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Five Risk Myths Demolished

Written by: Bruce Gerhardt, Industry Fellow of Construction Law and Adjunct Lecturer, University of Nebraska-Lincoln

We make decisions about risk every day in our personal and business lives. For construction business owners (and everyone in the construction industry), bad outcomes can mean the difference between staying in business or not. Here are five risk myths that get in the way of thinking about important risks you may be overlooking — and accepting.

1. THINKING ABOUT RISK IS FOR BIG COMPANIES

It is true that the larger the company, the more resources and time can be spent taking a broader look at risk. But for smaller companies, risk can be much more dangerous. Your margin for error with limited financial resources and cash flow is more critical than for most large firms. Less resilience means you need to pay close attention and think about how you identify and manage risk for your firm. You can use simple, cost-effective risk tools in place of the expensive consultants, complicated analyses, and dedicated internal teams that larger firms deploy.

Start with avoiding simple mistakes like overlooking things you know. How? Use checklists. Busy people who work with complex processes and systems are prone to forgetting a simple step, a required form, a critical safety check, etc. Those unforced errors can be costly. Dr. Atul Gawande wrote "The Checklist Manifesto" in 2010. He noted the dramatic effect checklists had on reducing and eliminating errors when used by doctors, pilots, and even investment fund managers: "[T]hey chose to accept their fallibilities. They recognized the simplicity and power of a checklist."

Too simple? You are already using one: your submittal schedule. Checklists can be made, refined, and used for everything from corporate filings and license renewals to field issues like safety and equipment maintenance. The most important ones for your company should be your go/no-go checklist for project screening and your risk register for project-specific risks. Using checklists regularly for all your company's operations will benefit your bottom line, over and over.

2. RISK COMES FROM OUTSIDE MY COMPANY

It is easy to fixate on external risks, but many of the most dangerous risks you face lurk inside your company. Because you understand your business and your company so well, there can be a tendency to discount your own risk — but that can

also create a blind spot right under your nose. In a Harvard Business Review article, Robert S. Kaplan of Harvard and Anette Mikes of Oxford University call these internal risks within an organization "preventable risks" that "are controllable and ought to be eliminated or avoided." Often, it is in your most profitable times that you are likely to overlook these risks.

Vince Lombardi said: "You block and tackle better than the team you're playing, you win." What is blocking and tackling for a construction company? Start with the start. What do you have in place to determine whether to pursue a new opportunity or not? A go/no-go process can screen out later failures and losses where you say: "I should have seen it coming!"

For projects that are won, do a thorough risk register. Identify risks to successful performance, develop mitigation measures, and continually update the plan during the execution. During performance, track and manage change orders, payment, and quality requirements. Reading and understanding the processes and requirements of the contract documents will make sure you are managing this specific project, and not defaulting to the usual practices you have adopted over time. These risks, and the losses they create, are the easiest for you to eliminate.

3. SMALL PROJECTS ARE SMALL RISK

It is only human nature to spend our time worrying about the biggest things, such as the biggest construction projects. You have probably been told the "80/20 rule" says you should spend 80% of your time working on the 20% of things that matter (usually meaning most profitable). But the saying, "It's the little things that come up to bite you" exists for a reason: We overlook the little things. Sometimes these are "pet projects" or an opportunity to get a foot in the door — projects that are taken on for various reasons but do not match the company's typical project size or type (or both). Small projects tend to suffer from a lack of sustained management interest, a lack of sufficient experienced staffing, and a lack of planning and risk identification. When one of these projects results in a claim or lawsuit, you may find your small project just brought on a big exposure. Physical injuries, consequential damages like lost profits and regulatory enforcement can mean you will have expenses that dwarf the small profit you could have made — if all had gone well. Many small projects miss a formal go/no-go process and a risk register because it "just wasn't worth it." Bottom line: Risk can be very disproportionate to project size.

4. ONLY BAD PEOPLE DO BAD THINGS

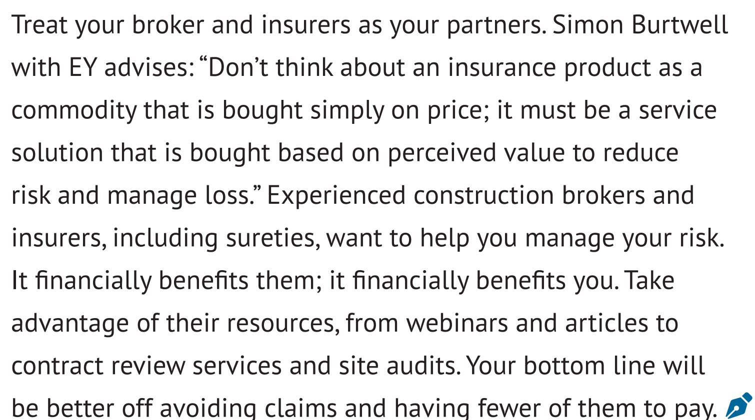
Mark Ingebretsen, author of "Why Companies Fail," wrote: "Perhaps nothing can bring a company down with such amazing speed as misconduct." Employee misconduct happens in smaller companies, and by people who friends and coworkers know as nice, quiet, and respected.

Florida Atlantic University College of Business (FAU) reports that "smaller businesses (less than 100 employees) are more vulnerable to fraud than larger ones. … " A business.org survey found 22% of small businesses had employees steal from them. FAU points to several causes: lack of internal controls, higher rates of fraud by small business owners and executives, and the tendency to have a single person in charge of many areas without effective oversight. But this couldn't possibly happen to your company, where you know everyone, right? According to a 2016 article by Andrew Donohoe and Stephanie Allgeyer with VonLehman CPA, 85% of employees committing fraud are first-time offenders. It happens over and over to the least suspecting.

You won't recognize anyone in your company as being someone capable of fraud, theft, or any other type of misconduct. If you could, you wouldn't have hired them in the first place. Internal systems and financial controls have to be in place for this reason — by the time you realize someone was stealing from you or engaging in other types of misconduct, it may be too late for your company to survive.

5. INSURANCE TAKES CARE OF RISK

Many employees, from the CEO to your front-line workers, think insurance takes care of everything. Other companies may think of your insurance that way too: "Just submit the claim to your carrier. What do you care?" Anyone who has been through the underwriting process for policy applications or renewals knows how important your company's loss experience is to the cost of insurance. Just as important to the insurer is how you manage your business, including claims and settlements. Premiums, coverage offered, exclusions, and deductibles or self-insured retentions — all are impacted by how you treat an insurer's coverage. Is it with as much care as you would show



for your own money? Those claim payments are recaptured in future premiums — think of it more as loss financing than loss coverage. Over time you will be paying it back.

Treat your broker and insurers as your partners. Simon Burtwell with EY advises: “Don’t think about an insurance product as a commodity that is bought simply on price; it must be a service solution that is bought based on perceived value to reduce risk and manage loss.” Experienced construction brokers and insurers, including sureties, want to help you manage your risk. It financially benefits them; it financially benefits you. Take advantage of their resources, from webinars and articles to contract review services and site audits. Your bottom line will be better off avoiding claims and having fewer of them to pay.

About the Author

Bruce Gerhardt is an industry fellow of construction law at the University of Nebraska's Durham School of Architectural Engineering and Construction Management. He teaches professional practice and ethics courses to construction management and architectural engineering students. A lawyer since 1994, he spent 22 years in the legal department of an ENR top 10 design firm, where duties included risk management and insurance issues.

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