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# Home Depot or Home Despot?

## Remodelers Grapple With Home Center Giant's Installed Sales Program

These days it seems everybody wants to get into the remodeling business. Home Depot Inc., a rapidly growing home center chain with 195 stores in 17 states recently began an installed sales program in ten markets, including Atlanta, Dallas/Fort Worth, San Diego, and New Jersey. Within the next two years, the program will extend to all of the chain's locations. While many "home centers," including Hechinger, Builders Square, and, of course, Sears, offer installed sales, some builders and remodelers believe Home Depot, because of its size and aggressive pricing strategies, poses a new and more dangerous threat. What WalMart does to small-town general stores, these contractors argue, Home Depot will do to the small contractor.

Home Depot's installed sales programs work the same way others do. When a customer purchases a product, such as a storm door, siding, flooring, or a hot water heater, the home center contacts one of its remodeling subs — typically a local remodeler or sub under contract with the home center — to do the installation. The remodeler is later paid a set fee for the work by the store.

In the past, most remodelers accepted home centers as healthy competition, especially since their prices are typically higher than those charged by remodelers. But Home Depot is able to sell products, complete with installation, at prices most remodelers can't match. Home Depot is so big and buys items in such quantities that it can practically dictate pricing to the manufacturers. The stores also do a lot of advertising and promote loss leaders — items priced tantalizingly low to lure customers into the store.

The remodelers most hurt by Home Depot are those who rely on small jobs and companies with handyman services. But even large remodeling companies are feeling, or will feel, the pinch as Home Depot expands its markets. That's because many large companies rely on small jobs, such as installing entry doors or windows, to introduce them to the customers who will later call them for bigger jobs.

***How low can they go?*** Lee Greer, a general remodeler in Atlanta and a certified installer for Peachtree windows and doors, says Home Depot sells Peachtree products at a price that undercuts Greer's — even with his certified installer discount.

"How do I explain that to my customers?" he says. "I have to rely on the fact that I can provide better, more personal service. Some of my customers might try a few projects with Home Depot, but eventually they'll be back."

Like Greer, Jerry McDaniel, president of McDaniel Remodeling Inc., also in Atlanta, is confident the attention to detail and service provided by his company's handyman division will win out in the long run over Home Depot.

"I've seen the kind of work home centers do," says Greer. "It can't compare with ours. Our handymen are well-trained, high-caliber remodelers. They aren't just carpenters off the street. These home centers are so big, they can't deliver the service and quality we can."

Remodeler John Sensenstein, however, isn't so confident. Sensenstein, who owns The Window and Door Mart in Wharton, N.J., says

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# 600 Bottles of Beer in the Wall

*These days, the glass in fiberglass insulation comes increasingly from recycled bottles and other glass containers. The insulation made by Schuller International, for instance, makers of Manville-brand insulation, is about 40% recycled glass, most of it purchased from landfills and recyclers. This means the average home insulated with recycled glass fiberglass contains the remains of about 600 bottles.* □

## A New Threat From Sears

As if Home Depot's expansion weren't enough to worry about, Sears, which has so far relied on installed sales, recently began testing the full-service remodeling market with pilot programs in Chicago and South Florida.

"The field is closely related to what we're doing now and we're always looking at new markets," says Bob Shamberg, field business manager for Sears. "While the full service side is more complicated and carries more risk, it may be a viable program in some parts of the country," he says.

Remodelers who have bid on jobs against Sears have learned that some people like the store's reputation for reliability and service, whether they are buying underwear or adding on a room. "The name carries a lot of clout," says Bob Krieff, a partner at First Southern Construction Corporation, the Miami-based construction firm handling Sears' Florida pilot program. "No one remembers our company's name. But everyone remembers Sears."

After working under the Sears name for less than a year, First Southern now has more jobs than it can handle. The company gets referrals from 22 Sears stores in South Florida. In return for using the Sears name and referral network, First Southern pays Sears a percentage of each job.

