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## HOW BUILDERS CAN AVOID BANKRUPTCY IN A DOWN MARKET

» PETER G. MERRILL

As we all know, there isn't any aspect of our economy that has not been affected by the deepening recession that we are all facing. Waiting for a silver bullet from the new Obama administration or a miraculous turn in the economy is a passive and ineffective method of keeping your business in the black and profitable. There will be many efforts attempted by the new administration to turn this recession around. I personally feel that it will be a very long time before we see an appreciable increase in the housing or construction market. If you wish to keep from losing money and avoid bankruptcy, you can take positive steps on your own to keep your business operating. This article can only suggest a few proven methods to minimize your expenses and increase your business. Not everything will work for everyone; however, any combination of my suggestions just might be enough to keep you in business. Please give serious thought to any decisions that you will make related to your business. Look at the short-term benefits, but don't lose sight of the full picture, including the future. Keep in mind that if you do not properly take care of the present, you will most likely not have a future. If possible, consult with other professionals with more knowledge and experience related to the decisions you will be making, such as an accountant or financial advisor.

If you have any credit card balances with interest rates in the 10 percent, 15 percent, 20 percent or higher ranges, talk to your credit card company about getting a lower rate. If they won't change their rates, let them know that you are considering transferring your balance with them to another

credit card company. Always ask to speak to a supervisor if the first person that you talk to gives you a "no" answer to lower rates. They must pass you on to a supervisor if you request to speak to one. If the credit card company will not bring down your interest rate, check with other credit card companies to see who has the lowest "balance transfer rate." Many banks have rates such as 0 percent for six to 12 months. I have recently seen several credit card companies who are offering 3.99 percent balance transfer rates that are good for several years. Obviously, if you get an interest rate lowered to 3.99 percent from 20 percent, you will be lowering your interest carrying costs by 80 percent.

While your company is in good or reasonable financial condition, consider arranging for a line of credit that you can access when necessary. That line of credit might allow you to pay a few invoices, avoiding more expensive late charges by paying your bills beyond their due date. If you get behind on your bills and your credit rating should drop, it will be more difficult arranging for a line of credit sometime in the future. Most lines of credit do not cost you anything until you access those funds.

**KEEP IN MIND THAT IF YOU DO NOT PROPERLY TAKE CARE OF THE PRESENT, YOU WILL MOST LIKELY NOT HAVE A FUTURE.**

Consider liquidating your inventory. Look at your inventory and make certain that you do not have more inventory than you will need in the near future. It is extremely difficult to sell your inventory at your cost. You might need to contact other builders and sell them the inventory at below your cost. I recently heard of a builder who bought a full trailer-load of sheetrock at a really great price just prior to his business greatly falling off. He went out of business with a large inventory of sheetrock. You can't pay your bills by delivering a load of sheetrock to a supplier. Liquidating or lowering your inventory, even at a small loss, can provide much-needed cash to cover your payroll and other expenses.

Consider selling off some of your equipment or tools. This is a wide-open area. If you own several backhoes, bobcats, graders etc., although you might lose money on them, selling them even at a loss may provide necessary cash, especially when you have no business or very little business. It will not be the end of the world if you have to rent the equipment that you need for future jobs. At least you will be in business when that future project comes your way. Consider an "equipment foreclosure" if you have new equipment with high payments. Let's suppose that you purchased a large piece of equipment for \$15,000, utilizing a \$3,000 deposit that left you with a \$450 monthly payment for three years. If you are in the first year of your payments, you will probably still owe about \$10,000. If the loan for the equipment was secured only by that piece of equipment, and you turned the equipment (that is standing idle in your back lot) in to the bank, you will lose not only the piece of equipment, but you will also not be responsible for the monthly \$450 payment that can now be used to cover other expenses. I call this an equipment foreclosure, as it very closely parallels

a house foreclosure, where the mortgage on the house is higher than the value of the house. A major piece of equipment that is sitting idle and will most likely not be utilized in the near future has very little if any value to you, while your payments (mortgage) are very much higher than the value of the equipment. You are the only one who can determine if the cash you will save on monthly payments will give you enough financial assistance to decide if you wish to turn the equipment back into the bank or company who financed the purchase. Taking a sizable loss on a piece of equipment is better than going out of business while still owning that equipment.

