homeowner for more money even if it is not due, or borrows money from his credit cards to make payroll.

He is in over his head and decides that he can find ways to charge the homeowner for more money. He issues invoices for things the customer assumed were in the original bid. There were no Change Orders created or signed prior to the work being completed.

Lesson: Sign a contract only if there is a fixed-price for the work.

A fixed-price contract can only be created if all of the design and materials decisions are completed before the fixed price quotation (not an estimate) is created. As part of the Design + Build process, homeowners are provided with accurate cost information before plans are drawn and then throughout the design process and details are determined. A selection list for the project for all selected fixtures and finishes is created and actual brand, part number, color, etc. are used to create the fixed-price quotation.

9. The contractor presents numerous change orders for items that were not included in the estimate or for materials more expensive than the allowances.

There are many arguments over money. The customer now does not trust the contractor to tell the truth so even when he does there is doubt and fear. There is severe tension on the job site. The contractor thinks the customer is unethical and cheap. It's a lovely way to spend the next eight months of your life.

Lesson: Contractors don't like change orders any more than homeowners do.

Creating change orders is a time-consuming process and the homeowner is often not happy with an increase in cost, even if they initiated the change. From both the contractor's and homeowner's perspectives the vast majority of these conversations take place as the project is designed and before a contract is signed. It is important to assure that all materials and labor are specified before the contract is signed to eliminate surprises.

10. Once most of the money has been paid for the current job, the contractor disappears.

He has signed a new job and is at that job site most of the time as he will be able to get more cash. It is like pulling teeth to get the job finished and when it is finally done, it is not the job the customer had envisioned and it cost much more than the contractor bid.

Lesson: Select a contractor who understands how to run the business of remodeling.

Remodeling is first and foremost a business. Contractors need to establish long-term relationships with material suppliers and subcontractors. They need to hire and manage employees in a professional manner. They need to stay on top of industry best practices. Jobs must be priced to cover overhead and a fair profit margin or cash flow will always be an issue and when it is, the relationship between the contractor and the homeowner is compromised.