Krieff and his partners anticipated most of their jobs would be in the $10,000 to $25,000 range. To date, many have been design/build jobs between $75,000 and $200,000. To satisfy demand, First Southern has a full-time architect on staff, as well as two draftsmen and 15 full-time office and field personnel. "With all the rebuilding as a result of the storm [Hurricane Andrew], we could triple our staff tomorrow and still not have enough help. We have 350 qualified referrals waiting," Krieff says. □

## STATE BY STATE

***California:*** Contractors here must now include a statement on their contract saying the state requires them to be licensed. Furthermore, the statement must advise homeowners that complaints against the contractor should be filed with the Contractors' State License Board, which can investigate them up until three years after any construction work is completed.

***Oregon:*** Most people associate earthquake damage with California, but geologists are discovering Oregon is also susceptible to quakes. In response, the state's building code is being updated with new seismic requirements. The change follows the Federal Emergency Management Agency's move to upgrade areas west of the Cascades to a seismic ranking of 3. The previous rank was 2B. By comparison, San Francisco and other quake-prone areas are ranked 4.

***New Jersey:*** The New Jersey Builders Association has decided it's time to draw a line in the sand. The group worked with state legislators to develop a bill that once and for all defines the difference between design/builders and architects. The bill would allow registered home builders and remodelers to offer and advertise design services to customers and to perform those services until professionally sealed drawings are required to obtain a construction permit.

***Michigan:*** If you saw the movie *Roger and Me*, you know parts of Michigan haven't fully recovered from the autoworker layoffs of the 1980s. To help revitalize housing in urban areas, the governor signed legislation creating housing enterprise zones. The bill provides a property tax break for anyone who fixes up their home or builds a new home within a zone. □

# Corian to Require Installer Certification

Ask customers to name a brand of solid surfacing material, and chances are they'll mention Corian. Since its introduction by Du Pont 25 years ago, Corian has dominated the solid surfacing market, and most veteran kitchen installers have fabricated a Corian top or two. But even the most experienced installers may get a little surprise next time they go to pick up some Corian — they may get asked for their papers.

In an effort to ensure quality control and back its ten-year warranty program, Du Pont Corian has initiated a new certification program for its installers. The certification standard doesn't forbid suppliers to sell Corian to non-certified installers; that is left up to the individual suppliers. But the product will carry its ten-year warranty only if it's installed by an "approved fabricator" or a "certified distributor/fabricator." Suppliers wanting the protection of the Du Pont warranty will have to sell only to approved or certified fabricators.

To become an approved fabricator, a company must follow Du Pont fabrication techniques, maintain a properly equipped shop, attend annual fabrication courses, and "demonstrate an ongoing commitment to quality." This is the most likely route for small contractors and K&B specialists. Certified distributor/fabricators are generally wholesale fabricators that inventory substantial amounts of Corian for both residential and commercial work, maintain a large shop, and have full-time sales personnel.

For more information, contact your local Corian distributor or Corian at 800/426-7426.

*— Carl Hagstrom*

## From What We Gather

***Tighter homes may be raising asthma rates among children,*** according to a recent study published in *The American Review of Respiratory Disease*. Citing a rise over the last 20 years in childhood asthma rates, researchers speculate that tight houses, by reducing air leakage, trap airborne particles, such as animal dander, dust, and other irritants, that can cause or aggravate an asthmatic condition.

***A glut of starter homes may bog down the housing market*** in the late 1990s as the baby boomers, who bought starter homes in the late '80s and early '90s, try to sell those homes and move up, according to a recent report in NAHB's *Housing Economics* newsletter. Unlike the '80s, when a large share of starter homes were bought by people under 40, repeat buyers and older first-time buyers will buy these starter homes. Some of these buyers, the report notes, may be older homeowners who have finished raising families and are looking for smaller homes.

***You knew open fireplaces lost energy***, but did you know the figure ran as high as 30% of a home's energy costs? That's the latest finding from a French study, which found that an open fireplace in a well-insulated house could increase bills by one third.

