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Points to Ponder

“It is not the beauty of a building you should look at; it’s the construction of the foundation that will stand the test of time.”

-David Allan Coe



PROFIT CLUE

Profitability Tips for Construction Businesses

Spring 2009

Consider All Angles Before Forming a Joint Venture

Joint ventures can be an enticing option to expand your capabilities and mitigate risk, whether you’re pursuing work farther afield or considering going after a new type of work. Normally in a joint venture, each firm has a specific talent or resources that the other needs to complete the project. For example, a project might require specialized equipment that would be supplied by one firm, while the other firm might have labor and management personnel not possessed by the other. But without a clear understanding of all parties’ capabilities, expectations and responsibilities, these arrangements can crash and burn.

Consider the case of a small, minority-owned contractor and a larger contractor that formed a joint venture to obtain a project neither one would have been able to win on its own. Driven by the desire to win the work, the two companies overlooked the fact that their companies had completely different cultures and ways of working. They rushed into the arrangement without taking the time to draft a comprehensive joint venture agreement.

Fireworks between the work crews started almost from the beginning, and it quickly became clear that the relationship wouldn’t work. But without a well-drafted agreement, the parties had no clear process for terminating the entity. This situation would have had a much more positive outcome if the contractors had thought through the following angles and drafted an appropriate joint venture agreement in advance.

- Who will be responsible for which elements of the project?
- Who will keep the accounting records for the joint venture?
- What form will the joint venture take? Will it be limited to a single job, or left



open indefinitely? To what degree will the parties share in profits and losses?

- What are the tax, legal and insurance consequences of a joint venture? (Consult your accountant, attorney and insurance agent before entering into a JV agreement.)
- What is the potential joint venture partner’s financial condition? Both parties should examine the other’s financial statements, credit history and work commitments. Surety companies usually require complete financial information on each of the joint venture partners, so it is imperative for each partner to consult with its bonding agent before considering such an arrangement.
- Is there a possibility of culture clashes? Clearly in the example above, failing to take this factor into consideration doomed the joint venture from the start.
- How will disputes be settled? What is the exit strategy? If the arrangement isn’t working out, what are the steps the joint venture partners will follow to terminate the entity?

Any new working arrangement is sure to hit some snags, but answering the questions above and documenting the answers in a joint venture agreement will put you on the path to a profitable alliance for all involved. ■■

Travel Tips: Approach “Away Games” Cautiously

Today, construction company owners are considering every option to bring in revenue, including traveling to new territories.

Proceed with caution!

Over-expansion – whether into new types of work or new geographies – is a leading cause of contractor failure. Before embarking on your first ‘away game,’ have a clear rationale for accepting out-of-state jobs, as well as a plan for growing in that region. Make sure you understand the territory, labor pool, local subcontractor market and regulations. And appoint a key trusted employee to oversee each job in a new territory to make sure the project is completed according to your company’s standards and culture.

In order to flatten the learning curve involved in working in a new territory, the Surety Information Office recommends the following tips:

- Leverage existing relationships. If possible, start off in a new territory working with a repeat client who’s expanding. Also try to use some subcontractors you’ve worked with before.
- Look to a major subcontractor to help with local relationships.
- Integrate long-standing employees with hired employees from the new geography.
- Limit any expansion to one new region at a time.
- Try to limit the scope of the project engagement to a skill-set that is well within your past experience and core competency.
- Involve a local joint venture partner.

Expanding into a new territory doesn’t have to be a nail-biting experience. Take the time to consider all your options before accepting out-of-state work. ■ ■

Who’s Who in ProfitCrew™

Who: John Winquist, CPA, is an audit manager and member of Wolf & Company LLP’s Construction and Real Estate Industry Group. He works with clients in various industries including construction and real estate. John is a member of the American Institute of Certified Public Accountants and Illinois CPA Society.

What he does best: Builds lasting business relationships with the clients he serves through dedication to quality service and timely solutions to everyday business issues. He recently joined the Home Builder’s Association of Greater Chicago to help foster future business relationships and learn more about the current issues affecting the homebuilding and related industries.

In his spare time: John enjoys living in Lincoln Park and attending as many summer festivals as possible. He spends a significant amount of time chasing his French bulldog/cocker spaniel, Parker, all over the place. His favorite sports teams are the White Sox, Bears, Bulls and Blackhawks - in that order. He also enjoys volunteering for Hearts for Hope, a non-profit organization dedicated to raising funds for families of children that go through Hope Children’s Hospital.



& Questions Answers

Question

While we’re not having our best year, my company is healthy. How can I take advantage of opportunities now to position my company for growth when the economy turns around?

Answer

Kudos for thinking strategically. Too many business owners become paralyzed by adversity and end up making short-term decisions that hamstring their long-term growth. Companies that are in a strong financial position right now can take advantage of some key opportunities to grow.

First, don’t stop working your strategic plan. If you budgeted for operational improvements, follow through. Sacrificing potentially profitable investments for the sake of short-term savings only makes sense if you’re in dire straits.

Consider the merits of growth and diversification. If competitors are struggling right now, you might be able to acquire a business or pick up some key employees at a discounted rate. However, you don’t have to merge to expand your market. When competitors go out of business, their clients are up for grabs, presenting an opportunity for you to diversify your client base. But remember that

expansion brings challenges, such as the need for additional capital and infrastructure. Grow carefully and strategically.

Capital investments. Equipment and real estate is available at a discount for those who have the cash to spend or access to credit. But only make these investments if they’re really necessary, and evaluate the benefits of buying, leasing or conducting a like-kind exchange.

These are all strategic decisions with long-term consequences, so don’t make them without input from your key advisors, including a construction-focused accounting firm, lender and bonding agent. ■ ■