If you are renting your offices, consider talking to your landlord about lowering your rent for a specified period of time. Landlords who have other tenants who have recently gone out of business cannot afford to have others go out of business. Lowering your rent is better for them, as opposed to having you go out of business when they will not get any rent from you. You might consider offering to extend your lease if the landlord will lower your rent. If you extend your lease and eventually go out of business and file for bankruptcy, the length of the lease will be of no concern to you at that time.

If you rent equipment, consider renegotiating your equipment lease with your supplier. I had a copy machine that I had leased for 60 months, about three years ago. I renegotiated our lease with the copy machine company and extended the lease at this time for another 66 months, which cut my monthly payments in half, increasing the available cash for other expenses.

Do not overextend credit to any of your customers. If you have accounts that you currently service and bill on a monthly or other regular basis, and they begin to slip backward in their payments, it is a sign that they, too, are

caught up in the recession. You can't afford to serve as their bank. It might hurt to cut off some of the only business that you have, but if you continue to service that account without them meeting your payment requirements, you will be absorbing their credit problems into your company and they will expedite bringing down your company along with their company. They may have been great customers over the years and you most likely will have developed a personal relationship with them. In spite of your relationship, you must be aggressive in controlling the credit that you extend to customers.

Look at cutting back employee hours. We all know that it is a tight market getting employment. Most of your employees can handle a small cutback in hours, which is better than losing their jobs. Some companies will cut back employees' pay 10 percent

while keeping normal hours. A one-hour cutback in open hours and pay will not only save you the direct payroll costs, but also the extra related costs, such as payroll taxes. A one-hour cut in payroll each day will save you about 12.5 percent of pay for a week (based on a 40 hour work-week). If you add the other payroll taxes and benefits related to the payroll, you will end up saving more of your total payroll costs. I know it is difficult to let employees go; however, if you do not bring your employees in line with the amount of work that you have, you will undoubtedly go out of business sometime in the future. Try going with a cutback in hours for everyone as mentioned above, but if that is not enough or will not work, you must fire the people you do not need to carry on your business. Remember that most employees will qualify for unemployment benefits if you let them go.

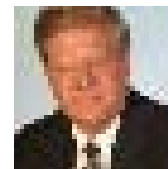
Consider expanding your services. Most builders who are caught up in this down economy are adding remodeling to their business services. Even offering handyman services might help you generate a little extra cash while helping you keep a few employees on your payroll.

I must also recommend that you review your sales contract to specify the use of binding arbitration to settle disputes as opposed to the traditional expensive and lengthy litigation process. Those homeowners who do build are usually on a very tight budget, and will be asking for as much as they feel they can get on their limited budget. Having an efficient and inexpensive dispute resolution mechanism specified in your contract that also can assure you that your disputes will be handled by construction-knowledgeable arbitrators is very much to

your advantage, as opposed to appearing before a judge with little or no construction knowledge who will base his/her verdict on whichever party presents the most convincing case instead of deciding on who is right or wrong. Many builders who do not have proper contract language end up losing all of their profits to the costs of litigation. (For further information on proper contract language, please refer back to articles that I have written this past year in the February, April, June, August and November 2008 issues of *BUILDERnews magazine*.)

Little things can also add up. Consider cleaning your own offices as opposed to having a cleaning service coming to your business on a regular schedule. Get a programmable thermostat to turn down your heat at night. Use recycled paper in your fax machine. Don't throw out manila folders until you have turned them inside out and used both sides, and so on.

Tough times call for tough decisions. No one ever said that being in business will always be easy. If you consider all of the options that are mentioned above, and you can keep your expenses down to a manageable level, you most likely can keep yourself in business during these slow times. Builders who are creative and open-minded to thinking out of the box have a much better chance of hanging on during these difficult times. ■



PETER G. MERRILL is president and CEO of Construction Dispute Resolution Services LLC, an NAHB Executive Board member and past president of the New Mexico Home Builders Association. He received Builder of the Year and Remodeler of the Year awards.

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