***Reducing clearcutting in national forests*** is part of the Forest Service's new attempt at "ecosystem management." Announced just before the Earth Summit in June, the 70% reduction in clearcutting will take place over the next three years. Forest industry officials say the change will reduce timber volume by about 10%. Some environmentalists fault the new plan, however, saying that its rhetoric has yet to be backed with substantive changes in policy and planning.

***Aluminum components take 80 times as much energy*** to make as equivalent wood components, according to information cited in the September/October 1992 issue of *The Environmental Building News*. By weight, brick and cement building materials take twice as much energy to make as wood; glass three times as much; fiberglass seven times as much; steel eight times as much; and plastic thirty times as much. ☐

# In-Grade: You've Read the Charts, Now See the Movie

As part of its ongoing effort to educate lumber users about the In-Grade wood grading system it introduced in 1991, the Western Wood Products Association has released a package of materials called *The Builder's Guide to In-Grade*. The package includes a 20-minute videotape and three WWPA literature pieces: *The Western Lumber Product Use Manual*; *In Grade: What It Means*; and *WWPA Grade Stamps*. Together, the WWPA says, these materials provide a solid overview of the In-Grade testing program, how its standards differ from the previous grading standards, and what the various grades mean.

At only $10 for the whole package and $2 a piece for extra sets of the printed materials, the *Builder's Guide* sounds like a good deal. To order, send a check to WWPA, Dept. BGIG, Yeon Bldg., 522 S.W. Fifth Ave., Portland, OR 97204. ☐

# NRCA: Architects Don't Know Roofing

The roof may be one of the most important elements in building design, but, according to a survey of architects and architecture schools conducted by the National Roofing Contractors Association (NRCA), architecture students aren't learning enough about roofing. As a result, roofs are often improperly designed and specified, leading to a disproportionate number of failures, lawsuits, and claims.

The survey found schools often devote only two class sessions (5 hours) or less to roofing, and students usually learn about metal and built-up roofing. Architects are expected to learn roofing system design, including slope/drainage, insulation types, and deck design, during their internships. However, if the firms they work with don't encourage them to research roofing systems, details, and plans, their knowledge will remain spotty.

Many architects do not perceive roofs as an architectural element, according to the NRCA. As a result, problems with roofing systems that should be resolved in the office are complicating matters in the field. These problems include specifying incompatible materials, allowing insufficient time for roof installation, and designing inadequate systems. If these problems are not solved in the field, the roofing contractor, along with the building owner and the architect, often meet again in court.

To help educate architects, NRCA has developed two educational programs, one for faculty and one for students. The faculty program is a 3½-hour presentation by roofing contractors who explore all aspects of roofing, including material selection criteria, energy savings with roof insulation, and single-ply systems. The student program is a seminar presented by contractors who encourage the students to ask questions. ☐

***Home Depot,*** *continued from first page*

Home Depot's price-oriented approach to remodeling is making it increasingly hard for him to make a living.

"Service and craftsmanship are the most important things I can offer my customers," he says. "If I have to compete on price alone, I can't provide those things. I'd have to go from being a craftsman to being an assembly-line worker. How many garage door installations can I do in a day? And when Home Depot offers to do kitchen design for free, I then have to justify to my customers why I'm charging for it.

"They're using their economy of scale to lowball the competition. If we remodelers don't do something about this, we can just forget it. They are putting installers out of business."

***Not aiming at handymen.*** According to Jerry Shields, senior manager for public relations for Home Depot, the home center chain is trying to compete with other home centers, not remodelers. "The small remodeler's overhead is much lower than ours — they don't have a $10 million store to operate. If we run a special, our prices might approach theirs. But it's not our intention to compete with handymen," he says.

As for the quality of the work, Home Depot hires competent people. "We guarantee our work," says Shields. "If it's not done right, we have to pay to redo it and our reputation suffers."

The chain prefers to hire remodelers who come into their stores to do business. "We have signs up asking them to contact us if they're interested in steady work and a good income," Shields says. "From their perspective, working for us should be the best of all worlds. We give them plenty of leads and they're guaranteed payment." The stores prefer remodelers who've been in business for at least two years and require that all applicants be insured and, where necessary, licensed.

