Overhead Is Not A Fixed Cost

“You already do a great job making direct cost estimates . . . to survive in tight times you have to carry that ability to your overhead budget”

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As a contractor in the wall and ceiling industries, you make it your business to control your costs for materials, labor and equipment. But there’s another cost that you’ve got to watch—your indirect cost. And you’ve got to control it just as you control all other costs—within the margin available to your company.

Several years ago, in 1974, I got a call from a small specialty contractor in west Florida, where the workload had turned down sharply. He told me that last year he did about $1.5 million volume of work and made some money. Then he said, “This year I’m going to lose, and lose severely, because I’m only going to do $800,000 worth of work. It looks like I’m going to have to go into bankruptcy.”

I said, “Fellah, before we start planning on your bankruptcy, let me ask you a few questions. Have you ever heard of a contractor in your type of business who did $800,000 worth of business and made money?” He said, “Sure.” “Have you ever thought of copying him?” I asked. He answered that it wasn’t that easy.

“Well, it is that easy,” I said, “and you’ve got to do it. I want you to make out a budget of your overhead. Many of your larger categories of overhead have variable costs. And don’t assume what you had in your budget last year. I want you to start with zero in each category of your overhead. Then ask yourself as you fill it in, ‘How much do I need to spend in each category with an $800,000 volume?’

“For example, look at that $50,000 you had in trucking expenses last year. That’s a lot for your operation. If you can only justify $30,000 this year, that’s the figure to put in the budget. And then really get those costs down to $30,000. I don’t care if you have to sell the trucks, put them up on blocks, stop the gas, stop the insurance, stop the drivers, stop the oil—but stop the expense on the other $20,000. You see, your problem isn’t depreciation, it’s paying out running expenses.

“You can keep your supervisory team together too, but you may have to downgrade a foreman to a journeyman. I know you’ll say they wouldn’t like it, but they’d like it better than collecting unemployment compensation in west Florida right now. They’ll understand.

“And what about office staff? If you don’t need that pretty girl to chase coffee as a receptionist, get rid of her—unless she’s your wife. That could be expensive.”

As a contractor, you must have your budget as a tool to control your overhead. You already do a great job of making direct cost estimates, or you wouldn’t be in business. To survive in tight times you’ve got to carry that ability one step further to your overhead budget. Do it quarterly—or, preferably, monthly.

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