

## Transparency: An Idea Whose Time Has Gone? Or Come?

*Note: David Gerstel is the author of the construction industry classic, Running a Successful Construction Company. The following article is in part adapted from his new book, Nail Your Numbers: A Path to Skilled Construction Estimating and Bidding.*

**Recently, I ran across a website** for a construction service that is a bit different from any I have encountered before. “CS,” as I will call the service here, recruits homeowners and builders, pairs them up with one another, and then supports their projects with its web-based management platform.

CS describes its service as “new” and “revolutionary” and “transparent.” It may be somewhat new. It may even have real value. But here’s what CS calls “transparent”: It charges a fee of 3% to 8% of construction cost for its service. It collects the fee by routing all payments from an owner to a builder through its management platform and taking its percentage before sending the balance on to the builder. Meanwhile, CS is at pains to avoid disclosing its take to homeowners. You can call that practice what you like. But transparent? Hardly.

While there are a number of definitions for “transparent,” for the sake of this article, a straightforward one will do: “Candid disclosure of the charges for a construction project.”

That’s simple enough. Even so, builders have strong opinions about the issue when it comes to their own charges. I have heard builders refer to one another as idiots, traitors, and un-American as they butt heads over just how much transparency they are obligated to provide with respect to their charges for labor, for material, for trade partners—and especially for overhead and profit.

Transparency is a subject I have given a lot of thought to over the years, and I have arrived at strong opinions about it myself. But let me hold off on my own views and first attempt a fair-minded presentation of the diverse views of other builders. They fall into two groups: those who resist the idea of candid disclosure in the form of detailed and undisguised breakdown of the charges in a bid, and those who think it is an ethical obligation, an effective business strategy, or both.

**Let’s hear from the anti-transparency camp first.** Their opinions range from matter-of-fact opposition to horror registered with true-believer intensity. At the matter-of-fact end of the spectrum is the opinion offered by veteran remodeler and construction business consultant Jerrald Hayes of ParadigmProjects.com. Jerrald

suggests that transparency is not much of an issue simply because it matters very little to clients. In support of his view, he cites a survey in which homeowners did not bring it up even as they noted a couple of dozen other concerns.

A legendary builder who has been my lifelong mentor once made a related point to me. Clients are buying “value, not price,” he said, and they are not concerned with the way in which charges are broken down in a bid. Other builders claim that transparency on costs and charges is unnecessary because it does clients no good—that spreadsheets filled with rows and columns of numbers just bewilder them.

Still other builders fear client abuse of transparency. A remodeler who operates in Alaska says he did for a time provide detailed breakdowns when he submitted bids to clients. But he gave up on trans-

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parency after clients repeatedly pointed to lower charges for similar items in competing bids to try and bargain down his charges on those items, while accepting his charges for the items on which he was low. He then switched to providing only one number in his bids, namely his total price to do the job.

A now retired remodeler, much admired for building a thriving company with unusually high gross profit margins, amplifies the Alaskan remodeler’s concerns. At a JLC Live conference, while proudly reporting that close to half of every dollar collected from clients went to their salary, other overhead, and profit, this remodeler warned the audience to never practice transparency. “Don’t give a client a breakdown of your charges,” they said. “That’s like giving them a 2x4 to beat you with.” If clients ask for more than a single number, maybe give them a minimal breakdown, but never show your overhead and profit markups. And if they insist on more

breakdown, tell them further information is “proprietary” and that you won’t share it.

Michael Stone, the widely read construction business consultant, responds to the very idea of financial transparency with disdain and dismay. Builders who claim to be practicing transparency are “just playing a numbers game,” he says. He considers even advocacy of the idea to be a betrayal of builders. It disturbed him, he reports, to discover an article in a magazine widely read by builders that encouraged transparency as the best thing for consumers, rather than “looking out for contractors.”

The objections to transparency are united around one primary concern: that by exposing their numbers for overhead and profit, builders risk erosion of their earnings. It is for that reason that one builder limits transparency and protects his markups by providing clients strictly with “retail” numbers. That is, for each item in his bid, he provides a single figure that includes both his direct costs and his markups. For example, if he figured wall framing was going to cost him \$1,000 and he wanted to mark up his costs by 30%, then in the breakdown he offered clients, he would charge wall framing at \$1,300. The builder uses such a presentation because it emphasizes that to reduce cost, clients must change scope by eliminating or changing an item of work, but that overhead and profit are not negotiable apart from scope reduction.

Another builder prefers to just fake transparency. In an interview I did with him for *Nail Your Numbers*, he explained his tactics: He pretends to offer transparency by breaking out overhead and profit because that, he has learned, wins a client’s trust. But his figures, he says, are purposefully “bullshit.” He shows clients what “they want to see.” If they want to see 10% for overhead and 10% for profit, that’s the figure he displays in his bid while concealing his substantial additional markup within labor, material or sub charges. If you want “to make a lot of money,” he says, “that’s what you have to do.” He contends there is “no way” you can make a lot of money in construction while “honestly expressing” your full markups.

**Paul Winans’ view:** Among the builders who have come down on the side of transparency is Paul Winans, formerly head of NARI and a long-time columnist for *Remodeling*. While Winans does not make a big issue out of it, he told a group of other remodelers that he had no problem fully expressing his charges for overhead and profit. He let clients see his gross profit margin of around 40%, explaining to them that’s what is required to run a full-service remodeling company that produced reliable work. Winans attracted plenty of projects and built such a strong company that he was eventually able to sell it in an all-cash deal and retire.