***What's a remodeler to do?*** Chances are good that installed sales programs are here to stay. Sears has been doing it for years, and other home centers are rapidly following suit. Most remodelers aren't happy about having their field invaded by these slick, well-organized corporate giants. Several local chapters of remodeling trade associations have reportedly organized Home Depot boycotts. But a more practical approach may be to find a way to hold onto your business and stay competitive.

Some remodelers have suggested forming cooperatives to increase their purchasing power. "Maybe by banding together," says Sensenstein, "we can get better pricing on materials and better quality control."

Dan Gagnon of Gagnon Homes, a remodeling and new construction firm in Weathersfield, Conn., says the key to success is your sales approach. He tells customers that dealing with a home center is like going to a Health Maintenance Organization (HMO) for medical care. "You don't get to choose your own doctor at an HMO and you don't get to choose your own carpenter at a home center."

Gagnon also funnels his business to local lumberyards and counts on them for referrals. "I believe in keeping my company's money invested in the local economy," he says. Staying involved in the community is another way to get your name out and secure business.

To differentiate his company, Jerry McDaniel provides 24-hour emergency service and a quick response time for non-emergency jobs. Like Gagnon, he stresses the importance of service and individual attention. "Once people get to know us, to know who we are and what we do, they stick with us," he says.

Only time will tell whether John Sensenstein's nightmare vision — that "the industry will end up being low-paid laborers trained in one or two things they do for Home Depot" — will become reality. Like the small-town hardware store owner who puts up "For Sale" signs the day he hears WalMart is coming to town, some remodelers will undoubtedly choose to switch rather than fight. Others will join instead, and become paid installers rather than competitors (see "A New Threat From Sears," page 5). Still others, such as Gagnon and McDaniel, will try to outservice and outsell the expanding giants — something like the service-intensive local hardware stores that manage to thrive in WalMart's shadow. But one thing seems clear: If Home Depot and Sears enter the remodeling business on a large scale, few remodelers will be able to ignore them. □

## TAX TALK

# Make That Year-End Bonus Painless

**by Irving L. Blackman**

Let's talk about the most important compensation plan of a closely held corporation — yours. The typical owner (let's call him Joe) starts out the year thinking:

"Will it be a good year?…bad?…can't tell yet?…better take a small salary." The last month of the year comes. Surprise! The year was better than expected. Joe takes a fat bonus, eliminating all or most of the profit. Enter the IRS. The year-end bonus trap has been sprung.

Most uninformed business owners play their personal compensation game just like Joe — dangerously. It doesn't make any difference if you have done it every year since you've been in business. Get caught, and you're in deep tax trouble.

Why? Well, your total compensation — salary taken during the year plus the year-end bonus — is reasonable. But reasonable compensation is not the issue. The issue is whether the year-end bonus is taken as compensation or a distribution of profits. The difference in tax cost is worlds apart: Compensation is deductible by your corporation, but a profit distribution is nondeductible. The courts simply hold that the year-end bonus is a nondeductible dividend, meaning the corporation has to pay taxes on it. Worse yet, there is a long line of cases where the courts have clobbered closely held corporations like Joe's for playing this bonus game. Getting out of this tax trap is expensive — involving additional taxes, interest, legal fees, and sometimes penalties.

But you can avoid it. Here are two ways. One: Early in the year, document in the corporate minutes the amount of your compensation and the specific services you will render to deserve it. Set the compensation high rather than low, but take a smaller current salary. For example, take $1,000 a week after setting a $100,000 salary for the year. If things work out. terrific…take the $48,000 balance at year's end; if not, then waive all or a portion of the $48,000.

Option two: Elect S corporation status. Then a bonus or high-low salary arrangement has no meaning. You can simply take some or all of the corporate profits (via an S corporation dividend) whenever you please, without fear of IRS attack. □

*Irving L. Blackman, CPA, JD, is with Blackman Kallick Bartelstein, 300 S. Riverside Plaza, Chicago, IL 60606.*