**Michael Anschel’s view:** Michael Anschel, owner of Design+Build in Minneapolis, has given an unusual degree of thought to the benefits and necessity of transparency. If you want to get his full take, check out “The Big Reveal” (the article that Michael Stone experienced as a betrayal of contractors) in the April 2018 edition of *Pro Remodeler*. In brief summary, Anschel concludes:

- Transparency is increasingly the way of the world. It is not a fad, but a requirement for doing business at a global and local level. Builders have to get with it, too.

- Real transparency by builders includes full and honest disclosure of all charges for a project, including project management costs, overhead, and profit.
- Transparency is a sound business strategy. It inspires client trust.
- Transparency makes closing a deal easier. It allows price adjustment for value engineering and cuts in scope to be made in full view of the client. Complicated and awkward attempts to “hide the ball” (as one construction attorney describes attempts to deceive clients about markups) are not required.

**My views:** At a glance, my take on transparency may seem contradictory. I am opposed to it in some circumstances, while in others, especially around markup for overhead and profit, I am so strongly in favor of transparency that I consider it to be an ethical obligation, and the failure to practice it an act of willful fraud.

**A single theme unites the objections to transparency: The naysayers argue that by fully exposing their numbers, especially their charges for overhead and profit, builders put themselves at risk for erosion of their earnings.**

In other words, as I see things, both the obligation to practice and the value of practicing transparency depends on context. It all depends upon the relationship between builder and client during the preconstruction process.

If you operate in the world of competitive bidding, if you create estimates and submit bids for projects at no charge, then in my view you should feel no obligation to practice transparency. Repeat: none.

As I have written in *Nail Your Numbers*, when you submit a bid for free, you have provided a valuable service without compensation. You have no obligation to give all the details of the bid to the client. Present your numbers in any way that you wish. Provide a single lump-sum figure for the whole job. Combine markup and direct costs into “retail” numbers. Play your cards close to your chest or put them on the table. Any demand for a highly detailed and transparent breakdown in a bid that you have spent many hours building and are not getting paid for is, in my view, out of line. You should feel free (to the extent the law allows) to present your numbers in whatever format you think is strategically advantageous.

I will be surprised if many readers disagree with that. But some will disagree with my opinion that in other circumstances—namely when they are charging for estimates rather than bidding

for free—builders do have an obligation to provide transparent, open, honest figures. I think that is the case when you are being paid for what I call “Cost Planning Services” (aka “preconstruction services”), of which the estimate is an important component, and you are working in a collaborative relationship with an owner and an independent designer. Likewise, I believe it to be an obligation if you are offering a design/build service. D/b necessarily includes estimating. Clients are paying for the estimates along with the design and other preconstruction guidance you are providing. They have a right to honest and complete disclosure in the product they are paying for.

Briefly, here are the specific items that I feel we owe clients when we charge for estimating:

- A complete line-item estimate of your direct costs for labor and material.
- Disclosure of any margins of safety, like the lines for “completion” for unforeseen minor items of labor and material such as I include in my estimates.
- So called “naked” costs; that is, the actual quotes to you from your trade partners and suppliers.
- All overhead charges and all profit charges called out on separate lines.
- Very importantly, no additional overhead and profit hidden in any of your figures for labor, material or trade partner costs. That would amount to purposeful deception.

- Copies of your quotes from your suppliers and subs and a spreadsheet displaying your burdened costs for labor at various skill levels so that clients can verify your transparency.
- Why do I ask for that level of transparency? When clients con-

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tract with your company for preconstruction services they are placing enormous faith in you. As part of their gesture of trust, they are

paying you to produce estimates that they can use to evaluate and shape their project. You owe them honest numbers. If you doctor or conceal charges, you are limiting the usefulness of the numbers that they are paying you for and relying upon. Responding with figures designed to serve yourself and deceive or limit them even as you take their money ... well, that is betrayal.

I do know that other builders will take issue with my view. In fact, I can almost hear certain objections likely to be voiced by remodelers and owners of design/build firms. Their objections are often (not exclusively) built around comparisons to other kinds of businesses. Thus, the remodelers will exclaim that restaurants don't show their markups, so why should we have to do it?

The answer is that restaurants aren't charging you to provide numbers. They are offering what amounts to a free competitive bid for, say, a hamburger or a pizza. You can readily compare their bids to other such free bids posted on menus at the burger or pizza places down the street and then choose a bidder. Ditto for lawyers, automotive shops, and toothpaste vendors. And if they want to charge you for their bids, well, then next time you bump into a Sushi joint that wants you to pay for telling you the price of its California roll, demand in return a candid breakdown of its direct costs and margins. You would be entitled to it.

As for the argument that clients are concerned about value not price: The two are joined at the hip. When was the last time you went out to buy something of value and ignored price? You want to get your

money's worth, right? Price is considered in any value calculation.

Now, it may be that some clients are not much interested in delving deeply into transparent numbers. Some may even feel they are not capable of comprehending detailed spreadsheets and will choose to ignore them. But I think that's their decision to make, not mine to make for them.

During my own career, I have almost entirely stayed clear of bidding for free, of so-called "competitive bidding," and have instead won contracts for construction via my Cost Planning service (described in detail in *Nail Your Numbers*). Using it, I get paid for all preconstruction as well as construction work. And, as part and parcel of the service, I do provide full disclosure of my numbers as suggested in the bulleted list above. But, I practice transparency not only because it feels like the right thing to do. I do so because, like Paul Winans and Michael Anschel, I have found it practicable and even financially advantageous. I have the strong sense that full transparency that is verifiable by clients creates trust. It persuades clients that they are working with a reliable builder. And in construction, the creation of such trust not only helps to close deals but, as I am sure every reader of this article knows, is a vital ingredient to the successful delivery of any project.

*David Gerstel has been a licensed builder for four decades. His new book, Nail Your Numbers: A Path to Skilled Construction Estimating and Bidding, is available from independent local and online booksellers.*

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